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IDEAS ON LIBERTY

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PERSPECTIVE

Shifting the Terms of the Debate

An ancient legend has it that a Roman emperor, asked to judge a singing contest between two entrants, heard only one contestant and gave the prize to the second under the assumption that the second singer could be no worse than the first. The problem with the Emperor's judgment, of course, was that his assumption was unwarranted. The second contestant might have been much worse.

Unfortunately, much of the popular debate concerning whether the market or government should be relied on to provide certain goods and services follows the same myopic pattern of behavior as that of the Emperor. When the market economy can be shown to "fail" in some area, it is simply assumed that the government can provide the service better. One of the most important tasks of economic education is to reverse this lopsided way of thinking.

Adam Smith, for example, argued in *The Wealth of Nations* that not only would the government not be in a position to efficiently judge the best use of scarce resources, but that "The statesman, who should attempt to direct private people in what manner they ought to employ their capitals, would not only load himself with a most unnecessary attention, but assume an authority which could be safely trusted, not only to a single person, but to no council or senate whatever, and which would nowhere be so dangerous as in the hands of a man who had folly and presumption enough to fancy himself fit to exercise it."

The great French economic journalist, Frederic Bastiat, wrote in his classic essay, "What is Seen and What is Not Seen," in *Selected Essays on Political Economy* that "There is only one difference between a bad economist and a good one: the bad economist confines himself to the *visible* effect; the good economist takes into account both the effect that can be seen and those effects that must be *foreseen.*" The full extent of the harmful effects of such government policies as taxes, public works, and restraints of trade unfortunately can only be gleaned by a careful and thorough examination of interventionism and its effects (both direct and indirect) on the economy.

Though the debate over government versus free market is old it is never ending. Each generation must fight the battle anew. The free market response to advocates of government intervention is twofold. First, it must be pointed out that many so-called market failures are not really failures of the market but instead the consequence of government failure to clearly define and strictly enforce private property rights. Second, it must be stressed that even in situations where the market could be said to fall short of the optimality conditions of the best of all possible worlds, the proposed government remedy may actually worsen the situation. This type of argument has been put forth by generations of economists from Adam Smith to J. B. Say to Ludwig von Mises to F. A. Hayek to Milton Friedman to James Buchanan. Sometimes their arguments have carried the day—if not in policy implementation at least in policy discussion. At other times, the teachings of economists who possess a boundless optimism concerning the ability of the government to solve our problems dominate. Economists who favor government intervention in a wide array of economic affairs, such as John Maynard Keynes, Paul Samuelson, and John Kenneth Galbraith, have more or less dictated the terms of the debate for most of the post World War II era.

During the 1980s, the terms of the debate shifted so that the burden of proof was on those who proposed government intervention. Unfortunately, the debate has shifted back again so that the presumption in the policy debate is that the government can provide an easy and efficient remedy to economic ills. The recently released *Economic Report of the President*, written by the administration's leading economists Laura D'Andrea Tyson, Joseph Stiglitz, and Alan Blinder, officially signaled the shift in the terms of the debate. The *Report* calls for economic intervention by the government, including "microeconomic initiatives to promote efficiency and productivity." As the *New York Times* (February 15, 1994) pointed out, the *Report* does not examine the age-old free market litmus test for justifying government action (i.e., identifying the market failure, and then examining whether the government could outperform the market in dealing with the problem). Instead, the *Report* identifies market failures alone. As Laura D'Andrea Tyson stated herself in the press conference to announce the publication of the *Report*, "I think there is something different in the whole tone of this. . . . There is a lot here implicitly about the role of Government to do something that would be beneficial . . ."

Laura D'Andrea Tyson, Joseph Stiglitz, and Alan Blinder are accomplished economists—in many ways leading representatives of their generation. Their arguments must be addressed in the most scholarly manner possible. We will find neither a complete nor effective answer to their arguments in Mises or Hayek or Friedman or Buchanan, let alone Smith or Bastiat. Repeating the basic principles of the free society taught by these great thinkers is not enough (though, of course, it is a good start). Instead, we must find the answer to these "new" challenges to the market economy ourselves.

As Mises pointed out in his preface to the Henry Regnery edition of Adam Smith's great treatise, "the reader will [not] find in the *Wealth of Nations* a refutation of the teachings of Marx, Veblen, Keynes, and their followers. . . . Read the great book of Smith. But don't think that this may save you the trouble of seriously studying modern economics books." Similarly, the debate has now shifted to a new generation. Free market thinkers must address the questions of 1994 and beyond, with fresh refutations of modern theorists who favor government solutions over the voluntary choices of individuals within the market.

—Peter J. Boettke

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LODGE DOCTORS AND THE POOR

by David T. Beito

Medical Care Before the Welfare State, 1900–1930

On the face of it, a historical study of fraternal societies seems to be a subject fit only for connoisseurs of the arcane. Few Americans these days come into contact with such groups. When many of us hear the word *lodge*, we think of it as a place where television characters from our youth, such as Ralph Kramden (of the Loyal Order of Raccoons) and Fred Flintstone (of the Loyal Order of Water Buffalos), escaped from their more sensible wives to engage in childish hijinks—parading around with silly hats and mouthing pretentious rituals.

There was a time, however, when fraternal societies could not be so easily dismissed. Before the rise of the welfare state, they were rivaled only by churches as organizational providers of social welfare. By conservative estimates eighteen million American men and women were members in 1920—at least three out of every ten adult males. While fraternal societies differed in ethnicity, class, and gender, most shared a common set of characteristics. In general, this included a decentralized lodge system, some sort of ritual, and the payment of cash benefits in times of sickness and death.

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By the turn of the century, an increasing number of societies began to add treatment by a doctor to their menu of services. This arrangement was known as lodge practice. It involved a simple contract under which a physician provided care in exchange for an annual salary determined by the size of lodge membership. To qualify, a prospective lodge doctor had to win an election by the members. Generally lodge practice plans did not extend beyond basic primary care and minor surgery, although a few provided hospitalization.

Lodge practice became particularly extensive in urban and industrial centers. In 1915, for example, Dr. S. S. Goldwater, Health Commissioner of New York City, went so far as to assert that in many communities it had become "the chosen or established method of dealing with sickness among the relatively poor." In the Lower East Side of New York City, he noted, 500 physicians catered to Jewish societies alone. Among blacks in New Orleans there were over 600 fraternal societies with lodge practice during the 1920s.

Nationally, the two leading providers of lodge practice among native whites were the Foresters and the Fraternal Order of Eagles. By 1910, both organizations had over 2,000 doctors under contract to look after the medical needs of about 600,000 members. Yet, aside from the common thread of lodge practice, the Foresters and Eagles were actually quite unalike as fraternal societies.

The Foresters

The Foresters traced their origins directly to the Ancient Order of Foresters, a British organization. The ritual drew inspiration from Robin Hood and his legendary adventures in Sherwood Forest. In keeping with the medieval motif, the lodges were called "courts" and the supreme leader a "chief ranger." Both women and men could join (although in separate courts) and the only tests for membership were belief in a supreme being and good moral character.

Foresters were quintessential internationalists. In an age of self-conscious Anglo-Saxon exclusivity, they were notable among fraternal societies for seeking converts not only in Europe but also in Asia. The chief ranger for over two decades was a Dr. Oronhyatekha, a Canadian Mohawk. Equally remarkable for the time, his ancestry was not a cause of embarrassment for the members; in fact, they wore it as a badge of distinction. One member boasted that "There is not a Forester in the wide world but knows that this full-blooded Indian chief is the one man to whom the Order should be thankful for its wonderful growth."

The Eagles

While the Foresters eschewed nationalism, their leading rival for lodge practice, the Fraternal Order of Eagles was almost a caricature of apple-pie Americanism. The Eagles opened their first lodge in Seattle, Washington, in 1898. The members embraced a fun-loving and informal style quite unlike more solemn co-fraternalists, such as the Free Masons. The aeries (as Eagles called their lodges), with their well-stocked bars, often served double duty as local community centers. This freewheeling behavior earned the Eagles an unsavory reputation in some quarters. In 1910, *McClure's Magazine* characterized the group as "a great national organization of sporting men, bartenders, politicians, thieves, and professional criminals." The Eagles later refurbished this unwholesome image somewhat by launching a highly visible, and ultimately successful, campaign for the proclamation of Mother's Day.

Less than ten years after the Eagles had been founded, they became noted (notorious in medical society circles) for engaging in lodge practice. For one dollar a year, a member and immediate family could receive basic medical services (including minor surgery). This fee did not pay for treatment for obstetrics, venereal disease, and "any sickness or injury caused or brought about by the use of intoxicating liquors, opiates or by any immoral conduct."

Ladies Friends of Faith

Unfortunately, primary data from individual societies with lodge practice is in very short supply. Nevertheless, some records survive which can shed light on the subject. Particularly helpful is a minute-book from the Ladies Friends of Faith Benevolent Association, covering the period from August 1914 through September 1916. It was a black female society of about 170 members which operated in New Orleans during the early twentieth century.

The Ladies Friends of Faith was not exceptional, at least within the broad context of New Orleans. It was only one of numerous such societies which offered lodge practice to blacks in the city. Among these were local affiliates of two prominent national organizations, the Eastern Star and the Household of Ruth. Much more common, however, were home-grown societies such as the Female Union Band, Young Men of Inseparable Friends, Francs Amis, Holy Ghost, and the United Sons and Daughters. A simple reading of 134 organizational names from a list assembled in 1937 indicates that no less than 40 catered primarily to females.

In terms of organizational structure and benefits, the Ladies Friends of Faith also fit the general local pattern. The rank-and-file voted in annual elections to choose a "society" druggist, doctor, and undertaker who provided services at a low flat rate. Those taken sick collected two dollars a week if they saw the lodge doctor and three dollars if they did not. To guard against false claims for cash benefits and to provide companionship, a visiting committee sat at bedside with the recipient. Those members derelict in these duties had to pay a one-dollar fine.

In this two-year period, the minute-book evidences great activity. One hundred and thirteen individuals (slightly over half the membership) collected sick benefits. Of these, 70 used the lodge doctor at least once; several a dozen times or more. Almost all these applicants obtained cash payments and medical service (including free medicine) without eliciting complaints from the other members.

This does not mean that the deliberation process of the Ladies Friends of Faith was without controversy. Most notably there was a persistent need to grapple with appeals from individuals who had fallen in arrears. At nearly every meeting, the society heard at least one plea from a member unable to pay because of unemployment or poor health. One of the most desperate of these concerned a woman who was "out of Doors, and had no money." In such cases, the society was generally ready to extend help. It allowed 24 members extra time to pay off their debts while it passed the hat for ten others. Not once did the Ladies Friends of Faith reject any of these appeals outright. Such liberality did not translate into open season on the lodge's treasury, however. Those delinquents who failed to explain their "unfinancial" status were readily dropped from the rolls.

Regardless of religious, ethnic, or political orientation, all fraternal societies, to the extent they relied on lodge practice, faced a similar set of obstacles. Without a doubt, the most serious was the organized opposition of doctors. By the first decade of the twentieth century, the spread of what became known to critics as the *lodge practice evil* elicited almost universal condemnation among medical societies.

At its core, this opposition represented fear for the future survival of the dominant fee-for-service remuneration. Writing in the *Wisconsin Journal of Medicine*, Dr. W. F. Zierath of Sheboygan, Wisconsin, put the matter succinctly when he chided certain fellow members of the profession for bowing so readily to "the keen business instinct of the laity" who have "discovered in contract practice a scheme to obtain medical services for practically nothing . . . they are organizing societies by the score with that feature as the excuse for their existence." Once doctors allowed themselves to be placed on a fixed payment system, he warned, loss of both income and independence would soon follow. The profession would then become tainted and demoralized by every doctor's cutthroat and undignified scramble to sell to the lowest bidder. Another opponent predicted that lodge practice, if not stopped, would depress fees to levels "comparable to those of the bootblack and peanut vendor."

Lodge elections were depicted as carnivals of corruption in which victory went to those doctors best able to ingratiate themselves with key players in the leadership through extravagant promises or outright bribery. Even when outright corruption did not occur, the critics portrayed the election campaign as dominated by unseemly wire-pulling and backslapping. According to Dr. Zierath, success of a candidate depended upon "the handshaking, the button-holing, the treating to cigars and drinks in public houses."

According to these critics, however, lodge practice was not only bad for doctors, but it also harmed the patient. While they conceded that the fees were low, they warned that the service given in return was shabby. Along these lines, a leading professional journal condemned lodge practice as a vain attempt by the patient to get "something for nothing."

Who Benefited?

Lodge practice, in my view, merits a far more favorable assessment than it received either from contemporary critics or more recent historians. At first blush, such a contention would seem impossible to defend. Most of the surviving sources on which the historian must rely already have turned in a ringing verdict of guilty. This research problem is not fatal, however. Ironically, the strident manifestos published in the medical journals contain a wealth of information which can cast a positive light on lodge practice. With great profit, these professional critiques can be supplemented and compared to the still extant defenses written by doctors and leaders of fraternal societies.

The most important beneficiary of lodge practice was, of course, the patient of modest means. He or she was able to obtain the care of a doctor for about two dollars a year—roughly equivalent to a day's wage for a laborer. If translated into 1994 dollars, this annual fee would be equivalent to about 14 dollars, the hourly wage of some construction workers today!

The remuneration paid to the lodge doctor was a far cry from the higher fee schedules favored by the profession. A local medical society in Pennsylvania was typical in setting for its members the following *minimum* fees: one dollar per physical examination, surgical dressing, and housecall (daytime) and two dollars (nighttime). Such prices, at least for continual service, would have been out of reach for many poor Americans.

Why were the lodges able to charge such low fees? The answer to this question lies with several organizational strengths peculiar to the fraternal structure itself. The fact that lodges could entice doctors with a large and stable market left them well positioned, as one opponent put it, to purchase medical services at wholesale and sell at retail.

Also exerting downward pressure on fees were lodge elections. While the election process was not without flaws, there is also ample evidence from both supporters and opponents that, on balance, it served members well. It gave patients an opportunity once a year to compare notes on the medical records of both the challenger and incumbent. John C. McManemin, the Past Worthy President of the Eagles, maintained that as "the members have the right of franchise in electing the lodge physician, so have they in deposing him, and it therefore results that unless the physician so selected, attends to the duties devolving upon him he is quickly brought to account." From a very different perspective, a leading opponent of lodge practice complained that during campaigns "colleagues and rival applicants are roundly 'knocked' and their mistakes and capabilities held up to public ridicule and censure."

Quality of Service

Closer inspection of the medical journals also gives some cause to be skeptical of blanket claims that lodges heedlessly sacrificed quality to elect the candidate bidding the lowest fee. The contrary, in fact, occurred in a campaign described by lodge-practice adversary Dr. George S. Mathews of Rhode Island:

> . . . in one lodge two members in good standing in the State Medical Society openly in lodge meeting underbid [each other]. One volunteered his services at $2 a head. The other dropped his price to $1.75. The first bidder then acceded to this price with medicines furnished. This occasioned a drop in bidder No. 2 in his price to include medicine and minor surgery. To the vast credit of the lodge neither bid was accepted but a non-bidder was given the job at $2.

Even the detractors, while generally disdainful of the quality of care provided, acknowledged that fraternal societies attracted some doctors of ability and high training. In Dr. Goldwater's opinion, for example, there were "many competent medical men and between the slip-shod service of the poor kind of dispensary, and the painstaking care of the conscientious lodge doctor, the choice easily lies with the latter." It is worthy of note that the hack often inspired less contempt than the physician with a lucrative private practice who took a lodge contract on the side. One leading critic excoriated such individuals as "inordinately selfish and avaricious men who have no neighbors in the profession, for they are not Samaritans by practice."

Proprietary Medical Schools

Also misleading were efforts to dismiss the abilities of lodge doctors by citing their low level of medical education. For many opposed to the system, it was merely sufficient to note that these doctors graduated disproportionately from the ranks of the proprietary medical schools. While as a description of reality this was probably accurate, it fails as an indictment. To understand why, a bit of background about proprietary education might be helpful.

These schools had two salient features. First, they were owned by doctors in regular practice and second, unlike the endowed university, they subsisted entirely on tuition. The owners earned income both from tuition received in exchange for delivering lectures and from sometimes lucrative referrals tendered by grateful graduates. The students often came from modest backgrounds and thus lacked both the contacts and financial pull enjoyed by many of their counterparts in the universities. The alumni of these proprietary schools would have ample incentives to be attracted to lodge practice. For a recent graduate especially, a contract with a fraternal society might be the only means available to obtain the necessary financing and community contacts needed to build up a practice.

To call these doctors *quacks*, however, as many critics did, would be a misnomer, at least in the strict meaning of the term. Like every other aspiring doctor, they needed to receive state certification to practice. By no means was this pro forma. Since the 1880s and 1890s, the requirements had become increasingly stringent and failure rates were high. In short, the lodge doctor may not always have been top-of-the-line but he or she had at least rudimentary training.

As the purchaser of these services, the fraternal society also had incentives to maintain the quality of care. An incompetent or arbitrary doctor could prove fatal to actuarial soundness. Moreover, if fraternal advertisements are any indication, prospective members were leery of organizations with high mortality rates. The publicity for the Foresters repeatedly contrasted the death rate of its members (6 per 1,000) with that of the same age group in the general population (9 per 1,000). It credited this low mortality to "Sherlock-Holmes-like acuteness in the detection of bad risks" exhibited by the doctors attached to its courts. This boast was more than hyperbole. In the first decade of the twentieth century, the doctors of the Foresters annually rejected between ten and twenty percent of all initiates.

Additionally to ensure quality of care lodges often imposed specific sanctions, in the form of fines, for doctors who neglected their duties. Among the possible infractions were failure to report at meetings, fraudulent approval of sick claims, and refusal to respond to a patient's housecall. For the latter violation, for example, both the Eagles and Foresters authorized a lodge to hire a substitute from the open market and then deduct the charges from the salary of the delinquent lodge doctor.

An important consequence of lodge practice for the patient was to facilitate habits of assertiveness. The members who used these services anticipated by several decades the *active patient* now very much in vogue. Many physicians, obviously unaccustomed to such treatment, denounced the willingness of members to quibble about fees and diagnosis. One doctor blamed excessive and unnecessary housecalls for engendering fears in the doctor "that he will lose his position if he fails to answer every call regardless of circumstances and his knowledge of the fact that he is being imposed on constantly by members who abuse their privileges."

For the patient, if not always the doctor, lodge practice had the additional virtue of affording accessible preventive care. Again, one need look no further for evidence than the repeated accusations in the professional journals that doctors were being pestered with trivial ailments. According to Dr. Zierath, the patient called on the lodge doctor at all hours of the night "to see cases repeatedly where a physician would not be called, were the regular fee to apply. One of the children in a family has abdominal pain, and the anxious mother promptly conjectures that it is appendicitis'' when it was nothing more ''than too much indulgence in mince pie. But it looks stylish to have the doctor's rig standing in front of house and excites the curiosity and envy of the neighbors, therefore the 'free' doctor is summoned.''

For fraternal societies, by contrast, the ability to readily call on the doctor for any complaint was a major selling point. Lodge practice, wrote a leader of the Eagles, ''accords perfectly with the modern theory of the prevention of disease . . . Many of the poorer members, under other circumstances might delay in calling a doctor until the disease made considerable headway.''

Lodge practice opened up rare opportunities for many working-class Americans to compare and experiment and empowered them with the necessary economic clout to break free from the confining view that health care was merely a generic good. It gave patients the wherewithal to use medical services more as a varied menu of choices, each adjustable to suit the particular need at hand.

The discernment of lodge patients was exemplified by their selective patronization of medical services. They may have readily turned to their lodge doctor for prevention, for example, but many looked elsewhere for a cure. On this note, an exhaustive study of blacks in New Orleans, who were members of fraternal societies during the 1930s, found that while 56 percent relied exclusively on the doctor hired by their lodge, the rest also hired private physicians in some cases. A member of one of these societies expressed a typical view when he commented, ''Well, I think there is nothing better than a society for when you're sick they give you the best possible attention, but if I were real sick I'd prefer calling a doctor not connected with a society, so that I could get the best of attention. Society doctors are too busy to handle extreme illnesses.''

Decline of Lodge Practice

Even before the Depression, lodge practice had begun to fall into a state of decline. The pressure exerted by the leaders of organized medicine hastened the demise. By the 1910s, doctors had launched an all-out war against lodge practice. Throughout the country, medical associations imposed a range of sanctions against lodge doctors, including expulsion from the association and denial of hospital facilities. In certain instances, campaigns were organized to deny patient care, even in emergencies, to members of offending lodges. Most commentary from both sides of this conflict indicates that these sanctions were highly effective. In any case, by the end of the 1930s, the once vibrant health care alternative of lodge practice, which less than two decades before had inspired trepidation throughout the medical establishment, had virtually disappeared. □

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A Feminist Lesson from Economics

by Deborah Walker

With the collapse of Communism, economists have finally figured out that economic planning does not work. This does not mean, of course, that the economic planners don't continue to try; some will never concede defeat, even when theory and history tell them to give up. Along with the economic planners are the social planners, who usually call themselves egalitarians or defenders of social justice. But the truth is, they, too, along with the economic planners, should throw in the towel. Interestingly, the reason why the social planners should give up is the same reason why the economic planners should consign their visions to the dustbin. It all has to do with knowledge.

Let me explain by focusing on one social movement in the United States which is ripe with social planning: mainstream feminism. Although feminists generally argue that the use of legislation as social planning has its limitations, they see legislative change as at least a partial means to positive cultural change.[1]

Complete cultural change requires an entire transformation of many existing institutions such as "the family, childrearing arrangements, the economy, the wage labor market, and human consciousness."[2] So, in fact, legislation is seen as a compromise to real reform, which requires the abolition of markets.

The Problem With Planning

Since the whole abolition of markets is not feasible to most, legislative mandates are the next best thing. Always keep in mind that planning is planning; whether on a large or small scale, the same problem arises. This problem is what F. A. Hayek calls a knowledge problem.

Each individual in an economy possesses knowledge only some of which is known by others. This *subjective* knowledge of particular time and circumstances is that of one's values, tastes, plans, talents, desires, and so on. This knowledge, of a contextual nature, is dispersed throughout the economy, and is constantly changing.[3] Furthermore, much of this knowledge is inarticulate or tacit. Because of the contextual and subjective nature of knowledge in society, any one person or group of persons cannot possess all of this knowledge. The basic economic problem that all societies face, therefore, is how to utilize this knowledge.

Ludwig von Mises explains exactly why economic calculation, the utilization of subjective and dispersed knowledge, in a planned economy is technically impossible.[4] According to Mises, there are really two processes of economic valuation in an economy: that of the consumer and that of

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the producer. Both processes are necessary for economic calculation and coordination. For example, even if the planners could know the subjective valuations of goods by the consumers in an economy (or even assume that they know what should be valued by consumers) and the best production techniques for producing these goods, economic calculation would still be impossible. This is because there would be no means for knowing or calculating how the scarce productive resources should be utilized. That is, how would the planners know if a piece of land should be used as a site for a factory or for a potato farm or for any other number of uses? Mises explains that what is necessary for economic calculation is private ownership of the means of production. Without the existence of *prices* and the profit calculations they make possible, central planners could never possess the knowledge necessary to direct resources so that people's basic wants are satisfied. It is the private ownership of the means of production which leads to a competitive bidding process among resource owners, which in turn generates market prices for these resources.[5] It is with the use of these market prices that economic calculation takes place.

What is important to note here is that the economic phenomena being conveyed or "calculated" in a market price are subjective in nature. That is, they are the subjective valuations of individual actors in any market. The "objective" price seen in a market is the result of the interaction of the subjective valuations of numerous market actors. As Mises explains, "The subjective use-value of each [commodity] is not immediately comparable as a purely individual phenomenon with the subjective use-value of other men. It only becomes so in exchange value [price], which arises out of the interplay of the subjective valuations of all who take part in exchange."[6] It is this subjective nature of economic phenomena that dismisses the possibility of economic calculation under socialism.

And it is also the subjective nature of social phenomena which dismisses the possibility of successful social planning. Just as economic planners must "guess" where resources should be utilized because it is impossible for them to know the subjective valuations of consumers and producers, social planners, attempting to produce equal opportunities for both men and women, must also "guess" at what the subjective term "opportunity" means to *all* women. But this is also an impossibility.

Opportunities Cannot Be Objectified

Opportunities are subjective in nature. Furthermore, the knowledge regarding what different individuals value as opportunities is dispersed throughout society, is contextual in nature, and is constantly changing. Social planners could never possess all of this information. How then, could they be successful at organizing society such that all opportunities are "equal." In fact, since opportunities are subjective in nature, they cannot be objectified or thereby "equated" one with another.

In a planned system, whereby women are told that they *must* play a certain role (or roles) in society, it is difficult to argue that this is a system which allows for individual women to plan their own lives and decide their own opportunities. This will always be the major problem with centralized social planning of any scale: the individual woman can never be the focus of attention, only women in some sort of generic sense. Therefore there will always be a large number, if not the vast majority, of women who are not satisfied with what the planners decide to do. Decentralized planning, with each woman planning her own life, would be more successful than centralized social planning in fostering an atmosphere in which opportunities remain where they actually are: in the minds of individual women.

Furthermore, planners do not seem to comprehend the complexity of our society. Because of the complexity of market orders, they cannot be planned with any degree of success. This is also true, for the social order in general. In fact, the more complex an order is, the more spontaneous it must be. Attempting to plan the order such that a particular end is reached will be futile. But just as important, this attempt will also produce unintended and undesirable consequences, only some of which can be predicted.

Important in this idea of markets as spontaneous orders, as Hayek explains, is that individuals within markets must be guided by general rules, *not* by specific commands. General rules provide a framework under which individuals act in a more or less similar way. Because these rules are general, they are applicable to a variety of circumstances and, most important, allow people to utilize their individualized "knowledge of time and circumstance." Hayek explains, "They [the rules governing a spontaneous order] will have to be applied by the individuals in the light of their respective knowledge and purposes; and their application will be independent of any common purpose, which the individual need not even know."[7]

In her book *Reclaiming the Mainstream: Individualist Feminism Rediscovered,* Joan Kennedy Taylor argues that the feminist movement in the United States has gone through several important changes since its conception. The most important of these was the movement from a focus on individualism to that of collectivism.[8] Another way of approaching this idea is that when feminists focused on the individual, the desire was to change the general rules of society so that they applied to both men and women in the same (or near same) manner. In other words, the focus was on equality under the law in general, or equality with respect to the process, to the rules of the game—not equality with respect to specific ends.

Women, therefore, demanded the right to own property, to sue, to make contracts, and to vote, all of which men could already do. Hayek explains that general rules, "must be the same, if not necessarily for all members, at least for whole classes of members not individually designated by name."[9] Although one can argue that there should be general rules which apply differently to men and women (for example, whether women should enter combat or not), these should be exceptions and not norms, especially if women themselves desire to have the same general rules in all cases. This is because the general rules of society should change as cultural norms change. In actuality, some general rules *are* cultural norms, while others are deliberately designed. And, in fact, these two "types" of general rules work together or influence one another.

It was a change in the cultural norms that led women to call for changes in the deliberately designed general rules of society (the demand for property rights and the like). And, in turn, these changes in the general rules influence cultural norms.[10]

Women Enter the Market Arena

Two of the most important changes individualist feminism made with regard to the general rules of society were giving women the right to own property and to make contracts. Both of these rules are prerequisites of a market order. Allowing women these rights, therefore opened up the possibility for women to enter the market arena.

Before explaining the importance of these particular changes, it should first be noted that both the freedom to own property and to make contracts are general rules, and not specific commands because the actual ownership rights and the terms of individual contracts are left to the market participants. The general rule is that contracts can be made, and then can be legally upheld. Legislative mandates, which force the terms of particular contracts, are not general rules, but are instead specific commands. The terms of contracts are no longer left to market participants, but are instead stipulated across the board.

It is unfortunate, but today most feminist goals are often set in very specific terms: the desire for more women in upper management or public office (a set number or percentage of population is often given), the desire for equal wage rates between men and women, or the desire for all businesses to offer very specific terms of employment, to name a few examples. Given these particular or specific goals, legislative mandates are set in place in order to bring them about. Instead of the intended goal, however, what we get are unintended consequences such as an increase in sex discrimination and a decrease in self-determination by women.

Now, why is freedom of contract, specifically, so important to women? First, again, as Hayek explains, "although we can endeavor to improve a spontaneous order by revising the general rules on which it rests, and can supplement its results by the efforts of various organizations, we cannot improve the results by specific commands that deprive its members of the possibility of using their knowledge for their purposes."[11] In other words, specific commands hinder market actors by not allowing them to adjust the general rules to their individual circumstances by utilizing their unique knowledge.

Women and the "Knowledge Problem"

Why is the utilization of individual knowledge in labor markets so important to women? In essence, employers face a "knowledge problem" regarding which employees to hire. They must trade off the costs of screening individual employees with the costs of missing out on hiring very productive workers. This is why firms, indeed market forces, have produced different ways by which employers can screen employees at lower costs. These include employment agencies, interviews, references, different types of employment tests (such as aptitude or skill level tests), as well as brand names in educational and vocational institutions.

All of these devices decrease screening costs for employers and thereby increase the likelihood that potential employees will be hired on the basis of their individual attributes rather than on the basis of their group membership. This is especially applicable to women because men and women are biologically, and sometimes culturally, different. These differences are often viewed by employers as statistical differences in terms of employment practices. For example, women, on average, have higher turnover rates than men; women, on average, are more likely to take time off upon the birth of a child, and so on. Anything which increases the flow of information regarding individual employees will lead to a decrease in employer discrimination based upon these group averages. Insofar as the flow of information is interrupted, employers' screening costs remain high and they resort to hiring on the basis of statistical averages. Legislation that prohibits the use of employment tests, for example, on the basis that the tests are biased against particular groups in society will actually decrease the likelihood that individual members of these groups can set themselves apart from the group and be hired on individual merit considerations.[12]

The freedom to make creative, individualized employment contracts can be a vital source of information to employers and thereby decrease discrimination. Legislative mandates take away this means for individual women to distinguish themselves, but more important, they take away the very method by which women can bring about social change without the use of legislation.

In fact, it is the unique ways in which individual economic actors can utilize their specific knowledge within a market order that will determine the changes in the order over time. "The particular content of the order will depend on the concrete circumstances known only to the individuals who obey the rules and apply them to facts known only to them. It will be through the knowledge of these individuals both of the rules and of the particular facts that both will determine the resulting order."[13] The point being, the order will change over time as individuals apply their particular knowledge to the rules of the order. But note that the order changes according to this knowledge, which contains individual tastes and subjective values of market actors. The resulting order is something which emerges spontaneously in the sense that there was no deliberate design of the whole order. Instead, the order adjusts to the individual actions of people within the order.

What message does this give to feminists who desire social change? It says that it is up to women themselves to change the order from within. The order cannot be changed through legislative mandates for two reasons: the unintended consequences which result in decreased opportunities for women, and because mandates actually destroy the very means to social change that women have—the utilization of individual knowledge through freedom of contract.

This idea of social change through freedom of contract does not appeal to many feminists because it places the responsibility for change on those who desire the change. It provides the message to women that they are not passive agents in social evolution, but are instead responsible for a large amount of that evolution. It maintains that markets do not take opportunities away from women, but instead, that markets actually provide opportunities for women to instigate social change. □

1. See, for example, H. Hill Kay, "Models of Equality," *University of Illinois Law Review*, 39, 1985; S. Law, "Rethinking Sex and the Constitution," *University of Pennsylvania Law Review*, 955, 1984; A. C. Scales, "Toward a Redefinition of Sexual Equality," *Harvard Law Review*, 95, 1981; and K. T. Bartlett & R. Kennedy, eds., *Feminist Legal Theory: Readings in Law and Gender* (Boulder, Colo.: Westview Press, Inc., 1991).
2. Law, p. 965.
3. Friedrich A. Hayek, "The Use of Knowledge in Society," *Individualism and Economic Order* (Chicago: University of Chicago Press, 1948), pp. 77–91.
4. Ludwig von Mises, "Economic Calculation in the Socialist Commonwealth," in *Collectivist Economic Planning*, ed. Friedrich A. Hayek (New York: Augustus M. Kelley, 1975 [1935]), pp. 87–130.
5. *Ibid.*, see p. 108.
6. *Ibid.*, p. 97.
7. Hayek, p. 50.
8. Joan Kennedy Taylor, *Reclaiming the Mainstream: Individualist Feminism Rediscovered* (Buffalo, N.Y.: Prometheus Books, 1992).
9. Hayek, p. 50.
10. The moral arguments for the rights of women to own property and to make contracts are beyond the scope of this paper. However, they are not considered to be unimportant.
11. Hayek, p. 51.
12. See Richard Epstein, *Forbidden Grounds: The Case Against Employment Discrimination Laws* (Cambridge, Mass.: Harvard University Press, 1992).
13. Hayek, p. 46.

THE FREEMAN
IDEAS ON LIBERTY

The Incredible Ticket Machine

by Jerry Ellig

Way back in high school, a far-from-right-wing teacher made our class sit through a short film called "The Incredible Bread Machine." The story's protagonist invented a bread-baking machine so productive that it vastly reduced bread prices and promised to end world hunger. But instead of praising his achievement, the government pilloried him as a monopolist, claiming that he drove competitors out of business and charged monopoly prices. He could do both because his wondrous invention dramatically slashed the cost of baking bread. Despite this boon to society, the movie implied that the inventor landed in the pokey for a Sherman Act violation.

Even during the malaise years of the late 1970s, the movie sounded like a stretch of the libertarian imagination. Surely, if someone invented a technology that is superior, even politicians and regulators would have to recognize him as a benefactor and let him go about his business.

Recent events in the airline industry have shown otherwise. During the past 20 years, several airlines developed a new, computerized technology to process reservations and issue tickets that is the equivalent of the "Incredible Bread Machine." Unfortunately, the developers of airline computerized reservation systems have fared little better than the ill-fated inventor of the bread machine.

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What Is a Computerized Reservation System?

The Airline Deregulation Act of 1978 freed airlines to enter new routes and charge whatever fares they could induce customers to pay. In this new, deregulated environment, an airline of any size has thousands of different route combinations, generating tens of thousands of different airline fares. Before the invention of computerized reservation systems, a travel agent making a reservation had to look up flights in a book called the *Official Airline Guide*, then phone the different airlines to find out if they actually had seats available at a particular date and time. If the customer wanted a hotel room or rental car, the agent had to make another round of phone calls to find out what was available and make reservations.

Computerized reservation systems automated and streamlined this process, often permitting travel agents to consult with the customer, search for available seats, and book the reservation within minutes. When a customer phones, a travel agent begins searching for suitable flights on a computer screen. The screen is linked through phone lines to a mainframe computer owned by the company that operates the reservation system. The mainframe contains information on millions of available airline flights and fares. As soon as the customer and agent select a flight and agree on payment, the agent can print out the ticket. Similarly, a travel agent can access information on available hotel rooms and rental cars, making reservations within minutes.

Computerized reservation systems slashed travel agent and airline costs while dramatically reducing the time it takes to make reservations. By 1981, use of these systems had become widespread, and a Harris survey in that year indicated that computerized reservation systems had increased travel agents' productivity by an average of 41 percent. In fact, "One travel agent estimated that his employees could make a reservation using a computerized reservation system in one-third the time it would take to look up schedules in a book and make reservations over the telephone."[1] United Air Lines estimated that a reservation system's booking fee is less than half the cost of making a reservation through the airline's own reservation staff.[2] Although travel agents retain the option of returning to pre-computerized reservation system technology, 95 percent subscribe to at least one system.[3]

Of course, if computer systems cut the time and effort needed to make reservations, they no doubt eliminated some jobs in the travel industry, and possibly in the airline industry's reservations departments as well. In effect, these systems substitute human brain power and the sand in a microchip for the brute force labor previously required to process airline reservations. They provide a textbook example of what the economist Joseph Schumpeter called "creative destruction": the replacement of old technologies and ways of doing things with new arrangements that drastically reduce the amount of resources required to get the job done. In so doing, the new methods and technologies may cause some temporary dislocations, but they vastly increase our standard of living by enabling us to satisfy more human desires with fewer resources. Schumpeter argued that the process of creative destruction is in fact the driving force behind economic progress.[4]

The Competition Issue

In the case of computerized reservation systems, some critics saw a great deal of destruction and very little creativity. Instead, voices in both industry and government perceived computerized reservation systems as a threat to competition in the airline industry.

There are currently four major computerized reservation systems in the United States, but most travel agents subscribe to only one system. Typically, a travel agent signs a long-term contract with a computerized reservation system provider, who then installs computer terminals and other equipment in the travel agent's offices. The contracts have included rollover provisions, so that when a system vendor adds equipment or features, the contract is automatically extended. Minimum-use provisions have required travel agents to book 50 percent of their flights on a given system, and liquidated-damages provisions have discouraged travel agents from switching to a new computerized reservation system.

There is also some evidence that this is a difficult industry for new firms to enter. The computer systems and software needed for a reservation system may not have much resale value if their developer chooses to leave the industry. Analysts at the Department of Transportation also found evidence of economies of scale, economies of scope, and learning-curve effects, which suggest that the first firms to enter this industry may enjoy a substantial advantage over new competitors.[5] The existence of long-term contracts helps augment this advantage.

Most of the policy controversy stems from the fact that all four major computerized reservation systems are owned by airlines or groups of airlines. The two systems with the largest market shares are Sabre, owned by the parent company of American Airlines, and Apollo, developed by United Air Lines and now owned by a consortium of domestic and foreign airlines. To be listed on a system, an airline must sign a contract with the system vendor, and it then pays the vendor a booking fee every time one of its tickets is booked using that system.

Critics charge that ownership of a reservation system gives an airline an unfair advantage over competing airlines. Computerized reservation system technology allows the airline owning the system to list its own flights before those of other airlines, update information on its flights before updating the information of rivals, and in general manipulate the information presented to travel agents in ways that promote the owner's flights over those of rivals. In the absence of regulation, the system owner could also charge discriminatory booking fees, forcing other airlines to pay a higher price when customers choose them.

These types of complaints are common among companies in many types of businesses; the "have-nots" can always be counted on to complain about the "unfair" advantages possessed by the "haves." But the airline case is unusual, because many defenders of airline deregulation agree that computerized reservation systems pose a threat to competition. Most economists, for example, agree that airline deregulation has lowered prices and greatly enhanced the convenience of air travel.[6] Yet even the most authoritative study on the impact of airline deregulation warned that computerized reservation systems might require regulation because they give the large, established airlines that own them an advantage over new upstarts.[7] An entire mini-industry of scholarly articles focuses on ways of achieving the full benefits of airline deregulation through government intervention to eliminate remaining "market imperfections," such as those created by reservation systems.[8]

In response to both theoretical and practical concerns, the federal government has issued a number of regulations that govern the conduct of computerized reservation system vendors. "Display bias" is outlawed; vendors are prohibited from giving preferential treatment to any airline's flights in constructing video displays or operating the system. Contracts between vendors and travel agents are limited to five years. The government prohibits discriminatory booking fees, tie-ins, and exclusive-use contracts. Travel agents must also be permitted to use software that would allow them to access all computerized reservation systems from the equipment supplied by one system vendor.

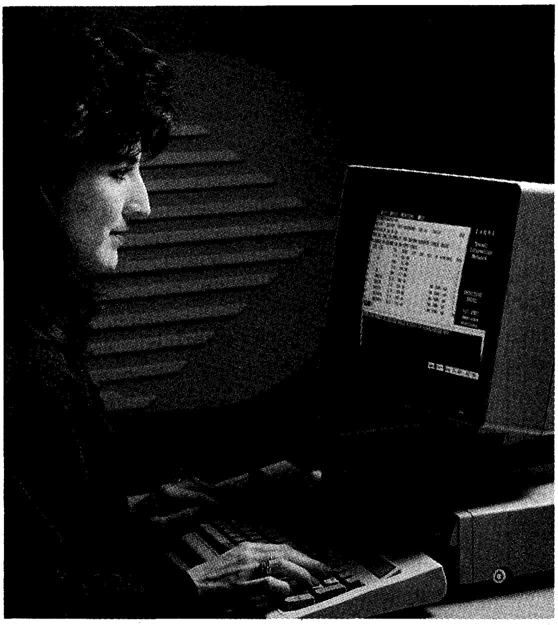
All of these regulations were adopted not by social planning zealots, but by the Civil Aeronautics Board under President Reagan and the Department of Transportation under President Bush. In both cases, the responsible officials appreciated free markets enough to firmly resist a return to the pre-1978 regulatory regime, under which the government limited entry and regulated airline fares. In fact, they saw the regulations as quite consistent with the goals of airline deregulation, which replaced a government-enforced cartel with a competitive marketplace.

In general, these regulations stemmed from the belief that ownership of a computerized reservation system constitutes a "barrier to entry" that will impede competition and prevent consumers from reaping the full benefits of airline deregulation. This policy position, however, begs a very important question about the true nature of competition in this and all industries.

The Importance of Conceptual Frameworks

What prompts some of the staunchest defenders of deregulation to advocate potentially extensive regulation of a new technology? The answer can be found in the concept of competition employed by most economists who analyze the airline industry. In modern neoclassical economics, "competition" means the abstract model of perfect competition. Perfect competition is characterized by numerous buyers and sellers, homogeneous products, perfect information, and costless entry and exit from the industry. Economists have logically proven that, under such conditions, decentralized markets allocate every unit of every resource to its most highly valued use. This result, termed "allocative efficiency," is the

Before regulators intervened, computerized reservation systems were a powerful marketing tool that gave owners a competitive advantage.



COURTESY AMERICAN AIRLINES/SABRE

standard of economic efficiency by which many economists judge policy proposals.

No one seriously argues that regulators or antitrust authorities should impose perfect competition on the airline industry, or on the computerized reservation system industry. However, many common economic policy prescriptions in this industry are based on the related model of "perfect contestability." A perfectly contestable market may have only one seller, but as long as there are no barriers to entry or exit, the threat of potential entry can force the monopolist to behave as if it had numerous competitors. The end result is the same as perfect competition: prices closely reflect marginal costs, and allocative efficiency is achieved.[9]

A key policy prescription that emerges from contestability theory is that government can promote efficiency by removing barriers to entry. These include not just government-imposed limitations on competition, but also private barriers to entry that take the form of "sunk cost" facilities.[10] A "sunk cost" is an industry-specific investment that a firm cannot recoup if it chooses to leave the industry. In the airline industry, examples of sunk cost facilities include airports, the air traffic control system, and computerized reservation systems. When facilities involving sunk costs exist, government policy can promote contestability by ensuring that all actual and potential competitors have equal access to the facilities. This might be accomplished by government ownership, as with airports and air traffic control, or it could be accomplished through regulation of privately owned facilities, as is done with computerized reservation systems.

Given this theoretical background, it should come as no surprise that many people who appreciate the virtues of free markets advocate regulation of computerized reservation systems. A good many analysts believe that free markets enhance human welfare by moving us closer to the ideal of allocative efficiency. When private market developments seem to thwart allocative efficiency, it is time for government to intervene.

A Different View of Competition

Such prescriptions make perfectly good sense, if indeed allocative efficiency describes the sum total of human welfare. But many advances in our standard of living occur because of phenomena that the models of perfect competition and contestability assume away. Both of these models describe a world in which all change that will occur, has occurred. The assumption of perfect knowledge rules out the possibility that someone might discover something new tomorrow. To the extent that technological progress is foreseen, market participants incorporate it into their plans today.

In the theoretical world that generates the policy norm of allocative efficiency, Schumpeterian creative destruction is ruled out by assumption. That does not mean that the conventional neoclassical economic models might not be useful for some purposes; they are just not particularly useful for understanding entrepreneurship and creativity. To the extent that entrepreneurship and creativity exist in the real world, we risk misperceiving them if we insist on interpreting them through the lens of the neoclassical model.

Airline computerized reservation systems provide a clear case in point. Several companies became the industry leaders because they were the first to capitalize on the new possibilities that information technology offered the airline industry. Indeed, the first computerized reservation systems began as extensions of American and United Air Lines' own internal computer systems. These pioneers quickly signed up many travel agents, and before regulators intervened, computerized reservation systems were a powerful marketing tool that gave the owners a competitive advantage in selling tickets on their own flights. The computerized reservation system owners earned high profits—in the form of booking fees and additional ticket sales—because they were the first to enter the market with an innovative new service.

These profits, however, are not a sign that government needs to eradicate imperfections in the airline market. Rather, the profits are the reward that the innovators received for entering a new, untried business. When government policy permits entrepreneurs to keep their profits, it promotes the alertness to new opportunities that is the first step toward achieving a more productive use of resources. When policy penalizes such profitability, it penalizes entrepreneurial activity aimed at the discovery of new knowledge.[11] Without such discovery, there can be no replacement of old methods or technologies by new ones. A consistent quest for allocative efficiency will sometimes impede the movement of resources to more highly valued uses, because it can undermine the discovery process that drives this reallocation.

"Where you stand depends on where you sit" is a common saying in the nation's capital. In the battle over computerized reservation system regulation, plenty of naked self-interest is in evidence. But the policy debate reveals more than self-interest; it reveals a clash of conceptual frameworks. Analysts who take allocative efficiency as their policy ideal will tend to seek regulation that eliminates any competitive advantage an airline might gain from owning a computerized reservation system. A minority will be more skeptical of regulation, because it erodes the incentive for entrepreneurial discovery. As the information age unleashes its creative potential, we can only hope that the minority view gains greater recognition and understanding. Economic progress depends on it. □

1. "New Reservations About Airline Computers," *Frequent Flyer* (December 1982), pp. 45–50.

2. Comments of United Air Lines, DOT Docket No. 46494 (November 20, 1989), p. 9.

3. U.S. Department of Transportation, *Study of Airline Computer Reservation Systems* (May 1988), p. 10.

4. Joseph Schumpeter, *Capitalism, Socialism, and Democracy* (New York: Harper & Row, 1942), pp. 81–108.

5. U.S. Department of Transportation, *Study of Airline Computer Reservation Systems* (May 1988), pp. 24–27. Strictly speaking, these may not constitute "barriers to entry" in the economic sense; see George Stigler, *The Organization of Industry* (Chicago: University of Chicago Press, 1983), pp. 67–70.

6. For a general study of the economic literature on airline deregulation, see Jerry Ellig and Wayne Winegarden, "Airline Policy and Consumer Welfare," *Transportation Practitioners Journal*, Spring 1994.

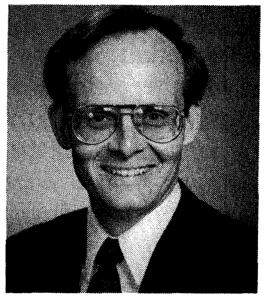
7. Steven Morrison and Clifford Winston, *The Economic Effects of Airline Deregulation* (Washington, D.C.: Brookings Institution, 1986).

8. See, for example, Severin Borenstein, "Hubs and High Fares: Dominance and Market Power in the U.S. Airline Industry," *Rand Journal of Economics* (1989), p. 344.

9. See William Baumol, John Panzar, and Robert Willig, *Contestable Markets and the Theory of Industry Structure* (New York: Harcourt Brace Jovanovich, 1985).

10. Elizabeth Bailey, "Contestability and the Design of Regulatory and Antitrust Policy," *American Economic Review* (May 1981), pp. 178–183.

11. Israel Kirzner, *Discovery and the Capitalist Process* (Chicago: University of Chicago Press, 1985).



As Values Collapse, Government Grows

The collapse of moral and ethical values in American society is frighteningly real and equally dangerous. Consider the findings of a recent Louis Harris poll of 5,000 young people.

Of those high schoolers in the poll, 65 percent said "Yes, I would cheat to pass an important exam." Fifty-three percent said they would lie to protect a friend who has vandalized school property.

One of the questions asked was, "What do you take to be the most believable authority in matters of truth?" One to two percent said science or the media. Three to four percent said religion or their parents. Most of the kids said "Me."

In a different study done by an international public relations firm, 67 percent of American high school seniors said they would happily inflate an expense account, 50 percent would pad an insurance claim, and 66 percent said they would willingly lie to achieve a business objective.

These and other appalling manifestations of a national moral and ethical vacuum were cited in a remarkable speech in 1991 by Rushworth Kidder, president of The Institute for Global Ethics in Camden, Maine. He was speaking at Principia College in Illinois.

Kidder recounted a true story about a 10-year-old child in Brooklyn, New York, who found on the street a wallet full of money, credit cards, and identification. The boy took the wallet into school and was unable to find either a teacher or an administrator who was able to tell him what was the right thing to do with the wallet.

"I can't possibly impose my values on you," Kidder said the teachers and administrators seemed to be saying. Even more incredibly, when he told this story "in the company of about seven very bright college juniors and seniors sitting around a dinner table at a very good liberal arts college in California," every single one said those teachers and administrators were absolutely right. This is worse than situational ethics; it's just no ethics at all.

Should it be any wonder, then, that crime is up? In a recent year—1990—one violent crime was committed every 17 seconds in America, compared to every 3 minutes in 1963. Thirty years ago, one murder occurred every hour in America; now it's every 22 minutes. Likewise for rape: one every 32 minutes then, one every 5 minutes now. Robbery: one every 5 minutes then, one every 49 seconds today. Burglary: one every 32 seconds then, one every 10 seconds now.

Just between 1986 and 1992, the murder rate was up 14 percent, the incidence of rape was up 12 percent, and street robbery was up 21 percent. Motor vehicle theft increased 15 percent, while robbery of convenience stores and aggravated assault both rose a whopping 26 percent.

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Twenty three hundred American youth between the ages of 15 and 19 were murdered in 1990—up by 53 percent since 1982.

As America prepares to enter the 21st century, Americans have become some of the most violent people on the planet. They feel less safe in their homes and on their streets than at any time in the history of the country. And when we're not assaulting or being assaulted, it seems we spend a lot of time cursing, conniving, lying, deceiving, backstabbing, and otherwise being unfaithful to spouse, family, friends, or associates. Our politicians seem to hit new lows of public and private morality with each new scandalous revelation. How can our society possibly retain any meaningful measure of freedom if these trends persist and deepen?

At the core of America's values crisis, Kidder pointed out so well in his speech, is the destructive, demoralizing notion that all values are in the eye of the beholder, that there are no "absolutes" against which the actions and decisions of people should be judged.

The teaching of values, Kidder says, may not yet be extinct, but it has been relegated (particularly at the college level) to a neutralist approach, where the teacher "is not to get in the way of kids discovering their own standards."

Distinctions between right and wrong are being eroded. Indeed, it seems that many people these days think the only choices are between right and right, that fewer and fewer things are really "wrong" when their "context" or the individual's motives are taken into account.

Moral and ethical relativism has suffused its poison throughout society, a major reason America has been losing its values compass. But that isn't the only thing we're losing.

The first casualty when the moral/ethical core of society evaporates is freedom. Law (government) fills the void—directing by threat of force those aspects of life that formerly were governed by our ethical standards.

Ethical people don't require fines for tossing trash out of car windows or for embezzling funds from their employer, because ethical people just don't do those things.

Nor do ethical people abandon responsibility for the education of their children or the care of their parents and expect society to do the job. Ethical people don't cast off their problems onto others because they have both a healthy dose of self-esteem and a respect for the lives and property of others. Moral people do not stake a claim of any kind on what doesn't belong to them. The erosion of values—ethical, moral, or whatever adjective you choose to employ —is freedom's single most lethal threat.

The choice, in other words, is to govern yourself or be governed. The less you do of the former, the more you'll get of the latter.

Ultimately, the standards by which we order our personal lives as well as our relationships with family, associates and others determine the sum and substance of our society. When those standards are strong, people take care of themselves and those around them; they work for a living instead of voting for one.

But when those standards decay, we pay the price in broken families, crime, drug abuse, child neglect, a loss of personal independence and greater reliance upon public welfare. If the rot gets deep enough, the price can be reckoned in terms of national bankruptcy and dictatorship. Whole civilizations in history have travelled this path and bit the dust.

Restoring our foundational values ought to be top priority for all Americans. There's just too much at stake for us to do otherwise. □

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THE MORAL CONSEQUENCES OF PATERNALISM

by Daniel B. Klein

Picture a man gobbling a second helping of chocolate cake, or chain-smoking a pack of cigarettes, or injecting heroin into his vein. Is there a crime being committed? Is aggression or violence being done to an innocent person?

In a sense, yes. A fleeting, short-term self that enjoys chocolate, nicotine, or heroin is working his will on an enduring self that pays the cost. Although we may fancy ourself a fully integrated and consistent being, it might make more sense to describe ourself as a bundle of multiple selves, selves that overlap, intermingle, and sometimes conflict.

Although you may not think of yourself as plural, the idea of multiple selves is really familiar. It is common for people to say that heavy drug users don't know what they are doing, that anorexic young girls are self-destructive, that people perpetrating violence suffer from "temporary insanity."

Some people recognize a dark self—a Mr. Hyde—that lurks within, and act strategically to defeat him. The reformed smoker will flush cigarettes down the toilet. Compulsive spenders put their savings in a Christmas Club account that levies a heavy penalty for early withdrawal. And some people, like myself, don't subscribe to cable television, not because we wouldn't use it, but because we would use it *too much*!

If such personal tactics are insufficient in subduing the Mr. Hydes that lurk, perhaps the government can lend a helping hand. After all, subduing bad guys is what the government is all about. This reasoning underlies numerous paternalistic laws in our country.

Anyone can suffer a fine for motorcycling without a helmet, or for driving a car with seat-belts unbuckled. States limit gambling to keep the poor from falling into bad habits. To help people preserve the family circle we have proscriptions on sexual commerce. Laws help us not to overuse a huge variety of substances, from heroin to penicillin. Other laws protect us from buying on impulse, from hiring incompetent plumbers or therapists, from not saving for our old age, and from murdering ourselves. All these laws are offered as a service to the erstwhile partaker.

Yes, people sometimes do things they regret. You'd be ridiculous to say that you never make mistakes, that you never do things to excess. But does that mean the government should step in and protect us from ourselves?

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One good reason to reject paternalism is that public officials, acting in some remote government office, do not in fact know better whether an activity is detrimental to our enduring self. Passing blanket restrictions on behavior rides roughshod on individuality. Some people drink too much, or gamble too much, but many others do not.

Another reason to reject paternalism is that it sets a nefarious precedent. Up to what point does the government get to play nanny? Where does it end? Sometimes it is the government that seems to suffer addiction—addiction to power—and it is the one that needs to show restraint. Furthermore, the justification of "it's for their own good" is bound to be abused. It will be used to justify all manner of special-interest plunder, such as excessive licensing laws.

But the chief reasons for rejecting paternalism do not deny irrationality in the private individual, nor even wisdom and benevolence in government stewards. The chief reasons to reject paternalism are its moral and spiritual consequences.

The Meaning of Life

What is it that gives one's life meaning? Meaning flows from narrative, from the drama of the story. But any old story won't give our lives meaning. It must be *one's own* story, a story that one feels is *of his own making*. To achieve a profound sense of *meaning*, one must be free to choose his behaviors. Hence, as Thomas Szasz has explained, paternalism is demeaning to the individual because it de-means his existence. It makes existence a happening rather than a willful action; it makes the story arbitrary and alien, rather than purposive and personalized.

The autonomous individual admits his inconsistencies, his contradictions, his bedeviling impulses, but insists nonetheless: Grant me the *dignity* of choosing which behaviors define my being, and charge me with the responsibility for the Mr. Hydes that lurk. If you suspect that some Mr. Hyde seeks to undo me, then I say, go ahead and let him try.

A first moral consequence of liberty, then, is dignity, the romantic sense of being the captain of one's soul and relishing the drama of one's existence.

There is a second moral argument against paternalism. To give our existence beautiful meaning, to make ourselves becoming, we must learn *how* to manage our troublesome impulses. But how do people learn self-command? The best teacher is liberty herself. The second moral argument is that liberty breeds responsibility (in the sense of trustworthiness or dependability, *not* in the sense of accountability). How does liberty teach responsibility? Return to the intimate contest of self-command.

Often hubris prevails. Beforehand we say we won't gamble at all, we won't get angry, we won't watch TV, we won't, we won't! We forget that the mood and vision in which plans are laid may vary greatly from the mood and scenes experienced as the course is traveled. So hubris produces unhappy experiences and a feeling of regret. From experience we gain awareness of the need for better self-command and a will to defeat our entrenched impulses.

Sometimes it is not our own outrageous fortune that sets us in search of better impulses, but the pleasing fortune of someone else. Nothing awakens our soul like the image of one we admire. As Matthew Prior wrote in 1708:

> Examples draw where precept fails,
> And sermons are less read than tales.

Rather than leaving the individual free to learn from experience and example, paternalism deprives him of these moral opportunities. By pre-empting choice, it weakens the moral faculty of choosing one's own course. And by presuming that the individual is incapable of choosing competently, paternalistic government may actually make him incapable. Wean a person in a world of decrees and proscriptions, and he may fear personal independence and responsibility (here, in the sense of *accountability*).

In 1792 the classical-liberal thinker Wilhelm von Humboldt came to similar conclusions about paternalism in his book, *The Limits of State Action.* He said: "A society in which the citizens were compelled to obey even the best behaviors might be a tranquil, peaceable, and prosperous one. But it would always seem to me a multitude of well-cared-for slaves, rather than a nation of free and independent men."

Albert Jay Nock argued similarly in his great essay, "On Doing the Right Thing": "The practical reason for freedom, then, is that freedom seems to be the only condition under which any kind of substantial moral fibre can be developed."

Two moral arguments against paternalism, then, are dignity—that is, our desire to belong to a culture of proud and romantic individuals—and responsibility—our desire to belong to a culture of decent and self-reliant individuals.

If a Mr. Hyde sometimes puts too much chocolate cake in my stomach, too much alcohol in my bloodstream, or too much television news in my head, that is *my* problem, and everyday I must practice the art of subduing him and negotiating with him. □

THE FREEMAN
IDEAS ON LIBERTY

THE PAST IS PROLOGUE

by K. Maureen Heaton

Time was when owning a home of one's own was not an impossible dream in America. Then, a determined young couple could find an affordable lot and build their dream themselves. I know. My husband and I did just that.

We had a small nest egg and a very sizeable dream. We paid for the lot with war bonds, and, on the strength of that equity, purchased a prefabricated house, which we put together ourselves. (Never mind that no nails—which were in short supply after the war—were included in our "package." A trip to San Diego and back from Redondo Beach where we lived at the time, stopping at every hardware store on the way, supplied enough to put the house together!)

When the parts were assembled, a roof over our heads, a living room and kitchen, two bedrooms and a bath were ours—for about seven thousand dollars, including the lot and the trip to San Diego.

Young people today can't do that.

Even if such a lot could be found today, it would be expensive, and the average young couple wouldn't be able to save enough to pay for it, anyway.

Our little house wouldn't have had the approval of a "planning commission." (Fortunately, there was none in those days!) It didn't have enough floor space for one thing (we thought it did). We moved in before the interior walls were installed, because they didn't come with the package, either, and we didn't have enough money then to buy them. (Today's Planners wouldn't let us do that.) I used the firebreaks between the studs to display my treasures, and missed them when the walls were finally installed.

We didn't have a garage, or even a carport, and the lot was so narrow we had to turn the house sideways to get it to fit. As a result, the front door didn't face the street. (Would that be permitted today?)

A few years later we built an addition on the back for my folks. There was no "zoning" then to say we couldn't, and no neighbors ran to the city fathers to object.

There were other ways as well for young folks to get their dream house then. Maybe the old folks had more property than they needed or wanted, and would cut off a piece for their kids. Many did that.

The Planners

Those were happy days—but it was just about then that the foolishness started and, surprisingly, found support among the general population. Just about then, the Planners moved into Our City. Their presence was not announced, but it was obvious—only we did not know it then.

The first any of us knew they were there was the night the city council held its first discussion of a "city plan." In short order, Our City had a "city manager," who quickly produced a Plan, and scheduled a "hearing" to present it to the citizens.

The citizen reaction was mixed. Disbelief was probably the strongest response from

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those present, because the Plan was so far removed from the projected layout of the city that had grown over the years. You couldn't call those early projections a "plan"—they were simply logical extensions of expected growth, sensibly preparing for a need which was already visible.

But with this Plan, the whole area within the City boundaries was to be metamorphosed.

Reconstruction

The visionary maps of a reconstructed City showed that the second high school planned for North City had, as if by magic, become a public park. Around our existing high school stood substantial homes—silent witnesses to the competence of those who had pioneered the City. On the Plan, those were gone. In their place, additions to the old high school spread out like a university campus.

City Hall (where the meeting was held), a lovely relic of a past era, was missing from the map. It was replaced by a "government center," which was shown in an area then occupied by hundreds of small homes.

The heart of the business district, situated at the waterfront, became a utopian dream of a marina—the businesses miraculously removed to outlying areas of the City, where small clumps of stores were surrounded by huge parking lots.

Someone asked what the reason was for all this transformation. The answer was almost mechanical: *"We must have planning."* "Why?" the citizens wanted to know. *"You don't want a pig farm next to you, do you?"* was the response. Well, of course no one did. But none had been proposed, either. How a pig farm might be set down in the middle of an established city was never explained.

The year was 1948. Despite strong opposition from the majority of citizens, despite an attempted recall of three of the members of the City Council (which, sadly, was unsuccessful by a slim margin), the Plan began to take on a life of its own, and Our City was never the same.

About Thanksgiving time, it suddenly became "necessary" to put new sewers in the downtown area. Main Street was blocked off, and merchants who had already put in their stocks for Christmas, found themselves isolated from their customers, who had to park outside the business district to do their Christmas shopping. It was a long uphill walk, especially with arms full of packages, and many regular customers found it more convenient to shop at stores elsewhere, which had parking close by.

Several merchants closed their doors after the holidays, and never reopened. Other businesses moved to the planned "shopping centers."

Awaiting the pleasure of Congress and federal funds, it was 20 years before the "marina" became a reality. By then, most of the downtown stores stood empty, or were occupied by fortune tellers, shady promotional entrepreneurs, tea-leaf readers, and the like.

And grass grew in the sidewalk cracks on Main Street.

The rest of that story unfolded just before the Fourth of July, 1988. The evening TV news had dramatic pictures of that marina going up in flames and smoke. It was reported completely destroyed. So much for Planner's plans!

A Man's Home . . . ?

The homes around the old high school, grand relics of a happier past, with their beveled-glass windows and door lights, beautifully planted yards, and huge graceful old trees, and those little homes in the way of the "government center" were condemned and demolished.

Gradually, the former owners disappeared from their usual haunts. So many of these were old folks, who had lived there all their productive lives, close to schools and shopping. Most had paid off their mortgages, and were looking forward to their "golden years," with only taxes to worry about. It was not possible for them to find housing they could afford for anything near what the government paid for their homes. Some went to live with their children, disrupting two families' lives. Some found apartments, and some just up and died, perhaps of broken hearts, frustration, or sheer anger at being put out of their own property.

A New Order?

This was the beginning of a new era for California—and the rest of the world, though few knew it then.

This was the activation of the National Resources Board Plan developed during the Roosevelt years.

Resistance was minimal, because citizens in one area did not know that what was going on locally was being repeated all over the country. The resistance met by Planners in the pilot areas was used by them as a lesson, to gain control in other areas.

There was a growing acceptance of the "planning idea." There was a growing body of opinion which was receptive to "government" taking control of such matters. There was a growing belief that no one could "live" in a one-room house—unless it had been there forever. Why the older one-room dwelling could be allowed and the other proposed structure not, was never explained. To an innocent, a new one-room house, surely seemed better than an old one!

Even a one-bedroom house was not to be countenanced, unless it met arbitrary standards: so much square footage; so many windows per room; the bedroom couldn't open off the kitchen; the rafters had to be so far apart; so much yard area to so much house; so much set back from the street, so far away from the lotline; and so on and on and on.

All these things added to the cost of a house, and the American dream moved further from reality for many people.

Then came the pressures for "urban renewal" and "modernizing the cities." Little houses from the past were in the path of the bulldozers everywhere.

All these interventions in the use of private property have resulted in many larger problems—no homes for the young folks just starting out on their own, no place for the oldsters to go when the children moved away, the emergence of the "street people"—and the also inevitable "necessity" for "government" to "solve" these problems.

The list of foolish interventions has grown exponentially. With each one accepted, new ridiculosities are concocted. They are made to seem so practical—no, *desirable*—that it would be considered quixotic to oppose them. It was all for our own good, you know.

Well, today, the birds have come home to roost. The way things are going, the birds may well be the only creatures with a place to call home.

I have no idea what that first home of ours would bring on the market today. I've heard that the "veteran's housing" which was built across the street from us a year or so later (which sold new for four, five, and six thousand dollars), was selling in the neighborhood of seventy thousand dollars several years ago. That's a nice neighborhood, if you can afford it. Certainly we who lived there after the war couldn't have.

Centralized planning has all but replaced the historic American method of *individual planning*. If unchecked, government will usurp all initiative for planning by citizens—not just for property, but for the whole of their lives. □

THE FREEMAN
IDEAS ON LIBERTY

King Charles' Ax: Property Rights, Human Freedom, and the Quality of Life

by John Robson

There is an old saw that "He who is not a socialist at twenty has no heart; he who is at thirty has no head." Perhaps then the world grew up in the 1980s, and learned the sad wisdom that the great schemes for bettering the human condition through government intervention did not actually work. The U.S.S.R. and its Eastern Europe satellites crashed in flames, while the widespread famines and other human tragedies in the Third World showed the Soviet development model of heavy industrialization and a squeeze on agriculture to be equally unsuited for developing countries.

Meanwhile the welfare state in the advanced industrial economies has proven itself unable either to produce overall prosperity or to remedy "social injustices" like poverty. Admittedly the rollback of the state in the 1980s in the United States, Britain, Canada, and elsewhere consisted much more of rhetoric than of action, but interventionism is on the defensive both politically and intellectually. It simply does not work. And as secure property rights are the indispensable foundation of free markets, they too are enjoying something of a renaissance.

Nevertheless that old saw lingers, in the form of a suspicion that the triumph of free markets has been a triumph for the mean-spirited; there are even those who still continue to believe that with sufficient will, sufficient compassion, intervention can be made to work.

It cannot, and the most immediate reason why it cannot is that everything in life is more complicated than it seems, and we simply cannot foresee all the consequences of our actions. For this reason we have over a long time developed general rules for both personal and public decisions, and the most important of these in the latter area is that the neglect or flagrant violation of property rights leads to counterproductive results. What Rudyard Kipling called "The Gods of the Copybook Headings" have persisted in returning afresh to the scene of each disaster and saying "We told you so."

But though this is a triumph of experience

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over hope, it is more than that. Free markets and their philosophical premise, property rights, are not a mean, grasping, Scrooge-like set of institutions collectively labeled "Devil take the hindmost." Rather, they represent the only way of organizing a society that really respects individual people.

Property rights are not *a* human right, they are *the* human right, and the reason that coercion fails practically is not a different reason from the reason that it fails morally. Coercion, even when "benign," founders on the rock of individual responsibility. You cannot as a practical matter take property rights away, and you cannot as a moral matter do so. People own themselves, but they do not own others, and there is nothing moral or idealistic about saying that they do. Property rights are a matter not only of the head but also of the heart.

The Challenge to Property Rights

There is no difficulty in demonstrating the importance of property rights to economic efficiency. There is no difficulty in demonstrating that historically societies with property rights are richer and freer than those without. Yet if we only present them in this way, saying that they have worked so far, we risk being cast as the man who, having fallen off the Empire State Building, was heard as he passed the tenth floor saying to himself "So far, so good."[1]

Some people will claim that conditions have changed, or that the longer-term negative consequences of respect for property are now surfacing (for instance with regard to the environment) and that they must now be jettisoned. Indeed, the very success of property rights in creating wealth can turn, as Schumpeter said it would in *Capitalism, Socialism, and Democracy,* into an argument that they can and should be abandoned.

Even now there is a persistent "progressive" claim that we are moving into a new age, that somehow our increased prosperity, our increased awareness, the environmental "crisis" or something else has produced a situation where what used to be good enough, or the best available, is now unacceptable. And part of this claim is that we must submerge our individualism and our materialism and march cheerfully into a glorious communal future as comrades. Economics, they say, is not all life is about. This, in fact, is taken to be the core of the "idealist" position, and it is against this claim that property rights must be defended.

King Charles' Ax

Yet the denunciation of property rights as materialist is quite inaccurate. They are the most fundamental human right, and they address themselves to the spirit and the meaning of life directly, and to the accumulation of material wealth only indirectly.

Indeed, those who would separate "mere things" from the "higher values" simply don't understand what the world is like. King Charles I of England would be the first to point out that an ax may undo a political philosophy. No matter how elegant it might have been, his theory of the divine right of kings could not withstand the practical test of whether it could govern a world of fleshly subjects and rulers, physical crops in the field, mere stone walls and lowly water in rivers. No matter how bright the eye of a child, or elegant the couplets of a poet, without food the child will die and without pen and ink the inspiration will pass unrecorded and be lost.

In this sense, and in this sense alone, a devotion to property rights is a triumph of experience over hope. For the essence of utopian philosophies is their unwillingness to accept the tragic element in life, whereas to accept property rights is to accept it. And to object to the tragic in life on the grounds of "idealism" is to object not to a political philosophy but to the fundamental nature of the universe.

Inevitably in this vale of tears our hopes and dreams assume physical form. Time passes and we must use it one way or another, and once we have it is gone and all we have is what we did with it then. To take an individual's property is to steal that time,

King Charles I declaring war on Parliament.

to steal the hopes and purposes embodied in the acts of transforming the world, and it is to say that the physical objects, the surds if you will, matter more than the hope that produced them. Thus it is that those who would violate property rights, not those who defend them, are the true materialists.

If we had world enough and time, it might be no offense for the state to take the fruits of our labor. If we were immortal, who could begrudge an hour's work? But the time we chose to invest in that transformation of matter will never come again, and as one of Clint Eastwood's characters once observed, it is a hard thing to take all a man has and all he will ever have. All we have is our time, our effort and our free choice, and to take what we do with these is to take of our essence, to violate our personal integrity, and to steal part of our soul.

Property Rights and John Stuart Mill

It may be alleged, of course, that the butcher has an obligation to other members of society, that it is his moral duty to give of his excess to those in want. To begin with, there is a world of difference between saying that everyone should be charitable and in saying that they should all agree on what charity is, and without elaborating much I would say that it is because of this that socialists must be at war with human nature. Until some way is found to produce unanimity in society, redistribution in violation of property rights remains only a way of producing the appearance of agreement and of charity, but not the reality.

There is also a world of difference between saying that it is the butcher's moral duty to be charitable, and saying that it is our moral duty (or right) to force him to act as though he were charitable. What we are asserting is not that we should force the butcher to *be* charitable (for we cannot get inside his head and rearrange his thoughts), but that we should force him to act as though he was, from our point of view, charitable. Coercion will make the butcher act as though he shared the majority—or government—view of charity, but it will not in fact make him share that view.

And this is crucial. For in forcing him to act according to our conception of generosity, rather than his own, we deprive him of any moral freedom, and put material above moral considerations. His physical goods will be transferred to another, and he may be compelled to produce more even once he knows it will be diverted to the purposes of others. But he will not be acting voluntarily. And so in an act of coercive redistribution, the material aspects are rearranged as they would be in an act of charity, but the intellectual and moral ones, the intentions and feelings, are not.[3]

As the great economic philosopher Frederic Bastiat wrote a century and a half ago, one's person, liberty and property are "the three basic requirements of life, and the preservation of any one of them is completely dependent upon the preservation of the other two. For what are our faculties but the extension of our individuality? And what is property but an extension of our faculties?"[2]

Adam Smith's famous observation that it is not from the benevolence of the butcher that we expect our dinner, and that we speak to him not of our needs but of his advantage, relies on this point. The butcher's stock embodies his time, effort, risk, and dreams, and to take it because we want it, for ourselves or for others, is to assault his person. To substitute our judgment for his, or to try to, is a monstrous violation.

Property Rights and the Grim Reaper

In a utilitarian sense, perhaps, my respect for your property rights is merely a concession to you in return for your respect for mine, and if that is as far as someone is willing to go it will have to do. But in a deeper sense my respect for your property rights is based on my practical and moral respect for your individuality. Not only will you resist my attempts to make you do what I want, but all I really know about your choices is that they are and must be yours.

Thus my respect for property rights is based fundamentally on humility. I believe that the purpose of life is, at best, somewhat obscure, and that living is a difficult activity that inevitably, in some sense at least, ends in failure. As Paul Newman's character put it in *Buffalo Bill and the Indians*, "the last thing a man wants to do is the last thing he does." And this fact stares everyone in the face, or at the very least peers over their shoulder constantly.

I am going to die. I don't know much about you, my readers, but I know that as Seneca wrote "You will die not because you are sick but because you are alive." And as death rushes toward you and all of us (and if you have one of those digital watches that beeps every hour you don't need to miss it happening) you have chosen to spend these moments reading this essay. Many people would consider this folly. And they aren't sitting, *The Freeman* in hand, absorbing ideas on liberty and property. They are out shopping, or skydiving, or fighting with their in-laws, or doing any number of things.

Once again, if the arrow of time were not unidimensional, this would not be a problem. If you didn't like what you had done, you'd just do something else. But in our universe making one choice means not making another, so we can in fact make our choices badly and be stuck with it.

Property Rights and Joseph Stalin

The only way to avoid these conclusions, and into the bargain to protect others from the terrible fate of justified guilt, is to reject the premise of individualism. We may say that it is simply not true that individuals are, or should be, left to face the universe of moral choices alone (we have already seen that the world of moral choices is a world of choices about material things with moral consequences, so we cannot avoid the moral choices by saying that where we went was merely physical. So is all motion, and all choice). We may say that the purpose of the individual is to serve the greater good and that the individual's choices will be dictated by the greater good, or its agents, and that only the greater good can feel any culpability for those choices.

In its purest form this is as a practical matter impossible to hold, and even the most rigid Stalinists would blame an individual worker who neglected his revolutionary duties. Even if you submit to the common will, if you do it badly you are to blame. Or, to quote Elizabeth Fox-Genovese's *Feminism Without Illusions: A Critique of Individualism,* "Here I am arguing that individualism actually perverts the idea of the socially obligated and personally responsible freedom that constitutes the only freedom worthy of the name or indeed historically possible."[4] There's that darn personal responsibility again, in the writings of a self-described foe of individualism.

But in fact I simply do not accept the collectivist vision as a description of the world, let alone as a prescription. I observe and I believe that if told what to do for the common good I must myself decide whether to obey, and I must live with my choice. Even if disobedience means death, I cannot turn on the Zyklon B and say "Just following orders."

This is very much the same as C.S. Lewis' argument at the beginning of *Mere Christianity*: even if you say "I do not believe in individual responsibility" you will observe as a matter of fact about the operation of your personality that you do. You will in fact consider yourself responsible for your actions, even if only in that you take pride in complete submission to authority.[5]

So I begin by taking the intellectually humble position that I do not know what other people should do. If asked by the shoppers and sky-divers whether they should be reading these words or doing what they are doing, I can certainly inform them. I can inquire as to how they expect to benefit from what they are now doing, and what they think they might experience by choosing something else. If I find that there is something wrong or suspect about their expectations in one or both cases, I can pursue the matter as long as *they* want me to. I can even make a suggestion as to what I think they should do. But I do not know. And since I do not know, I take the intellectually humble position that I will not compel them.

The knowledge that we do not know must make us more profoundly humble. To assert that I know what you should do implies necessarily that I know what I should do, and who among us will cast the first stone on that account? No one makes all decisions perfectly because there are so many and life is so difficult. We all, to be blunt, mess things up, and it's mostly a question of avoiding mistakes as much as possible, making amends where necessary, and not getting too down over our own fallibility. It's just life.

But I also take the morally humble position that even if I did know, I could not compel others. I do not know the meaning of your life, nor of mine, and I have my hands full with the latter. Yet I do not spare time to run yours not because I hate you or scorn you, but because I do not believe that I can make your choices for you at all. It's not just that I shouldn't; I can't. This is a matter of definition: no matter what I say, you must choose whether to do it, even if it's "Your money or your life." And if I do try I will only get in your way.

The meaning of your life is the meaning of your choices, so to make them for you is to void your life of meaning in pursuit of material, not moral, situations that I prefer.

Money Can't Buy Happiness

Indeed, it is always vital, in my view, to go back to first principles, in this case asking what society is for and what the good life is. To take a rather trivial example, the reason that airports should be private is not that private property increases the wealth of society and moves us closer to the New World Order. It is that private airports let people go where they want.

And to treat government as some institution for achieving the greater good, and asserting that it can and should override individual rights when "prosperity" requires it, is not only to advocate a policy that almost certainly won't work. It is also to assert that individual freedom is a good like any other, and with a low price. It is to say that we would be better off in an unfree society with a per capita income of $20,000 than in a free society with a per capita income of $3,000, and that is simply not so. As Booker T. Washington wrote in his autobiography, "I have learned that success is to be measured not so much by the position that one has reached in life as by the obstacles which he has overcome while trying to succeed."[6]

Thus while I enjoy luxury as much as the next guy, I would prefer my own log cabin to a gilded cage. And I would not dream of calling "idealistic" any philosophy that did not respect this same preference, in me or in others.

The Constitution of Liberty

Respect for property rights means respect for individual choice, and therefore we can quickly identify laws and institutions inimical to respect for individual choice by their impact on property rights. You in the U.S. are blessed with a Constitution that firmly protects them, though you are cursed with a Supreme Court that has all but destroyed them, while we in Canada have a Constitution that ridicules them and a Supreme Court that does likewise. But we should aim for a legislative and ultimately a Constitutional order that does protect them, when we do not have one, and for a restoration of judicial sense and hence Constitutional government when we do.

In order to do this we must win the intellectual battle, and we cannot win it on the terrain of Pareto Optimality not because our arguments are so weak there but because they are so strong. Anyone who really understands the terms "utility maximization" will not fall for "beneficial" legislation.

No, where we must win is on the enemy's terrain, where we argue that property rights literally are human rights. We own ourselves, not other people, and we may exercise that ownership as we see fit. But our ownership of other people, which we do not possess, we may not exercise. Thus rent-seeking, the curse of modern government, is ruled out *a priori*. A government that respects property rights is not in the business of redistributing income, period.

Property Rights Are Human Rights

And so we must remember that a Constitution that protects property rights is a Constitution that protects not the exploiter or the pampered heir, but one that protects individuals.

In fact there is no "human right" that is not best understood as a property right, including free speech, freedom of religion, the right to bear arms, the right to be free of arbitrary search and seizure, and the right to freedom of contract.

Even the ninth and tenth Amendments to the U.S. Constitution are, from this point of view, easily explained. Since no one may delegate to government a power he or she does not possess, the government may not go about assuming powers it hasn't expressly been given, even on the grounds that "it's for the best." Like the entire Bill of Rights, this section was questioned by some who argued that no one could possibly take any other view. Fine and good, said the doubters, if it's that obvious let's put it in just for good measure. History has proved that even they did not doubt strongly enough, but the other parties were right that, given the nature of the U.S. Constitution, the government could not possibly have the power to undertake any sort of coercion of its citizens not expressly enumerated.

Moreover, if human rights literally are property rights and vice versa then the so-called "positive" rights are not rights at all. For they are the right to someone else's property, which means the right to someone else's person, and that you do not have. Not having it, you certainly cannot delegate it to government. And from this point of view we will not lose sight of why you may not, and will not fall into practical or moral errors.

To take a rather less cosmic example, consider the coercive, universal, shoddy education currently afflicting youth in North America. What is particularly remarkable about this problem is that for thirty years we have been throwing money at our schools, like good materialists, yet as the quality of education declines still further the only thing we can think of to do is to throw more money at them. This is even empirically silly, since those nations that outschool us—for instance Japan—have much shabbier, much more crowded schools than we do.[7] The problem is that our educational system does not allow people to take control of their own or their children's education, to make the important choices themselves. This is a practical error and it is a moral error, but it is not two errors. It is one very big one.

For you do not have the right, through any means at all, to make other people's choices for them. You do not have the ability either. This is where and why practicality and idealism intersect. The attempt to make other people's choices for them will fail because they are fundamentally theirs to make. You can, of course, reduce the choice set available to them, but if you do you are engaged in a deplorable violation of their personal integrity, not in an act of benign and magnanimous charity.

Conclusion—A Prison Called Heaven

This was driven home to me quite forcefully in a rather unlikely setting in December of 1992, when the Fraser Institute hosted a round-table luncheon where the guest speaker was Karlhermann Klottschen, director of the *Treuhandanstalt* (the agency charged with privatizing the "economy" of the former German Democratic Republic). My thesis, as I noted at the outset, is that property rights are not material in nature, except insofar as the universe is. The right to property is first and foremost the right of self-ownership, and becomes a right to things only because the universe is made of material stuff and the arrow of time is unidirectional. In such a universe it is the height of miserable materialism to constrain the free choices of others, and the height of idealism to allow them.

And when Herr Klottschen was asked what was the most lasting damage done by socialism in East Germany, this is what he said:

> I think they have robbed people of the most precious thing they have; that is, to spend their time in a way that they wish. They have taken away this very precious thing which we cherish, and that is the freedom, the liberty to move where you want, and to do what you want, and this they have basically forbidden. I think that is a very serious crime for which there is no penalty. . . . What I find is very disastrous is to put 16 million people in a prison for 45 years and pretend they are in heaven.[8]

There is no doubt at this point in history that violations of property rights do not achieve their goals, and indeed East Germany was not a prosperous place. But money cannot buy happiness, and what was really wrong with the GDR, as Herr Klottschen rightly stated, was that people's dreams and ideals were destroyed. Even if the GDR had enjoyed greater material wealth than, say, eighteenth-century England, the latter would have been a better place to live.

So it is wrong, even preposterous, to call property rights materialistic. They are the most basic human right. They are the only human right. They are what makes life worth living. □

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1. This analogy was in fact used by environmentalist Paul Ehrlich in an ongoing debate with economist Julian Simon about the so-called "limits to growth," after he had lost $500 in a bet with Simon about metal price trends in the period 1980–90, *The Economist*, December 21, 1991, p. 26.
2. Frederic Bastiat, *The Law* (Irvington-on-Hudson, N.Y.: The Foundation for Economic Education, 1974 [first published 1850, in French]), p. 6.
3. In this sense those who respect property rights manifest true idealism. But rather than become involved in a squabble over terminology, let us regard the term as the rattle on a rattlesnake, and avoid any "idealism" we may encounter. In this we would be following Thoreau, who warned us that if we saw a man approaching bent on doing us good we should flee for our lives.
4. Cited in Joan Kennedy Taylor, *Reclaiming the Mainstream*, p. 11.
5. Unless, of course, you decide to get really messed up and feel guilt over feeling proud of your humility before Allah.
6. Booker T. Washington, *Up from Slavery*, p. 39.
7. See for instance the survey of education in *The Economist*, November 21, 1992.
8. In the elision he spoke of the inappropriateness of trying Erich Honecker for the shooting of a handful of people when the whole regime was a monstrous crime.

THE FREEMAN
IDEAS ON LIBERTY

Owls, Ferrets, and Free Markets

by K. L. Billingsley

Ranchers in the western states like black-footed ferrets because they wreak havoc on the prairie-dog towns that cause ranchers much grief. But when ranchers see a black-footed ferret, they are likely to shoot, shovel, and shut up about it. What would lead ranchers to act against their interests?

Federal regulation. The black-footed ferret has been declared an endangered species, like spotted owls and various brands of woodpeckers and snails. If an endangered species is discovered on your property and federal regulators find out about it, they will make life very difficult for you. In fact, you may not be able to use your property.

The Constitution of the United States stipulates that you may not be forced to quarter soldiers on your property without compensation. As Montana State economics professor and former Interior Department official Richard Stroup points out, "the military pays for what it takes," but environmental bureaucrats do not. Stroup notes that current regulations require landowners to quarter all manner of species, or even a wetland, with no compensation.

To many observers, this constitutes a "taking" and should be compensated. John Echeverria, chief legal counsel of the Audubon Society, disagrees, seeing the call for compensation as a money-making scam and radical reinterpretation of the Constitution. Echeverria favors stepping up the regulatory enforcement that has become quite draconian.

According to Nancie Marzulla, formerly of the Justice Department and now chief legal counsel for Defenders of Property Rights, some 800 people have been jailed for environmental infractions since 1982. That figure includes seven for violating wetlands policy.

According to Vice President Al Gore, the world and nation stand at the brink of an environmental apocalypse. By Gore's standards, then, the regulatory approach is protecting neither the environment nor the individual rights that constitute the bedrock of American government and society. Some people see a better way: free-market environmentalism, which is more than a theory.

The government of Zimbabwe has come to the rescue of dwindling elephant herds by privatizing hunting rights. Poaching has virtually disappeared, the elephants are thriving, and the income of the villagers has doubled.

In the United States, the group Ducks Unlimited has preserved more wetlands than government departments boasting much larger budgets, resources, and legal clout.

Hank Fischer, the Northern Rockies representative of Defenders of Wildlife says

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that the Endangered Species Act (ESA) has been ineffective on private lands, which harbor fifty percent of endangered species. Fischer's group compensates ranchers when wolves kill livestock. The group also pays ranchers to let wolves develop on their land.

R.J. Smith of the Competitive Enterprise Institute is an avid bird-watcher and former president of the Monmouth (N.J.) Audubon Society. Smith notes that around the turn of the century the wood duck became an endangered species. The ducks now thrive, not due to government regulation but to private landowners who built boxes for the ducks to use in nesting. Something similar happened with the osprey. But things have changed since the ESA.

At present, Smith notes, "there is no incentive to help the spotted owl," since building boxes for the birds will only attract predatory regulators. In this way the ESA, Smith adds, provides "perverse incentives" and creates a "lose-lose" situation.

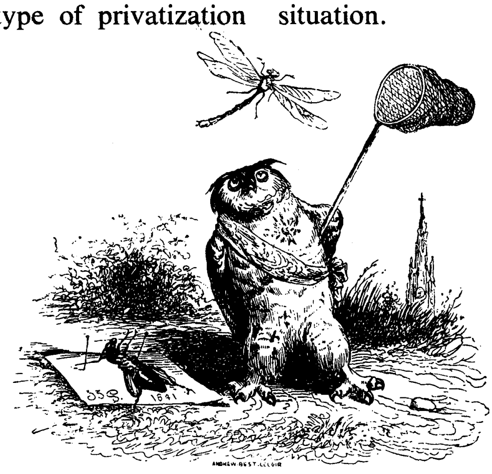
The largest landowner in the United States is not some tycoon or corporation but the U.S. Government, which still controls about one-third of the nation's land. Economist Terry Anderson, Senior Research Associate at the Montana-based Political Economy Research Center (PERC) and co-author of *Free Market Environmentalism*, advocates a plan in which the federal government could sell some of this land to private groups such as the Sierra Club, which are interested in preserving old-growth forest. This type of privatization would force people to face both costs and benefits. According to Anderson, the federal government lost $23 million on recreation last year.

Parks could be privatized and companies could lease their land to hikers, hunters, and fishermen. Another market measure would be the trading of permits. For example if a logging company owned some old-growth forest, it could trade that area for a timber region that they could harvest.

"When you own assets you take better care of them," says Richard Stroup, who adds that the market "forces even short-sighted people to account for the future." Stroup argues that, contrary to what many believe, the government is more short-sighted than the market. He cites the case of a government official he worked with who agreed that a certain inexpensive research project had merit but who failed to fund it because it outlasted his tenure in the Interior Department.

While those on opposite sides of the environmental debate disagree with each other's beliefs, observes Stroup, a market system based on common law will force them to respect each other's rights. And since there is no perfection in human affairs, Stroup urges all sides to ask the "compared to what?" question.

In the end, there are only two ways to solve the environmental question: by regulation or by property rights. According to the best evidence to date, the property rights approach comes closest to a win-win situation. □



THE FREEMAN
IDEAS ON LIBERTY

Post-Communist Traumas East and West

by Tibor R. Machan

[We] cannot say that democratic institutions reflect a moral reality and that tyrannical regimes do not reflect one, that tyrannies get something wrong that democratic societies get right.

—Professor Richard Rorty,
The New Republic, July 1, 1991

During an international conference on political theory several of us were sitting in a restaurant in Tallinn, Estonia. Among us was a participant from Bucharest, Romania, a young woman, who listened as some from the West poked fun at the evident inefficiency of the Russians who still have a significant presence in the Baltic countries and who happened to be running this establishment. We noted the drabness of the decor, the ineptness of the help, the slowness of the service, and reminisced about the even worse olden days when the gray-looking Russians who dominated the Communist culture would run roughshod over everyone in sight.

Suddenly we saw our friend from Bucharest in tears. She was apologizing but unable to keep herself from sobbing. We were stunned—we didn't know what we did to upset her. We all searched our minds for what we might have said but could not come up with a sensible answer. In a while she calmed down a bit and told us.

All of this amusing banter called to our friend's mind not only what she had been living with for all of her life but what in her country is still largely the case, namely, the complete control of the Soviet-type bureaucracy over the society. She then went on to recount, in halting English and tearfully, how the daily lives of her family and friends had been utterly trapped in the abyss that so many in the West championed as the promising wave of the future. She gave example after example of how people suffered, from moment to moment—how every ounce of some modicum of joy and pleasure, never mind genuine happiness, was rendered utterly impossible and inconceivable for them. She noted that people simply lost the will to live, that they could not even smile, not to mention laugh heartily, and how the most minute matters, such as the way in which parents played and talked with their children, suffered from this totalitarian impact.

It is often only when one finds oneself facing the facts directly, inescapably, that

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one can appreciate their meaning. This is especially true about facts that so many people would just as soon obscure with clever rationalizations.

In the West, especially in American newspapers, academic journals, and college classrooms, the collapse of the Soviet empire is now nearly forgotten. People everywhere are talking about why there isn't some kind of major economic boom in response to this fall. A *Business Week* editorial remarked, "Communism has been vanquished in much of the globe, the victim of its own failure to deliver a decent living to its citizens under its rule. Yet capitalism in the industrialized nations is limping along." It is as if "one, two, three," and our world will simply put 40 to 70 years of bloody dictatorship and command economy out of mind and bounce back as if nothing had happened.

Assessing the Damage

The damage inflicted by the Communist reign is not nearly well enough understood. It is certainly no longer treated as a big deal. What has taken its place as a vital item of concern is just how bad conditions are in the wake of the efforts to live without Communism, without the mighty Soviet State imposing its warped vision of human life on all the colonies within its sphere of impact. The question that seems to titillate the interest of many people is why the recovery is so slow, if a recovery was needed in the first place. The question on the minds of many prominent journalists, for example, is: "What should be substituted for the admittedly harsh and clumsy form of socialism, in the wake of the evident unworkability of the freedoms that the people gained after the fall?"

Despite all the talk about free markets and free institutions in the newly liberated countries of Eastern Europe, the intellectual consensus among political theorists and scientists seems to be that some kind of middle way is needed between socialism and capitalism. There is little encouragement toward a truly vibrant capitalist system either from our politicians and political theorists or the voices of moral leadership.

Just consider what the word on this is from the Vatican Secretary of State, Angelo Cardinal Sodano: "Capitalism is no less dangerous [than Communism] because of its basic materialism and the unbridled consumerism and selfishness it encourages" (*La Stampa*, December 28, 1992). Instead of the truly productive capitalist system, the preferred alternative seems to be social democracy, the welfare state or communitarianism, a hybrid of liberalism and socialism, with the emphasis not on the value of the freedom of the individual, including freedom to engage in free production and trade, but on the value of individuals' responsibilities to the community, not unlike the creed preached by Marx and his followers. The new vision involves a system in which free trade is here and there "permitted," but only under the watchful eyes of planners and regulators who know just when to limit people's liberty good and hard.

The one system that gets the least play as a proper candidate to replace the tyranny just overthrown is free-market capitalism or, as the Europeans call it, classical liberalism. No, that would unleash all the beasts. Such freedom cannot work and must not be tried, lest anarchy and rapaciousness break out all over. Look what freedom's promise has already unleashed on Bosnia-Herzegovina. Look how greed and profiteering has already spread all over the old Soviet sphere. So the proper answer is not to let it happen—some people must become the stern tamers of the rest, if only we could quickly decide who are so clever and dependable as to take the reins of power.

Not only, then, is there little left of true capitalism and free-market economies in the West but there is little chance of such a system taking over where the Communist dictators failed. In addition to this, few people in the West seem to fully appreciate just how horrible the Soviet experiment really was and how difficult it is to recover from it. There are no expressions of earnest *mea culpa* anywhere. Publications such as *The Nation, The New Republic, The Pro-*

gressive, The New York Times, The Washington Post, and the hundreds of other more scholarly outlets or related media do not spend much time acknowledging that their different degrees of softness on Communism, the thesis of moral equivalency between capitalism and Communism, their subtle but evident apologies for the Lenins, Stalins, Brezhnevs, and others in the Soviet debacle may have had a bit to do with the horrors the people had been subjected to, as well as with their current difficulties in recovering from these horrors and starting a new life, and recapturing some measure of hopefulness and the will to live and flourish.

I was rereading *Naming Names,* the book about the black list period in America during the 1950s by Victor Navasky, editor of *The Nation* (which is still proudly championing socialism with some kind of human face for all countries). In it Navasky made clear that he thought that despite the brutality of Soviet Marxism there was something morally noble about the system because its intent was to help the poor and powerless. I also read some passages ridiculing the Russian-born American novelist Ayn Rand who once claimed that a movie that depicted Russians smiling was a travesty, a sly propaganda piece since no ordinary Russian could be presented in such a way without a gross distortion of the truth—it would be comparable to depicting Jews in concentration camps having a good time playing volleyball. Not that this may never have happened, but that highlighting such characters in a work of fiction amounts to a vile distortion. Navasky and his ilk, of course, scoffed at this and still do.

A Complex, Painful Ordeal

But that is just what our Romanian friend was telling us about the millions and millions of victims of the Soviet terror, one that only a lunatic could imagine to have been motivated from compassion and care. What is worse, today many of these same naive reporters of the meaning and impact of Soviet socialism still do not appreciate just how complex and painful an ordeal it is to attempt to recover from it all.

People are not simply changing from one game to another when they finally are able to leave the Soviet system behind. They are undergoing recovery from massive and prolonged injury to their whole beings. They and everyone they know and love had been beaten and derided and terrorized by thugs for decades on end. When finally they are left alone, they are expected to, as the song says, just pick themselves up, brush themselves off, and start all over again—with cheer in their hearts.

We are seeing some extremely painful recovery as well as relapses in the lives of those who had been the victims of the Soviet experiment that so many of our comfortable intellectuals watched with vile neglect. We will see normal imperfect human beings undergo a slow convalescence or stand around hesitatingly coping with new problems and nearly forgotten ones as well.

For the many people who have given their support to socialism and Communism over the years—if only by not being brutally honest about them—on such grounds as that, well, these systems were motivated by compassion for the poor and downtrodden, the failure to see all this is a blatant confession of hypocrisy. The victims of the Soviet vision of human life deserve compassion and caring and yet all they seem to be getting is the callous disregard for their plight and the quick judgment that they are, after all, unable to handle freedom, aren't they? What the yearning for self-justification will not permit some people to do in the face of the gravest of human tragedies! □

THE FREEMAN
IDEAS ON LIBERTY

The Economic Way of Thinking

Part 8

by Ronald Nash

In June of 1992, I was nearing the end of a set of lectures in Moscow, Russia, when I learned that a member of the Congress of Peoples' Deputies was coming by my hotel to meet some people in our party. I decided that I would use the meeting to try to learn more about what makes Boris Yeltsin's opponents in the Russian Congress tick. When the deputy revealed that he was an important player in economic decisions made by the Congress, I brought up the subject of the massive increase in Russia's money supply that had just been announced. In a matter of weeks, Russia planned to double its money supply. Didn't anyone in the Russian Congress realize, I asked the deputy, what the announced action would do to the Russian economy? Didn't anyone understand the horrendous inflation that would result?

The deputy made it clear that he and his allies in the Congress did not care about the long-term results. The huge inflation in Russia's money supply was necessary in the short-run because, he claimed, it would alleviate serious problems resulting from his nation's movement away from Socialism. Had the deputy been a bit more candid, he would have admitted that the planned inflation in the money supply was going to benefit the deputy and thousands of other Russian bureaucrats like him.

Actions like those just described, along with the blasé attitude toward the future exhibited by the Russian deputy, are an example of the folly that results whenever individuals or governments ignore the fourth principle of the economic way of thinking, which is the subject for this, the last in my eight-part series. This fourth principle of the economic way of thinking is the importance of always asking what the long-term consequences of any economic action will be.

Short-Run Versus Long-Range Consequences

Economic theories are testable in terms of their success in predicting and explaining what takes place in the real world. One way of assessing any economic proposal is to ask what its long-range consequences will be. It is a mistake to notice only the short-term or immediate consequences of economic activ-

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ity. Any proposal or policy can affect the way people view a situation and thus can alter their incentives in ways that change their choices. Such a change in incentives often produces other effects that become noticeable only in the long run.

American politicians excel at adopting economic policies because they appear to produce desired consequences in the short run. What "the short run" usually means for American politicians is an effect likely to last through the next election. This has often been true of policies adopted because of the help it was claimed they would bring to the poor. But measures that appeared beneficial when viewed in the short term often look quite different after a longer period of time. This has certainly proved to be the case with the Russian government's continued expansion of its money supply that has gone far beyond the one-hundred percent increase in mid-1992. The Russian ruble has become worthless and the incomes of tens of millions of Russians continue to plummet, leaving them further behind each week in their quest for the basic necessities of life. As the inflation rate continues to escalate, the leftist-controlled Congress has continued to slow down Russia's feeble efforts to move towards democracy and a market economy.

But there is no need to say more about the insane economic policies of the Russian government; there are abundant examples of equally foolish acts by the American government.

How the U.S. Government Destroys Industries and American Jobs

In 1955, the United States produced half of the world's cotton (some 18 million bales a year). But by 1969, only 11 million bales were being harvested in the United States. This dramatic decline resulted from growing competition from foreign cotton growers and synthetic fabrics. Lost in the fog of history and government statistics is the sad but true story of how U.S. governmental intrusion into the cotton and textile markets gave added strength to foreign intrusion in these markets.

The first leg of this governmental intervention were federally mandated price supports for U.S. cotton that by 1955 had reached a peak of 32 cents a pound. The short-run justification for this price support was the alleged good of cotton growers whose income would increase because of the government's "wise and benevolent action." But as we saw earlier in this series, every economic action involves some cost. If you artificially raise the price of U.S. cotton to raise the income of U.S. cotton producers, you open the door to the importing of lower priced cotton from foreign producers. Even more serious was the fact that the price supports raised the price of U.S. cotton above the world-wide market price, cutting dramatically into sales of U.S. cotton abroad. U.S. cotton producers were rapidly losing their niche in the world market.

The federal bureaucracy's answer to this was to subsidize the price of U.S. cotton exported overseas in 1956. This immediately created problems for the American textile industry whose manufacturers were now forced to pay more for U.S. cotton than their foreign competitors. This meant that foreign producers of cotton goods could manufacture and sell their goods more cheaply than American millers. The U.S. government's response was to add still another subsidy, this one for U.S. millers.

There was nothing mysterious or surprising in any of these long-term consequences resulting from our government's intervention with the cotton and textile markets. Anyone attuned to the economic way of thinking could easily have predicted what was going to happen; and of course many economists and businessmen issued their warnings. But those warnings were ignored in the mad rush to produce some immediate but short-lived "solution" to some problem. Notice also that many American businessmen were eager accomplices in what eventually became the destruction of their industries.

Once the dangers of the government subsidies became apparent, assorted changes were made. But the damage had already been done. Foreign growers had already become established because the U.S. government's actions gave them an incentive to enter the cotton market. Foreign millers became established because the U.S. government's actions gave them an incentive. To appreciate fully the damages resulting from this last fact, it is necessary to visit some of the American communities that used to provide tens of thousands of textile jobs. The factories are closed, the jobs were terminated years ago, and the local economies were devastated. But few people recognize the role of the federal government in bringing about all this loss. And fewer people still recognize how inattention to the fourth principle of the economic way of thinking helped produce the situation. When contemplating any economic action, always ask what the long-term consequences of that action will be.

How Government Destroys a Housing Market

Failure to calculate the long-term consequences of an act has been a major factor in the housing crisis in New York City. When a locality like New York City imposes rent controls, it does so under the pretense that rent controls will stifle the greed of selfish property owners, reflect the greater compassion of the liberal bureaucrats who run the city, and presumably make more decent housing available at a lower cost. But anyone familiar with the principle of long-range consequences knows that the end result of rent controls will not be more available housing but less; and on top of all that, the condition of available housing will continue to deteriorate.

As we learned earlier in this series, people respond to incentives. Property owners think they are entitled to some return on their investment. When they begin losing money because of coercive rent controls, the first thing they begin to do is cut back on required maintenance of their property. As the condition of the property declines, it becomes increasingly less desirable to responsible people who find other places to live. As the apartments become increasingly occupied by lower-class residents, the lack of maintenance coupled with the tendency of people to treat other people's property with something less than loving care leads to still a further decline in the quality of the property. Many such properties deteriorate so badly that they eventually become condemned or mysteriously burn to the ground. If one doubts that this happens, all one need do is make a brief visit to the borough of New York known as the Bronx.

Other property owners will survive the rent controls by finding creative ways of getting around the restrictions. A black market in rental property may arise. People able to rent an apartment at the governmentally approved price may still have to make additional payments under the table, perhaps by renting additional furniture or paying for a cleaning service. A good exercise in the economic way of thinking would be to consider what would happen to housing in New York City if all rent controls were ended. The short-term consequence, of course, is that the price of housing in the city would jump dramatically. But, of course, the ultimate blame for this would be the original, short-sighted view of the city bureaucrats. But the long-term consequence would be an enormous increase in the quantity of new housing as entrepreneurs rush into the market to build new housing in response to the incentives of higher rents. But as the quantity of new housing increased, as it would, another long-term consequence would be the significant decrease in the cost of such housing when the quantity of acceptable housing then supplied by the market increased.

Given the obvious answer to New York's housing crisis, the question to ask is why the liberal bureaucrats don't admit their mistakes and abandon their self-destructive policies? One possible answer, of course, is that one must never underestimate the stupidity of politicians. Whatever the truth may be in the case of these bureaucrats, it is clear that the real losers are the people who live or would like to live in the city.

Conclusion

Another worthwhile exercise for the reader would involve the identification of other self-destructive economic policies that fail to consider long-range consequences. Even as I write, there is proposed legislation that would produce automatic increases in the minimum wage in response to inflation. Minimum-wage laws are justified as acts that will help low-skilled workers earn a living wage. But it is clear that such laws only force employers to lay off more unskilled workers. And so, the very law that was supposed to help unskilled workers earn more money has the long-range effect of costing many of them their jobs. Such is the nature of liberal "compassion" that ignores the economic way of thinking. □

LENDING DISCRIMINATION: THE UNENDING SEARCH

by Robert Batemarco

H. L. Mencken once called politics "the art of looking for trouble, finding it everywhere, diagnosing it incorrectly, and applying the wrong remedies." You don't have to spend much time looking around to see just how right he was. Mencken's characterization fits some recent regulatory follies to a tee.

One problem the politicians and bureaucrats set out to find was discrimination in lending. They found it in just about every rundown neighborhood in which mortgage lenders failed to extend credit because there wasn't a sufficient probability of recovering money lent. This avoidance by lenders of certain areas, known as red-lining (so-called because red lines were supposedly drawn around areas where banks would not make loans) was outlawed by the Community Reinvestment Act of 1977. Other types of lending discrimination were forbidden under the Equal Credit Opportunity Act of 1974.[1] Interestingly enough, despite the current political climate, which encourages members of officially designated victim groups to make any of life's little disappointments into a federal case, the Federal Reserve System's office that deals with credit discrimination has received but a trickle of complaints, not one of which was found to entail illegality. The Fed's response to this dearth of activity was to seek out complaints from civil rights activists. Even this had no discernible effect.[2]

The misdiagnosis was the idea that these areas were rundown *because* they couldn't get loans. Dysfunctional families, public schools incapable of imparting the skills to prepare children for a productive adulthood,

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pervasive dependency on government largesse, high unemployment, and rampant crime which prevents those who are productive from enjoying the fruits of their labor get nary a mention as contributing factors. Certainly, the notion that these factors, which cannot help rendering a neighborhood rundown, might also make loans there a losing business proposition seems not to have occurred to those who are so quick to cry "discrimination."

Indeed, the very existence of racial discrimination in lending is only plausible because of the misinterpretation of the available data. The finding by the Federal Reserve Bank of Boston that, in 1991, 15.0 percent of Asian, 17.3 percent of white, 26.6 percent of Hispanic, and 37.6 percent of black applicants for mortgage loans were denied credit is taken by regulators as proof of such discrimination.[3] Whether it is or not, however, depends on a number of factors which such summary statistics are incapable of revealing. Unless the members of each of these groups possessed identical levels of such characteristics relevant to credit-worthiness as income, net worth, employment stability, and quality of the collateral they can post as security for the loan, to name a few, the numeric discrepancies mentioned above provide but the flimsiest of circumstantial evidence regarding the existence of discrimination.

Those studies which have taken such factors into account have discovered that Asians, whites, Hispanics, and blacks with similar levels of credit-worthiness do indeed have similar rejection rates. A study of lending behavior at a Detroit-area bank which controlled for factors related to credit-worthiness found no correlation between one's likelihood of having his mortgage application approved and one's race.[4] Even the study conducted by the Federal Reserve Bank of Boston, which has been held by many as evidence of widespread discrimination, shows that taking credit-worthiness into account reduces the differences in rejection rates among racial groups. Its author, Alicia Munnell, has conceded that her study does not prove discrimination.[5]

Default Rates

If any statistic could shed some light on the presence or absence of discrimination among various ethnic groups, it would be the relative default rates among those groups. If lenders both made loans only on non-discriminatory profitability criteria and were able to avoid systematic errors, default rates would be identical for all groups. As a matter of fact, data cited by Ms. Munnell establishes the absence of any statistical relationship between race and default rates.[6] Any fair-minded observer would have to conclude from this evidence that lending discrimination, if it exists at all, is a non-problem. Indeed, the very regulators charged with enforcing Community Reinvestment Act guidelines have rated nearly 90 percent of commercial banks as "satisfactory" or "outstanding" regarding their fair lending records.[7]

Not only are the numbers incapable of supporting the charge of lending discrimination, but so are theoretical considerations. To the extent that loan officers' incomes are based on the number and the value of the loans they generate, indulging whatever prejudices they may have against members of other races who in point of fact are fully qualified for loans would be a pricey indulgence indeed.[8] Furthermore, as long as such prejudices were not acted upon by all lenders, any qualified applicant turned down by one lender because of his race would represent a profit opportunity for those lenders not blinded by prejudice.

It should be noted that those who single-mindedly seek to find discrimination are not deterred by anything as pedestrian as the absence of evidence or logic on their side. Thus, Richard F. Syron, President of the Federal Reserve Bank of Boston, while realizing that loan rejection rates have more to do with weak credit histories than with race, nevertheless exhorts lenders and regulators to stop asking if there is a problem and begin to work to solve it.[9] Alicia Munnell continues to insist that lending discrimination occurs even though she had admitted that neither she nor *anyone else* has any evidence of it.[10] Indeed, some regulators, when they can't find discrimination, are still not satisfied. Federal Reserve Board Governor Lawrence Lindsey, for instance, sought to prevent First Interstate Bancorp from acquiring another bank, not because there was any evidence that it discriminated, but because he did not think that it worked aggressively enough to make mortgage loans in particular low-income and minority areas.[11] Atlanta's Decatur Federal Savings & Loan was put through the wringer for not advertising in black media and not giving special treatment to black borrowers, specifically not making loans at below-market rates to black borrowers who did not qualify by traditional banking criteria.[12]

Mencken Was Right

As Mencken realized, regulators would not be so hell-bent on finding problems unless they were itching to try out their (invariably counterproductive) pet solutions on them. One preferred solution is to foist on lenders the same types of affirmative action requirements which become so much a part of the business landscape. Regulators' ability to withhold approval of new branches or acquisitions until their mandates are complied with in full is a potent threat indeed.

Shawmut Bank, New England's third largest banking company, knows by painful experience just how effective it is. The bank has seen its efforts to expand through acquisition of other banks, a virtual necessity in today's fiercely competitive environment, halted abruptly not because it has been convicted of, or even indicted for any violation of any law, but merely because of suspicion that Shawmut *may* be guilty of lending bias, which is being investigated by the Justice Department.[13] Until the banks' officials comply with the commands of regulators, they will remain at a competitive disadvantage. Some of the actions which they have taken in an effort to placate the powers-that-be include requiring lower down payments of certain low-income applicants, earmarking $25 million for applicants whose unstable employment histories would not qualify for loans under traditional standards, and paying $100,000 to a left-wing community activist group which one would expect to otherwise make further accusations of discrimination.[14] Similar pressures forced Decatur Federal to "pay heavy fines, institute lending quotas, pay bonuses to people who didn't qualify for mortgages, hold racial brainwashing sessions for employees, and pay a hefty ransom to liberal community groups."[15]

Another proposed "solution," while less punitive, may set an even worse precedent. This is the Community Development Bank, (CDB) whose mission is to "stimulate the economy in areas where other bankers are loath to lend."[16] The CDB is modeled on some private institutions which already exist—although these generally enjoy some subsidy either from the government or private foundations. (In any case, they have sufficient private capital invested that must seek out only the credit-worthy.) Government CDBs, on the other hand, are likely simply to depend far more on political criteria and to end up making mostly uneconomic loans. Critics hold up the federal Farm Credit System, which required $4 billion of government funds to cover the losses it incurred on agricultural loans in the early 1980s, as an example of the likely fate of these CDBs.[17] Of course, given that credit, as are all economic goods, is scarce, if the government makes loans to those who fail to meet traditional qualification criteria, it must be taking credit away from those who do meet them. Thus, it diverts credit from those more able to repay it to those less able to do so.

Ultimately, all of these proposed solutions constitute an attack on the rational economic calculation which Ludwig von Mises identified as the *sine qua non* of the market economy. Each of these measures replaces calculations based on expected profits and losses with those based on political criteria. Furthermore, such actions also erode the rights of property owners, specifically the right to use their property where it offers the greatest potential for gain.

What the government has been doing to lenders is not an isolated case. Government attempts to suppress decisions based on the profit motive in the name of some unattainable notion of fairness or equality are quite widespread in the United States today. The insurance industry has also come under attack for alleged red-lining. Community ratings statutes in a number of states have prevented health insurers from "discriminating" between good and bad risks. The Clinton Administration and several key Congressmen are now considering extending the Community Reinvestment Act to cover mutual funds and other financial institutions.[18] Even the use of information regarding prospective employees has come under attack by our courts, with the bizarre legal principle of "compelled self-publication," under which your telling a prospective employer the official reason why you were fired by a previous employer, gives you standing to sue that previous employer for slander.[19] These examples are but the tip of the iceberg. And if our country does not shift course soon, that iceberg is likely to sink the Good Ship Capitalism. □

1. This act includes among its prohibitions a bank's refusal to lend money to welfare recipients.
2. Statement by John P. LaWare, Chairman, Federal Financial Institutions Examination Council and Member, board of Governors of the Federal Reserve System, before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, February 24, 1993, *Federal Reserve Bulletin*, April 1993, p. 194.
3. Peter Brimelow and Leslie Spencer, "The Hidden Clue," *Forbes*, January 4, 1993, p. 48.
4. Jonathan Chait, "Bad Examples," *Reason*, December 1993, p. 58.
5. Brimelow and Spencer.
6. *Ibid.*
7. Dean Foust with Kelley Holland, "Taking A Sharper Look at Bank Examiners," *Business Week*, April 19, 1993, p. 99.
8. Jack M. Guttentag, "Most Lenders Would Rather Profit Than Discriminate," *American Banker* 158, January 6, 1992, p. 4.
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The Mother of All Myths

"Analysts watch consumer spending closely because it represents roughly two-thirds of all economic activity."

—*Associated Press*
(October 30, 1993)

In the early 1990s, in the depths of the recession, Range Rover, a British maker of sports-utility vehicles, ran an unusual ad in *USA Today*. It announced its formula for ending the downturn: "Buy Something." Of course, Range Rover wanted you to buy their car, but in any case, purchase something. "Buy a microwave, a basset hound, theater tickets, a Tootsie Roll, something." Anything to get the economy moving again.

In late 1991, Federal Reserve chairman Alan Greenspan suggested that the economic contraction was caused in part by retrenchment in consumer and business debt during the early 1990s. The implication is that the economy could be on its way to recovery if only consumers and business would start spending again, even if it meant spending beyond their means.

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Falling Under the Keynesian Spell

For decades, members of the media and the financial community have fallen under the Keynesian spell, emphasizing the importance of demand over supply, of deficits over surpluses, of debt over equity, and of consumption over saving. For them, the key to prosperity is found in encouraging a high level of consumption, even if it means going deeply into debt. The establishment press is so enamored with consumption that it highlights monthly changes in consumer spending, consumer debt, consumer prices, and surveys of consumer confidence, looking for any encouraging signs. After all, doesn't consumer spending represent two thirds of total economic activity?

Pro-Consumption Mischief

Well, no, it doesn't. The idea that consumption is the largest sector of the economy is based on a grave misreading of Gross Domestic Product (GDP).

According to 1993 data, consumption expenditures represents 66.1 percent of GDP, or approximately two thirds. Government purchases are second at 18.3 percent, and investment, which includes residential housing, comes in third at 15.6 percent. Business fixed investment is only 11.5 percent of GDP. By making the standard assumption that GDP measures total economic activity, the unsophisticated journalist has concluded that consumer and government spending are by far the most important sectors of the economy, while business investment rates a poor third.

Much mischief in government policy has arisen in consequence of this misinterpretation of national income statistics. Many lawmakers have passed legislation encouraging consumption at the expense of investment. At the same time, they see no reason to cut capital gains taxes or corporate income taxes, since the business investment sector appears to be relatively small and unimportant.

The Source of the Fallacy

What's gone awry? The source of the error is that GDP is *not* a measure of total economic activity. As anyone who has taken Econ 101 knows, GDP measures the purchase of *final* goods and services only. GDP deliberately leaves out spending by business in all the intermediate stages of production before the retail market. It does not include spending (what economists call "working capital") by natural resource companies, manufacturers, and wholesalers. Obviously, financial journalists need a refresher course in economics.

In sum, GDP does not measure total spending in the U.S. economy, only final retail purchases by consumers, business, and government.

Introducing a More Accurate Statistic

To determine total economic activity, we need to look at Gross Domestic Output (GDO), a statistic I developed in my book, *The Structure of Production* (New York University Press, 1990). It measures gross expenditures at all stages of production, from raw commodities to finished products. Based on the input-output data prepared by the U.S. Commerce Department, I estimate that consumption expenditures actually represent only about 33 percent, or one third, of economic activity in the United States, not two thirds as is commonly reported. Moreover, gross investment by business represents the majority (54 percent) of total spending in the economy if you add together gross intermediate expenditures ("working capital"), business fixed investment, and residential housing. Government purchases represent the remainder, or 13 percent.

This new statistic, GDO, provides a more complete indicator of total economic activity. As such, it suggests a far different interpretation of how the world works. In fact, we come to the opposite conclusion: Investment is far more important than consumption. The U.S. economy, like all economies, is investment-driven, not consumption-driven. Consumption is ultimately the effect, not the cause, of a nation's prosperity.

An individual becomes wealthy by producing and investing first, then increasing his consumption—not the other way around. To go on a spending spree using credit cards or other forms of debt may initially give the impression of a higher standard of living, but eventually the individual must pay the piper or face bankruptcy. The same principle applies to a nation as a whole.

"But," retort the big spenders, "if consumers stop buying, business will eventually stop producing." Granted, the whole purpose of production is eventual consumption. Per capita consumption is usually a reasonable measure of national wellbeing, and business must be responsive to consumer needs. But the real question is, how do we *improve* our standard of living? There is only one proven way, and that is by raising the amount of capital invested per worker. Economic progress is achieved when business increases its profits by providing customers with better products at cheaper prices. That requires a direct investment in capital. Those who postpone consumption now and invest their savings productively will be rewarded with higher consumption later.

Consumer Spending Not a Leading Indicator

If the U.S. economy is consumption-driven, why aren't retail sales a leading indicator of economic activity? Of the eleven components in the U.S. Department of Commerce's Index of Leading Indicators, only one, the Consumer Expectations Index, is directly linked to future retail sales. The other leading indicators are almost entirely related to capital investment and earlier stages of production, such as manufacturers' orders, sensitive materials' prices, contracts for plant and equipment, and stock prices.

Retail sales are in reality an unreliable indicator of where the economy and the stock market are headed. Industrial output is a much better forecaster. And, contrary to what the national media often reports, retail sales are relatively stable compared to industrial production, just as consumer prices are nowhere near as volatile as commodity prices. Financial analysts seeking to pinpoint changes in the direction of the economy and the stock market will be disappointed if they rely entirely on retail sales as a guide.

The Crisis in Productivity and Investment

Stimulating consumer spending in the short run will undoubtedly encourage some lines of investment. If people go on a buying spree at a local grocery store or mall, merchants and their suppliers will see their profits go up. But the consumer spending binge will do little or nothing to construct a bridge, build a hospital, pay for a research program to cure cancer, or provide funds for a new invention or a new production process. Only a higher level of saving will do that. Thus, in nations following Keynesian pro-consumption policies, it is not surprising to see luxurious retail stores and malls along side dilapidated roads and infrastructure. Their consumption/investment ratio is systematically out of balance. Peter Drucker chastises the United States and other Keynesian industrial nations for a "crisis in productivity and capital formation" and "underinvesting on a massive scale."[1] The current administration has done little to reverse this trend.

Saving, investing, and capital formation are the principal ingredients of economic growth. Countries with the highest growth rates (most recently in Southeast Asia and Latin America) are those that encourage saving and investing, i.e., investing in new production processes, education, technology, and labor-saving devices. Such investing in turn results in better consumer products at lower prices. They do not seek to artificially promote consumption at the expense of saving. Stimulating the economy through excessive consumption or wasteful government programs may provide artificial recovery in the short run, but cannot lead to genuine prosperity in the long run.

Using our new statistic, GDO, we now see that cutting taxes on business and investments (interest, dividends, and capital gains) will have a dramatically favorable effect, far more than previously thought. When business investment represents 54 percent of the economy, not 15 percent, reducing investment taxes can have a multiplying impact on the nation's economy.

In sum, it is capital investment, not consumer spending, that ultimately drives the economy. As economist Ludwig von Mises declared forty years ago, "Progressive capital accumulation results in perpetual economic betterment."[2] □

1. Peter Drucker, *Toward the Next Economics and Other Essays* (Harper & Row, 1981), p. 8.
2. Ludwig von Mises, "Capital Supply and American Prosperity," *Planning for Freedom*, 4th ed. (Libertarian Press, 1980), p. 197.

BOOKS

Monetary Policy in the United States: An Intellectual and Institutional History

by Richard Timberlake

University of Chicago Press • 1993 • 502 + xxv pages • $28.95 paper • $65.00 cloth

Reviewed by Steven Horwitz

Both the public and most economists have generally agreed that of all the sectors of the economy, the production of money and financial services requires a significant amount of government intervention in order to work "properly." The common view is that, more than any other industry, supposed laissez-faire has failed consistently in banking and has been responsible for various crises, panics, and difficulties throughout American history. This trend has begun to reverse itself in the last twenty years, however, as more economists and bankers are beginning to understand how regulations can destabilize the banking system and how various free-market alternatives might provide monetary order.

Richard Timberlake's study is sure to push this debate to the next level. In a comprehensive and readable book, he carefully scours the history of American banking from Colonial times to the early 1990s to document the increase in government intervention and its deleterious effects on both the banking industry and the economy more broadly. His book is a perfect complement to the more technical and statistical work of Milton Friedman and Anna Schwartz and will likely, like their work, be considered a classic of monetary history.

Two themes form the backbone of Timberlake's historical story. The first is the way in which increased government intervention has occurred not because laissez-faire has failed, but because various interventions served the revenue-raising interests of the political sector. Timberlake carefully documents how each of those interventions led to further crises and failures, resulting in calls for even more government regulation and more problems down the road. Although he does not mention it explicitly, the story he tells is a perfect historical example of what Ludwig von Mises called the "logic of interventionism."

Timberlake's second theme is that this increasing encroachment by government has moved us away from the rule of law in the monetary realm, to the rule of all-too-fallible humans. Each successive intervention undermined the Constitution's attempts to prevent government from doing any more than stipulating the gold or silver content of the medium of exchange, leaving the production of money to the private sector. As earlier systems and now the Federal Reserve System have led to increased government power, the quantity of money and the range of financial services available have become the products of intentional human-designed policy, rather than the more automatic and unintended consequences of the market.

The danger in this shift is that when human policymakers are unable to provide rational solutions, they will turn to those policies that work to their own self-interest, or the interests of the political actors to whom they answer. As Timberlake's historical story reveals, one of the primary purposes of various bank regulations and other government powers has been to facilitate growing government deficits and the vote-seeking of elected officials.

For example, one of the regulations of the National Banking System (1863–1914) forced banks to purchase federal government bonds to serve as collateral for the currency they created. This law provided the federal government with a captive market for its bonds, both to finance the Civil War and other government expenditures. The result was a lack of flexibility in the currency supply leading in turn to the periodic panics during the late 1800s and early 1900s. Many would ascribe these crises to the failure of the market, but as Timberlake and others have demonstrated, the problems of the system were the result of mistaken, and politically self-interested, regulations.

A second example Timberlake notes is the Fed's acquisition of open market powers in the mid-1930s. The Fed increases the supply of bank reserves by buying government debt in the open market. Having this power enables the Fed to purchase, if it so chooses, any level of debt Congress creates. Without such powers, debt creation is limited to the amount the public willingly purchases. With open market operations, the Fed can always buy any amount of debt the public does not voluntarily wish to hold. Congress was more than happy to give the Fed open market powers so that it could finance the debt of both the New Deal and World War II.

These are only two examples of the kind of historical evidence that Timberlake has documented. Some of his best work is on the 1960–1990 period, particularly the inflation of the late '70s. He also effectively demolishes the myth that monetarism was tried and failed in the 1979–82 period as well as unmasking the confusion that underlay most Fed policy since World War II.

Of particular importance is his discussion of the final nail in the coffin of the gold standard—the closing of the international gold window in 1971. Franklin Roosevelt had ended the American public's ability to exchange Federal Reserve Notes for gold in 1934, but foreign holders of U.S. currency could redeem them for gold at a stipulated price. This process put some limits on the Fed's ability to increase the money supply. However, as Timberlake argues, President Johnson's decision to finance the Vietnam War and the Great Society through inflation forced the end of even international redemption.

As the money supply grew in the mid and late 1960s, more foreign recipients of U.S. dollars began to return them to the Fed, leading to a significant outflow of gold. Rather than lose the gold or reduce inflation, President Nixon ended international redemption in 1971. Since then the U.S. dollar has been a complete fiat currency. Once again, the spending proclivities of the federal government drove monetary policy in directions that benefited the political process at the expense of the general public.

Timberlake's book is sure to quickly become a genuine economic classic. Unlike many such books, however, it is readable by the nonspecialist and of important relevance for current events. As Washington is debating the consolidation of bank regulatory agencies, and the possibility of a new regulatory push, a careful examination of the history of bank regulations, and their role in causing monetary disorder and economic disaster, could not be more important. Richard Timberlake has given us just such an analysis, and a masterful one at that. □

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Cities without Suburbs

by David Rusk

Johns Hopkins University Press, A Woodrow Wilson Center Book, 1993 • 130 pages • $13.95 paper • $29.00 cloth

Reviewed by Dean Stansel

Watch out, suburbanites.

New, multibillion-dollar federal program proposed to solve America's urban crisis by putting public housing projects in the suburbs.

Though we haven't seen that headline yet, it's not because the idea does not exist. For decades America's cities have been in decline, in mocking defiance of the explosion of new government-spending programs designed to save them. Nevertheless, many urban advocates still seem to think some elusive new government program will miraculously reverse the cities' decline.

One such person is David Rusk, former mayor of Albuquerque and the author of a new book entitled *Cities without Suburbs*. Rusk says the solution to the urban crisis lies in "regional governance." That is, he wants cities to annex their thriving suburbs—with or without their consent—or consolidate with their counties, thus creating "cities without suburbs." According to Rusk, that will transform declining cities into booming cities by forcing suburbanites to pay what he feels is their "fair share" of the costs of urban decline.

Though some cities—most notably, Nashville, Indianapolis, and Jacksonville—have successfully annexed their suburbs or consolidated with their counties, the political and legal obstacles are usually prohibitive. So Rusk suggests other ways—short of suburban annexation or city-county consolidation—to reduce the racial and economic segregation that he thinks is "the heart of America's 'urban problem.'"

One such plan would put public housing projects in the suburbs. Rusk argues that this would integrate the underclass into mainstream society, exposing them to the positive role models therein.

However, having subsidized housing in their neighborhoods is nearly as objectionable to most suburbanites as is annexation. Therefore, Rusk suggests the provision of federal "incentives" to get suburbs to cooperate. That's the catch. (Even Rusk admits that "'incentives' is a euphemism for federal money.") According to Rusk, the so-called "incentives" would cost federal taxpayers $23 billion a year.

Though touted as a new approach, Rusk's proposal is just another big spending program. To make matters worse, his expensive proposals have support in high places. Speaking at a Spring 1993 conference on urban policy sponsored by President Clinton's favorite think tank (the Progressive Policy Institute), Secretary of Housing and Urban Development Henry Cisneros explicitly endorsed Rusk's proposal, saying, "If we cannot open up suburban communities to subsidized housing . . . , we will not succeed."

Since then, Cisneros has proposed a massive expansion of "Moving to Opportunity" (MTO), a program created by his predecessor Jack Kemp. MTO will be tested in six major cities over the next two years, moving 6,200 households from inner-city public housing units to suburban ones, at a cost of $234 million.

While Rusk contends that "in any constitutional sense, the federal government has no role" to play, he advocates implementing these types of programs through either the provision of federal dollars or "new requirements on federal grants in aid."

In further contradiction, Rusk calls for larger, more centralized governments, while gushing that "in many ways the belief that 'smaller government is better government' resonates *emotionally* within me" (emphasis added). He even muses that larger government "may be less efficient and less responsive as a deliverer of services than smaller governments."

Rusk is correct about that. Studies have consistently shown that large, centralized governments have significantly higher unit costs of providing public services than small, decentralized governments. Nevertheless, Rusk insists that larger, more centralized governments are the answer, listing as "key goals: unification of the tax base and centralization of planning and zoning authority . . . under a *dominant* local government" (emphasis added).

Only in America do you still hear arguments such as Rusk's for larger, more centralized government. The last few years have witnessed a worldwide revolution. People have been throwing off the yoke of big, centralized government with rampant enthusiasm. Rusk ignores that reality, or perhaps he was too busy researching and writing his book to notice.

Rusk states that his primary motivation in creating cities without suburbs is the elimination of economic and racial segregation. He cites statistic after statistic to "prove" that cities that have annexed their suburbs are less segregated than those that have not. But what does that really mean? Few would disagree that redrawing the borders of a central city to include its suburbs will create a new "city" that has a greater proportion of middle- and upper-class whites than the old central city. Thus, by definition, Rusk's solution does indeed reduce measured segregation in "the city."

However, isn't that just semantics? After all, "the city" is no longer the central city. It is now the central city plus its suburbs. There is no reason to believe that creating cities without suburbs will in any way reduce the racial and economic disparities between the central city and what used to be the suburbs. Rusk's so-called solution to what he sees as the "heart of the urban problem"—racial and economic segregation—is, to be kind, a sham.

As Rusk himself says, his real goal in creating cities without suburbs is "tapping a broader tax base." He further states that "sustained success requires . . . moving dollars from relatively wealthy suburban governments to poorer city governments." Although Rusk uses the term "suburban governments," it is suburban taxpayers who will take the hit. Could Rusk's rhetorical chicanery be intended to camouflage the fact that his plan is simply a Robin Hood-esque effort to take from the suburbanites and give to the city dwellers? And what about the phrase "moving dollars"? Most people would call that stealing.

Furthermore, Rusk's proposals are imbued with the traditional left-wing notion that the solution to the problems of the inner city (or any problem for that matter) is more government spending. However, that argument rests on the assumption that the cities simply have not been spending enough. Nothing could be further from the truth.

In 1960 the average city government spent $470 per resident (in inflation-adjusted dollars). By 1991 that amount had more than doubled, rising to $1,070. Few city residents would argue that the quality of municipal services has doubled. Most would say just the opposite.

Twenty-five years ago Harvard's John Kenneth Galbraith said that there was nothing wrong with New York City that doubling the city's budget wouldn't solve. Apparently, New York City's leaders took him to heart; since then their budget has nearly tripled (in real terms). Surely, no one believes that New York City is in better shape today than it was twenty-five years ago. In fact, the recent efforts of the boroughs of Queens and Staten Island to secede from the city are damning evidence to the contrary.

Rusk admits that "cities, in the battle over middle-class America, have lost to their suburbs." To many, the central question of the "urban crisis" is why. Why are Americans voting with their feet by fleeing the inner cities in such large numbers?

Rusk seems to realize that higher taxes and spending are part of the problem, not the solution, saying, "Many middle-class families . . . went to the suburbs *to flee high city taxes*" (emphasis added). However, Rusk then goes on to say, "Admittedly, some factors in suburban growth in the early postwar decades were nonracial . . . [but] racially motivated 'White flight' was *undeniably a major factor* in suburban growth" (emphasis added).

While racial prejudice certainly exists, the idea that it is a major factor in the decline of America's cities smacks of a conspiracy theory. Besides, it is no longer just whites who are fleeing the inner city; middle-class blacks have been leaving in droves as well. Does Rusk really contend that suburban exiles from declining cities such as Oakland, New Orleans, and Birmingham are more racist than their same-state neighbors in the more prosperous cities of San Diego, Baton Rouge, and Mobile? Or could it be that the high tax burdens in declining cities—often twice as high as in booming cities—are simply forcing middle-class Americans to flee to areas with lower taxes?

Many urban advocates argue that America's large, declining cities cannot cut their taxes without slashing crucial municipal services. However, one reason taxes are so high in those cities is that the per unit cost of providing municipal services is often twice as high as in smaller cities.

The underlying problem is that most city governments are simply too big and centralized. They are too far from the people they govern. As a result, residents of large, centralized cities have relatively little ability to influence their leaders and to control how well their government is run. In contrast, public employee unions have substantial influence in such cities. For example, in New York City, some public employees get as many as 51 days off a year. That means they work the equivalent of a four-day work week. Such generous spending of city taxpayers' dollars on members of public employee unions is well documented in other large cities as well. It is a major factor driving up the cost of providing municipal services in large cities.

Rusk's solution would create more wasteful centralized governments. Thus, the cost of providing public services such as trash collection and police protection in Rusk's cities without suburbs would be even higher than it is now. Those higher costs would require still higher taxes. Since tax hikes cause residents and businesses to leave, Rusk's solution would only perpetuate the downward spiral of America's cities. It is the exact opposite of what should be done. Cities should move, instead, toward more decentralized governments and seek to privatize municipal services. That would enable them to enact the pro-growth tax cuts necessary to make the cities places where the middle class and businesses again want to, and can afford to, live and work.

Ignoring that centralization leads to inefficiency and higher costs, and that taxes have consequences, Rusk's "solution" to the urban crisis is ultimately just an elaborately constructed house of cards. He fails to even consider the possibility that many suburban businesses and residents, faced with higher taxes after being annexed by their central city, would simply choose to move farther and farther away from the inner city to avoid those tax hikes. Perhaps Rusk plans to build a Berlin Wall around the new cities without suburbs to ensure that businesses, people, and capital cannot escape. Without such police-state restrictions, Rusk's proposal is doomed to failure. His house of cards will inevitably come crashing down.

Nevertheless, given the huge amount of tax dollars at stake and Rusk's powerful supporters, at a short 130 pages, *Cities without Suburbs* is a worthwhile read—especially for suburbanites. The proposals it contains are a haunting harbinger of things to come.

If Rusk, Cisneros, and Clinton have their way, we will all soon be living in cities without suburbs. So start forming your grassroots organizations now, suburbanites. And hold onto your wallets. The tax man cometh. □

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The Fortune Encyclopedia of Economics: 141 Top Economists Explain the Theories, Mechanics, and Institutions of Money, Trade, and Markets

edited by David R. Henderson

Warner Books, Inc. • 1993 • 876 pages • $49.95

Reviewed by Raymond J. Keating

Initially, one might think that reviewing an economics encyclopedia would be an arduous task—slogging through esoteric theories, statistical models, and academic prose. However, *The Fortune Encyclopedia of Economics* successfully dispels such commonly held concerns. The 157 essays in this collection, as well as an appendix of short biographies on a variety of economists, are well written, clear, and often lively. Considering the fact that economists are not generally known as engaging writers, this amounts to nothing less than a momentous achievement for editor David R. Henderson.

No less of an achievement is the fact that this tome weighs in heavily with essentially free-market views. With a few exceptions, the issues addressed in this encyclopedia are examined from a sound, market-based perspective. Henderson has largely banished hyperbole in favor of well-grounded economic reasoning.

This combination of style *and* substance makes *The Fortune Encyclopedia of Economics* invaluable to a wide variety of readers. For example, students and professors should find that this collection serves as an excellent supplement to various texts and courses in economics, while also as a reliable desk-top reference book when researching and writing, or for those occasional moments when the mind falters and a refresher on certain issues is in order. Both business executives and government policymakers also should find this volume a good resource in helping to sort through the jargon of economics as well as often conflicting economic news reporting.

As for the topics addressed in this one-volume, oversized encyclopedia, the editor has cut a wide swath through the economics discipline. Included are such basic topics as efficiency, profits, opportunity cost, fiscal policy, investment, inflation, and property rights, as well as more specialized areas like privatization, deposit insurance, the gold standard, recycling, natural gas regulation, public schools, and sportometrics. While such a book really is not designed to be read from cover to cover—but rather to serve as a reference or educational guide with each essay standing alone—the format does allow one to read straight through if he so desired. In fact, it offers a much smoother read than many economics textbooks.

While the essays that stand out will vary from reader to reader, depending on one's particular interests, I found several worth mentioning here. Armen A. Alchian offers a good essay on how private property rights "protect individual liberty." Thomas W. Hazlett writes an interesting and informative piece on apartheid and how it developed in South Africa. Deborah L. Walker and Robert Hessen supply good summary essays on Austrian economics and capitalism, respectively. Also, Allan H. Meltzer's article on monetarism includes a good evaluation of recent monetary policy in Great Britain. Supply-side economics is given fair treatment by James D. Gwartney, as well as by Alan Reynolds in a piece focusing on marginal tax rates. Also, William Niskanen presents one of the more balanced views of Reaganomics that one is apt to find.

David Ranson's essay on inflation registers as an outstanding piece, as he illustrates that: "Inflation has tended to increase in periods of slow growth or recession and decrease in periods of expansion,"—a fundamental point missed by most economists. John Cogan offers an interesting essay on the federal budget, noting that spending growth accelerates the more decentralized the federal budget process.

The growing field of free-market environmentalism is introduced well by Richard Stroup, while Jane S. Shaw supplies an essay on recycling that needs to be distributed to any policymaker or elected official dealing with the issue. In a similar vein, the Pat Buchanans and Ross Perots of the world should be supplied with Alan Blinder's contribution on free trade. Individuals perpetuating myths about so-called shortsightedness of American business and the destructive effects of junk bonds need to read Steven L. Jones and Jeffry M. Netter's article on efficient capital markets and Glenn Yago's piece on junk bonds. Also of note are Mark Casson's essay on entrepreneurship, George Gilder's piece on the computer industry, John Chubb's overview of public schools and educational choice, John Haring's contribution on telecommunications, as well as editor Henderson's essays on the true sources of economic growth in post-World War II Japan and Germany.

More disappointing are Blinder's attempt to defend Keynesian economics, James Tobin's archaic essay on monetary policy, and Kevin D. Hoover's equally archaic article on the Phillips Curve. In addition, Joseph J. Cordes' piece on capital-gains taxes offers a workmanlike analysis of the "lock-in" effect of high capital gains taxes, as well as the effect of inflation on capital gains, but nothing substantial on such critical issues as the effects of such taxes on incentives and the trade-off between risks and potential rewards.

On the whole, however, this is a stellar collection of essays by some of the world's most knowledgeable economists. While it might seem strange to those who view economics as a dismal science, a lucid, market-oriented encyclopedia of economics is worth getting excited about. *The Fortune Encyclopedia of Economics* is an astounding feat. □

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Playing the Field

by Charles Euchner

The Johns Hopkins University Press • 1993 • 205 pp. • $24.95

Reviewed by Jeff A. Taylor

Cities across America are caught in a headlong rush to land a professional sports franchise. Five cities—Memphis, Jacksonville, St. Louis, Baltimore, and Charlotte—recently ended a competition to entice the National Football League into their towns. When it was over, the tab for public financing of playing fields had climbed into the hundreds of millions of dollars. Charles Euchner, a political science professor at Holy Cross, provides insight on why cities do this and why it is a bad deal for local taxpayers.

Euchner has studied several cities' attempts to woo teams and finds much of the competition centers on which locality can provide the biggest cut of public money to team owners. Owners, in turn, make the most of this situation by actively pitting cities against one another with threats to move the franchise to more lucrative environs.

In 1988, the Chicago White Sox effectively used a threat to move to Florida to win public funding for a new baseball park built literally on top of the existing one. The White Sox's spurned suitor, St. Petersburg, is stuck with an empty Suncoast Dome for which Euchner estimates local residents pay $7.7 million a year in debt service.

Euchner makes the case that franchise owners have adroitly played upon officials' political fears of "losing" a franchise to win backing for stadium upgrades. The big payoff for the owners is control of stadium skyboxes—luxury suites which can sell for hundreds of thousands of dollars apiece. The Houston Astrodome originated the skybox in 1965, but they now number in the hundreds for each new stadium built.

Euchner notes that if building stadiums was such a good business venture, more private entities would be willing to step forward and build them. And in fact, where the facilities are privately owned cities earn money rather than spend it. The hugely successful Dodger Stadium in Los Angeles pays $400,000 a year in property taxes.

The oft-repeated mantra that sports franchises generate economic growth is also disputed by numerous studies collected by Euchner. One local official compared the decision on NFL expansion to "whether or not the railroad was coming to your town in the Old West." But, as the evidence shows, filling a stadium eight times a year does not have the same economic impact as a manyfold increase in transportation capacity. By definition, dollars spent on sporting events are highly disposable and would likely be spent on other forms of entertainment—movies, plays, participatory sports—absent the franchise. The difference is that all the economic activity doesn't occur on a single day, at a single site.

Euchner also argues that when compared to other forms of social spending, such as job training, government subsidies for sports teams lag behind in generating a return. However, that line of argument is dangerous: it could entice local officials to graft a "job training" element into their stadium building plans rather than eschew the endeavor outright. It also overlooks the cost of taking of resources from the private sector in the first place.

There is every sign the frenzy for sports franchises is intensifying. The state of New York recently authorized funds to help communities keep and attract *minor* league baseball teams while two Chicago suburbs now spar over a farm team. Officials from every city, town, and hamlet would do well to listen to Euchner's warnings lest they get sucked into a game they cannot win. □

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