THE
# FREEMAN
IDEAS ON LIBERTY

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## From the President



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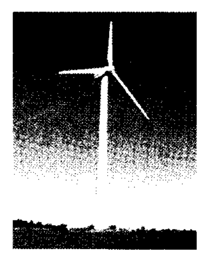

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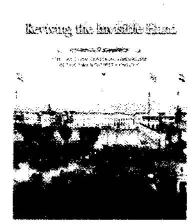
## Book Reviews





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From the President

# Principles Must Come Before Politics

**BY RICHARD M. EBELING**

We live in a time of quick fixes and patent medicines. The "physicians" offering to spoon-feed the elixirs for what ails us are the politicians running for office. Rarely do people step back and ask themselves whether there is really any ailment at all, or whether the politicians' snake oil can cure anything. And the political charlatans certainly have no incentive to tell us that their rose-colored sugar water is all a con to get them elected.

It has become a platitude that too many people are unable to focus on anything that requires more than five minutes' thought. Whatever the various reasons for this—and explaining it has itself become an academic growth industry over the years—the fact is that many people do not seem to look much beyond the short run when it comes to thinking about social, political, and economic problems.

This is not new. In the 1950s the German free-market economist Wilhelm Röpke observed that "people do not seem to stop and think and to ask themselves quietly what exactly they are doing. 'We must do something, no matter what' seems to be the unspoken motto of our age. . . . More and more people no longer know what it means to put first things first and to think in terms of the principles involved. Consequently, only a very few still have a real philosophy which separates the essential from the accidental and which puts everything in its place. . . . We are running after current events, instead of stopping to reach the solid ground of principles and to ask ourselves seriously what might have been the reasons why so much goodwill, energy, intelligence, time, and money have been wasted or not given the results we had a right to expect."

Even when principles are supposedly talked about, the discussions are often shallow and without much substance. "Democracy" has become the watchword of the day in political discourse about events at home and abroad. But whether it be the television pundits or high political officeholders, talk about democracy means nothing more than voting rights and an expression of the "people's will." As long as people can have their say when they pull the lever in the voting booth, the world will somehow miraculously have peace and prosperity.

In an era of "feel good" politics no one's mind is to be taxed by political philosophy or economics because someone's self-esteem might be harmed if he found the intellectual exercise too uncomfortable. So little is said about the true meaning of freedom and its actual relationship to democratic practices.

"Freedom" thus becomes anything that relieves a person from responsibility for the consequences of his own actions—with politicians shifting the cost of those consequences to other people's shoulders. And a person's "rights" refer to requiring others to provide the financial means to satisfy whatever ends will make him happy—even if the government has to coerce those others to part with what they have honestly earned.

At the same time, there are many people who talk about dealing with the dangers of bigger and bigger government and the budgetary burdens it imposes on all of us. But, again, rather than focusing on fundamentals, theirs is often only an attempt to find short-term gimmicks to deal with the problems.

This, too, is the result of focusing on politics. It's often pointed out that the political preferences of voters are distributed in the shape of a bell curve. At the ends are the political "extremists," collectivists and individualists respectively. In between, under the dome, are the vast majority of voters who are somewhere "in the middle."

If a politician is to be elected, it is explained, he must appeal to a significant number in that middle, since there are just not enough votes at either end of the curve to win an election. Thus he must weave together a patchwork of inconsistent and often contradictory positions

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that will reflect the diverse political views of his potential constituents.

This also limits what market-oriented think tanks in either Washington or in the various state capitals can offer as policy options in the debates about the role of government. Even while seeming to be nudging the debate more in a free-market, smaller government direction, the boundaries in which they can frame their proposals are constricted by what the politicians consider "politically possible." Beyond those boundaries the policy advocate becomes a "kook," a pie-in-the-sky "nut," an extremist who does not realize that "nobody" is going to take *those* views seriously. The policy advocate risks losing political legitimacy and a hearing in the halls of power—which is why his organization is located in that center of political decision-making.

This often means that policy proposals are "watered down" to be politically acceptable. Even the defense of a policy is often couched in terms designed to avoid the impression that its advocates support anything as radical as, well, laissez faire and the end to the interventionist welfare state.

Any detailed and fundamental discussion of government policy is therefore implicitly ruled out of court. Once attention is focused on influencing what government is doing right now, the debate is defined by what is politically practicable today.

## Moving the Curve

The real political task, however, is not to try to attract votes or nudge policy in the context of the existing bell curve of voter preferences. Rather, it is to move the curve in the direction of individual freedom, limited constitutional government, and a truly free market. In other words, the task is to shift the curve's dome over to where its individualist tail end is today, so that someday the middle mass of voters will more or less hold views generally consistent with classical-liberal ideas.

But this requires looking beyond what is politically expedient today. Indeed, it requires ignoring what seem to be the boundaries of the politically possible and instead thinking in terms of the politically desirable. If policies really consistent with individual freedom are ever to be implemented, we must first explain to our fellow citizens what such a society of freedom would look like, how it would work, and why it is desirable. They must slowly but surely come to see the vision of liberty.

Maybe part of the reason so many people seem unable or unwilling to think beyond five minutes is that they are so infrequently challenged to do so. Maybe our fellow citizens find it hard to break out of the current mindset of the existing interventionist welfare state because they are too rarely offered a clear and consistent case for the classical-liberal ideal and why it would be good for them and others they care about. Maybe people are often trapped in the policies of the short run precisely because they almost never are presented with a political and economic philosophy of freedom for the long run.

Politics will always only reflect the existing distribution of people's political views. Political campaigns, therefore, will never be the primary method for transforming society from less free to more free. This will only happen outside of the narrow political process—through a change in the climate of ideas.

Though most people don't know it, they *are* guided by an implicit set of political and economic principles when they think about and decide on what they want government to do. These principles are the ideological residues of nineteenth- and twentieth-century collectivism. They need to be replaced with a new set of political and economic principles, those of classical liberalism. When a sufficient number of our fellow citizens accept classical liberalism, politics will follow principle and the interventionist welfare state will be opposed and finally abolished. This is why a radical change in principles must come before any successful change in politics.

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Perspective

# Why Cut Taxes?

Judging by the popping corks at the White House, taxes are cut to increase government revenues so the budget deficit can be shrunk without reducing government spending. Tax cuts are good, but this reason leaves me cold.

President Bush announced recently that "This economy is growing, federal taxes are rising, and we're cutting the federal deficit faster than we expected." The latest numbers bear him out. The *Washington Post* reports "a 13 percent rise in tax receipts for the nine months ended in June." Thus "the administration projects that the deficit will narrow to about $296 billion. That would be down from the $318.3 billion of 2005." Only $296 billion!

And the *Wall Street Journal* added, "Government revenues are expected to grow 11%, or $246 billion, from 2005 to 2006, OMB said. So far this year, receipts have totaled $2.4 trillion, $115 billion higher than expected. That boost accounted for 90% of the reduction in the deficit projection."

The exultant President said, "Some in Washington say we had to choose between cutting taxes and cutting the deficit. Today's numbers show that that was a false choice. The economic growth fueled by tax relief has helped send our tax revenues soaring."

But we shouldn't want tax revenues to soar. They don't understand this in Washington, but nothing is more likely to produce mischief, and impede wealth creation, than a politician with a dollar in his hand. Imagine 535 politicians, and a President who misplaced his veto pen, with 115 billion dollars more than they expected to have. As the Antifederalist Melancton Smith wrote, "[A]ll governments find a use for as much money as they can raise." And that was in 1787!

Federal spending last year ate up 20.1 percent of what Americans produced. That's more than when this President took office. And the administration's projections through 2011 don't have it falling by much. After that point the picture is far bleaker, when Social Security and Medicare hit their icebergs. This also leaves out the open-ended bill for war spending.

Mr. Bush concedes that economic growth alone won't end the deficit. According to the *Post*, "He called on Congress to help cut 'wasteful spending' and to tackle what he said was 'unsustainable growth in spending for entitlement programs.' "

But how credible is that from a president who has yet to veto an appropriations bill? Besides, reducing "waste" will get us nowhere. One congressman's waste is another's essential project.

The only way to shrink government is to approach it at the mission level. Every line in the budget should be subjected to the question "Should the government be doing this?"

On second thought, that's not likely to get us very far either. If no one thought the government should be doing something, it wouldn't be doing it. Gremlins don't take over the Office of Management and Budget each midnight and insert projects no one asked for.

So where does that leave us? Not in a good place.

The government is out of control; in principle there are few remaining limits on what it may do. Yet even a badly hampered market economy is capable of producing a huge amount of wealth, so the spenders can enjoy themselves for a long time. The key questions are: how much better off would we be (especially those with the least) if government didn't have all that cash to play with, and how far off is the day of reckoning?

We shouldn't take our eye off the explicit tax burden, but that's not the only burden to watch. Spending is a better (albeit incomplete) measure of how much the government hurts us. If tax-rate cuts leave the government with more revenue than before, that's an excellent reason to keep cutting.

* * *

Are corporate CEOs paid too much? If this were a really free economy, the answer would be easy. But what about in a corporatist mixed economy? Robert Murphy leads the way through the labyrinth.

It's widely believed that the way for a less-developed country to become more developed is to find markets for its exports. As Christopher Lingle recalls, that idea was debunked some time back by a guy called Adam Smith.

How can dispassionate economists give economic advice? Israel Kirzner concludes his three-part series on this seeming paradox.

Proposals to mandate the use of renewable "green" energy find favor until people see the price tag. Michael Heberling explains.

France has had a rough time lately, with students demonstrating and even getting rowdy in opposition to a loosening of the labor laws. That was just the tip of the iceberg, Pierre Garello reports.

Twenty years after the nuclear-reactor explosion at Chernobyl, an authoritative study reports that the health consequences were much less severe than predicted. But some people don't want to hear about it. Jim Peron has the details.

Some people labor under the misconception that government can run a business, whether an electric company or a hospital. But as Murray Rothbard argued in this 1956 FEE Timely Classic, the nature of government and the nature of business are poles apart.

Our columnists' labors have yielded a varied crop: Richard Ebeling on principles and politics, Lawrence Reed on growing up, Thomas Szasz on college suicide-watch, Stephen Davies on incentives, and Russell Roberts on the need for a multimedia approach to teaching liberty. Gene Callahan, reading Paul Krugman's claim that inflation is nothing to worry about, protests, "It Just Ain't So!" Sad to say, after seven years this is Roberts's final *Freeman* column. We've enjoyed working with him, and we will miss him. We wish him well. His space will be ably filled by David Henderson, who is familiar to readers of these pages.

In the book department, our reviewers have scrutinized tomes on twenty-first-century liberalism, a top social democrat's legal philosophy, the abolition of slavery, and the gender wage gap.

—Sheldon Richman
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# Inflation Is a "Phantom Menace"? It Just Ain't So!

**BY GENE CALLAHAN**

Princeton University economist Paul Krugman, in his *New York Times* column of June 16, argues that the current fears about an increase in the U.S. inflation rate actually pose a more serious threat to the American economy than rising prices.

As he puts it: "I'm worried too—but not about recent price increases. What worries me, instead, is the Fed's overreaction to those increases. When it comes to inflation, the main thing we have to fear is fear itself."

Krugman acknowledges that there has been a general rise in prices of late, but says, "[T]he real issue is whether there's a serious risk that inflation will become embedded in the economy." He continues: "The classic example of embedded inflation is the wage-price spiral . . . of the 1970's. Back then, whenever wage contracts came up for renewal, workers demanded big raises, both to catch up with past inflation and to offset expected future inflation. And whenever companies changed their prices, they raised them by a lot, both to catch up with past wage increases and to offset expected future increases."

Krugman fails to explain how employers were able to *pay* ever-higher wages to their workers without going broke, or how consumers could afford to offer more and more money for the goods they wanted. Almost everyone would like to be able to charge a steadily higher price for whatever he offers on the market. If one person is able to do so while most others cannot, the higher price will make him genuinely better off, as it enables him to claim a larger share of total economic output than he previously could. But it is clearly impossible for *all* market participants to increase the relative size of their "cut of the pie" at the same time. (Of course, in a growing economy, the pie itself is getting bigger, so successive slices that are proportionally identical still will grow absolutely larger over time.)

If prices are rising across the entire economy, it usually means that an increase in the supply of money is reducing its value relative to other goods. It is true that this process will enrich those whose wealth is concentrated in stocks of commodities rather than in cash, but that happens at the expense of those holding the bulk of their wealth in bank accounts, money market funds, and fixed-income pensions. Inflation redistributes wealth toward people who, by foresight or by luck, have anticipated rising prices, but it cannot create prosperity—only saving and the effort to produce what other people will appreciate can do that.

Krugman tacitly acknowledges that the real source of inflation is the treasury's printing press, not abstract "pressures" or "spirals," when he notes, "The Fed eventually brought the inflation of the 1970's under control" by raising interest rates to slow the growth of the money supply. If the source of that inflation hadn't been the flood of new money pouring from the monetary authorities in the early '70s, then how could choking off that flow have alleviated the problem? Sellers, no doubt, would have *liked* to continue to get steadily higher prices for their offerings, but when the Fed stopped inflating the money supply, they were no longer able to do so.

Krugman contends there is little chance of a "wage-price spiral" setting off today, because wages aren't increasing much. That leads him to ask: "But if wage pressures are so moderate, where's the inflation coming from? The answer is soaring oil and commodity prices."

Once again, money is notably absent from Krugman's

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story. If the amount of money in circulation hasn't increased, then a rise in the price of, say, oil, gold, or wheat must be offset by a decline in the price of various other goods, making for a relatively stable purchasing power for the dollar. People can only spend more on some things without spending less on others when there is more money around than there was before the price increases. (Since Krugman makes no claim that rising commodity prices have had an impact on the "velocity" of money, I see no need to introduce that complication in responding to his argument.)

Krugman even tries to get us to make friends with inflation: "And bear in mind that many economists . . . have said that a little bit of inflation... is actually good for the economy." Sure, and many economists once claimed that socialism could provide a higher standard of living for the common man than capitalism could. Those temporarily mistaking a general rise in prices for increased demand for their product or service may briefly be spurred into increasing their output, creating the appearance of a booming economy. But since the increase in production is prompted by a misunderstanding of the real economic situation, it inevitably will result in the misuse of scarce resources. Once it becomes apparent that consumers were not really expressing a greater demand for the goods whose prices were rising, but were only bidding more because more dollars were available than before, then many producers will come to regret their decisions to increase output.

The spurt of business activity generated by "a little bit of inflation" is closely analogous to the spurt of physical activity following the ingestion of "a little bit of speed." Both seem to create positive results in the short run but prove to be unsustainable and costly in the long run. Keynes attempted to dismiss such objections to his own inflationary prescriptions by noting "in the long run, we are all dead." However, in the case of an inflationary boom, the "long run" is short enough that most of those who were present for the opening act will still be around for the denouement.

## Could Be a Problem

To his credit, Krugman does admit that he "can think of ways in which inflation could become a problem." But that mental exercise shouldn't tax a prize-winning economist very much. For instance, it does not require an esoteric appreciation of some arcane economic theory to conceive that inflation could become a problem by tearing apart the very fabric of social cooperation in a nation, as it did, say, in Germany in the 1920s, Argentina in the '70s and '80s, or Hungary at the close of World War II. It might also have occurred to Krugman that even "moderate" inflation is problematic, since it distorts the price system, rewarding some people not for their productivity but because they correctly anticipated rising prices, while penalizing others whose only sin was to be holding too much cash during an inflationary period.

Krugman declares that he is far less concerned by the specter of inflation than he is about other possible economic troubles, such as "a rapidly deflating housing bubble." But what pumped up the housing bubble in the first place? It is simply a manifestation of the easy money that the Fed previously supplied to lenders. The aim of that policy was to maintain consumers' enthusiasm for spending, an enthusiasm generated by the steady and strong rise in the price of their houses, thus enabling homeowners to upgrade their lifestyles through refinancing and second mortgages.

Krugman is surely aware of the many economists who insist that the root of every inflation is an increase in the money supply, since that group includes such prominent figures as the Nobel-prize-winner Milton Friedman. Why, then, doesn't he even *mention* monetary theories of inflation in his column? The only reason I can imagine is that Krugman's commitment to increasing the power of the state blinds him to the fundamental character of inflation: it is the consequence of the government printing new money to achieve some policy goal by stealth, without the unpopular move of raising taxes.

# Are CEOs Paid Too Much?

BY ROBERT P. MURPHY

One of *Reader's Digest's* more popular sections is "That's Outrageous!" When the feature spotlights government pork-barrel projects, absurd zoning restrictions on homeowners, or illogical regulations on small business, libertarians can applaud. Unfortunately the October 2005 issue featured a column that focused on "outrageous" CEO packages, an enduring controversy. The writer, Michael Crowley, displayed precious little knowledge of economics, and at times his complaints were downright contradictory.

The article begins with the anecdote about Stephen Crawford, then the co-president of Morgan Stanley. A few months after accepting this promotion, Crawford quit during a "management shake-up" and "strolled off with a severance package that included two years' salary and bonus," which amounted to $32 million. To make sure his readers are sufficiently outraged, Crowley points out that "Crawford pulled in $54,000 *per hour*!"

Before delving into the conceptual issues, let's be clear on where that number comes from. It is obviously due to Crawford's quitting much sooner than anyone (probably including himself) predicted when the contract was originally negotiated. (Had the shakeup occurred six weeks earlier, Crawford would've earned over $100,000 per hour, according to this method.) This is certainly a misleading approach, especially when contrasting it with the mean annual earnings of workers (as Crowley does). If one wants to show how much more CEOs get paid—and of course they *do* get paid far, far more than the average worker—then a fairer comparison would have been mean annual earnings of workers versus *mean annual* earnings of CEOs. (Later, Crowley follows this more reasonable route and reports that in 2003 "CEOs were paid over 300 times what the average production worker made.") To pick an example like Crawford rigs the comparison; one could certainly find cases of average Joes who quit or were laid off after only working a very short time, and hence whose "hourly earnings" would appear vastly inflated.

For example, I myself was once sent home after only working about ten minutes as a receptionist in a law firm; I had been sent there by my temp agency, and it turned out I was unfamiliar with the phone system at the firm. Nonetheless, I still got paid for at least one hour (possibly more, I can't remember) of work. Using Crowley's approach, he could argue that the case of Robert Murphy shows that some Irish workers are paid six times more per hour than the median temp worker.

Even on its own terms, the calculation is suspect. Crowley isn't explicit about where the $54,000 per hour figure comes from, but we do know that the total package was $32 million and that Crawford quit "[a]bout 100 days" after starting in the new spot. Well, $32 million divided by 100 is $320,000 per day, which works out to $40,000 per hour if we assume eight hours of work per day. Thus to get the higher figure of $54,000, Crowley must be assuming that, in addition to working only eight hours per day, Crawford only worked five days per week. Now I don't know too much about being co-president of Morgan Stanley, but even so, I'm quite sure that this job requires more than 40 hours of work per week.

Of course, these minor quibbles about the figure overlook the biggest objection: So *what* if CEOs earn more money than most other workers? In a free market (and below we deal with the complication that in today's world there *is* no truly free market), the price of labor

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corresponds to its marginal product. That is, competition ensures that workers are paid according to how much additional revenue they bring in to their employer. The fact that some types of labor command thousands of times more market value is no more surprising or outrageous than the fact that some goods in the marketplace (such as a house) have a price hundreds of thousands of times higher than the prices of other goods (such as a pack of gum).

Oddly enough, it is the *critics* of capitalism who implicitly claim that market value should correspond to ethical worth. No competent economist would argue that Stephen Crawford was a good person because he earned so much money, just as no economist would argue that a television set is ethically superior to a copy of the Holy Bible because of its higher price. No, the only thing economic science can say is that Stephen Crawford's services were in higher demand than the services of (say) the janitors at Morgan Stanley. So long as the labor contracts are voluntary, there really isn't an issue of fairness (subject to the complication noted above).

Later in the article, Crowley raises concerns that may trouble even a genuine supporter of the free market. Of course it makes perfect sense that successful corporate executives earn millions of dollars. But what of the strange cases of "corporate leaders actually *failing* their way to riches"? Crowley gives us some allegedly outrageous examples of this trend:

> Viacom CEO Sumner Redstone took home about $28 million in 2004, including a bonus of $16.5 million, even as his company's stock dropped 11 percent during the fiscal year. Applied Materials CEO Mike Splinter got a tidy $5 million bonus in 2004, despite a stock slide of more than 22 percent. That same year Rick Wagoner, CEO of General Motors, saw GM stock plunge 25 percent, yet he still pocketed a $2.5 million bonus—only slightly less than his award in 2003, when GM stock actually rose. So much for accountability.

As noted, this phenomenon is initially quite puzzling. Why would firms reward incompetent executives? Don't they want to make money? Yet before dismissing power brokers in the business community as self-destructive and/or incredibly stupid, perhaps we should give them the benefit of the doubt and search for a rational explanation.

The most important point that scoffers like Crowley overlook is that the business world is uncertain. When a company brings in a new executive, it is not at all obvious what steps he or she should take to turn the company around and boost profits. (If it *were* obvious, the company wouldn't waste millions of dollars hiring the executive.) Now regardless of the executive's competence, it is entirely possible that the plan will fail—and the executive knows this as well as anyone else. Because of this, it would be very risky for such an executive to sign a contract in which, say, he or she earned $20 million if the company were profitable, but $50,000 if the company tanks. Rather than sign *that* contract, the executive (who must be quite skilled to be offered such a job in the first place) could consult or take a less glamorous position and earn, say, $5 million for sure.

This principle—that an executive gets paid handsomely even if the company does poorly—doesn't seem outrageous when the numbers are lower. For example, when GM stock plunged 25 percent, did Crowley expect the assembly-line workers to give back a quarter of their wages for that year? If not, why not? After all, if the public stops buying GM vehicles, the services of the assembly-line workers aren't as valuable. The simple answer, of course, is that the assembly-line worker doesn't want his contract contingent on the overall profitability of the company; he wants to be paid—and to get his pension and other benefits should he retire or quit—whether or not the company's stock does well. If it's acceptable for the assembly-line workers, why not for the CEO too?

## Greater Influence

Naturally, there is one obvious difference in this respect between assembly-line workers (or janitors and receptionists) and CEOs: Far more so than these other employees, the CEO can greatly influence the profitability of the company. Rather than giving the CEO a well-specified set of instructions to mechanically implement, the people hiring him allow far more discretion. After all, the CEO is brought in to run the company.

Yet this difference shows up quite clearly in the market: CEOs and other executives *do* get paid according to how well the company does. In addition to a base salary, these executives are often paid in stock options. A stock option (specifically a *call*) gives its owner the right to purchase shares of stock at a specific price, called the strike price. Therefore, if the actual market price of the stock is lower than the strike price, the option is worthless. But if, through their behavior, executives can boost the company's stock price above the strike price, the options are valuable in proportion to the difference between the strike and actual prices.

Given his outrage over executives being paid regardless of profitability, one would expect Crowley to be a huge advocate of paying CEOs in nothing but stock options, which perfectly tailor earnings to the success of the company. Yet Crowley complains about the fairness of this too, even with highly successful companies. He cites the case of Yahoo! CEO Terry Semel, who took advantage of $230 million in stock options in 2004:

> The average Joe might be more outraged if he understood the sorts of payouts and benefits that corporate brass are getting. Stock grants still provide a windfall for many chief executives, despite new regulations that force companies to account for options as expenses. Yahoo! CEO Terry Semel exercised $230 million in options last year. His company has had strong earnings of late so it's fair to say that Semel earned his $600,000 salary, plus a hefty award for boosting the stock price. But $230 million? Come on.

Now what exactly is Crowley's definition of *fairness*? If Semel is paid a large chunk of options, and under his leadership Yahoo! stock rises tremendously, why shouldn't he be rewarded in proportion to this gain? At this point we can see past Crowley's other alleged arguments; his basic objection is obviously that $230 million is more than *anyone* should earn, period.

## Arbitrary Limit

There are three problems with this popular view. First, the upper limit that "decency" allows is arbitrary; no doubt many people would also deny the fairness of Semel's $600,000 base salary. ("We've got starving children in the streets and some guy who heads a company of spammers gets 600 grand a year?!")

Second, we must accept that in the modern economy, with billions of potential consumers worldwide, certain individuals have extraordinary earning power on the open market. If someone like Semel (or, a stronger case, Bill Gates) can add hundreds of millions of dollars of value to an organization (as judged by the spending habits of consumers), then to *not* pay him accordingly just means that someone *else* gets the money. Whatever happened to the principle of labor being paid the full value of its product? If Semel only got, say, $1 million, then Yahoo! shareholders (a group hardly in need of charity) would be $229 million richer. Would this outcome be fairer than what actually happened?

> If the compensation packages are as high as they are, it's because that's what firms need to offer to attract and retain these highly skilled individuals.

Third, we must consider the problem of incentives. If certain market exchanges are prevented because people such as Crowley find them unconscionable, then the individuals involved may stop working as much or as hard. For example, if Semel knew that outsiders would confiscate his stock options if the stock price rose too much, then he wouldn't have put in the long hours and sleepless nights that he undoubtedly did during the year in question.

This is a point liable to misinterpretation, and it's probably easier to switch contexts to professional sports. Economics tells us that placing a limit of, say, $1 million on salaries would reduce the incentives for star athletes. Now the critic might scoff and say, "Come on! Whether they make $1 million or $30 million, people will still go into the NBA. That type of cap isn't going to affect anybody's career choice." Yet this objection overlooks the *marginal* nature of economic decisions. Yes, a first-round draft choice will still go pro (rather than become an accountant) even with a $1 million cap. But he'll probably retire much earlier. (In the extreme, consider the heavyweight champion of the world—once he earns his title, he won't defend it nearly as often if people like Crowley get to dismiss multimillion-dollar payments as unfairly high.)

This reasoning applies even more so to leadership positions in large companies. Especially when considered in the aggregate, if "outrageous" compensation packages are forbidden, the quality of corporate leadership will suffer. These people aren't qualified for *just* CEO spots, and they're well aware of the social stigma against big business. If the compensation packages are as high as they are, it's because that's what firms need to offer to attract and retain these highly skilled individuals. Of course, this phenomenon isn't peculiar to corporate-leadership positions; if we declared tomorrow that brain surgeons could only make 50 percent of their current salaries, the frequency and quality of brain surgery would plummet.

## Entrenched Management?

Of course, any reader who has actually worked in (or owns stock in) a large corporation may reject the above description as naïve. In the real world, such a reader might object, most shareholders in practice exercise no control over management. Suppose, for example, that 85 percent of the shareholders (consisting of thousands of people who each owned far less than 1 percent of the stock) thought the CEO made far too much money. Even so, would it really be worth it for them to organize and demand that the corporate board do something? After all, the increased dividends made possible by such cost-cutting wouldn't translate into very much per shareholder. In this environment, management becomes entrenched and a lavish corporate culture takes over, with kept board members approving the jet-setting lifestyle of the CEO and his cronies.

As some of the recent scandals suggest, there definitely seems to be at least a grain of truth in such claims. Yet it nonetheless remains a puzzle to the free-market economist. For even if individual shareholders wouldn't find it worthwhile to organize and put an end to profligate abuses by management, such waste would nonetheless show up in the *stock price* of the firm. If, for example, management collectively frittered away $10 million per year in unjustifiable expenses, the total shares of the corporation would be valued around $200 million less than they otherwise would be, assuming an efficient stock market and an interest rate of 5 percent. (This is because $200 million is the present discounted value of a perpetual stream of $10 million annual dividends.) Such a corporation would then be a prime target for the much reviled *corporate raider*. The raider would institute a "hostile takeover," in which he bought up a controlling share in the corporation (by offering far more than the current price per share to the stockholders) and then used his power to fire or straighten out the inefficient managers. After cleaning house the corporation's dividends and/or stock price would rise accordingly, netting the raider a profit.

> Government regulation muffles this threat and thus allows entrenched businesses a margin of profligacy that they otherwise would not enjoy.

Thus we see that in the free market, even the realistic problems with "democratic" mechanisms can always be overcome in the final analysis by a "strongman," i.e. the corporate raider. (It should go without saying that these political metaphors are just that; in a free market all transactions are voluntary exchanges of property.) Consequently, if CEOs and other members of upper management make incredibly high earnings year after year, it must be that the shareholders find their services worth the expense. In some cases it may take the outside analyst some effort to discover *how*, but we shouldn't doubt that the shareholders are careful with their money.

Unfortunately, I cannot close the analysis on this optimistic note. For the above relies on the assumption of a free market in corporate takeovers, and that is decidedly lacking. In the present legal and cultural environment, so-called corporate raiders are even more despised than golden-parachuting CEOs. Regulations severely restrict so-called hostile takeovers, and hence hamper the ability of shareholders to restrain their managers. For example, the federal Williams Act (1968) compels a would-be raider to declare his intentions after acquiring 5 percent of a corporation's shares. Declaring one's intention to take over a company would likely push up the stock price, making the takeover plan unfeasible.

The market's other checks on inefficient management are stifled as well. After all, even before the financial innovations allowing the issue of "junk bonds" and hostile takeovers, there was always a sure-fire way to keep corporate officers in line: any firm that wasted too much money on fancy offices and executive perks would be vulnerable to its competitors. Again, this initially poses a puzzle for critics such as Crowley; if outrageous compensation for CEOs is so endemic in American corporate culture, why don't new firms enter these industries and drive the old ones out of business?

But as with hostile takeovers, so too with new entrants to industry: Government regulation muffles this threat and thus allows entrenched businesses a margin of profligacy that they otherwise would not enjoy. Many people (especially young students) new to the ideas of laissez faire believe that big business opposes government meddling, but this is naïve and contradicted by the history of actual legislation. Ironically, the profitability of big business can actually be *enhanced* when the government regulates an industry, because the big firms can more easily handle the fixed costs of filling out paperwork, providing a "safe" working environment, proving that they are making every effort to comply with affirmative action goals, and so on. In this environment, would-be competitors face additional hurdles if they want to challenge the large incumbents, and thus the latter may indeed get away with lavish expenditures that would be short-lived in a truly free market.

> In the opinion of the demagogues inequality in what they call the "distribution" of wealth and incomes is in itself the worst of all evils. Justice would require an equal distribution. It is therefore both fair and expedient to confiscate the surplus of the rich or at least a considerable part of it and to give it to those who own less. This philosophy tacitly presupposes that such a policy will not impair the total quantity produced. But even if this were true, the amount added to the average man's buying power would be much smaller than extravagant popular illusions assume. In fact the luxury of the rich absorbs only a slight fraction of the nation's total consumption. The much greater part of the rich men's incomes is not spent for consumption, but saved and invested. It is precisely this that accounts for the accumulation of their great fortunes. If the funds which the successful businessmen would have ploughed back into productive employments are used by the state for current expenditure or given to people who consume them, the further accumulation of capital is slowed down or entirely stopped. Then there is no longer any question of economic improvement, technological progress, and a trend toward higher average standards of living.
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> —**Ludwig von Mises**, "Inequality of Wealth and Incomes"

# Export-Led Recovery, Multipliers, and Other Fanciful Notions

**BY CHRISTOPHER LINGLE**

Many developing and emerging market economies are struggling to keep their economic growth rates high enough to raise local standards of living. Moreover, many governments responded to lagging economic conditions by promoting export-led growth, evident in their obsession with restraining the appreciation of their currencies. While China will immediately come to mind in this regard, it is joined by many others, including Japan, South Korea, and Taiwan, to name a few.

The simple logic behind export-led growth is that higher foreign demand for domestic goods and services will boost local economic activity and bring higher rates of long-term growth. Underlying this logic is a technical notion that economists refer to as an "expenditure multiplier."

> The simple logic behind export-led growth is that higher foreign demand for domestic goods and services will boost local economic activity and bring higher rates of long-term growth.

Multipliers are explained by tracing the effect of new spending through the economy as it supposedly passes through many hands. For example, assume that most Taiwanese consume 80 percent of each additional dollar they earn while saving the rest. Under these conditions, a rise in the earnings of exporters by $10 billion would induce them to spend $8 billion. As they buy more inputs or expand their production capacity, those who receive payments from that round of spending will consume 80 percent of the $8 billion of their increased income. Adding up this continuous series of spending rounds supposedly generates $200 billion.

And, voilà! More spending begets more spending, so the slump ends. And we all live happily ever after. Wouldst that real life were as simple as it is in such fairy tales.

As it turns out, expenditure multipliers are the stuff of fanciful fiction. Despite many empirical studies to seek them out, they remain elusive beasts and when sighted have been of small and disputable consequence. As such, multipliers are rather like Elvis.

In all events, without the supporting argument of multipliers, export-led growth becomes a hollow concept.

It turns out that the demand by foreigners is not the source of greater wealth, nor for that matter does greater wealth depend on domestic consumption. Instead, the direction of causation is the reverse. Wealth depends on production being made possible through increased investments in capital goods that depend on more funds being made available through savings.

Increased demand for exports cannot have a multiplier effect since each economic activity requires a funding source. But the competition for scarce funds means that spending more on one good or service has to come at the expense of another. This logical limit on the nature of economic activity and spending means that the multiplier effect cannot function as predicted.

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It would seem plausible that the multiplier effect might work if a country were able to divert buyers for its exports from other countries. In a static framework this would be a rearrangement of global spending that might be offset by declines in spending by foreigners on some other country's domestic production. In reality, spending "multipliers" are a Keynesian phantom. The only way to have multiple advances in wealth is for there to be a sustainable increase in wealth to support an increase in overall production.

Another logical flaw in the notion that rising export demand can boost the production of wealth is the implicit suggestion that demand is the determinant of supply. Yet it is impossible to consider demand as being independent of the production of goods and services. Demand can only be satisfied if preceded by production.

The ideology behind export-led growth is contradicted by economic theory and reality. The notion that the advantages from trade come from exporting was the basis of mercantilism, a creed discredited several centuries ago. Adam Smith pointed out that the real advantages of trade come from allowing producers and consumers to buy from least-cost providers, regardless of their national origins.

And so it is that increasing imports is a better way to boost growth since enhanced economic efficiency and increasing real purchasing power are what benefit people.

For one thing, foreign competition provides domestic producers with an incentive to become more innovative and efficient in their local operations. When such improvements lead to gains in labor productivity, higher wages will allow household incomes to rise so that there can be more consumption and savings.

Increasing productivity will also lead to higher profits due to declining per-unit production costs. This will also enhance shareholders' wealth to allow more consumption and savings.

And then the benefits begin to extend to the international sector of the economy. Allowing export sectors to import inputs or intermediate goods will lower operating costs. Falling costs and rising productivity will enhance their ability to export. Rising profits allow domestic multinational enterprises to shop around for overseas production facilities and better sources of raw materials.

Recently Taipei announced plans to relax restrictions on inward-bound investment capital by ending the qualified foreign institutional-investor scheme. This opening of the capital market is certainly a sensible step in the right direction.

## The Market That Never Sleeps

Since global capital does not sleep, it will continuously seek out those countries with the most hospitable economic structures. Those with weaknesses will experience net capital outflows and economic slowdown. Economies with healthy and open domestic sectors will perform the best.

So why were people misled into thinking that export-led growth was the best model for emerging economies? Much of the confusion comes from believing that increasing demand can bring higher economic growth. The perpetuation of the expenditure multiplier continues to interfere with the formulation of sensible economic policy.

In all events, it turns out that much of the growth associated with the years before 1997–98 in the "miracle" performance of some East Asian economies turned out to be illusory. But this fact seems to be overlooked by promoters of export-oriented growth.

Instead of muddying up the policy waters with confusion sown by a dependence on exports, political leaders in developing economies should push for more competitive and flexible domestic markets for goods, services, labor, and other resources. Then a sharp rise in imports could set the path for their economies to embark on a higher long-term growth trajectory.

# Growing Up Means Resisting the Statist Impulse

**BY LAWRENCE W. REED**

A few months ago, I walked into a restaurant in Naples, Florida, and said, "A nonsmoking table for two, please." The greeter replied, "No problem. All restaurants in Florida are nonsmoking by law. Follow me."

For a brief moment as we walked to our table, I thought to myself, "Good. No chance of even a whiff of a cigarette. I like that!"

And then I felt shame. I had fallen victim to the statist impulse. For 40 years I thought I was a passionate, uncompromising believer in the free society. Yet for a few seconds, I took pleasure in government trampling on the liberties of consenting adults in a private setting. If I were Catholic, I would have headed straight to confession.

This incident troubled me enough to think about it a long while. I wanted to know why my first instinct was to abandon principles for a little convenience. And if a committed freedom-lover like me can be so easily tugged in the wrong direction, what does that say for ever getting nonbelievers to eschew similar or more egregious temptations?

> We consider ourselves adults when we learn there are boundaries beyond which our behavior should not tread.

At first I thought about the harm that many doctors believe secondhand smoke can do. Perhaps it wasn't wrong for government to protect nonsmokers if this is a case of one person imposing a harmful externality on an unwilling other. Then I quickly realized two things: 1) no one compelled me to enter the place and 2) the restaurant belonged neither to me nor to the government. The plain fact is that in a genuinely free society, a private owner who wants to allow some people in his establishment to smoke has as much right to permit it as you or I have to go elsewhere. It's not as though people aren't aware of the risks involved. Moreover, no one has a *right* to compel another citizen to provide him with a smoke-free restaurant.

Besides, I can think of a lot of risky behaviors in which many adults freely engage but which I would never call on government to ban: sky diving and bungee jumping being just two of them. Statistics show that merely attending or teaching in certain inner-city government schools is pretty risky too—and maybe more so than occasionally inhaling somebody's smoke.

The statist impulse is a preference for deploying the force of the state to achieve some benefit—real or imagined, for oneself or others—over voluntary alternatives such as persuasion, education, or free choice. If people saw the options in such stark terms, or if they realized the slippery slope they're on when they endorse government intervention, support for resolving matters through force would likely diminish. The problem is, they frequently fail to equate intervention with force. But that is precisely what's involved, is it not? The state government in Florida did not *request* that restaurants forbid smoking; it *ordered* them under threat of fines and imprisonment.

I tried this reasoning on some of my friends. Except for the diehard libertarians, here were some typical attitudes and how they were expressed:

*Delusion*: "It's not really 'force' if a majority of citizens support it."

*Paternalism*: "In this instance, force was a positive thing because it was for your own good."

*Dependency*: "If government won't do it, who will?"

*Myopia*: "You're making a mountain out of a molehill. How can banning smoking in restaurants possibly

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be a threat to liberty? If it is, it's so minor that it doesn't matter."

*Impatience*: "I don't want to wait until my favorite restaurant gets around to banning it on its own."

*Power lust*: "Restaurants that won't keep smoke out have to be told to do it."

*Self-absorption*: "I just don't care. I hate smoke, and I don't want to chance smelling it even if a restaurant owner puts the smokers in their own section."

On a larger scale, every one of these arguments can be employed—indeed, they are *invariably* employed—to justify shackling people with intolerable limitations on their liberties. If there's one thing we must learn from the history of regimes, it is that you give them an inch and sooner or later, by appealing to popular weaknesses, they will take a mile. The trick is getting people to 1) understand that liberty is more often eaten away one small bite at a time than by one big gulp and 2) it's wiser to resist its erosion in small things than it is to concede and hope that bigger battles won't have to be fought later.

Delusion, paternalism, dependency, myopia, impatience, power lust, and self-absorption: All are reasons people succumb to the statist impulse. Pondering this, it occurred to me that they are also vestiges of infantile thinking. As babies or adolescents, our understanding of how the world works is half-baked at best. We expect others to provide for us and don't much care how they get what they give us. And we want it now.

We consider ourselves adults when we learn there are boundaries beyond which our behavior should not tread; when we think of the long run and all people instead of just ourselves and the here and now; when we make every effort to be as independent as our physical and mental abilities allow; when we leave others alone unless they threaten us; and when we patiently satisfy our desires through peaceful means rather than with a club. We consider ourselves adults when we embrace personal responsibility; we revert to infantile behavior when we shun it.

## Demands on the State

Yet survey the landscape of American political debate these days and you find no end to the demands to use the force of the state to "do something." Tax the other guy because he has more than I do. Give me a tariff so I can be relieved of my foreign competition. Subsidize my college education. Swipe that property so I can put a hotel on it. Fix this or that problem for me, and fix it pronto. Make my life easier by making somebody else pay. Tell that guy who owns a restaurant that he can't serve people who want to smoke.

I wonder if America has become a giant nursery, full of screaming babies who see the state as their loving nanny. It makes me want to shout, "Grow up!"

Societies rise or fall depending on how civil its citizens are. The more they respect each other and associate freely, the safer and more prosperous they are. The more they rely on force—legal or not—the more pliant they are in the hands of demagogues and tyrants. So resisting the statist impulse is no trivial issue.

In my mind, resisting that impulse is nothing less than the *adult* thing to do.

# The Anatomy of Economic Advice

## PART III

BY ISRAEL M. KIRZNER

In the first article of this trilogy we explored some of the ambiguities and difficulties that surround the very idea of "economic advice" based on economic science. In the second article we set forth some of the basic foundations of economic science (with special reference to what the science can teach us about what we called the "benign" character of the spontaneous market process). We are now ready to draw together the various strands of our discussions and to set forth the scientific legitimacy of economic advice based on an accurate understanding of the nature and significance of the free-market process.

As was developed in the preceding article, economic science has explicated the nature of the forces that govern the market process. What we saw was that the market process is made up of powerful tendencies set into motion by "erroneous" market decisions. Such "erroneous" (that is, uncoordinated) market decisions are responsible for "imbalances," in which over-optimistic expectations are frustrated and disappointed, while over-pessimistic expectations are translated into overlooked opportunities for mutually beneficial exchanges. The market process consists partly of forces that tend to modify over-optimism, replacing erroneously hopeful decisions by more realistic market bids and offers (and more realistic production plans); and it consists, in addition, of "entrepreneurial" tendencies toward the discovery of hitherto overlooked opportunities. At any given time these coordinative tendencies are operating to eliminate the earlier errors—at the same time as "exogenous" changes in consumer preferences, resource availabilities, and technological possibilities are altering the very framework against which "error" is to be defined.

To the extent that production decisions are geared, not to the satisfaction of *current* consumer needs, but to the satisfaction of *future* needs, our above capsule description of the market process must be deepened. We must recognize that a production decision may be "over-optimistic" not only in overestimating the urgency of consumer demand for today's fresh milk, but also in overestimating the future demand for a particular style of automobile. Such a production decision may be "over-pessimistic" not only in failing to realize that today's market will express an unsatisfied demand for cheese products (which might have been even more profitable than the production of fresh milk), but also in failing to realize that (perhaps as a result of advances in medical research), in five years' time the demand for fresh fish (and thus the profitability of *now* producing fishing trawlers) may increase substantially.

To recognize all this does not require us to change our basic understanding of the nature of the forces that make up the market process. It merely requires us to recognize that these forces operate along channels that permit us to apply our elementary understanding of the "law" of supply and demand to levels of intertemporal complexity not noticed previously. Ultimately, however, the intertemporal coordinating forces unleashed by the "law" of supply and demand operate in ways fundamentally similar to the operation of this "law" in the simplest of markets. Market decisions are continually modified to take more realistic account of future possibilities; entrepreneurs are continually alert to the possibilities of

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discovering hitherto unnoticed gainful opportunities (whether these opportunities are short-run or long-run in their nature).

## Is the Market Process Really Benign?

Our discussion in the preceding section (and in parts of the preceding article) may suggest that each step of the market process is, at least in its tendency, socially beneficial. After all, this process tends to correct the erroneous expectations that individuals may have. It tends to discourage individuals whose over-optimism might otherwise inspire them to undertake projects doomed to failure. And it tends to inspire individuals to discover hitherto overlooked ways in which they can be useful to each other. To the extent that we would hope that such opportunities would be discovered, the market process, it would seem, is "benign" in its tendency. But what about the possibility that the successful achievement of mutually beneficial exchange between parties A and B is seen by party C as an undesirable development? (Economists term such situations "externalities.") We may consider several different scenarios.

a) Suppose, as a result of newly discovered trade possibilities between A and B, C (who had previously enjoyed B's spending as a customer in his store) now finds his income reduced. Of course he is dismayed by the newly discovered mutually gainful exchange opportunity between A and B. (C would be similarly dismayed if, as one who *used* to buy from A at a low price, he now finds himself forced to match the higher price that B is now paying A in their newly discovered mutually gainful exchange.) While C certainly feels himself to have been "hurt" by the discovery, does this compromise our earlier judgment that the latter discovery is socially beneficial? The basis for our earlier judgment was the implicit assumption that the trade between A and B benefits them both (which is certainly the case) without affecting anyone else negatively (which is *not* the case in our present scenario).

Without entering into any deep philosophical issues revolving around comparisons between the "harm" suffered by C and the gains enjoyed by A and B, let us carefully notice that C has *not really been harmed at all.* What has happened is merely that C, who *had* enjoyed income received by selling to B *as a result of B's earlier ignorance*, is now no longer able to do so. (Or, in our alternative case, C, who *had* enjoyed being able to buy cheaply from A, *as a result of A's earlier ignorance*, is now no longer able to do so.) C has *not* been harmed in the sense of having lost any of his physical assets. Nor, as we shall see, has he been harmed in the sense of having lost some of the established *true value* of his assets; his "harm" consists strictly in his having now to live with a *more realistic* assessment (by himself and others) of what his physical assets are worth, and have *really* been worth, to others. Up until now he has, as is presently apparent, been extracting an unrealistically and unjustifiedly higher value from others, in exchange for what was really a lower-value asset.

But what if the exchange between A and B does indeed physically harm C; suppose that what A sells to B is his service as a musician and that this music played by A is so loud and so repulsive to C that the latter feels as if physically assailed. Let us consider this as scenario b).[1]

b) A sells live music to B; C's life is totally disrupted by what he considers atrocious noise. Surely we cannot describe the discovery by A and B of this opportunity for mutually gainful exchange as constituting an unambiguously socially benign development. Surely the gain to A and to B has to be offset, at least in part, by the harm caused to C. Let us distinguish two cases: (i) one in which the law recognizes C's right not to be disturbed by other people's music and (ii) one in which the law does not restrain individuals from disturbing others with their noise. In case (i), C's right not to be disturbed will certainly have to be taken into account by A and B. They will, if they wish to trade with each other, have to pay C to persuade him to permit them to do so. If C accepts such a payment, we would have a three-way trading arrangement in which everyone (at least in his own estimation) has been made better off. B gets to hear music at a total cost that he apparently believes to be worthwhile; A plays his music for a net price (after paying C) that he finds worth his while; C, while he must now sacrifice his peace and quiet (to which he is legally entitled), finds that the payment he receives from A and/or B is more than sufficient to make it worthwhile to do so. *Everyone* (to whom the trade between A and B is of relevant interest) has gained from trade.

In case (ii), in which the law does *not* recognize any right not to be disturbed by the noise of next-door music-lovers, C's pain will be *legitimately* ignored by A and B (unless of course they choose to act altruistically to consider C's suffering). But C *has* a way of making sure that his pain is taken into account by A and by B; he can offer them money to sign a contract undertaking not to play music during agreed-on periods. If they accept his money, C will consider himself to have gained (since he has purchased peace and quiet, to which he had *not* previously been legally entitled). If they do *not* agree to such a contract, C will indeed suffer from the music; but it is the legal system that is the source of this pain. The market process merely translates the legally recognized rights of A and B into corresponding realities. In both case (i) and case (ii) the market process benignly tends to reveal *all* relevant opportunities for mutually beneficial gain—*within the given framework of legally recognized (and enforced) individual rights*. We may approve or disapprove the morality of the legal system of rights, but *given that system*, whatever it may be, the market process benignly tends to inspire mutual discovery; it tends to *bring about coordination among the decisions of all those who are considered relevant by society's adopted system of law*.

## Has Economics Proven the Market Process to Be Morally Good?

We have seen that elementary economic reasoning shows that the market process tends to promote the discovery of hitherto overlooked possibilities for mutually beneficial exchanges. We have therefore described the process as "benign" in its tendency. Does this mean that the market process is morally "good"? Have we shown that, since the market process is *economically* good, we have scientifically demonstrated that public policies which promote the market process are *morally* good policies, while those which hinder the process are morally bad? Have we used science-based "is" statements to generate morally compelling "ought" statements? Careful examination of our reasoning will show that we have *not* demonstrated any necessary moral goodness in the market process—but that we have nonetheless succeeded in securing a valid basis for economic policy, properly understood.

What we have called the "benign" results that tend to flow from the spontaneous market process are benign in a very special, limited, sense. It seems a pity that Jones, who prefers *a* (which he does not have) to *b* (which he does), is somehow (let us say as a result of unnecessary ignorance—unnecessary in the sense that it could be eliminated with virtually zero cost) held back from trading with Smith, who prefers *b* (which *he* does not have) to *a* (which he does). A market process that tends to reveal to both Jones and Smith a way in which they can mutually benefit each other (without harming anyone else) seems to be an obviously "socially" beneficial process. But the beneficial character of this process is strictly relative to Jones's and Smith's *given* preferences. *If* these preferences are, in a moral sense, praiseworthy, the process that promotes their fulfillment can be seen as morally praiseworthy too. But suppose that the *a* which Jones prefers is a cholesterol-laden dessert that is likely to trigger a heart attack; suppose further that the *b* which Smith prefers is a hectic ride on a wildly unsafe motorcycle on a busy highway. Surely many observers would think the world a morally better place *without* the implied exchange. But—and this is the important point—the economist who applauds the market process is doing so *not* as a moralist; he is doing so strictly within the "instrumentalist" framework of his profession. He is pointing out that, from a purely *economic* point of view (that is, in terms of *given* preferences and given resources), free exchange is "beneficial" in its tendency, for all relevant parties.[2]

An educational psychologist who has been consulted on the best color that might be chosen for the walls of a classroom may recommend a bright color that will stimulate alertness and learning. But before pronouncing this color to be *morally* superior to other possible classroom-wall colors, we would want to be sure that the classroom is to be used for morally good teaching purposes. If the classroom is to be the arena in which students are indoctrinated into hateful ideologies, we would probably consider a color which *slows down* the learning process to be morally superior to the alertness-inducing color. "Goodness" is strictly relative to the professional focus of the expert. For the educational psychologist this focus is the promotion of alertness to new information—regardless of the moral status of that information. For the economist the professional focus is the fulfillment of mutually beneficial opportunities for exchange, based on given preferences and resources—regardless of the moral status of those preferences.

But if this is properly understood, it does not appear to be wrong to label a coordinative economic policy to be "good economic policy," since it does promote mutual discovery among the Smiths and the Joneses. The economist who argues that one economic policy is economically better than another policy is doing so strictly within his professional framework.

## What We Have Not Claimed

There are other claims that are not implied by our claim on behalf of the economic goodness of the market process. To show this does not, however, call for philosophical or moral insight; it simply requires rigorous economic reasoning.

For example, take the idea that free markets maximize national wealth. Now the great economists who were the founding fathers of the discipline—the "classical economists"—did indeed define their science as the "science of wealth." It is well known that the (short) title of Adam Smith's classic work is *The Wealth of Nations*. As we noted in the first article, Smith, followed by the other classical economists, took it for granted that the objective of good economic policy is to increase national wealth. Yet the very meaning of the term "aggregate national wealth" (especially if confined as it was in classical economics to *material* wealth) begins to crumble away, as a scientifically useful term, as soon as it is subjected to analysis.

Two bushels of wheat *may* certainly appear as more wealth than one bushel. But are they also more wealth than, say, a package of one bushel of wheat and one sack of potatoes? And even when we consider only wheat, are we sure that two bushels owned by a single wealthy person constitutes more wealth than one bushel that has been somehow distributed among several desperately poor large families? Simply drawing attention to the valuation problems of adding up apples and oranges, or to the complications introduced by the insights of subjectivist (and especially, Austrian) economics, explains why economists at the end of the nineteenth century sought to replace the criterion of aggregate national wealth by less-physical concepts. One such concept, which came to be associated particularly with the work of British economist A. C. Pigou, was that of the aggregate national "economic welfare." What good economic policy seeks to maximize, according to this approach, is the aggregate economic well-being of the members of society.

But the idea of treating individual economic welfare as something that might in principle be added together with someone else's individual economic welfare is one which could hardly be sustained. In particular Austrian economics, which had pioneered the subjectivist understanding of consumer utility, could never accept any such aggregate notion. Moreover, attempts to replace *direct* notions of aggregate welfare by less-direct formulations (that is, those implied in the notions of aggregate efficiency in the allocation by society of its economic resources) are easily seen to be doomed to failure.

Thus, it turns out, economic policy advice cannot meaningfully claim to be based on the idea that a particular policy should be described as economically "good" because it tends to promote aggregate wealth, or aggregate economic welfare, or a more efficient allocation of a society's economic resources.[3] We seem to be forced back to the more modest (but yet enormously important!) claims examined earlier—that certain economic policies may be shown to promote mutual discovery by potential market participants (and may therefore be considered to be "economically good" policies). Sometimes, as we have indicated, this is expressed by pointing out that such policies promote "coordination" among the decisions made in a society. They tend to alert relevant market participants about the possibilities available to them, tending thus to ensure that potentially beneficial opportunities for innovative production, and mutually gainful exchange, do not go unnoticed and unexploited. Implicit in the work of Ludwig von Mises, however, are insights into several *additional* criteria for judging economic policies to be good or bad.

## Ludwig von Mises and the Goodness (or Badness) of Economic Policies

Mises never did fully explain the basis on which he felt able to pronounce an economic policy to be good or bad. He never (as far as I am aware) explicitly discussed the "coordination" criterion for good economic policy to which we have repeatedly referred. But there are grounds for believing our position in this article to be consistent with Mises's philosophical and economic perspectives. In his explicit discussions Mises seems to have grounded his judgments (on the goodness or badness of economic policies) on one or more of three separate foundations:

*Self-Frustrating Economic Policies*: A policy that can be shown by economic science to bring about results that are emphatically *not* desired *by the policymakers themselves* is bad policy. A classic Misesian example of this was the policy of urban residential rent control. Whatever the merits might be of the results hoped for from a policy of rent control, it must be pronounced a bad policy. Economic analysis shows that it tends to generate housing shortages—which were *not* (one hopes!) the objective of the legislators.

*Unsustainable Policies*: A policy that can be shown to be *inherently* impossible to be successfully carried out is an obviously flawed policy. For Mises a policy of monetary inflation (to fuel a boom in the initiation of long-term capital-using ventures) is a bad policy because economics shows how extremely unlikely it is that any such sustainable boom will result. Such a boom can be sustained only through long-run consumer sacrifices, which the consumers are *not* in fact prepared to make. Such policies amount to attempts to run simultaneously in two opposite directions. Economics can show that a particular policy cannot expect to be successfully completed. Such a policy may be described as bad policy.

*Violations of Consumer Sovereignty*: Mises (like most economists) apparently supposed that most people believe it to be a "good thing" for members of society to fulfill their preferences. He therefore shared the conviction of most economists that a policy which structures a society's allocation of resources in patterns clearly at odds with the dynamics of consumer preferences is an economically "bad" policy. A policy that creates a pattern of excise taxes tending to nudge consumer purchases away from goods and services the *consumers* prefer, toward goods and services *legislators* believe to be "better" for consumers—is a policy that Mises believed to be "bad," because it violates consumer sovereignty.[4]

## Science and Passion

We noted in the first article in this series that writers have been puzzled by the *passion* with which Mises denounced what he believed to be bad economic policies. Fritz Machlup, an eminent economist and devoted student of Mises, was one of these writers. Mises's passion seems, at first glance, difficult to reconcile with his own insistence on the absolute necessity for scientific *wertfreiheit*—detached objectivity—in social science. When Mises denounced socialism as a disastrous economic system—one that tends to impoverish society, to bring misery on its members, and to threaten the very survival of Western civilization—he waxed passionate. He was firmly convinced that economic science shows all this to be true. (In particular he was convinced that economics demonstrates how the most benevolent of would-be national planners would not be able to plan [that is, to *coordinate* individual activities] at all! Thus a policy of socialism—that is, a system in which an integrated, single, national plan is sought to replace the "anarchy" of innumerable individual plans in a free-market society—is one that is simply impossible to carry out [just as would be a policy aiming to run in two opposite directions at the same time].)

But by now it should be clear that there is *no* inconsistency in Mises's positions. Because Mises believed—on *objective, scientific* grounds—that socialism is a sure recipe for misery and worse, he believed it to be his *moral duty* to communicate his belief to society with whatever passion might be able to command attention and inspire political relief. Machlup may have seen this as a violation of *wertfreiheit*. Mises would have vehemently disagreed. His passion was—like the passion of someone earnestly preaching the health dangers of tobacco smoking—based on cold, objective science.

As we saw in the first article, the eminent economist George Stigler believed that *any* "preaching" by any economist for *any* particular economic policy is, on grounds of consumer sovereignty, out of order. Stigler believed that the public *already* knows full well what the likely results of any economic policy are likely to be. If the economist is preaching against a policy voluntarily adopted by the public through its political channels, he is simply attempting to promote what *he* believes to be better for society over what *society* believes to be better.

But economic science surely has, again and again, revealed how particular policies result in outcomes *not* foreseen by policymakers, or by those who elected or appointed them. Economics shows how imperfect knowledge may be responsible for enormously valuable (and completely overlooked) opportunities remaining unexploited. It is no violation of consumer sovereignty to demonstrate where such ignorance has been (or is likely to be) responsible for disastrous results. In fact, to demonstrate this is to *promote* consumer sovereignty. As long as the philosophical and moral detachment of economic science is well understood, this science *can* be used, *in a wertfrei manner*, to inform the public of *what it does not yet know*. Where the results of such ignorance are likely to be serious, the economist (in his capacity now of a citizen fully alive to society's suffering) may consider it his *moral* obligation to bring the results of his objective scientific researches to the attention of the public. Such moral obligation may indeed be expressed with Misesian white-hot passion—but this is, in principle, in no way inconsistent with the cold objectivity with which those researches were conducted.

1. This scenario has been extensively explored in a literature pioneered by Nobel laureate Ronald H. Coase; see his celebrated paper, "The Problem of Social Cost," *Journal of Law and Economics*, Vol. III (October 1960).

2. For the classic statement of these insights, see Lionel C. Robbins, *An Essay on the Nature and Significance of Economic Science*, 2d edition (London: Macmillan, 1935), especially Ch. VI.

3. See further my paper, "Welfare Economics: A Modern Austrian Perspective," published as chapter 11 in Israel M. Kirzner, *The Meaning of Market Process, Essays in the Development of Modern Austrian Economics* (London: Routledge, 1992).

4. For a pioneering discussion of coordination, as introduced into normative economics by eminent Austrian economist Friedrich A. Hayek, see Gerald P. O'Driscoll, *Economics as a Coordination Problem, The Contributions of Friedrich A. Hayek*. See also my "Coordination as a Criterion for Economic 'Goodness,'" published as chapter 7 in Israel M. Kirzner, *The Driving Force of the Market, Essays in Austrian Economics* (London: Routledge, 2000). See also Israel M. Kirzner, *Ludwig von Mises: The Man and His Economics* (Wilmington, Del.: ISI Books, 2001), pp. 163–71.

# Mandating Renewable Energy: It's Not Easy Being Green

BY MICHAEL HEBERLING

Environmentalists abhor all fossil fuels (coal, natural gas, and petroleum) and nuclear energy. They collectively refer to this type of energy as "brown" power. Along with a bipartisan collection of Washington politicians, they instead advocate "green," or "renewable," power. This earth-friendly alternative energy includes: geothermal, hydroelectric, biomass, solar, and wind. While we all know that brown power has its share of problems, a close look at green power reveals a surprising number of serious environmental and consumer-related problems that advocates would rather not talk about. As it turns out, environmentalists are far more united in their opposition to brown power than they are in their support of green power.

Geothermal energy is derived from heat beneath the earth's surface and is used to drive steam turbines and heat pumps. Unfortunately, sites capable of producing geothermal energy are rare. Operational geothermal facilities are found in just four western states: California, Utah, Nevada, and Hawaii. Geothermal power plants need sufficient magma close to the surface to heat the surrounding rock and water. The best potential new sites are frequently on federal park lands or in protected wilderness. This complicates, and in many cases even precludes, development. Do we really want to use Old Faithful in Yellowstone National Park as a green-power source?

While geothermal energy is "free," extraction is extremely expensive since developers are frequently required to drill up to a mile or more underground. The remote locations require extensive infrastructure (roads and power lines) and large amounts of cooling water, which is at a premium in the arid west. Various forms of pollution also complicate geothermal energy production. This includes groundwater contamination (thermal and toxic), gas emissions (hydrogen sulfide—which produces a rotten-egg smell, ammonia, and methane), and the mineral-rich discharge sludge that contains mercury and other heavy metals. Closed-loop systems that re-inject all the fluid and gas waste back into the ground will minimize the environmental impact. However, these environmental precautions make the cost of operation far more expensive than gas-fired power plants.

Hydroelectric power, which would seem to be an ideal source of green power, has unfortunately fallen from grace. This dam-derived power source disrupts river ecosystems by hampering (or preventing) the migration of some fish species. As a result, a number of leading environmental groups no longer promote hydro as a legiti-

Hydroelectric power, which would seem to be an ideal source of green power, has unfortunately fallen from grace. This dam-derived power source disrupts river ecosystems by hampering (or preventing) the migration of some fish species.

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mate green-power candidate. In fact, they want to dismantle hydroelectric dams in order to return rivers to their natural pristine state.

Biomass energy involves the burning of plant material. For some reason, environmentalists find the burning of *recent* plant material to be acceptable, but the burning of *aged* plant material in the form of coal to not be acceptable. For biomass to be anything more than a cottage industry of "gee whiz" token pilot projects, large tracts of land would have to be dedicated to growing green power. Will these tracts come from areas previously used for food crops or will this require additional habitat destruction?

Solar power is inexhaustible (especially when the sun shines). It doesn't pollute and best of all—it's "free." Most solar-power advocates will gloss over the fact that to produce one megawatt of electricity would require covering up to 17 acres of pristine land with solar panels. This compares with 1/25th of an acre for one megawatt of electricity produced by fossil fuels. In other words, to be an advocate for solar power, you must at the same time be an advocate of . . . "sprawl." In Michigan solar energy is not practical because of our many cloudy, rainy, and snowy days. How many environmentalists does it take to remove the snow from 17 acres of solar panels in the middle of winter? Bottom Line: Solar energy, even though it is "free," still costs consumers four times more than electricity derived from fossil fuels.

Wind power, just like solar power, is inexhaustible (so long as the wind blows). It doesn't pollute and again, it's "free." Unfortunately, wind is not available on those hot, humid dog days of summer when energy demands peak. The same is true for those quiet (read: windless) bone-chilling winter nights here in Michigan.

While environmentalists loathe a lone cell-phone tower on a hill, they are surprisingly enamored with acre upon acre of wind tower "sprawl" on what were unspoiled vistas. To produce the same amount of energy as a conventional gas-fired power plant, wind farms would need 85 times more area. To its credit, however, wind power is far more economical than solar power. It is only twice as costly as electricity generated from fossil fuels.

However, the most troubling aspect of wind power from an environmental perspective is not sprawl, but the devastating impact it has on bird populations. According to the U.S. Fish and Wildlife Service, between four and five million birds are killed annually in collisions with the 45,000 communication towers (cellular, radio, telephone, and television) located across the country. Many environmentalists and politicians support the "Wind Energy Initiative" that calls for obtaining 5 percent of our electricity from wind turbines by the year 2020. However, to achieve this goal we will need to erect over 132,000 wind-power towers. Do environmentalists and politicians view the additional 12–15 million bird deaths per year as an acceptable tradeoff to meet the green-power goal?

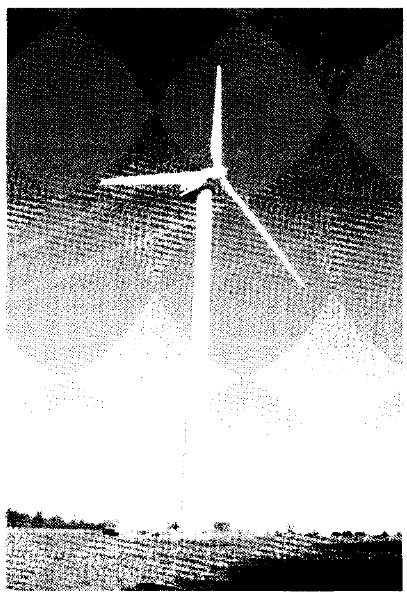
> When utility customers are surveyed asking if they would be willing to pay more for green power to help the environment, there is always an overwhelming and enthusiastic positive response. However, when customers are then asked to actually sign up and pay extra, the euphoria disappears.

An analysis of the bird deaths caused by the existing communication towers suggests that the additional 12–15 million bird deaths from wind turbines is a conservative estimate. When compared to a communication tower, the cross-sectional surface area of a wind turbine is far more deadly to birds because of those rotating "sling blades of death." A 295-foot-tall wind turbine can be viewed as a "communication tower" with an additional bird-killing surface area of 21,113 square feet. That is an area about half (44 percent) the size of a football field.

It is interesting to note that the primary objection that environmentalists have with petroleum exploration and development in the Arctic National Wildlife Refuge (ANWR) is that it *may* harm wildlife. Environmentalists instead propose an alternative form of energy that is *guaranteed* to destroy wildlife by the millions—year after year after year. Defending such hypocrisy serves to reinforce what Kermit the Frog said over 30 years ago: "It's not easy being green!"

## Bad for the Consumer, Taxpayer

If at this point you are starting to have trouble distinguishing between good green power and bad brown power, here is an easy way to keep the two straight. If the power in question requires taxpayer greenbacks to stay afloat, it is definitely green power. Consumers have no idea how expensive green power really is, because the true costs have been hidden by politicians using massive taxpayer subsidies and other preferential treatment. Over the past 30 years federal, state, and local governments have spent between $30 billion and $40 billion promoting renewable energy through grants, subsidies, production credits, accelerated depreciation, publicly funded research, and tax credits. And what do we have to show for this massive taxpayer investment? Today, green power makes up roughly 2 percent of total energy usage in this country.


Wind turbine, Traverse City Light & Power

While geothermal, wind, and sunlight are free, capturing this energy and transporting it from remote, sparsely populated areas to where the people actually live is a costly undertaking. For wind power the ideal lower-cost sites will be developed before higher-cost sites. Consequently, the costs and the NIMBY (not in my backyard) factor will dramatically increase as we expand wind-energy generation in the future. Wind may be considered an *infinite* resource; however, the land on which to capture this wind is a *finite* resource. Where are we going to put all those 132,000 wind-turbine towers? We could start with the Hamptons or Martha's Vineyard and see what happens.

When utility customers are surveyed asking if they would be willing to pay more for green power to help the environment, there is always an overwhelming and enthusiastic positive response. However, when customers are then asked to actually sign up and pay extra, the euphoria disappears. Among the 85 utilities that offer their customers the option to pay extra for green power, the participation rate rarely exceeds 3 to 6 percent, with the majority being around 1 percent. In 1996 Traverse City (Michigan) Light & Power installed a wind generator near Lake Michigan. Under their voluntary green-pricing program, customers could expect to pay from 17 to 23 percent more for their electricity. The electric bill for Dick Dell'Acqua's Omelette Shoppe & Bakery in Traverse City went from $1,600 to $1,900 a month after signing up.

Since the consumer is not voluntarily buying into green power, it should not be surprising that our elite class wants to take away our freedom of choice. Across the country at the local, state, and federal levels there are efforts to mandate green power. Sixteen states (Arizona, California, Colorado, Connecticut, Hawaii, Iowa, Maine, Maryland, Massachusetts, Nevada, New Jersey, New Mexico, New York, Rhode Island, Texas, and Pennsylvania) have "Renewable Portfolio Standards" (RPS) that require varying percentages of green power in their energy mix. Three other states (Illinois, Minnesota, and Pennsylvania) have RPS-like programs that are not quite as onerous as the other 16.

A common theme in each RPS is to have the mandated percentage of green power increase over time. California is required to produce 20 percent of its electricity through green power by 2017. In Nevada state law requires 15 percent by 2013. The New York RPS requires 25 percent by 2013.

In the majority of the RPS programs, government-owned municipal utilities have aggressively (and successfully) lobbied for exemption from their own state's costly and unrealistic green-power requirements. This raises a question: If green power is so wonderful, why are government utilities allowed to opt out? At least under the green-pricing programs, consumers had a choice. Under state RPS programs, consumers who have the misfortune to be served by investor-owned utilities are forced to pay a hidden and unconscionable energy tax. Do the elite ever think about the poor or the elderly on fixed incomes when they impose "good for the environment" taxes?

## A National Tax Coming?

Those of us who are lucky enough to live in the 31 RPS-free states are not out of the woods just yet. Even if our state legislatures are able to resist the siren song that "mandated green power is good for the environment," our federal legislators are hard at work trying to impose a national RPS energy tax. In October 2003 a national-RPS provision was pulled at the last minute from the energy bill. Had this been included, we would have seen a mandatory 1 percent green-power requirement in 2005. The requirement would then have risen to 10 percent by 2019.

Last year bipartisan legislation was introduced again to establish a federal RPS energy tax. This legislation seeks to mandate a 20 percent green-power requirement by 2025. As in most of the state RPS programs, this national mandate would exempt government-owned utilities from this costly and unreachable goal.

Given that 30 years of central planning and $40 billion of taxpayer money have done little to facilitate the growth of green power, perhaps we should now consider an alternative consumer-friendly approach. It is time to permanently remove the government-subsidized training wheels from green power. Let the marketplace, not the government, determine what types of energy will be the winners and the losers. Considering the numerous problems associated with green power, a market-based solution will, ironically, be good for both the consumer and the environment.

The only way that the information needed to make sensible energy decisions can be communicated by those who have it to those in the best position to respond appropriately to it, and communicated in a way that motivates appropriate responses, is through market prices—assuming these prices are not distorted by politically imposed caps.

Market prices allow consumers to inform producers, and one another, how much they value different energy uses, and allow producers to inform consumers how much it costs to provide different types of energy. In response consumers will decrease their energy use in ways that minimize their inconvenience when that inconvenience is less than the value of the energy saved. And producers will expand production of energy sources that provide the most value to consumers for the cost required, and will expand those sources as long as consumers value the additional energy by more than the value sacrificed to produce it. The result is a combination of conservation and production that best harmonizes the interests of us all.

—**Dwight R. Lee**, "Energy Production versus Conservation"

# The Therapeutic Temptation

**BY THOMAS SZASZ**

"Lead us not into temptation, but deliver us from evil," enjoins the Lord's Prayer. Temptation to commit what wrongful act? For the men who wrote that warning and the people to whom it was addressed, there was no doubt about the answer: concupiscence.

Today, the term is obsolete and the bodily-mental state to which it refers—intense sexual desire—is not an evil from which we seek deliverance but a psychosexual condition we crave and endeavor to achieve by means of drugs prescribed by doctors.

In the Age of Faith people feared engaging in behaviors prohibited by God. Modern secular man—although liberated from fearing God—still fears being led into temptation. To be sure, he no longer calls the object of the dreaded behavior "sin." He calls it "sickness." Worshiping health and especially mental health, people fear the temptation of engaging in behaviors prohibited by mental-health laws. Deprived of the moral vocabulary of agency and action, modern man does not conceptualize his experience as temptation and sinning. Instead, he fears "falling ill" with the great "no-fault diseases" of our age—drug abuse-addiction and depression-suicide.

A woman physician is sentenced to 50 years in prison for "overprescribing" pain medications and "causing" several people to kill themselves. She says: "I'm saddened by the fact that those that I tried to help so hard, to improve their lives, to reduce their suffering, turn against me and make me look like the devil." A parent who had lost her daughter and son asked the judge to give her the maximum sentence: "I have two children, your honor, that I'll never see again. . . . [T]he only way I get to see them is at the graveyard."

Charged with drug-law violations, radio talk-show host Rush Limbaugh repents, confesses his sins, and submits to a purification of his faith. "As a primary condition of the dismissal [of the charges against him], Mr. Limbaugh must continue to seek treatment," explained his lawyer. Limbaugh the drug-user is not a responsible agent but the victim of an illness brought on by temptation. William Bennett, America's self-appointed expert on virtue, is a victim of gambling addiction. Do I exaggerate? Alas, if only that were so. The American Medical Association, the American Psychiatric Association, the U.S. Supreme Court, the media, and the public all *define* addiction as a disease. Diseases have causes. The causes are the individuals who tempt the addict or fail to prevent his "illness."

Fearful as the temptation to take drugs may be, it pales in comparison with the temptation Americans dread the most—suicide. Of course, in this case too, the language of action and responsibility is taboo. No "psychiatrically enlightened" person talks about the temptation to kill oneself. Such persons *know* that suicide is the cardinal consequence of the no-fault disease called "bipolar illness," a.k.a. "depression." How right Josh Billings was when he observed, the "trouble with people is not that they don't know but that they know so much that ain't so."

On May 22 the feature article of *Time* magazine was titled, "When Colleges Go On Suicide Watch." The subtitle spelled out the problem: "Schools are getting sued for doing too little—and too much—to help mentally ill students." The "problem" is part of the false premise that lies at heart of the article, namely, that it is, in some undefined way, the job of colleges to prevent their students from killing themselves. Suicide is an action. The only person who can control—bring about or prevent—an action is the actor. Why not hold colleges responsible for students becoming obese or going bankrupt?

Ought implies can. Since no one can prevent anoth-

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er person from killing himself, the expectation that colleges, psychiatrists, or anyone else ought to be responsible for preventing a student's suicide is nonsense. An individual held responsible for another person's suicide has only one viable option, separating himself from the subject deemed "dangerous to himself." This may take the form of: 1) depriving the "offender" of liberty, by incarcerating him, with the aid of psychiatrists, in a mental "hospital"; or 2) divorcing him, literally, if the subject is a spouse, metaphorically, if he is a college administrator and the offender a student. We may do well to remember that only a few decades ago—before the advent of the suicide-prevention lobby—no one seriously expected anyone to prevent suicide.

Sadly, none of what I am saying here can be said in the pages of the mainstream press. Revealingly, the subtitle of the *Time* article treats as fact a non-fact: it calls students regarded as suicide risks "mentally fragile": The number of students "diagnosed as mentally fragile appears to be rising. . . . A lot of students who may not have gone to college five years ago are able to attend today because their illness has been recognized earlier and they are on medication," explains a bureaucrat at a New York-based "college suicide-prevention program."

To be sure, many a college-age student faces a difficult period of life that has nothing to do with his "mental ill health." It has to do with the fact that he is leaving childhood and entering adulthood. Expelled, literally or figuratively, from the home of his parents, the young person is suddenly homeless. He must make a temporary home for himself at college, a challenge some are better prepared to meet than others. Redefine this elementary existential trial as a medical disease amenable to diagnosis, prevention, and treatment—and students, parents, psychiatrists, and colleges are off to the races.

The transition from childhood dependence to adult independence is often experienced as depressing. It is dangerous to frame this in psychiatric terms. The *Time* article presents the story of a young woman "struggling" with anorexia who told a Cornell University counselor that she felt like killing herself. What did she expect the counselor to do? The student "agreed to spend the winter break at a psychiatric hospital." After the university "threatened to suspend her," she "took a voluntary medical leave." The key terms in these sentences are as phony as is the medicalization of growing up.

## Troublesome, Not Troubled

The students' parents and psychiatrists call such students "troubled." Again, the wrong term. Such students are "troubling" and "troublesome": they are "trouble" for universities, which are held responsible by courts for their suicides. Trying to escape that trap, some colleges opt to expel troublesome students. But if they do that, the students or their parents sue the school for discrimination under the provisions of the Americans with Disabilities Act, which "protects" people suffering from mental illnesses. From what?

Each party affected by this Alice in Wonderland tragicomedy deserves the fate that, some 30 years ago, I predicted would follow inexorably from defining the voluntary act of self-killing as the unintended consequence of a no-fault disease.

Cornell University, we learn, "pushes a hundred or so of its students each year to take a voluntary medical leave." "Voluntary medical leave" is code for involuntary psychiatric leave. The anorexic Cornell student continues to be clueless about what happened. "I knew if I stayed at Cornell one more week, I would kill myself," she told *Time*. "After lengthy discussions with her therapists [sic]," the student went home and entered a mental hospital. She "is disappointed that Cornell hasn't made any follow-up calls to see how she is doing."

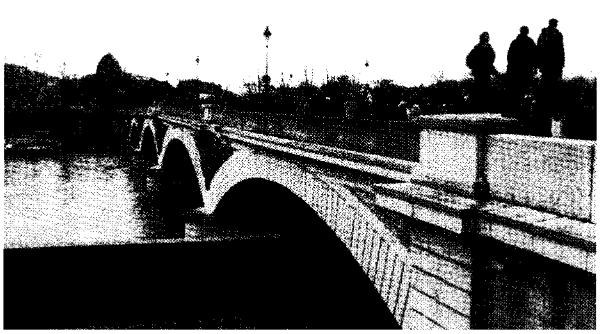
This woman has been unable to resist the temptation to think of herself as having a disease. This is what happens when Sartrean "bad faith" becomes "good faith" —when the person who lies to himself comes to truly believe his own self-deception.

# What Is Going on in France?

## BY PIERRE GARELLO

It is sometime painful for a liberal—I will be using that word in its old, continental, sense—to live in France, especially in southern France: so much light, so many beauties given by nature, and at the same time so much wealth wasted! Riots; strikes; blockage of roads, schools, universities, factories; or simply so many adults not working, sometimes by choice, sometimes by force (the 35-hours-per-week law).

But beside the waste, what makes the lover of freedom really sad is that *apparently* most of his or her fellow citizens don't see the waste and firmly believe that "we" in France have developed a political system that strikes the right balance between wealth creation and redistribution. "We" have realized the old dream of such socialists as Sismondi, who in the early nineteenth century was looking for a way to combine the efficiency of Manchester industrialism with the *douceur de vivre* (softness of living) of Tuscany. "We" have high-tech industries (the national champions: EDF, Alcatel, Airbus-EADS, Total, Veolia, Sanofi-Aventis), and at the same time "we" are able to guarantee decent health care and decent education to everyone. Indeed, the list of the famous *droits acquis*—positive rights that demagogic governments under the pressure of unions have ordained throughout the previous decades—is a long one. (It might be interesting for the rest of the story to recall that France is among the very few countries in the world to have almost no private university, and where anyone holding a high-school diploma can enter the university of his choice at no charge.)



Zayyani.free.fr

Hence liberals experience a deep frustration when realizing that the perception of their fellow citizens is so different from theirs. In a way it is a well-known frustration, probably similar to that felt by advocates of free trade in an often-protectionist but nonetheless relatively prosperous U.S. economy, or to that experienced in the '60s and early '70s by those opposing Keynesian policies in a globally booming economy. You try to convince others that those *droits acquis* don't make them wealthier but poorer, but you and they apparently don't live on the same planet! Before commenting on such apparent divergence of perceptions, it is necessary to run a more detailed analysis of the situation, considering individuals instead of abstract groups such as "the liberals" and "the others." For indeed, the set of people who demonstrate in the streets of Paris, Lyon, Marseille, and other cities was far from homogeneous. So we need, if only briefly, to tell the story of the last months in order to identify the various subgroups and what was motivating them to act as they did.

The story started with the riots of November 2005. At that time some parts of the country were in a state of

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chaos (cars burned, policemen stoned, shops vandalized), so much so that a "state of emergency" was officially declared and curfew ordained in some municipalities. A few days or weeks later, once order was (more or less) restored, a consensus emerged that something had to be done, and we all know what that means: a new law must be passed that will solve the problem. Prime Minister Dominique de Villepin was asked to quickly come up with a proposition to show that President Jacques Chirac cares, that the government is responsible (keeping in mind that the next presidential elections are scheduled for April 2007). Hence, in a few weeks, a law was prepared and ready to go to the National Assembly.

One article of that law (article 8) was to become famous: the introduction, in the midst of an already existing jungle of specific labor contracts, of a new contract designed for youth (under 26) without professional qualifications. The hope of the government was to bring down the rate of unemployment in that subset of the population from 25 percent to a more "reasonable" level. In France, as in many countries, freedom of contract is limited in employer-worker relations. In particular, French law distinguishes between *Contrat à durée déterminée* (CDD) and *Contrat à durée indéterminée* (CDI). Both types are regulated, with the latter offering a wide "protection" for employees, making it particularly costly for the employer to breach it. As indicated by its name, a CDD is a labor contract with predetermined duration (in any case less than 19 months), while a CDI does not specify any duration.

Because of the *droits acquis* associated with CDIs, employers were reluctant to offer such contracts, especially to a young person without working experience, and tended in such cases to favor short-term CDDs. The strategy of the government had been to give tax allowances or grants to any company willing to employ an inexperienced youth. In January 2005 a new regulated labor contract (*Contrat Initiative Emploi*) had been created, granting up to 45 percent of the minimum salary to any employer entering such a contract. (It must be recalled that the minimum salary is fixed by the law at €1,357, or $1,682 a month.) Then, after November 2005, instead of sponsoring short-term contracting, the government decided to create a new CDI contract (baptized *Contrat Première Embauche*, or CPE), which for the first two years permitted layoffs of young employees without specific justification (but with compensation). To a liberal mind, this was a further contractual option, and therefore was going in the direction of greater freedom.

Probably anticipating opposition from the central and left parties in the Assembly and therefore everlasting debates, Villepin, who had prepared the law without much discussion with the labor unions, decided to use Article 49-3 of the constitution to put the law to vote without discussion by senators and MPs. Since his party (the UMP—*Union pour un Mouvement Populaire*) benefited from a disciplined majority in the Senate and Parliament, the law passed as expected.

Ironically, this was great news for the leftist parties (socialists, communists, and greens): Villepin had unwittingly created a unique opportunity for them to convince electors that the right and the left have different views on what should be done. Such an opportunity does not present itself often, since Chirac, seconded by his successive prime ministers, has often followed socialist lines.

The socialist response to the government was simple: the "ultra-liberal" legislation gives up major social advances (again, *les droits acquis*) and will greatly penalize youth entering the job market. Seen from the perspective of "*la lutte des classes*" (the class struggle), the new contract was not perceived as a minor advance of freedom, but as "greater flexibility," that is, greater freedom for the employer to exploit the young worker. Interestingly, in August 2005 a contract similar to the CPE but available only to firms of fewer than 20 employees, the *Contrat Nouvelle Embauche*, was approved and no demonstration followed. Maybe in the socialist dialectic, exploitation by a small company is not as bad as exploitation by a big company.

## Labor Monopoly

Another key player in that drama was the labor unions. Because of a 1936 law, labor unions in France benefit from a large monopoly; even though membership is low (8 percent), the unions' political power is huge. (More precisely, only so-called "representative unions" can present candidates for election as workers' representatives and are called for negotiation at the national level. To become a "representative" union you must be one of the five unions named by the 1936 law or prove your "representativeness.")

To the unions, too, Villepin offered a great opportunity to show that they can make a difference. But they were facing a major difficulty: they are not representatives of the population targeted by the law: the youth looking for a first job and without qualifications. To circumvent that handicap a two-tier strategy was to be implemented. First, create agitation in the universities. This is much easier than reaching out to the unemployed in the suburbs, and it was likely to work because university students, although not concerned by the new contract because they, supposedly, will be qualified, are worried about their future. Second, motivate union members by arguing that if they let the government start dismantling the actual labor law with all its *droits acquis*, employers will soon have free hands to exploit *all* employees.

One may wonder what the reaction of the business community was. Two employers' unions play a significant role in France: the MEDEF, which represents the "large" companies, and the CGPME, which represents the small and medium enterprises. (France's deficit in medium-size enterprises is well known. This is, surely, one of the main explanations for its high unemployment.) If both unions were supportive of the CPE, their voices did not make much of a difference, and one is tempted to add . . . as usual! The reason is surely that they have for a long time been "institutionalized" and have made too many compromises in the past with the successive governments. Surely they are not strong supporters of the "class struggle," and here and there they pay lip service to the market, but they also ask for protectionist policies each time they feel endangered by competitive pressures. (It is therefore not surprising that those unions typically back all the propositions in favor of a more centralized and "harmonized" Europe, including the imposition of a single currency.) Furthermore, most CEOs of France's largest companies went to school with the technocrats and politicians who run the country, and in those schools they were taught that engineering—not entrepreneurship—is the main engine of economic growth. For all these reasons, there was not much hope for employer-union support of the CPE.

Finally, in order to win, the coalition needed the support of the media and the intellectuals (and in particular the teachers). I will not comment on that aspect of the conflict since it would necessitate a long digression. It is enough to say that this support was gladly offered and that, consequently, this was too many battles for a government and a majority unsure of their own convictions.

The end of the story is known: in a curious move, President Chirac started by saying that, although the law was passed, it will not be applied. Then, a few weeks later, he asked the government to prepare a new law, which was passed on April 21, 2006. The CPE lived only a couple of weeks! Should the youth rejoice?

## What Should the French Youth Worry About?

If the youth had nothing to fear from the CPE, there are other good reasons to be worried. Some are to be found in the present state of the French economy; others, even more worrisome, in the state of the rule of law prevailing in this country.

Let me first focus on the economic reasons why the youth should worry about their future. To start, France has little growth and creates no employment. The unemployment rate has been stuck at 10 percent (and this is probably an underestimation) for the last quarter-century. Among the youth, as I said, the figure is 25 percent. Nothing to rejoice about indeed!

The reasons for that state of affairs are well known. The main engine of growth, the entrepreneur, is not a popular figure in France. In the country of Colbert, Saint-Simon, and Napoleon, the popular figure is that of the engineer, or the top civil servant. Worse, it is commonly thought that if an entrepreneur makes a profit, it is necessarily at the expense of the employees. The "class struggle" is the Economics 101 of a large part of the population. This is, by the way, one of the saddest things to a liberal: while people could live in harmony, they choose envy and anger. Lower entrepreneurial spirit translates into a sluggish labor market. To this add the usual ingredients that increase the total cost of hiring:

- A minimum wage around $1,700 a month (interestingly, one quarter of the total working population is paid the minimum wage!);

- The cost of laying off (first you must "justify" your decision, second you pay high monetary compensation);
- Lack of flexibility in working time;
- High unemployment benefits (which might create a moral-hazard problem in low-skilled positions where being fired is not seen as a disaster);
- Lack of good training (due to a quasi-absence of competition in the school and training system).

But that's not all. Another great source of concern for the youth is their parents' *droits acquis*, which will cost the grown children a lot of money. In particular, like many Western countries France has opted for the pay-as-you-go pension system, and demographic projections are such that the bill to be paid by coming generations will be high. We can predict much more violent confrontations between generations when the youth realize how irresponsible their parents have been. And of course, borrowing will soon no longer be an option—or it will be a very costly one: over the last quarter century the public debt has increased by a factor of more than 10 (from €73.8 billions to €992 billions) and as percentage of GDP, by a factor of 3 (moving up from 21.3 to 63.7 percent). As a consequence, the interest charge is already the second-highest expenditure in the budget, reaching in 2004 2.34 percent of GDP or 10.9 percent of total public expenditures and 14.35 percent of tax revenues.

So the situation is worrying, but there is something that surfaced once again during the recent events which is even more frightening for the freedom lover because it indicates we are losing something that is probably more difficult to teach than Economics 101: the spirit of the rule of law.

## A Degraded Rule of Law

The rule of law is the precondition for growth, and more generally for the flourishing of a harmonious society. Attacks on property rights have, however, been recurrent during the twentieth century. This is nothing but the logical consequence of choosing to live in a social democracy based on a high level of redistribution. It is also the down-to-the-earth meaning of *droits acquis* since those "rights" must be acquired from someone! (Note that the French disease has reached the European Union; in Brussels the two most-used French words are *acquis communautaires.*) But we are now going one step further: private citizens have lost the possibility of expressing their opinion through the political system; or more precisely, that right has been emptied of meaning. If you elect a representative, it is so that he can convey your opinion in the lawmaking process. But Article 49-3 of the Constitution (which allows the government to bring a bill to a vote without legislative debate) has been used 86 times since the fifth constitution was enacted in 1958. This time it was worse: a president of the Republic asserted that a law just passed will not be applied, and a couple of weeks later he asked for a new law that abrogates part of the previous one. One may wonder what's left of the predictability of the law?

Of course one may respond that the rule of law has often been violated by a regular vote of a majority of the representatives, but shouldn't we prefer the rule of the majority to the rule of the street? Doesn't the French love for public, and often violent, demonstrations destroy any respect for the legislative process and, more importantly, for the law? Some commentators welcomed young people's sudden interest in what is done by the government. But I don't share that opinion: first, because, as explained above, the demonstrations were not that spontaneous, and second, because the recent events clearly show that governments as well as MPs are mere puppets and the law is written in sand. This, I am afraid, is the message that Chirac has sent to the French youth.

Voting with one's feet is of course an option whenever one's voice is not taken into account. As a matter of fact, France has been losing entrepreneurs and attracting low-skilled workers. This is not surprising and will undoubtedly worsen the economic situation. Exit remains nonetheless an essential attribute of freedom and might at some point (but when exactly?) invite the government to engage in the right reforms.

Assuming one decides to stay (maybe because the cost of exit is too high), what can be done? One possibility is to resort to some kind of retaliation. For instance, one could decide to boycott the elections for a while. That would be a way to tell everyone that the parliament and even the executive have lost all legitimacy.

But that strategy, however tempting, is likely to be misinterpreted, and one runs the danger of ending with the worst possible representatives. Maybe a more efficient way to express one's discontent with the way decisions are made would be to invite one's fellow taxpayers to join a fiscal revolt. Indeed, why should we pay taxes if there is no representation and if decisions concerning the level of taxes are made in the street by the most excited, the least educated, and the communists who have no respect for your property? No representation, no tax!

A somewhat softer strategy would consist in educating the youth. (As argued above, the problem goes beyond the teaching of sound economics, which of course is necessary). To fulfill that task we know that we cannot count on the state education system largely controlled by socialist-minded individuals. An urgent battle is therefore to be engaged against the state monopoly on education. At the same time we must use all the media available—Internet, newspaper, radio, television, books, and conferences—to articulate the liberal vision of a free and responsible society. As a matter of fact, a cheerful aspect of the past months lies in the creation and development in France of many free-market think tanks and other liberal initiatives coming from civil society.

Meanwhile, one can and must rely on the most natural way to provide education: the family. It was indeed shocking during the recent events to hear that some associations of parents called on their members, and beyond them all parents, to demonstrate with their kids against the CPE. This way, those associations claimed, parents could not only make the demonstrations safer (another way was to forbid your 16-year-old to miss class and have fun downtown during all afternoon!), but could also show their kids that they share their fears and desire to see the law abrogated. I remain convinced, however, that even though they don't take the time to explain to their kids what their vision is, most parents *do not* share the vision motivating the demonstrations. The family probably being the best place to learn about the rule of law and more generally the responsible life, it is time for the parents to behave in a responsible way.

# Chernobyl in Perspective

**BY JIM PERON**

When the Chernobyl nuclear reactor exploded in 1986 the world held its breath. In the aftermath, we were told that a catastrophe had taken place. Ten years later Greenpeace said the accident was "blamed for the deaths of some 2,500 people, has affected millions and displaced hundreds of thousands, many of whom have still not been able to return to their homes." Greenpeace called nuclear power "the most dangerous energy source yet devised by humankind."

Since those claims were made another long ten years have passed. But now the United Nations has released a report showing that, first, the accident has not been nearly as deadly as originally projected, and second, that although the accident was horrific, the official response made things worse for large numbers of people. Chernobyl also has some lessons on the detrimental effects of welfare. Moreover, even after hundreds of scientists have produced an exhaustive report on the matter, the environmental ideologues refuse to change their tune, but instead denounce the scientists.

The myth-busting report, "Chernobyl's Legacy," was published in two versions by the Chernobyl Forum, a collection of international organizations formed in 2002, including the World Health Organization, the UN Development Program, and the World Bank, along with the governments of Russia, Belarus, and Ukraine. (The second version of "Chernobyl's Legacy: Health, Environmental and Socio-economic Impacts and Recommendations to the Governments of Belarus, the Russian Federation and Ukraine" is online at http://chernobyl.undp.org/english/docs/chernobyl.pdf. Quotes in this article appear in both versions, except one, which is taken from the second version.)

When Unit 4 of the Chernobyl reactor exploded it was predicted that tens of thousands would die. The report notes that "Claims have been made that tens or even hundreds of thousands of persons have died as a result of the accident. These claims are highly exaggerated."

> The Chernobyl report notes that "Claims have been made that tens or even hundreds of thousands of persons have died as a result of the accident. These claims are highly exaggerated."

This doesn't mean no one died. But the numbers directly attributed to the accident are much lower than most would assume. The year of the accident 28 people died from exposure to acute radiation syndrome (ARS), all of them emergency workers at the reactor. From 1987 until 2004 19 more emergency workers died from a variety of causes, "however their deaths are not necessarily—and in some cases are certainly not—directly attributable to radiation exposure," the second version reported.

The main problem found in the general population was for young children who drank milk that was produced by cows that ate contaminated grass. For them there was a clear increase in thyroid cancer. But this

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cancer is highly treatable. The report noted: "For the 1152 thyroid cancer cases diagnosed among children in Belarus during 1986–2002 and treated, the survival rate was 98.8%."

Except for these two groups, the direct medical impact of Chernobyl was minimal. According to the report, "Among the general population affected by the Chernobyl radioactive fallout, however, the radiation doses were quite low, and ARS and associated fatalities did not occur."

Chernobyl took place in 1986. The Soviet Union's socialist system finally collapsed in 1991. In the years immediately following the collapse living standards dropped. The economy was a disaster, and medical care had become almost nonexistent. People all across the region saw life expectancy decline. Chernobyl's effects were tiny in comparison to the larger picture.

The 50-some deaths are firm numbers. But the projections of possible other deaths are estimates. The Chernobyl Forum reported: "[T]he number of deaths over the past 20 years that may have been attributable to the accident are only estimates with a moderately large range of uncertainty. The reason for this uncertainty is that people who received additional doses of low-level radiation have been dying from the same causes as unaffected people. Moreover, in all the groups studied, of both emergency workers and resident populations, *any increase in mortality as compared to control groups was statistically insignificant or very low.* Estimates related to projected deaths in the future are even less certain, as they are subject to other major confounding factors. In reality, the actual number of deaths caused by the accident is unlikely ever to be known with precision."

A year ago the *New York Times* reported that "for the millions who were subjected to low levels of radioactive particles spread by the wind, health effects have proved generally minimal." It added that there was no rise in leukemia rates except for a small number of plant workers. Nor has any increase in birth defects been noticed nor decrease in fertility rates.

The reason for this is simple. Only people in the immediate vicinity of the accident were exposed to sufficient radiation to cause problems. As the U.S. Nuclear Regulatory Commission explains in its "Fact Sheet on Biological Effects of Radiation," "Radiation is all around us. It is naturally present in our environment and has been since the birth of this planet."

Most people seem unaware of this. The average American is exposed to 300 millirems of radiation per year, and over 80 percent of that is from natural sources. Residents of Denver receive about 1,000 millirems because of the altitude. A person working in a nuclear power plant is exposed to about 300 additional millirems per year, while regulations limit annual occupational exposure to 5,000 millirems. However, pilots, airline crew members, and frequent flyers can be exposed to an additional 500 to 600 millirems. That's quite a bit when you consider that living next door to a nuclear power plant only increases exposure by 1 millirem per year. If that worries you, remember that the human body produces about 40 millirems per year entirely on its own.

For most people affected by the reactor accident, levels of exposure were not extraordinary. "Chernobyl's Legacy" states that "the average doses received by residents of the territories contaminated by Chernobyl fallout are generally lower than those received by people who live in well known areas of high natural background radiation in India, Iran, Brazil and China."

Dr. Burton Bennett, chairman of the Chernobyl Forum, told the BBC last year: "This was a very serious accident with major health consequences, especially for thousands of workers exposed in the early days who received very high radiation doses, and for the thousands more stricken with thyroid cancer. By and large, however, we have not found profound negative health impacts to the rest of the population in surrounding areas, nor have we found widespread contamination that would continue to pose a substantial threat to human health, with a few exceptional, restricted areas."

## Mass Evacuations

At the time of the explosion entire regions were evacuated—due more to panic than anything else. Dr. Fred Mettler Jr. of the Chernobyl Forum, a Veterans Affairs hospital radiologist, said, "People were evacuated from areas that now have dose levels lower than where I live in New Mexico." And the evacuation itself caused many problems and possibly harmed far more people than the accident.

At first the Soviet Union tried to hide the accident from the world. This unnecessarily exposed people in the immediate vicinity to risk, especially children who now suffer from thyroid cancer. As Bronwen Maddox of the *Times of London* wrote last year: "Better warnings in the first week could have averted this. But the Government's desire at first to cover up the explosion meant that it delayed warning people or moving them to safety."

Later, when the disaster became public knowledge, the Soviets exaggerated the health effects. Maddox wrote: "The underlying level of health and nutrition [in the region] was abominable; there was every interest in exaggerating the impact to get aid money; the Soviet culture had never been shy of using science for political ends."

Of course environmental activists and antinuclear ideologues also had reasons to exaggerate the consequences, hence the predictions of hundreds of thousands of deaths as a result of the accident. Add to that the natural tendency of the media to prefer the sensational aspects of any story, and it is no wonder that people around the world were in an induced panic. Individuals who lived in the vicinity suddenly found themselves being relocated, often against their will. They lost their homes and were subjected to regular medical checkups, all of which had to raise their anxiety levels. Many of these people simply came to assume that they had been exposed and were doomed.

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Fear of course is detrimental to health. "People have developed a paralyzing fatalism because they think they are at much higher risk than they are, so that leads to things like drugs and alcohol use, and unprotected sex and unemployment," Dr. Mettler said. In an article about the Chernobyl report, the *Washington Post* noted "that lifestyle disease, such as alcoholism, among affected residents posed a much greater threat than radiation exposure."

Tomihiro Taniguchi, a deputy director general of the International Atomic Energy Agency, was quoted in the *Guardian* as saying, "[T]he situation was made even worse by conflicting information and vast exaggerations—in press coverage and pseudoscientific accounts of the accident—reporting for example, fatalities in the tens or hundreds of thousands." Taniguchi added that "many of the 350,000 people evacuated and resettled by authorities would have been better off staying home."

The Chernobyl report states that "individuals in the affected population were officially given the label 'Chernobyl victims,' thus frequently taking on the role of invalids. It is known that if a situation is perceived as real, it is real in its consequences. Thus rather than perceiving themselves as 'survivors,' the affected individuals have been encouraged to perceive themselves as helpless, weak and lacking control over their future."

Predictably, people have taken advantage of the accident. Kalman Mizsei, a director of the UN Development Program, said "an industry has been built on this unfortunate event," which has a "vast interest in creating a false picture." The Russians and environmental ideologues have already been mentioned. Moreover, millions of people were paid benefits on the basis of being victims.

The negative consequences of welfare for Chernobyl "victims" are real. Seven million people received various benefits from the Russian government due to their exposure. Although the effects of radiation diminish with time, the number of people claiming to be disabled is climbing. In Ukraine in 1991, 200 people were considered permanently disabled from Chernobyl. In 1997 the number was 64,500, and by 2001 it was 91,219. The report is blunt: "The dependency culture that has developed over the past two decades is a major barrier to the region's recovery. The extensive system of Chernobyl-related benefits has created expectations of long-term direct financial support and entitlement to privileges, and has undermined the capacity of the individuals and communities concerned to tackle their own economic and social problems."

## Furious Reaction

How has the UN report been received? The media found it a fascinating story because it has the element of sensationalism that sells papers and boosts ratings. But the beneficiaries of Chernobyl, and the ideological groups that use the accident for their own agendas, are furious. They refuse to accept the report and instead denounce the UN for producing it.

Greenpeace in particular was most upset. William Peden, a Greenpeace researcher, said that the projection of 4,000 deaths total "is ridiculous" and "many thousands more may die in the decades to come." Jan van de Putte, another Greenpeace activist, says the UN was "denying the real implications" of Chernobyl and that is "insulting [to] the thousands of victims." He also said the report is dangerous because it may lead to "relocating people in contaminated areas."

Greenpeace also asserted that the low death projection omitted the harm to much of Europe. But this was omitted because there wasn't any. Most of the radiation fell within a few dozen miles of Chernobyl.

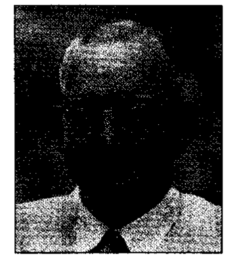
It's yet another example of how environmental ideologues will bend science around politics.

## Robert Higgs Named Winner of 2006 Thomas Szasz Award

*Freeman* columnist Robert Higgs has won the 2006 Thomas Szasz Award for Outstanding Contributions to the Cause of Civil Liberties. Higgs won in the general category; Australian psychologist Robert Spillane won in the professional category.

The award is given annually by the Center for Independent Thought.

For years Higgs, Senior Fellow in Political Economy at the Independent Institute, has documented in books and articles how government maintains its power over people, and hence steals their liberty, by exploiting various fears: fear of external enemies, fear of social insecurity, fear of government itself. He has been a *Freeman* contributing editor and columnist for more than a decade.

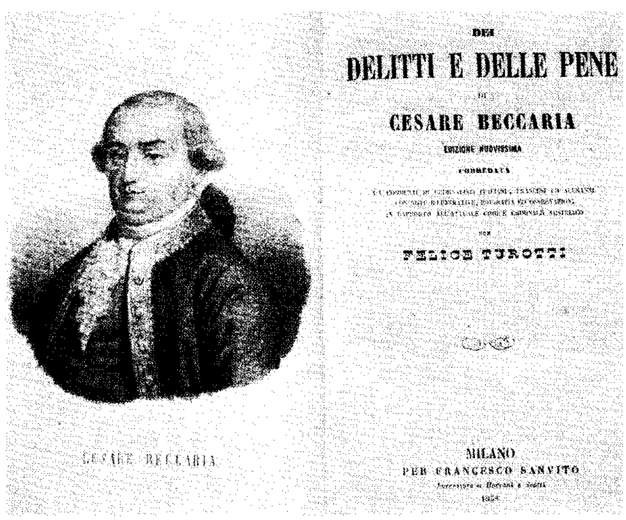


# Always Think of Incentives

BY STEPHEN DAVIES

While visiting FEE a few years ago, I was lucky enough to hear a talk by the "armchair economist," Professor Steven Landsburg. In it he remarked that most of economics could be summarized in just two sentences: "Resources are scarce" and "People respond to incentives." These two apparently simple and obvious observations are in fact profound insights into the nature of human beings, the world they inhabit, and the social life they lead. As Landsburg said, exploring them and their implications leads to an enormous body of thought and insights, often surprising.

It is the second one that concerns me here. All human beings have to act in order to survive, and these acts involve choices between alternative courses of action. We choose according to the perceived balance between benefits and costs accruing to any action. This is what is meant by responding to incentives. The obvious corollary is that if the incentives change, then choices and subsequent behavior will change as well. The change may be actual or one of perception or a change in the subjective evaluation of the alternatives, but that is a secondary matter. The crucial point is that the pattern of incentives will tend to shape the way people choose and act.




**Frontispiece and title page of an 1858 edition of Cesare Beccaria's work on crime and punishment**

Thus if you want to understand human behavior, the pattern of incentives must be established. If you can do this, then in many cases you will have found a way to explain what might otherwise seem incomprehensible. This is even, or perhaps particularly, true in the case of behavior that is apparently self-destructive or pointless. It also means that one way of changing human behavior is either to change the incentives directly or else to change the subjective evaluation of the payoffs and hence the choices made. This can help us to understand both the nature and origin of major social problems and what will or will not work in trying to resolve them—or indeed if they can be resolved by deliberate action at all.

A common response is to say that this is a narrow and impoverished view of human motivation that relates only to the realm of money and economic incentives in the narrow sense. However, understood properly, this principle has much wider application. Incentives clearly include financial or monetary costs and benefits, and it is foolish and naïve to underestimate how important these are. However, the term also includes all sorts of other benefits, which are often more powerful than money. The most significant is social status. When we think about incentives in this wider sense, it is possible to make sense of areas that at first sight have nothing to do with economics as it is generally understood.

One of the best examples of this is the criminal-justice system. Historically this was one of the first areas of human life to be analyzed using this insight, and the effects were profound. In eighteenth-century Europe the penal system, which had largely been created during the later Renaissance (roughly 1450 to 1650), was exceptionally harsh and brutal. Many crimes

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attracted the death penalty, which had a central place in the system. As time passed, the number of capital crimes grew steadily. In England there were about 100 capital crimes in 1700, but by 1815 this had risen to over 250. Execution was invariably in public and attended with all kinds of ritual and ceremonial. The commonest form was hanging, which often did not involve the "drop" so that the condemned felon would die a slow and agonizing death by strangulation. Even those who escaped the death penalty suffered punishment that was public and painful. Moreover in most of Europe (though not in England) torture was widely used to extract confessions.

However, this grim system was ineffective and became more so as it became harsher. All contemporaries believed that crime of all sorts was increasing, and so far as we can tell they were correct in this assumption. Moreover, looking at the records reveals several paradoxes, the most striking being that while the number of capital crimes increased, the proportion of criminals who actually were executed went down. In fact so many were acquitted or had their sentences commuted that it seems a minor miracle that anyone ever was executed. What you had was the worst of all worlds, a system both inhumane and ineffective.

This was to change largely as the result of one man and one short but brilliant book. The man was Cesare Beccaria, the Marquese de Bonesana (1738–94). He was a leading figure in the Milanese Enlightenment, and in 1764 he was persuaded by his friends Alessandro and Pietro Verri to write a book called *Dei Delitti e delle Pene* (*On Crimes and Punishments*). This was one of the first works to apply the principle that human beings respond to incentives to the brutal yet incompetent judicial systems of the time.

Beccaria argued that criminals were motivated by the balance between the possible benefits of crime and the likely costs, which were essentially those of being caught and punished. He also argued that future punishments and benefits both counted for less than those inflicted in the present or near future. (This is an early version of the economic concept of "time preference.") The problem with the system, he argued, was that for the individual criminal the chance of being caught, and if caught convicted and punished, was too low. In response punishments were made even more severe so as to maintain the deterrent. However, after a time this did not work. One reason was the slowness and sheer incompetence of the system, which meant that punishment was still uncertain and often long delayed. More serious was the way that the sympathy of jurors and judges led them to acquit those charged or to manipulate the system to find them guilty only of a lesser charge because they saw the punishment as excessive and unreasonable compared to the actual crime.

## Mild, Swift, and Predictable

Beccaria argued that punishment should be comparatively mild but also both swift, so it occurred soon after the offense, and certain and predictable rather than uncertain and arbitrary. This, he said, would produce a criminal-justice system that was more humane but also more effective because it would have a greater deterrent effect. He was particularly opposed to the death penalty and its widespread use. One separate argument he made was that it was both morally wrong and dangerous to give the state the power to kill people. His incentive-based argument was that the widespread use of execution not only did not deter but might even encourage certain crimes. The reason was, first, that for many people the prospect of their own death was hard to envisage and actually less terrible than the prospect of lifelong confinement, and second, that the public nature of the event actually cast a romantic glamour over the crime and its perpetrator, which might lead some individuals to seek it as a route to fame.

Beccaria's little book was soon translated into most European languages and had a tremendous intellectual impact. Its effect on actual policy, however, was delayed, not least because of the conservatism of the legal profession. Eventually, his arguments were accepted, and the result was a radical reform of the criminal-justice system throughout Europe. The consequence was exactly as he had predicted—the system became both more humane and more effective, with a gradual decline in both actual and recorded criminality. (There were several other reasons, but the reforms inspired by Beccaria were a major part.) By 1900 recorded crime rates in almost every part of Europe and North America were at an all-time low.

# Government in Business

BY MURRAY N. ROTHBARD

In the midst of nationwide prosperity, some economic and social problems keep nagging at the public. All over the country, they take the same form. What are they? Traffic congestion, inadequate roads, overcrowded schools, juvenile delinquency, water shortages. Such matters have proven troublesome in many ways; above all, they seem to breed conflicts. Fierce battles are raging between warring groups of Americans. Some want "progressive" education; others want varying blends of the traditional. Some want socialism taught in the schools; others favor free enterprise. Some want religion in the schools, and others proclaim separation of Church and State. Some Americans want water fluoridated, and others want it unmedicated.

Is there anything special about water or schooling that creates insoluble problems? How does it happen that there are no fierce arguments over what kind of steel or autos to produce, no battles over the kind of newspapers to print? The answer: There *is* something special—for the problems of schooling and water supply are examples of what happens when government, instead of private enterprise, operates a business.

> Have you ever heard of a private firm proposing to "solve" a shortage of the product it sells by telling people to buy less?

Have you ever heard of a private firm proposing to "solve" a shortage of the product it sells by telling people to buy less? Certainly not. Private firms welcome customers, and expand when their product is in heavy demand thus servicing and benefiting their customers as well as themselves. It is only *government* that "solves" the traffic problem on its streets by forcing trucks (or private cars or buses) off the road. According to that principle, the "ideal" solution to traffic congestion is to outlaw all vehicles! And yet, such are the suggestions one comes to expect under government management.

Is there traffic congestion? Ban all cars! Water shortage? Drink less water! Postal deficit? Cut mail deliveries to one a day! Crime in urban areas? Impose curfews! No private supplier could long stay in business if he thus reacted to the wishes of customers. But when government is the supplier, instead of being guided by what the customer wants, it directs him to do with less or do without. While the motto of private enterprise is "the customer is always right," the slogan of government is "the public be damned!"

Conflicts and bitterness are inherent in government operation. Imagine what would happen if all newspapers were published by government. First, because a government operation gets its revenues from coercive taxation instead of voluntary payment for services rendered, it is not obliged to be efficient in serving the consumer. And, second, conflicts among groups of taxpayers would rage over editorial policy, news content, and even tabloid versus regular size. "Rightists," "leftists," "middle-of-the-roaders," each forced to pay for the paper, would naturally try to govern its policy.

*The late Murray Rothbard was an economist, political philosopher, historian, and prolific author. Among his works are* Man, Economy, and State *and* The Ethics of Liberty. *This article appeared in the September 1956 issue of* The Freeman.

On the free market, in contrast, each group finances and supports its own preferred product, whether newspaper, school, or package of baby food. Socialists, free enterprisers, progressives, traditionalists, gossip-lovers, and chess-lovers, all find schools, papers, or magazines that meet their needs. Preferences are given free rein, and no one is compelled to take an unwanted product. Every political preference, every variety of taste, is satisfied. Instead of a majority or the politically powerful tyrannizing over a minority, every individual may have as much as he can afford of precisely what he wants.

The standard government reply to charges of inefficiency or shortage is to blame the public: "Taxpayers won't give us more money!" The public literally has to be forced to hand over more tax money for highways, schools, and the like. Yet, here again, the question arises: "Why doesn't private enterprise have these problems?" Why don't TV firms or steel companies have trouble finding capital for expansion? Because consumers pay for steel and television sets, and savers, as a result, can make money by investing in those businesses. Firms that successfully serve the public find it easy to obtain capital for expansion; unsuccessful, inefficient firms of course go out of business. In government, there are no profits for investors and no penalty charged against the inefficient operator. No one invests, therefore, and no one can insure that successful plants expand and unsuccessful ones disappear. These are some of the reasons why the government must raise its "capital" by literally conscripting it.

There is no way to gauge the success of a product that the customers are compelled to buy.

Many people think these problems could be solved if only "government were run like a business." And so they advocate jacking up postal charges until the Post Office is "run at a profit." Of course, the users would be taking some of the burden off the taxpayers. But there are fatal flaws in this idea of government-as-a-business. In the first place, a government service can *never* be run as a business, because the *capital* is conscripted from the taxpayer. There is no way of avoiding that. (Finance by bond issue still rests on the power of taxation to redeem the bonds.) Secondly, private enterprise gains a profit by *cutting costs* as much as it can. Government need not cut costs; it can either cut its service or simply raise prices. Government service is always a monopoly or semi-monopoly. Sometimes, as in the case of the Post Office, it is a compulsory monopoly—all competition is outlawed. If not outlawed, private competition is strangled by taxes to cover the operating deficits and raise capital for tax-exempt government operation.

## Calculational Chaos

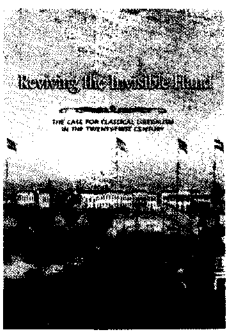
There is another critical problem in government operation of business. Private firms are models of efficiency largely because the free market establishes prices which permit them to *calculate*, which they must do in order to make profits and avoid losses. Thus, free "capitalism" tends to set prices in such a way that goods are properly allocated among all the intricate branches and areas of production that make up the modern economy. Capitalist profit-and-loss calculation makes this marvel possible—and without central planning by one agency. In fact, central planners, being deprived of accurate pricing, *could not* calculate, and so could not maintain a modern mass-production economy. In short, they could not *plan*. There is no way to gauge the success of a product that the customers are compelled to buy. And every time government enters a business, it distorts pricing a little more, and skews calculation. In short, a government business introduces a disruptive island of *calculational chaos* into the economic system.

No wonder, then, that our economic problems center in government enterprises. Government ownership breeds insoluble conflicts, inevitable inefficiency, and breakdown of living standards. Private ownership brings peace, mutual harmony, great efficiency, and notable improvements in standards of living.

# Book Reviews

**Reviving the Invisible Hand: The Case for Classical Liberalism in the Twenty-First Century**
*by Deepak Lal*
Princeton University Press • 2006 • 320 pages • $29.95

Reviewed by Richard M. Ebeling



UCLA economics professor Deepak Lal is one of the most articulate defenders of the free market and an outspoken critic of interventionist and welfare-state polices around the world.

Over 20 years ago, when central planning was still considered a panacea for economic development in third-world countries, Lal published *The Poverty of "Development Economics"* (1983), a devastating critique of collectivist ideas and policies then dominant in underdeveloped countries. More recently, in *Unintended Consequences* (1998) he traced the unique institutional changes in Medieval Europe that led the West out of poverty.

In his latest book, *Reviving the Invisible Hand,* Lal explains why the world has only one hope for a free and prosperous future—the politics of classical liberalism and the economics of a radically free market. While well trained in mainstream neoclassical economics, he rejects many aspects of the textbook equilibrium models for a more realistic conception of man and markets derived from the classical economists and more modern theorists, such as the Austrian economists F. A. Hayek and Joseph Schumpeter.

Incorporating as well insights of the Public Choice theorists, Lal demonstrates why governments should not be viewed as manned by "Platonic Guardians" only concerned with some hypothetical common good. Rather, government should be viewed as full of predators using the coercive powers of the state to plunder others.

Lal then debunks many of the theoretical and factual myths of the day. He shows that both in the nineteenth-century heyday of classical liberalism and in the post-World War II period, the freer the trade among nations, the greater the benefit for all. Nineteenth-century laissez faire brought rising living standards and more market opportunities not only for the wealthy few, but also for the poor. The result was a growing middle class. Nor did free trade and enterprise harm the poor in underdeveloped countries. The more integrated they have become with Western economies, the greater and the more rapid their climb from economic desperation.

Accusations of the increasing "income gap" between rich and poor, both within developing countries and between them and Western nations in recent years, are shown to be based on either false or misused data. Indeed, Lal explains that more people than ever are now outside any reasonable measurement of poverty.

Precisely because it is possible to end poverty, Lal turns his analytical guns against the anti-capitalist and anti-globalization groups that have infiltrated non-governmental organizations (NGOs), as well as the United Nations, the World Bank, and many other international agencies. At the core of this opposition to a free market is the environmental movement. In a brilliant tour de force Lal demolishes each of their doomsday nightmares. For example, he draws on the relevant scientific evidence to argue that there is no catastrophic global warming and no significant climate change caused by industrialization. He shows that in general the earth is far cooler than it was in the Middle Ages, when a cooling trend set in for several centuries. The swing back to a warmer climate appears to be part of the planet's natural cycles and may be highly beneficial to parts of the globe—if it actually materializes.

A central chapter turns to "morality and capitalism." Lal reminds us that anthropologists and psychologists generally agree that human nature has not changed much since the Stone Age. Man is a chooser of ends, an applier of means, and an evaluator of tradeoffs to get the most out of what he has. In addition, men have within themselves the potential for risk-taking and creativity.

It is from this latter possibility that come society's merchants, innovators, and entrepreneurs. In agrarian society, social order follows the seasons; relatively unchanging societal patterns are essential for survival and intergenerational continuity. Merchants and entrepreneurs, by their nature, are experimenters with the new—breakers of the existing order. Thus they have usually been shunned and disliked; in addition they seem to conjure up wealth out of nothing, unlike those who mix their labor with the soil or who fashion goods out of the materials of the earth.

In Europe during and after the Middle Ages, changes in economic institutions and the philosophical conceptions of man and society stimulated growth of the market economy and gave a degree of legitimacy to these men of the market and their bourgeois virtues. These changes were grounded, Lal explains, in Christian doctrines: a universal morality that focused on the individual, his autonomy, and his salvation. Other faiths, for example, Hinduism, Buddhism, and Confucian philosophy, emphasized communalism, societal hierarchy, and an exclusionary morality for the faithful. They also fostered subservience to a given order of things, with a suspicion of worldly pursuits.

The individualistic foundations of Western moral philosophy were undermined by the rise of positivism. The Victorian era attempted to balance scientific insight and faith-based values and moral conduct. But these values were eaten away in the late nineteenth and twentieth centuries until, Lal argues, there was no shared foundation for moral conduct other than "anything goes" as long as it makes you feel good and doesn't seem to be too harmful toward others.

Lal says that much of the resistance to globalization in other parts of the world has little to do with rejection of market-based institutions. Rather, people fear that with those institutions must come the perceived amoral and immoral "lifestyles" of the West. Lal responds that acceptance of market-based institutions does not require the adoption of Western "permissive" culture.

Thus we in the West should be more interested in seeing others adopt free markets and less concerned with whether they accept Western "values." Attempting to impose such values may only have the perverse effect of causing other people to reject capitalism.

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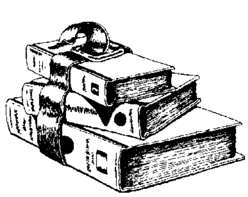
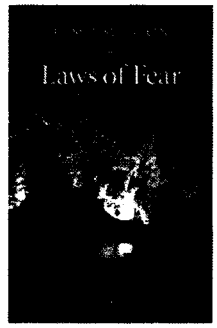


## Laws of Fear

*by Cass Sunstein*

Cambridge University Press • 2005 • 234 pages • $65.00 hardcover; $23.99 paperback

Reviewed by Donald J. Boudreaux




Cass Sunstein is much like his University of Chicago Law School colleague Richard Epstein. Both publish articles and books at a breathtaking pace. Both use economics lavishly. Each would be the smartest person in any group of 10,000 randomly chosen people. Both are academic superstars.

But while Epstein sees the world through the lens of a classical liberal, Sunstein wears the lens of modern American liberal—or a "progressive," as such well-meaning champions of vigorous government regulation and heavy taxation are (misleadingly) called.

Unlike many "progressives," however, Sunstein brings genuine intellectual firepower to the debate. His arguments, in this book and elsewhere, are serious and challenging. And while I often disagree with him, I must say that 90 percent or more of this book is spot-on correct.

He opens *Laws of Fear* with a devastating attack on the so-called "precautionary principle." This "principle" advises that we steer clear of actions that might generate substantial harm even if we don't know what this harm might be and its chances of occurring. If it's *possible* that action X will cause some great harm, the precautionary principle demands that the action be avoided.

Environmentalists love that principle because it rationalizes almost any piece of restrictive regulation—or so they think. Because, for example, drilling on the Arctic National Wildlife Reserve might unleash a series of events that doom all of the flora and fauna of the northern wilderness, that's sufficient reason to prevent drilling even if the chances of this outcome are tiny.

Sunstein points out, however, that "the Precautionary Principle is literally incoherent, and for one reason: There are risks on all sides of social situations. It is therefore paralyzing; it forbids the very steps that it requires."

Indeed so. A proponent of ANWR drilling can turn the precautionary principle's logic around by pointing out that there's a chance, however small, that *failure* to drill on ANWR might lead to catastrophe.

No matter how loudly it's done, no such illogical posturing for (and against) regulation can substitute for sound cost-benefit analysis. A regulation cannot be justified on the possibility that some extreme scenario may materialize. Instead, sound estimates of the probabilities of various outcomes, along with estimates of the costs and benefits of those outcomes, are the intelligent way to determine what actions are appropriate.

Sunstein is correct about this, and he makes a strong case that "assignment of monetary values to risks is far more plausible and intuitive than it might seem." I agree completely—if government is going to regulate, it should do so on cost-benefit grounds.

But how wide are those grounds? In my opinion, nowhere near as wide as Sunstein believes them to be. First, as Elinor Ostrom's research shows, people are surprisingly creative at arranging their affairs voluntarily to solve many problems of a kind that too many of us simply assume can be solved only by government. When the robustness of private arrangements is overlooked (as Sunstein tends to do), the benefits of government regulation are overestimated.

Second, people tend to abuse power. Although Sunstein sometimes seems aware of Public Choice concerns, too often he writes as if they are either nonexistent or exaggerated. When the dangers of government-power abuse are overlooked, the costs of government regulation are underestimated.

So in my view, the soundest cost-benefit analysis counsels against almost all government regulations and in favor of reliance on the law of property, contract, and tort. Put another way, cost-benefit analysis counsels in favor of laissez faire.

Sunstein would disagree, for two reasons. First, he overestimates the benefits and underestimates the costs of regulation. Second, and more interesting, Sunstein is a legal positivist—he believes that all law is created by government. From this belief it's a short step (which Sunstein seems to take) to the conclusion that all law is consciously chosen.

This isn't the place to challenge legal positivism. I mention it only because it is the largest flaw in all of Sunstein's work.

Still, *Laws of Fear* is a solid work, informed by sound economic understanding—including many useful applications of behavioral economics. I recommend it to readers of *The Freeman* with more enthusiasm than I expected I would have.

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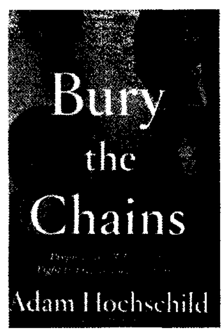
## Bury the Chains: Prophets and Rebels in the Fight to Free an Empire's Slaves

*by Adam Hochschild*

Houghton Mifflin Company/Mariner Books • 2005/2006 • 468 pages • $26.95 hardcover; $16.00 paperback

Reviewed by Becky Akers




Does anyone today think slavery a good thing? Probably only politicians and bureaucrats would defend some men's lording it over others, living off their labor, and ordering them about; everyone else grasps the inherent immorality. This renders modern screeds against slavery not only needless but sanctimonious. Perhaps that's why *Bury the Chains*, an otherwise fascinating account of the anti-slavery movement in late eighteenth- and early nineteenth-century Britain, ultimately annoys: the author's piety seeps from its pages.

Adam Hochschild is a journalist who writes for the *New York Times Magazine* and *Mother Jones,* which he co-founded. That explains his piety. It may even explain his inability to place himself in the age he surveys, which he resolutely judges by modern standards and finds wanting. For starters, he sees democracy as Leviathan's worthiest guise; that eighteenth-century Britons (and Americans) disdained democracy as mob-rule earns his censure, however excellent their reasons against it. Not that Hochschild considers or even seems aware of those reasons. Instead, he assumes that a universal British franchise would have demolished the slave trade years before Parliament did and that the lack of said franchise is almost as tragic as slavery itself.

Likewise his attitude toward Christianity. However it may disconcert modern agnostics, Quakers and devout, Bible-believing Christians led the fight against slavery. Hochschild seldom tries to understand their convictions or ideas and how those inspired their actions. Rather, he condemns them for "hypocrisy" and for not going far enough in their endeavors; that is, for not behaving as modern socialists would. The famous hymn writer John Newton is Hochschild's most egregious victim. Newton briefly captained slave ships after his conversion to Christianity, and while God may have forgiven him, Hochschild certainly hasn't. He repeatedly ridicules Newton for obsessing over his relationship with the Almighty instead of the abolition of slavery.

Those flaws aside, *Bury the Chains* is a riveting read. It will resonate with anyone who hates the state because of the parallels between slavery and statism, anti-slavers and anti-statists. Like us, the anti-slavers confronted a pervasive, unquestioned, and even beloved system. Hochschild emphasizes that slavery reigned everywhere when the activists began their campaign, with most of the world's contemporary and historical peoples held in bondage of one kind or another. And like statism today, slavery was dismissed as inevitable and natural.

Those anti-slavery crackpots who bothered themselves about the justification for such an obviously wicked scheme found that they bore a staggering burden of proof, as do we who oppose Leviathan. Most people then were as willing to excuse slavery's horrors as people today excuse the state's. Perhaps this was because slavery, like the state, offered a road to riches; those directly involved in the slave trade could reap enormous wealth, as can modern politicians and their cronies. A host of others, indirectly connected, found their fortunes tied to slavery's success, even as corporations that manufacture war materiel, prison and school supplies, and the rest, depend on the state for their profits.

The similarities end, however, when we come to the anti-slavers' rate of progress and eventual victory. It took them only 20 years to proscribe the African slave trade and another 30 years to outlaw nongovernment ownership of one human by another.

Hochschild's subject is dramatic by its nature, and his novelistic style enhances it. He often departs from his story to introduce us to such characters as William Wilberforce, the emaciated member of Parliament whose zeal against slavery almost literally consumed him, and Granville Sharp, remarkable alike for his music and his hatred of slavery. Sharp lived with his seven musical siblings aboard a barge that was towed along the Thames and other waterways while they performed; Handel's *Water Music* comes by its name honestly.

Equally intriguing are Hochschild's explanations of the customs and technology of a vanished world. We learn that the slops bucket in a printer's shop was used to clean the type because the ammonia in urine dissolves ink, and that female slaves performed the back-breaking field work of cultivating sugar cane since more valuable males were saved for skilled labor. We read about Toussaint L'Overture, a national hero in Haiti because he led a rebellion among the slaves. Tragically, Toussaint became as big a tyrant as the masters and overseers he deposed. No man, black or white, slave or free, seems able to withstand the toxin of political power.

Because *Bury the Chains* narrates an obscure chapter in the struggle for freedom, it ought to cheer all who love liberty. It's too bad, then, that its sanctimony and politically correct subtleties overshadow the joy. *Bury the Chains* greatly exasperates while it educates.

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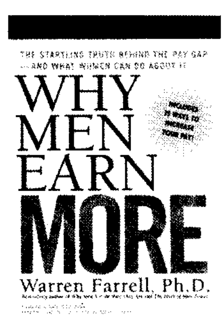
## Why Men Earn More

*by Warren Farrell*
AMACOM • 2005 • 233 pages • $23.00

Reviewed by George C. Leef




Warren Farrell's *Why Men Earn More* is a businessman's explanation for an economic phenomenon that gets many people up in arms. The book won't be popular among the purveyors of the notion that the so-called gender earnings gap is due to a defect in the economy because Farrell gives no credence to that idea, so popular among feminist scholars. Farrell provides the reader a dispassionate—and often amusing—look at the differences between men and women in the market and shows that there are perfectly rational explanations for the fact that men who are fulltime labor-force participants on the average have higher earnings than women. In sum, the book is a crushing refutation to the contention that capitalism is inherently unfair to women and that government must promote "gender justice."

This is not unexplored terrain, of course. There have been academic studies on the differences between men and women in the labor market for decades. What Farrell does so well is to package that information, mixed generously with his own observations and experiences, to create a highly readable, nontechnical analysis that should persuade all but the most die-hard exploitation theorist that the attacks on capitalism are unwarranted.

Farrell's big point is that men tend to make decisions about employment—including such key factors as hours per week, risk, and the possibility of mandatory relocation—that lead to higher pay, but entail offsetting difficulties. Women, conversely, tend to make choices that lead to lower compensation, but with offsetting advantages. Accordingly, there are ways for individual women to increase their earnings, but they require individual action, not government intervention.

Speaking of government intervention, Farrell easily disposes of the feminists' pet solution to the earnings gap, namely "comparable worth" legislation. Here is his discussion: "The problem with comparable worth is that it creates higher pay for higher fulfillment positions that everyone wants and lower pay for lower fulfillment positions that are hard to fill unless we pay more. Thus, it leaves us with few people to build highways, bridges, or homes; pick up garbage, clean sewers, mine coal; or do most any job that employs almost all men. Why? Test this out yourself. Imagine that for a month you have neither had your garbage picked up nor an opportunity to read about new anthropological discoveries. Which would you pay more money to remedy?"

That's the way the whole book is: sharp, clear, relentlessly logical.

The willingness to accept risk is one of the main reasons men on average earn more. To get people to take jobs where there is a danger of injury, employers have to offer higher pay. Biology seems to have hard-wired men to be more willing to want to make that tradeoff than women. Jobs in mining, fishing, forestry, and more are overwhelmingly male despite governmental antidiscrimination rules. Farrell cites the chilling work on an Alaskan floating cannery to help make his point. Very few people will work under those conditions, hardly any of them female.

My favorite pages occur near the end of the book when Farrell turns to policy questions. He argues against the affirmative-action crusade for greater equality in the numbers of men and women in occupations where men have historically been dominant. His reason is that it's anticompetitive: "Affirmative action effectively adds a tax to domestic labor that makes it more difficult to compete with foreign labor. . . . Whenever the government requires companies to pay workers more than the market would bear, to pay for long vacations and extraordinary health benefits, the unemployment rate soars and the country risks the political rebellion, now happening in countries like France, Germany, and Sweden."

Quite right, and the reader may notice that Farrell has given a sound argument for abolishing *all* labor-market interference.

While Farrell does an excellent job of showing that women can do better in today's labor market without statist interventions, the book would have been stronger if he had paid some attention to the ways in which the status quo is biased against workers in general. Specifically, our economy is constricted at many points with laws and regulations that make it difficult for newcomers to enter the market and compete. Women entrepreneurs could find many new opportunities for profitable businesses if we had a truly free market that didn't protect existing businesses (mostly owned by men) against competition.

*Why Men Earn More* is a potent antidote to the victimhood of the women's movement. Women (and men) who read it will learn much about the way business decisions are made and will come away with a strong sense that the spontaneous order of the free market works in the best interests of all.

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# We Need Multimedia Economics Teaching

**BY RUSSELL ROBERTS**

Earlier this year I was invited to give a talk at an art gallery in Georgetown, the posh area of Washington, D.C., down the street from the White House, abutting the Potomac River. I confess this doesn't happen to me very often. Okay, I exaggerate—it never happens to me. This was my first invitation ever to speak at an art gallery.

The occasion was an evening of entertainment sponsored by the Institute for Humane Studies (IHS). IHS was trying out a new approach to communicating the virtues of liberty and free markets. It had rented the gallery for the night and put on display work by Morgan Ashcom, a fine-arts major at George Mason University who is interested in liberty and economics. Morgan spoke briefly about how he had become interested in economics (he credited a phenomenal GMU teacher—Tom Rustici) and described the work that was hanging nearby—a set of photographs surrounded by notes from classic works on liberty (quotes from Hayek, Friedman, Sowell, and others), along with a sculpture and a short film that both captured the power of liberty and the threat of totalitarian oppression.

> The real lesson I took away from the evening is how hard it is get people to understand economics. We have lots to do, and we need more people who work outside the printed page, our time-honored medium for explaining how markets operate and the virtues of freedom.

Morgan was followed by Ben Parizek, who sang folk songs he had written about the virtues of spontaneous order and the lack of virtue to be found in the life of Che Guevara. Both Morgan and Ben were very inspiring. I closed the evening with a reading from the book I'm currently working on.

The event was marred and enhanced at the same time by an unscheduled speaker. After Morgan had finished describing what he was trying to achieve in his art, he asked if anyone had any questions.

A man in the back of the room raised his hand and was recognized. Rather than ask a question, he proceeded to make a speech. He opened by making a few brief remarks about Morgan's dedication and persistence in making sure the works were presented the way he intended them to be seen. It turns out he was the owner of the gallery. He explained how he and Morgan had spent hours hanging the photographs to make them look appealing.

Having expressed his respect for Morgan, he launched into what can only be described as a diatribe against the ideas that Morgan was trying to portray, particularly concerning capitalism and the way it treats the poor. He wanted us to know that the quotes surrounding the photographs were dangerous—they might lead people to think that capitalism was a good thing. It wasn't, he explained. Americans, especially the poor, were oppressed by corporations and capitalism. Besides, he added, America wasn't a capitalist country anyway. He also wanted the assembled people to know that capitalism required unemployment of at least 6 percent (I think that was the number he chose) at least until Bill Clinton showed how it could actually be less than 4 percent.

It was a fascinating and awkward moment. Most if not all the people in the audience were passionate

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believers in free markets. How would they respond? Would they shout the man down? Angrily denounce his comments with their own diatribes? Politely disagree and marshal the case against the views he had outlined?

We did nothing. We said nothing. I quietly ignored the counterarguments and facts that leaped into my mind. Others must have done the same thing. The organizer of the event thanked the owner for his comments and went on to the next raised hand. It was as if the interruption hadn't happened at all. I suspect that the decision by each of us individually to refrain from responding was a combination of politeness and pragmatism. There was no need to voice a defense of capitalism—those arguments spoke loudly through the words and pictures that Morgan had so artfully combined.

For me the episode was also a reminder of how far we have to go in clearly explaining economics and claiming the moral high ground for liberty. Here was a guy who had spent a lot of time with this talented and thoughtful student. And yet he viewed his artwork as dangerous. Here were these photographs surrounded by the words of Hayek, Friedman, and Sowell, and they had no impact on opening his mind to an alternative world-view.

In a way it was the ultimate compliment to the artist. The owner of the gallery viewed the art as being sufficiently provocative that it had to be denounced. I was also reminded of the graduate students in social work I had once taught who also believed that capitalism needed a reserve army of unemployed to function—a strange view that misunderstands how unemployment is defined and measured in government statistics. Theirs was a Marxist interpretation that presumed that everyone who was measured as unemployed was desperately out of work for a long period of time. In fact, zero unemployment is essentially impossible the way government defines it—anyone who is looking for a job and doesn't find one immediately is defined as unemployed.

Interestingly, we all shared one point of complete agreement—that America was not a true capitalist society. The disagreement was over where to go from here—toward more freedom or away from it.

## Lots to Do

But the real lesson I took away from the evening is how hard it is get people to understand economics. We have lots to do, and we need more Morgan Ashcoms and Ben Parizeks, people who work outside the printed page, our time-honored medium for explaining how markets operate and the virtues of freedom. Books and articles and words are wonderful, and we need more of them. But they do not speak to everyone. To reach a wider audience, we need more art exhibits, more folk songs, more rock songs, more operas, and a lot more movies. Maybe if that gallery owner knew a few more Morgan Ashcoms and listened to a few more Ben Parizeks, he might be able to imagine that at least those of us who long for an America with more economic freedom are not monsters to be denounced.

This is my last column as a regular columnist for *The Freeman*. I've been doing this for seven years, and it's time for me to move on to other things and to give someone else a chance to put this space to good use. I've enjoyed talking with you, the readers of *The Freeman*, and hope you'll stay in touch. And I'm grateful to both Beth Hoffman and Sheldon Richman for wonderful editing over the years, and to Don Boudreaux, who got me involved in the first place.