IDEAS ON LIBERTY

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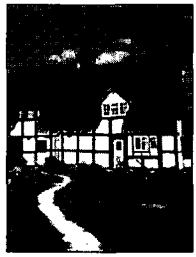
FEATURES

Bill Gates



COLUMNS

DEPARTMENTS

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IDEAS ON LIBERTY

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Cover photo of young Irish musicians playing for tourists by Galen R. Frysinger

PERSPECTIVE

Redundancy

Private property is again getting the attention it deserves, thanks to two recent books. Tom Bethell's *The Noblest Triumph* and Richard Pipes's *Property and Freedom* won't be the last words on the subject, nor should they be. The subject is too important.

The centrality of property to a free and prosperous society cannot be overstated. It's therefore also at the center of the *case* for a free society. Full freedom cannot exist without property or with attenuated property. Every dictator has known this and so has denounced private property as antisocial. The identity between property and liberty is something that today's seekers of the "third way" refuse to recognize.

The more one examines the term "private property" the more one finds packed into it. It's been noted that the ideas of limiting government power and the rule of law necessarily follow from the concept. So do the other trademarks of classical liberalism. It says it all. The rest is elaboration.

In fact, the term is twice as long as necessary. "*Private* property" is redundant; "*public* property" is a contradiction in terms. The public is an abstraction not an entity. It cannot own. "People are ill served by the manufacture of spurious entities," wrote James Sadowsky in his classic essay "Private Property and Collective Ownership." (Beware the term "environment"; it is laden with collectivism.)

If it's not private, it's not property. And if it's called "public property" but is under the control of discrete individuals, as it must be, then it is de facto private, albeit illicitly acquired property. Maybe this is why the qualifier "private" was thought superfluous by so many of the early liberals.

Property is not just a device economists posit to assure efficiency. It is liberty in concrete form.

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In January the Economic Policy Institute and Center on Budget and Policy Priorities issued the latest in the regular stream of jeremiads about wealth inequality in the United States. For the authors, the state-by-state report of the widening gap between the top and bottom earners is, ipso facto, evidence of injustice. In response, we reprint a classic essay from Ludwig von Mises. This one is definitely worth reading again.

Fans of paternalistic government have a simple answer for those who think the Second Amendment, which identifies and protects the natural right to keep and bear arms, is necessary in the modern world: dial 911. Richard Stevens explains why legally and practically the right to keep and bear telephones can't hold a candle to the Founding Fathers' handiwork.

Ludwig von Mises defeated socialism intellectually by arguing that since the planners can't calculate, they can't plan. After having shown that free markets and entrepreneurship are necessary in an open-ended world rife with error, Israel Kirzner extends Mises's argument to lesser forms of intervention.

Even some friends of free enterprise think they see a good side to an eventual breakup of Microsoft as a result of the government's antitrust case. D. T. Armentano reviews a similar case from the annals of antitrust and comes to a radically different conclusion.

The judge in the Microsoft case set out a detailed set of findings as a prelude to the penalty phase. Scrutinizing the findings, William Shughart has trouble finding anything worthwhile.

When students brought up in the theology of state-worship encounter heresy in the form of a good college course in economics, the results can be interesting and exasperating. Paul Cleveland has the details.

As the horizon of a new century approaches, are we on the threshold of a big leap in economic freedom and living standards? Christopher Lingle surveys the world and likes much of what he sees.

Politicians like power and dislike giving it up. Where then lies the hope for liberty? A trip to Ireland taught James Payne a good lesson in political theory.

The population-control lobby carries on, undeterred by all empirical indications that they are wrong to believe that our growing numbers endanger mankind. Jim Peron shows that the lobby's own program would bring the very catastrophe they claim to want to avert.

Christopher Mayer points out that if flexibility in the face of an uncertain future is a virtue, then free trade is certainly no vice.

As for this month's columnists: Donald Boudreaux takes a trip around the world without ever leaving New York. Lawrence Reed says that government will only disrupt the Internet if it tries to guarantee access. Doug Bandow counsels that we should keep our eyes on taxes, not the national debt. Dwight Lee writes that there is no substitute for a commitment to liberty if we want to check government power. Mark Skousen identifies a major reason why prognosticators are so often wrong. Walter Williams is wary about government action in the name of preventing harm. And Joseph Salerno, reading William Safire's plea for vigorous antitrust prosecution, declares, "It Just Ain't So!"

Our book reviewers look over volumes on "equal opportunity," allegedly amateur sports, sexual equality, Hayek versus Keynes, and multiculturalism in the classroom.

—SHELDON RICHMAN

Thoughts on Freedom

by Donald J. Boudreaux

Trade

American Culture

Among free trade's most vocal opponents are those who insist that American culture is hegemonic—that without protectionism, people around the world will mindlessly adopt bland, boring, and monochrome American culture.

Put aside the breathtaking arrogance of those who yearn to use the state to prevent people from spending money in ways that elites think are gauche. Instead, consider the very idea that there is an American culture. It is far more accurate to say that there is a world culture formed in America. In other words, what is called "the American culture" is the ever-evolving amalgam of influences from around the world.

To demonstrate, let me share with you some notes on an ordinary day in the life of my wife, Karol, our 2-year-old son, Thomas, and me. I use boldface type to identify just some of the products, people, and ideas that, on this normal day, affect us from outside of the United States.

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On awakening to **Beatles music** blaring from my **Sony clock-radio**, I shamble to the kitchen to brew **Guatemalan coffee** in our trusty **Krups auto-drip coffee maker**. It's then off to the shower where I lather up with **soap milled in France**. Following the shower, I put in my **soft contact lenses** (the invention of a **Czech scientist**), shave with my **Braun electric razor**, and splash on some **French cologne**.

I then dress Thomas and myself. Following our breakfasts, I succumb to Thomas's plea that he be allowed to watch his favorite video: **Thomas the Tank Engine**, a character as British as Buckingham Palace. We then drive to the babysitter's home in our **Nissan**. I pop in a **CD** (invented by the **Dutch company Phillips**) to enjoy the original and best-selling **Three Tenors** recording— made, by a **British company**, in **Rome** of selections from **Italian, German, English**, and American **operas**, sung by a **Catalán**, a **Spaniard**, and an **Italian**. The tenors are backed by an orchestra conducted by an **Indian**.

After dropping Thomas off, I stop at the bagel store owned and operated by **Hondurans**. In addition to a **bagel,** I buy another cup of coffee, this time a **cappuccino** made with **coffee grown in Ethiopia**.

At my office I begin my workday by booting up my **Sony computer.** Among my tasks this particular morning is to find someone to translate from French into English **Frederic Bastiat's collected correspondence**. Later that morning, while writing a talk, I consult books by the **Austrian F. A. Hayek**, the **Scotsman Adam Smith**, the **African George Ayittey**, the **Hungarian Michael Polanyi**, the **Italian Bruno Leoni**, the **Swede Eli Heckscher**, the **Canadian David Henderson**, and the **South African born in Britain of Lithuanian parents, Israel Kirzner**.

All this work makes me hungry, so for lunch I wolf down some **moo goo gai pan**.

Donald Boudreaux is president of FEE.

Karol and I then spend a fascinating afternoon playing hosts to visitors from **Argentina** and **Ecuador**. We introduce our guests to FEE's interns, one a **Bulgarian**, another a **Mexican**, and the third a **Sri Lankan**.

That evening, Karol, Thomas, and I dine at a popular nearby **Indian restaurant**. (Thomas, incidentally, is crazy about **papadam**.) After leaving the restaurant I stop to fuel our car at the local **Shell (as in Royal *Dutch* Shell) gasoline station**. On our return home, we bathe Thomas, dress him in his pajamas decorated with images of Britain's enormously popular **Teletubbies**, and then read to him some of the delightful children's stories penned by **Beatrix Potter, an Englishwoman**.

With the little one fast asleep, it's time to relax. While I put on some Stan Getz and **João Gilberto bossa nova music from Brazil**—played on our **Japanese-made CD player**—Karol pours each of us a glass of **Chilean wine**. Life is good . . . but our days are tiring, so we soon go to bed. Before turning out the lights, though, we each read for a few minutes—me, an article by the **Australian economist Geoffrey Brennan**, and Karol some pages from the autobiography of the **Russian novelist Vladimir Nabakov**.

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What's going on here? We Boudreauxs aren't an unusual American family (although Thomas has yet to be swept up in the nationwide mania for the **Japanese Pokémon characters**). Yet a review of an ordinary day in our lives reveals that all three of us—from the moment we awaken until we fall asleep—continually enjoy comforts, conveniences, culture, knowledge, and entertainment created by people from around the world.

The answer is that America's culture is in fact a world culture. It's a delicious gumbo of global influences. And it's also dynamic. The same openness and freedom in America that attract people, products, and ideas from across the globe also ensure that tomorrow's gumbo will differ slightly from today's gumbo. A new insight or inspiration from a Korean, an Indian, a Portuguese—no less and no more than a new insight or inspiration from a Californian, a Minnesotan, a Virginian—will further improve the mix. And consumers worldwide will each have a meaningful say in deciding whether or not that new insight or inspiration is worthwhile. (No Peruvian or Algerian is compelled to eat at McDonald's or to read Tom Clancy any more than any Pennsylvanian or Alaskan is compelled to eat at a Mexican restaurant or to read Milan Kundera.)

Is it senseless, then, to label the cultural milieu in bloom from Maine to Hawaii as "American"? Not quite. While in one sense this culture is truly global and resists a nationalist label, in another sense it is indeed uniquely American. But it is uniquely American precisely in a way that reveals the distorted perspective of those who fret about American cultural hegemony. What justifies labeling this culture "American" is that America contributes the essential openness and freedom for millions of people from hundreds of nations to add their inspirations to it—both as its producers and as its consumers. America's culture is unique because, in its details, it is not principally an American culture! Truly, it is a world culture.

Recognizing that American culture is not a homogeneous glob of fast-food-eating, blue-jeans-wearing Ally McBeal addicts will not calm the fears of the world's cultural snobs. Indeed, these self-appointed elites are frightened by American culture precisely because it is so vibrant and variegated—and, hence, attractive to millions of ordinary people. Elites do not and cannot control it; it has stripped them of their exalted status. Finally extinguishing the power of elites to control the lives of ordinary people might well turn out to be America's great contribution to the 21st century. □

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APRIL 2000

Antitrust Protects Competition?

It Just Ain't So!

Conservative William Safire's column "The Curse of Bigness" (*New York Times,* December 13, 1999) is dedicated to "exploding myths" allegedly spread by MCI, WorldCom, Sprint, and other large firms seeking government approval for prospective mergers that will serve to magnify their market power. Safire opens innocuously enough with the comfortable platitude that "Competition is the driving force of free enterprise." It becomes almost instantly clear, however, that he misconstrues the real meaning and role of competition, for in the very next sentence he warns that "Concentrated power is the greatest danger to capitalism."

Evidently Safire follows Karl Marx in believing that an unregulated market economy is fundamentally prone to increasing concentration of industry in the hands of a few gigantic firms. If "the rising momentum toward concentration throughout American big business" is left unchecked, it may well culminate in "two oil companies, two telecommunications combines and two bank-brokerage-insurance leviathans." These "superpowers" will then find it "infinitely easier" to "fix prices or squelch innovation." No thoroughgoing Marxist, Safire admonishes us that "what we do not want" is a return to "regulation, with government as the cartel-keeper."

So who, then, is to save us from this merger mania and guide our economy safely between the Scylla of private monopoly and the Charybdis of government cartels? Why the vigilant "government watchdogs" of the Federal Trade Commission and the Justice Department, of course. To assist these gallant protectors, Safire seeks to demolish several recent "anti-antitrust" myths that have been contrived to muzzle them.

Unfortunately, Safire's attempt to expunge those alleged myths is itself an exercise in mythmaking based on the discredited dogmas of yesteryear. At its root, Safire's case for antitrust is fallacious because it invokes an unrealistic and irrelevant notion of competition based on the number of firms producing and selling an identical good or service. Before criticizing the specific objections Safire raises to the argument against antitrust, a few words on the true nature and role of competition are in order.

To begin with, the size and number of firms in a particular industry are not the essence of competition but merely an outcome of it. The essence of competition is the rivalry among entrepreneurs who seek to earn profits and avoid losses by producing at the lowest possible cost those goods most urgently demanded by consumers. However, since production takes time, and because consumer tastes, technological knowledge, and the quantities and qualities of available resources are constantly changing, each entrepreneur must continually forecast and attempt to adapt production to uncertain future market conditions. On the basis of these forecasts, the entrepreneur invests his capital in the purchase of resources—various kinds of labor, natural resources, and capital goods—and transforms them into consumer goods. He does this because he anticipates that the selling price of the output will exceed the sum of the prices he paid for the inputs including interest on his invested capital. The entrepreneur earns a profit if he is correct in his expectation. If his forecast is mistaken, he suffers a loss.

What is important to understand is that the success or failure of every entrepreneur's quest for profit is determined solely and completely by consumers at the moment when, confronted by the array of competing products, they choose which and which not to purchase. In their eagerness to acquire the goods they desire most at the lowest possible prices, consumers do not care one whit about the size of producers and their record of past success. A giant established firm is no less likely than a small upstart firm to suffer losses if it supplies a good that most consumers consider inferior to similar products or whose costs of production turn out to surpass its selling price because of inefficient production techniques. The competitive process determines precisely the optimum size as well as the number of firms producing any given product. It does so by exerting unrelenting pressure on entrepreneurs, in the form of prospective profit and loss, to continually seek out the lowest-cost techniques for combining and transforming scarce resources.

The irresistible power of the competitive market process to revolutionize the structure of long-established industries at a moment's notice is manifested time and again in U.S. business history. The steel, bookselling, and computer industries are three recent, dramatic examples.

In sum, competition, correctly understood, is a hardy and inexorable process that needs no antitrust watchdog to protect it from the "curse of bigness." Antitrust policy can only stifle and distort the real-world competitive process.

We can now briefly address some of Safire's rebuttals of "myths" disseminated by the opponents of antitrust. One such "myth" is that "Technology is changing so fast that a little pipsqueak company can bring a giant to its knees." According to Safire, however, "every time that happens, a thousand small cap operations are driven out of business or absorbed by the giant out to cover its posterior." This statement, while true, misses the point.

Giants like IBM and U.S. Steel were indeed brought to their knees by competition from small companies that were the first to recognize the commercial potential of a new technology. In probably many more instances, superior entrepreneurial forecasting and the economic efficiency of large firms have driven small firms from the field. So what? The competitive process operates to produce a size of firm that tends to ensure the lowest costs of production.

Some 299 other automobile firms competed with Ford Motor Co. in 1910, most of which were driven out of business after Henry Ford pioneered the moving assembly line, which rendered the mass production of autos commercially viable. But it was not Ford's market power that did these competitors in. It was the consumers who chose to ignore the products of these tiny garage-shop operations and purchase the Model T in great quantities, because the economies of scale from mass production permitted Ford to more than halve the price between 1910 and 1914 from $780 to $360. Yet despite its tremendous success, when consumers tired of the clunky old black Model T with its old-fashioned mechanical brakes in the 1920s, an upstart company, General Motors, jumped into the competitive fray. By 1927, the competition from GM's colorful and modern Chevrolet forced Ford to shut down and retool. The market determined that one rival provided more effective competition for Ford than hundreds had previously.

A related "myth" that Safire seeks to debunk is that "Mere size is no sin; each case should be handled on its own merits." According to Safire, even if it is true that some large firms are sinless, "it is the momentum of merger mania that cries out to be reversed." To the contrary, any firm that has attained dominance in the market not only has committed no sin against competition but has been immaculately conceived, so to speak, within the competitive process itself. Furthermore, competition itself reverses so-called "merger mania" when it is ascertained via the profit test that its results no longer conduce to optimum consumer satisfaction. Or has Safire forgotten the "down-sizing" phenomenon of the 1990s that undid many of the conglomerate mergers of the 1980s?

—JOSEPH T. SALERNO
Pace University

IDEAS ON LIBERTY
APRIL 2000

Inequality of Wealth and Incomes

by Ludwig von Mises

The market economy—capitalism—is based on private ownership of the material means of production and private entrepreneurship. The consumers, by their buying or abstention from buying, ultimately determine what should be produced and in what quantity and quality. They render profitable the affairs of those businessmen who best comply with their wishes and unprofitable the affairs of those who do not produce what they are asking for most urgently. Profits convey control of the factors of production into the hands of those who are employing them for the best possible satisfaction of the most urgent needs of the consumers, and losses withdraw them from the control of the inefficient businessmen. In a market economy not sabotaged by the government the owners of property are mandataries of the consumers as it were. On the market a daily repeated plebiscite determines who should own what and how much. It is the consumers who make some people rich and other people penniless.

Inequality of wealth and incomes is an essential feature of the market economy. It is the implement that makes the consumers supreme in giving them the power to force all those engaged in production to comply with their orders. It forces all those engaged in production to the utmost exertion in the service of the consumers. It makes competition work. He who best serves the consumers profits most and accumulates riches.

In a society of the type that Adam Ferguson, Saint-Simon, and Herbert Spencer called militaristic and present-day Americans call feudal, private property of land was the fruit of violent usurpation or of donations on the part of the conquering warlord. Some people owned more, some less, and some nothing because the chieftain had determined it that way. In such a society it was correct to assert that the abundance of the great landowners was the corollary of the indigence of the landless.

But it is different in a market economy. Bigness in business does not impair, but improves the conditions of the rest of the people. The millionaires are acquiring their fortunes in supplying the many with articles that were previously beyond their reach. If laws had prevented them from getting rich, the average American household would have to forgo many of the gadgets and facilities that are today its normal equipment. This country enjoys the highest standard of living ever known in history because for several generations no attempts were made toward "equalization" and "redistribution." Inequality of wealth and incomes is the cause of the masses' well-being, not the cause of anybody's dis-

Editor's Note: Last January the Economic Policy Institute and the Center on Budget and Policy Priorities released a study decrying the growing income inequality in America and calling on government to rectify this alleged injustice. "The economic prosperity of the 1990s has not been shared equally," wrote the authors. There is no better response than what Ludwig von Mises (1881–1973), the great economist of the Austrian school, wrote in Ideas on Liberty *in May 1955.*

tress. Where there is a "lower degree of inequality," there is necessarily a lower standard of living of the masses.

Demand for "Distribution"

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.

When Marx and Engels in the *Communist Manifesto* recommended "a heavy progressive or graduated income tax" and "abolition of all right of inheritance" as measures "to wrest, by degrees, all capital from the bourgeoisie," they were consistent from the point of view of the ultimate end they were aiming at, viz., the substitution of socialism for the market economy. They were fully aware of the inevitable consequences of these policies. They openly declared that these measures are "economically untenable" and that they advocated them only because "they necessitate further inroads" upon the capitalist social order and are "unavoidable as a means of entirely revolutionizing the mode of production," i.e., as a means of bringing about socialism.

But it is quite a different thing when these measures which Marx and Engels characterized as "economically untenable" are recommended by people who pretend that they want to preserve the market economy and economic freedom. These self-styled middle-of-the-road politicians are either hypocrites who want to bring about socialism by deceiving the people about their real intentions, or they are ignoramuses who do not know what they are talking about. For progressive taxes upon incomes and upon estates are incompatible with the preservation of the market economy.

The middle-of-the-road man argues this way: "There is no reason why a businessman should slacken in the best conduct of his affairs only because he knows that his profits will not enrich him but will benefit all people. Even if he is not an altruist who does not care for lucre and who unselfishly toils for the common weal, he will have no motive to prefer a less efficient performance of his activities to a more efficient. It is not true that the only incentive that impels the great captains of industry is acquisitiveness. They are no less driven by the ambition to bring their products to perfection."

Supremacy of the Consumers

This argumentation entirely misses the point. What matters is not the behavior of the entrepreneurs but the supremacy of the consumers. We may take it for granted that the businessmen will be eager to serve the consumers to the best of their abilities even if they themselves do not derive any advantage from their zeal and application. They will accomplish what according to their opinion best serves the consumers. But then it will no longer be the consumers that determine what they get. They will have to take what the businessmen believe is best for them. The entrepreneurs, not the consumers, will then be supreme. The consumers will no longer have the power to entrust control of production to those businessmen whose products they like most and to relegate those whose products they appreciate less to a more modest position in the system.

If the present American laws concerning

the taxation of the profits of corporations, the incomes of individuals and inheritances had been introduced about sixty years ago, all those new products whose consumption has raised the standard of living of the "common man" would either not be produced at all or only in small quantities for the benefit of a minority. The Ford enterprises would not exist if Henry Ford's profits had been taxed away as soon as they came into being. The business structure of 1895 would have been preserved. The accumulation of new capital would have ceased or at least slowed down considerably. The expansion of production would lag behind the increase of population. There is no need to expatiate about the effects of such a state of affairs.

Profit and loss tell the entrepreneur what the consumers are asking for most urgently. And only the profits the entrepreneur pockets enable him to adjust his activities to the demand of the consumers. If the profits are expropriated, he is prevented from complying with the directives given by the consumers. Then the market economy is deprived of its steering wheel. It becomes a senseless jumble.

People can consume only what has been produced. The great problem of our age is precisely this: Who should determine what is to be produced and consumed, the people or the State, the consumers themselves or a paternal government? If one decides in favor of the consumers, one chooses the market economy. If one decides in favor of the government, one chooses socialism. There is no third solution. The determination of the purpose for which each unit of the various factors of production is to be employed cannot be divided.

Demand for Equalization

The supremacy of the consumers consists in their power to hand over control of the material factors of production and thereby the conduct of production activities to those who serve them in the most efficient way. This implies inequality of wealth and incomes. If one wants to do away with inequality of wealth and incomes, one must abandon capitalism and adopt socialism. (The question whether any socialist system would really give income equality must be left to an analysis of socialism.)

photo by J.D. Hammond

Ludwig von Mises

But, say the middle-of-the-road enthusiasts, we do not want to abolish inequality altogether. We want merely to substitute a lower degree of inequality for a higher degree.

These people look upon inequality as upon an evil. They do not assert that a definite degree of inequality which can be exactly determined by a judgment free of any arbitrariness and personal evaluation is good and has to be preserved unconditionally. They, on the contrary, declare inequality in itself as bad and merely contend that a lower degree of it is a lesser evil than a higher degree in the same sense in which a smaller quantity of poison in a man's body is a lesser evil than a larger dose. But if this is so, then there is logically in their doctrine no point at which the endeavors toward equalization would have to stop.

Whether one has already reached a degree of inequality which is to be considered low enough and beyond which it is not necessary to embark upon further measures toward equalization is just a matter of personal judgments of value, quite arbitrary, different with different people and changing in the passing of time. As these champions of equalization appraise confiscation and "redistribution" as a policy harming only a minority, viz., those whom they consider to be "too" rich, and benefiting the rest—the majority—of the people, they cannot oppose any tenable argument to those who are asking for more of this allegedly beneficial policy. As long as any degree of inequality is left, there will always be people whom envy impels to press for a continuation of the equalization policy. Nothing can be advanced against their inference: If inequality of wealth and incomes is an evil, there is no reason to acquiesce in any degree of it, however low; equalization must not stop before it has completely leveled all individuals' wealth and incomes.

The history of the taxation of profits, incomes, and estates in all countries clearly shows that once the principle of equalization is adopted, there is no point at which the further progress of the policy of equalization can be checked. If, at the time the Sixteenth Amendment was adopted, somebody had predicted that some years later the income tax progression would reach the height it has really attained in our day, the advocates of the Amendment would have called him a lunatic. It is certain that only a small minority in Congress will seriously oppose further sharpening of the progressive element in the tax rate scales if such a sharpening should be suggested by the Administration or by a congressman anxious to enhance his chances for re-election. For, under the sway of the doctrines taught by contemporary pseudo-economists, all but a few reasonable men believe that they are injured by the mere fact that their own income is smaller than that of other people and that it is not a bad policy to confiscate this difference.

There is no use in fooling ourselves. Our present taxation policy is headed toward a complete equalization of wealth and incomes and thereby toward socialism. This trend can be reversed only by the cognition of the role that profit and loss and the resulting inequality of wealth and incomes play in the operation of the market economy. People must learn that the accumulation of wealth by the successful conduct of business is the corollary of the improvement of their own standard of living and vice versa. They must realize that bigness in business is not an evil, but both the cause and effect of the fact that they themselves enjoy all those amenities whose enjoyment is called the "American way of life." □

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APRIL 2000

Just Dial 911? The Myth of Police Protection

by Richard W. Stevens

Underlying all "gun control" ideology is this one belief: "Private citizens don't need firearms because the police will protect them from crime." That belief is both false and dangerous for two reasons.

First, the police cannot and do not protect everyone from crime. Second, the government and the police in most localities *owe no legal duty to protect individuals from criminal attack.* When it comes to deterring crime and defending against criminals, individuals are ultimately responsible for themselves and their loved ones. Depending solely on police emergency response means relying on the telephone as the only defensive tool. Too often, citizens in trouble dial 911 . . . and die.

Statistics confirm the obvious truth that the police in America cannot prevent violent crime. In 1997 for example, nationwide there were 18,209 murders, 497,950 robberies, and 96,122 rapes.[1] All those crimes were unprevented and undeterred by the police and the criminal justice system.

Many criminals use firearms to commit their crimes. For example, in 1997 criminals did so in 68 percent of murders and 40 percent of robberies.[2] Thus criminals either have or can obtain firearms. The existing "gun control" laws do not stop serious criminals from getting guns and using them in crimes.

Richard Stevens is a lawyer in Washington, D.C., and author of Dial 911 and Die *(Mazel Freedom Press, 1999).*

Practically speaking, it makes little sense to disarm the innocent victims while the criminals are armed. It is especially silly to disarm the victims when too often the police are simply unable to protect them. As Richard Mack, former sheriff of Graham County, Arizona, has observed: "Police do very little to prevent violent crime. We investigate crime after the fact."

Americans increasingly believe, however, that all they need for protection is a telephone. Dial 911 and the police, fire, and ambulance will come straight to the rescue. It's faster than the pizza man. Faith in a telephone number and the local cops is so strong that Americans dial 911 over 250,000 times per day.

Yet does dialing 911 actually protect crime victims? Researchers found that less than 5 percent of all calls dispatched to police are made quickly enough for officers to stop a crime or arrest a suspect.[3] The 911 bottom line: "cases in which 911 technology makes a substantial difference in the outcome of criminal events are extraordinarily rare."[4]

No Duty to Protect

It's not just that the police cannot protect you. *They don't even have to come when you call.* In most states the government and police owe no legal duty to protect individual citizens from criminal attack. The District of Columbia's highest court spelled out plainly the "fundamental principle that a government and its agents are under no general duty to provide public services, such as police protection, to any particular individual citizen."[5]

In the especially gruesome landmark case the "no-duty" rule got ugly. Just before dawn on March 16, 1975, two men broke down the back door of a three-story home in Washington, D.C., shared by three women and a child. On the second floor one woman was sexually attacked. Her housemates on the third floor heard her screams and called the police.

The women's first call to D.C. police got assigned a low priority, so the responding officers arrived at the house, got no answer to their knocks on the door, did a quick check around, and left. When the women frantically called the police a second time, the dispatcher promised help would come—but no officers were even dispatched.

The attackers kidnapped, robbed, raped, and beat all three women over 14 hours. When these women later sued the city and its police for negligently failing to protect them or even to answer their second call, the court held that government had no duty to respond to their call or to protect them. Case dismissed.

The law is similar in most states. A Kansas statute precludes citizens from suing the government or the police for negligently failing to enforce the law or for failing to provide police or fire protection. A California law states that "neither a public entity nor a public employee is liable for failure to establish a police department or otherwise provide police protection service."[6] As one California appellate court wrote, "police officers have no affirmative statutory duty to do anything."[7]

The state legislatures and courts protect government entities and police departments from civil liability for failing to provide adequate police protection. Some states invoke the "sovereign immunity" defense, a throwback to the days when the subjects were forbidden to sue the king. Other states have statutes that prevent legal challenges to police "discretionary" functions. Courts preclude lawsuits in those states by holding that answering emergency calls or providing police protection are "discretionary" functions.

Many states evade liability by relying on the ironically named "public duty" doctrine. Like a George Orwell slogan, that doctrine says: police owe a duty to protect the *public* in general, but *not* to protect any particular *individual.*

Police Advice: "Get a Gun"

A Massachusetts statute spells out the rule there: the government has no legal duty "to provide adequate police protection, prevent the commission of crimes, investigate, detect or solve crimes, identify or apprehend criminals or suspects, arrest or detain suspects, or enforce any law."[8] That "no-duty" rule brings tragedy, as one Massachusetts woman learned in the worst way.

James Davidson had been abusing and harassing his wife, Catherine Ford, after their separation.[9] Catherine got a court order against James to stop his misconduct. The Grafton police knew about James, and told her that they couldn't provide protection around the clock. One officer frankly advised her to "buy a gun because the only way to deal with violence is violence."

Catherine did not take that advice. Over the next 15 months James continued to harass and stalk Catherine, and he repeatedly threatened to kill her and her family. James terrorized Catherine and her family at their homes. He attacked her at her workplace. James's own psychiatrist warned Catherine that James had plans to kill her. Despite all of his vicious and unlawful behavior, the police never arrested James for violating the court order.

James issued his final death threat on January 16, 1986. Catherine reported this threat to the police. At about 6 o'clock the next evening, James started kicking down Catherine's back door. When she ran out the front door, James spotted her and chased her even as she charged through moving traffic on the street. She pounded on a neighbor's door, but no one would let her inside. As she ran to the next house, James caught her and shot her three times in the face and neck. He then shot himself. Miraculously Catherine survived, but was totally paralyzed for life.

Catherine sued the town of Grafton for failing to protect her. Her lawyers argued that the police owed a legal duty to stop James, and thus the police owed a legal duty to protect Catherine. A Massachusetts statute required the police to arrest James for his repeated violations of the court order, but the police had failed to arrest him.

The Massachusetts court in *Ford v. Town of Grafton* held the city was not liable. The court order that was supposed to restrain James and protect Catherine did not amount to an "assurance of safety or assistance" from the police department. According to the court, when the police advised Catherine "to get a gun for protection," that was a warning to her that the police were unable to assure her safety or protect her. Because she got no assurances of safety from the police, she had no legal right to rely on the police to protect her. Case dismissed.

Catherine Ford might have escaped James's murderous intentions unharmed if she had taken the police officer's advice to "get a gun" and had received a basic course in defensive firearms handling and safety. Studies show that Americans use firearms successfully up to two million times each year to stop criminals.[10] Tragically, she chose instead to rely on a court order and the police.

These two cases are not legal oddities. The general rule of law in the United States is that government owes a duty to protect the public in general, but owes no legal duty to protect any particular person from criminal attack. Neither the U.S. Constitution nor the federal civil rights laws require states to protect citizens from crime. As a federal appeals court bluntly put it, ordinary citizens have "no constitutional right to be protected by the state against being murdered by criminals or madmen."[11]

Exceptions to the no-duty rule apply when the police have expressly promised to protect a specific person from an identifiable danger. Informers in a witness protection program, for example, might have an enforceable right to protection. Yet it will make little difference to a dead victim if a court some years later decides that the police did owe a duty but failed to protect him, and then awards damages to next of kin.

Picture the situation: government establishes a police force and installs 911 emergency call service. Then the government announces to the world that "you don't need a firearm for self-defense," and so enacts "gun control" laws to make it difficult or impossible legally to get and use a gun. Meanwhile violent criminals remain illegally armed with guns and other weapons.

Now imagine you are snapped awake one night by the sounds of your door breaking in. You reach for the telephone to dial 911. The 911 emergency operator never answers. Or the police answer, take your frantic report, but don't come. Or they come too late. In any of these scenarios, the burglar gets in, knifes you, and steals your VCR.

Crouching behind a chair with a telephone in your hand, you were defenseless because the government took away your private defense tools and handed you a telephone number to call for emergency help. You relied on that telephone number, and the help never came. The government's policy made you a crime statistic.

Government lulls the public into trusting it to provide everything, takes away the people's means of providing for themselves, and then claims it has no duty to provide after all. Noting the fatal irony in the "gun control" context, James Bovard has written that "government has a specific, concrete obligation to disarm each citizen, but only an abstract obligation to defend the citizen." "Gun control," Bovard notes, "is one of the best examples of laws that corner private citizens—forcing them either to put themselves into danger or to be a lawbreaker."[12]

Laying Bare the State Protection Myth

The drive to prohibit private firearms ownership highlights the statists' goals in a way everybody can understand. They aim to disarm ordinary nonviolent citizens, even those who face high risk of criminal attack, and substitute police protection in place of self-defense. Meanwhile the police will not be held liable to individual citizens for failing to defend them.

Government "social programs" and various mandatory "insurance" programs operate in the same way. First, the government programs distort the market forces that provide housing, food, medical care, transportation, and other goods and services. People shift to depending on the government programs instead of taking individual decisions and action.

When the government programs fail, however, the people relying on those programs have little or no effective recourse. At best, dissatisfied people can file bureaucratic appeals to the very agencies that harmed or cheated them. There can be judicial review of bureaucratic decisions in some cases also, but the judges are usually part of the same government, and they typically defer to the original government agency's decision anyway.

In nearly all cases the citizen bears the stress and expense of pursuing appeals of bureaucratic decisions. The cost of appealing a government decision is already high. The effect of high appeal costs is to stop people from appealing—which gives results just like the "no duty," "sovereign immunity," and "public duty" rules. Government grabs power but sheds accountability.

The problem with government programs is not just that citizens have only narrow and costly avenues for appeals of decisions. While a government social program is operating, it is likely making worse the very problem it was trying to "solve." People cannot get out of a government program and return to private action or free-market solutions because of the effects of the program itself. Legislators point to the "failure" of the market, whine about the problems with the government program, and then prescribe more government. The voters reward those legislators by re-electing them.

Government power ratchets up the same way under a "gun control" regime. As laws discourage innocent citizens from defending themselves, the violent criminals remain undeterred. Absent some other, overweening factor, violent crime cannot possibly decrease in that environment; it more likely must increase. The statist response will naturally be to restrict firearms ownership even more, and to enhance the police presence. Greater police presence means more police, more surveillance, more reporting to government what citizens are doing. Nearly 170 million citizens lost their lives to their own governments in the twentieth century.[13] There is little reason to celebrate a police state.

Revealing the lie underlying the "gun control" agenda strengthens the case against socialism and the welfare state on many levels. If the argument advances the cause of individual liberty, then it is an argument worth making. □

1. Federal Bureau of Investigation, *Uniform Crime Reports for the United States* (1997), pp. 9, 22, 19.
2. Ibid., pp. 14, 25.
3. Gordon Witkin, Monika Guttman, and Tracy Lenzy, "This is 911 . . . Please Hold," *U.S. News & World Report*, June 17, 1996, p. 30.
4. Ibid., quoting Northeastern University Professor George Kelling and lawyer Catherine Coles.
5. *Warren v. District of Columbia*, 444 A.2d 1, 4 (D.C. 1981), quoting the trial court decision.
6. California Government Code, § 845.
7. *Souza v. City of Antioch*, 62 California Reporter, 2d 909, 916 (Cal. App. 1997).
8. Mass. Gen. Laws Ann. Ch. 258 § 10(h).
9. The facts and law of this case are set forth in *Ford v. Town of Grafton*, 693 N.E.2d 1047 (Mass. App. 1998).
10. See Gary Kleck and Marc Gertz, "Armed Resistance to Crime: The Prevalence and Nature of Self-Defense with a Gun," *Journal of Criminal Law and Criminology* 164 (1995), p. 86.
11. *Bowers v. DeVito*, 686F. 2nd 616, 618 (7th Cir. 1982).
12. James Bovard's introduction to Richard W. Stevens, *Dial 911 and Die* (Hartford, Wisc.: Mazel Freedom Press, 1999).
13. R. J. Rummel, *Death By Government* (New Brunswick, N.J.: Transaction Publishers, 1994), pp. 1–25.

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Toward an Austrian Critique of Governmental Economic Policy

by Israel M. Kirzner

In preceding articles we outlined the way in which Austrian economists understand the entrepreneurial competitive market process that is responsible for the law of supply and demand. In the present article we pursue this understanding further, to permit us to see why government interventions in spontaneous market processes tend to frustrate and obstruct the coordinative tendencies that the market process generates. The most extreme sense in which such obstruction may occur is in the pure socialist economy (in which all productive activities are governed wholly by a central planning authority). Here the obstruction is total; market tendencies toward spontaneous coordination are completely paralyzed. But less extreme (less "total") forms of government intervention, particularly so-called "mixed" systems, incorporating significant central regulation of market activity, will be seen to suffer from the same kind of difficulty—the frustration of market tendencies toward spontaneous coordination.

Mises on Socialism

It was in 1920 that renowned Austrian economist Ludwig von Mises enunciated his thesis that centralized socialist planning was, in a definite sense, simply *impossible*. What he meant by this provocative assertion has often been misinterpreted. Mises did not claim that a socialist system cannot exist; nor did he predict unequivocally that such a system cannot survive for many years. What Mises meant was that, with the best will in the world, with the most dedicated and incorruptible central planners in the world, it is simply impossible *to plan centrally* for an entire economy. The decisions made by the central authorities in an economy without a market for productive resources cannot possibly take into account all the alternatives that would, in principle, need to be taken into account in order for decisions to be able to be described as socially efficient. Without a market for productive resources (and thus without market *prices* reflecting the urgency with which consumers in *other* industries are demanding the services of these resources), central planners have no way of ensuring that resources flow to satisfy the more urgent, rather than the less urgent, demands among consumer preferences.

In a market economy the price of a resource expresses the priority with which consumers wish entrepreneurs to direct that resource for the satisfaction of their preferences; a high resource price means that entrepreneurs, somewhere, are aware of a productive employment for this resource that consumers value highly. For an entrepreneur to allocate this resource to any particular industry, he must, in the market competition for the resource, outbid other entrepreneurs; that is,

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he must be convinced that he has identified a use for it which consumers value more highly than consumers value alternative uses for that resource. Without themselves necessarily being aware of the nature and value of these alternative uses, the entrepreneurs are led, yes, as if by an invisible hand, to allocate resources in a way that takes account, in effect, of these alternative uses.

But for the central planners, operating as they must without market prices for resources (since there can, by definition, be no resource markets in the socialist economy), a decision made as to whether to allocate steel to the construction of a bridge or to the construction of an apartment building cannot be made on the basis of any measures of alternate urgencies of need; there simply are no such measures. The central authorities may decide to build the bridge, but their decision is not "rational" (in the sense of expressing a rational selection among alternatives). Central planning, in the ordinary sense of the term "to plan" (which expresses the idea of taking into account the need to balance conflicting objectives), is, as Mises showed, impossible.

The Myth of So-Called "Nonmarket" Prices

In the interwar debate that ensued as a result of Mises's provocative assertion, one attempted socialist response stood out among the others. This was the suggestion, offered separately in the 1930s by two competent socialist economists, Oskar Lange and Abba P. Lerner, that socialist planning might be possible, provided decisions, to be made by socialist employees, could be guided by nonmarket "prices" for resources—that is, by prices promulgated by a central authority, *without* any resource market, but as based on regular reports to the authority of shortages or surpluses of each particular resource during the preceding production period. Space limitations do not permit us here to spell out the details of this suggestion. As we shall see, its central, damning weakness is the notion that resource "prices" can be promulgated without the spontaneous interplay of the bids and offers of profit-hungry competing entrepreneurs.

Remarkably, but in a sense disastrously, mainstream economics for some four decades ignored this weakness and pronounced the Lange-Lerner suggestion a valid and definitive solution to the problem identified by Mises. Only during the past two decades have economists finally conceded the power of Mises's argument. In an outstanding 1985 revisionist work devoted to the socialist economic calculation debate—a work rooted in the Austrian understanding of the market process—Donald Lavoie effectively dissected the fallacies that underlay the mainstream illusion that Lange and Lerner had solved the Misesian dilemma.* The source of the illusion is the mainstream preoccupation with states of equilibrium, to the exclusion of any appreciation for the way in which the dynamically competitive ventures initiated by profit-seeking entrepreneurs are responsible for the calculative usefulness of real-world market prices. To imagine that a central planning bureaucracy might generate numbers in a manner that might remotely resemble the way in which prices are generated in the course of market competition is fundamentally to misunderstand the way markets work.

To put this in somewhat different terms: the mainstream's willingness to accept the Lange-Lerner notion of nonmarket "prices" parallels precisely that mainstream's enunciation of the "law of supply and demand" in strictly equilibrium, nonentrepreneurial terms. Mises's (and also F. A. Hayek's) refusal to acknowledge meaningfulness in such nonmarket "prices" parallels precisely the Austrian insistence on understanding the law of supply and demand as the manifestation of an entrepreneurial process.

The Economics of Government Intervention

Our articulation of the Austrian version of the law of supply and demand, and our corresponding understanding of the Austrian refusal to accept the Lange-Lerner solution (in terms of centrally promulgated nonmarket

*Donald Lavoie, *Rivalry and Central Planning: The Socialist Calculation Debate Reconsidered* (New York: Cambridge University Press, 1985).

prices) to the socialist economic calculation problem first identified by Mises permits us to push the logic a little further. It seems reasonable to interpret Mises's well-known *general* rejection of government intervention (not only for the socialist model, but more particularly for the "mixed" economy) as a consistent application of his insights into the impossibility of rational central planning in a socialist economy. Each and every act of government regulation constitutes, no matter what noble intentions for social betterment such regulation may reflect, an act of interference with the spontaneous market process generated by entrepreneurial competition.

No one claims that the results of this spontaneous market process are, at any given moment, those that would express perfect social efficiency as seen from a vantage point of imagined omniscience. What Austrians claim for the spontaneous market process is that it is the *only* procedure available to less-than-omniscient humans to move systematically in the direction of social efficiency, properly defined and understood. For government regulators to believe themselves able systematically and deliberately to improve on the results of the free-market competitive process is not only arrogantly to assume themselves able to approximate the omniscience needed to do so; it is also to fail to realize how their activities are inevitably destined to distort and/or paralyze that market process through which society grapples creatively and constructively with its lack of omniscience. It was Ludwig von Mises who, in his critique of the possibility of socialist planning, drew indirect attention to the central planner's crippling lack of the knowledge necessary to plan centrally. It was Mises's subtle understanding of the dynamics of the competitive market process that made him, more than all other twentieth-century economists, the complete skeptic regarding the social usefulness of government intervention in otherwise market economies.

We commenced this four-part series with an Austrian critique of the textbook version of the law of supply and demand. Consideration of the Austrian understanding of that law in terms of a competitive-entrepreneurial process of mutual discovery and coordination led us to a thoroughly negative perspective concerning well-meaning attempts to "maintain competition" through so-called antitrust policies. We have now concluded with brief attention to the manner in which the Austrian view leads, not only to a critique of the pure socialist economy, but also toward the critique of interventionism in *all* its forms. □

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Internet Access Should Be Left to the Free Market

The explosive growth of the Internet in recent years has transformed the lives of millions of people at home and work in ways that were unimaginable a generation ago. The benefits to society have been enormous. The proliferation of e-mail addresses, personalized Web pages, and e-commerce are now integral parts of our burgeoning "cyberculture." Always eager to crash the party, governments and their special-interest allies are looking for excuses to tax, regulate, censor, and otherwise spoil the fun.

Access to the Internet is one issue that already elicits controversy and promises to generate even more. Do-gooders itching to regulate argue that the marketplace will not be able to sustain competitive, affordable access in many U.S. communities because cable companies are in a position to monopolize something new called "broadband" technology. Some form of government intervention, say the do-gooders, must counter this so that everyone can afford to be "wired" in the future.

Broadband technology allows cable-television providers to offer Internet access through their cable connections. Its emergence represents a challenge to the more traditional dial-up (narrowband) technology that uses telephone lines. Largely because broadband permits much faster Internet speeds, its popularity is growing enormously. One projection suggests that the number of Internet users who use narrowband will fall from nearly 100 percent just a couple of years ago to 50 percent by 2005. Cable firms will even be able to offer telephone service because unlike narrowband, broadband technology can transmit voice and data simultaneously.

Lobby for Intervention

Rather than standing up to this challenge with the money and effort required to compete, major Internet service providers (ISPs) such as Mindspring Enterprises have joined with some telecommunications firms and "consumer advocacy" groups to form a new lobbying organization called the OpenNet coalition. OpenNet is trying to convince federal, state, and local regulators to intervene and force cable television companies to "share" their broadband cables with other companies. Legislation pending in many states would do just that. The Clinton administration endorses forced access as well. Meanwhile, any economist worthy of the name would argue that the likely result will be higher costs for consumers and no significant increase in the number of Internet access options.

This story is typical of what happens when innovation opens new vistas for free enterprise. Some people are always in better position to take advantage of a new opportunity than others. But that doesn't justify the government's stepping in and disrupting the

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process by which the market shakes out supply and demand. If that happens, it sabotages a process that most often produces the best and widest variety of services for the lowest price.

The late economist Alfred E. Kahn put it well when he explained the importance of deregulating the airline industry. His observation is just as relevant to a discussion of the market for Internet access: "The essence of the case for competition is the impossibility of predicting most of its consequences. The superiority of the competitive market is the positive stimuli it provides for constantly improving efficiency, innovating, and offering consumers diversity of choice."*

If government implements "forced access," the edge will come off the urgent market incentive for ISPs—including new upstart companies—to develop broadband capacity. The incentive for cable operators to take advantage of their head start also will diminish. And the competition over price that would naturally ensue in an unhampered market—to the advantage of consumers—will be far weaker and produce far fewer options and advantages.

This is precisely what happened when Congress passed the 1996 Telecommunications Act, designed to "level the playing field" in telephone service by forcing established telephone companies to make their network facilities available to competing firms. Here in Michigan, instead of facilitating competition, "forced access" stifled it. In 1998, despite all the advertising we heard from new companies, the big local telephone companies Ameritech and GTE-Michigan still earned 96 percent of all local service revenues.

A recent study from the Mackinac Center for Public Policy argued that by all measures the market for Internet access is dynamic and competitive and will remain so if government butts out. Author Donald Alexander, a telecommunications economist from Western Michigan University, maintains that consumers who want access to the Internet can, in many localities, purchase this service from a wide range of suppliers, with each one offering a different technology with distinct advantages and disadvantages.

Undermining Innovation

Alexander points out that if government requires cable firms to provide access to its cables to any ISP, the resulting increase in users would cut transmission speeds—a major reason why people prefer broadband in the first place! Congestion problems would undoubtedly then be blamed on the cable companies. In the long run, those companies would likely cut back on their investments in broadband technology, which would have the effect of limiting future access options for consumers—the exact opposite of what OpenNet says it wants to achieve.

For these reasons and a host of others, says Alexander, politicians and regulators should reject specious claims about "leveling the playing field" and refrain from passing "forced access" legislation.

Instead, they could actually stimulate competition by ending the system by which cable companies gain monopoly franchise agreements in local areas. Since the 1960s, local governments have granted cable operators monopoly status, stifling what would otherwise become a healthy competition among cable operators. This—not the cable operators' broadband capability—is the real inequity lawmakers should address. Nationwide, only 3 percent of cable subscribers can select from competing providers. That enforced lack of competition boosts prices to consumers while allowing local governments to rake in millions in franchise fees.

What's the bottom line? Government should not force cable operators to make their cables available to their competitors, and it should not grant exclusive local monopolies to those cable operators either. Better Internet access, better cable television service, and even cheaper telephone calls are all on the horizon as broadband technology spurs innovations. Free markets, not new regulations, will bring that about. □

*Alfred E. Kahn, "Deregulation and Vested Interests: The Case of Airlines," in Roger G. Noll and Bruce M. Owen, eds., *The Political Economy of Deregulation* (Washington, D.C.: American Enterprise Institute, 1983), p. 140.

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The Microsoft Case: Divestiture Won't Help Consumers

by D. T. Armentano

Critics of Microsoft, rallied by Judge Thomas Penfield Jackson's finding that the company has monopoly power over much of the computer industry, have urged a breakup of the company. For example, the Consumer Project on Technology (affiliated with Ralph Nader) suggests that Microsoft be forced to divest its Web browser, Internet Explorer. But other far more radical divestiture proposals are under consideration. The 19 state attorneys general who were co-plaintiffs in the antitrust suit are said to be pressing for a horizontal breakup that would divide Microsoft into three companies: one with the operating system, one with applications software, and one with Internet businesses. Still other critics have called for a vertical divestiture that would divide Microsoft into three or more fully integrated companies ("Baby Bills") that would then, presumably, compete with one another in the marketplace.

Even friends of liberty have suggested that some sort of divestiture might make economic sense. Peter Huber, in an important article in the *Wall Street Journal* ("Breaking Up Isn't Hard to Do," November 10, 1999) argued that it could be good for Bill Gates and for Microsoft's investors since "the children of broken up corporate marriages tend to fare remarkably well." He cites Standard Oil, Alcoa, and AT&T, all of which prospered after the government broke up the parent companies.

Yet it strains belief to imagine that the trustbusters or courts know how to maximize shareholder return better than private entrepreneurs. If divestiture were better for John D. Rockefeller or Bill Gates, they could always have spun off their own companies. When firms are worth more apart than together, they are broken up by management or, when management is oblivious to market realities, by outsiders in hostile takeovers, such as occurred with many large conglomerates in the 1980s.

Contrary to Huber and others, government divestiture is no panacea. Standard Oil, American Tobacco, Alcoa, United Shoe Machinery, and AT&T were all broken up with mixed results for the companies and consumers. Standard Oil did well after the 1911 breakup because it was still the largest integrated domestic refiner. American Tobacco prospered because divestiture did not affect the success of its popular brand names. Alcoa survived its split from Alcan in 1951 because the breakup had no significant effect on domestic aluminum production or sale. However, United Shoe Machinery declined rapidly after divestiture in 1968, and the AT&T situation is clouded because radical telecommunications deregulation—and not the antitrust breakup per se—was responsible for the explosion in post-divestiture revenues.

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Effect on Consumers

The effects of divestiture on consumers are even more problematic. In petroleum, for example, refined oil prices fell for decades prior to divestiture; in the decade after the breakup—and even before World War I—prices increased sharply and stabilized. Alcoa had a near "monopoly" in virgin ingot aluminum for almost 50 years, and prices declined from $5 per ingot pound in 1887 to 22 cents in 1937, when the monopoly trial began; after the decision against Alcoa in 1945 and after the divestiture of Alcan, prices increased and stabilized.

Subsequent to the oil and aluminum breakups, dominant firm market shares declined somewhat and smaller competitors expanded their business. But this development was not necessarily efficient or pro-consumer. More likely, the breakups prevented the exploitation of the efficiencies from integration (especially in the oil industry), causing increases in costs and prices that allowed less efficient competitors to expand production and sales. In aluminum, the court-ordered restraints on the purchase of World War II aluminum facilities, plus the compulsory licensing of patents to rivals, made Alcoa a less efficient supplier. In both cases particular competitors, but not necessarily consumers, benefited from antitrust regulation.

The closest case to Microsoft is the 1968 breakup of United Shoe Machinery, which was blatantly anti-consumer and anti-investor. Like Microsoft, United Shoe was an aggressively competitive dominant firm that maintained its market position through massive investments in shoe machine technology and low prices. And like Microsoft, it often bundled the lease of its machines with certain services. The trial judge in the case actually praised United's overall economic efficiency.

But as in the Microsoft case, smaller rivals found it difficult to compete with United's superior line of machines and favorable long-term leases. That difficulty—and not any concern with consumer welfare or efficiency—was the judge's determining consideration. He shortened the leasing contract arbitrarily and ended the bundling in order to help smaller competitors. In 1968, at the insistence of the Department of Justice, the Supreme Court went further and ordered United Shoe to spin off significant shoe machine assets, subsidize a new "competitor," and refrain from active competition with the newcomer for up to five years. This regulatory attempt to "create competition" proved disastrous: United Shoe Machinery, and the domestic shoe industry that it served, both declined steadily after divestiture. Now most shoes are made overseas.

Bill Gates

Standard Oil, Alcoa, United Shoe Machinery—and especially Microsoft—all earned their initial market positions by being more efficient than their rivals. Any regulation or devolution of a successful corporate organization is likely to reduce efficiency and consumer welfare. Antitrust history is littered with attacks on successful companies and with regulatory attempts to redistribute the spoils of success to less efficient rivals. Such antitrust protectionism is both immoral and destructive of productivity and wealth.

Judge Jackson, having already decided incorrectly that Microsoft is a monopoly that restrains trade, ought not to compound his errors of "fact" by ordering some punitive and socially harmful industrial reorganization. □

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Barbarians at Bill Gates

by William F. Shughart II

It was a glorious fall day on the East Coast when Assistant Attorney General for Antitrust Joel Klein stepped up to the microphone at a news conference called hard on the heels of the release of Judge Thomas Penfield Jackson's "findings of fact" in the government's case against the Microsoft Corporation. An obviously pleased Mr. Klein declared that Judge Jackson's findings, which accepted the Justice Department's charges nearly in total, proved once again that no company—and no man—is above the law. Adding unintended irony to the scene, Bill Clinton's guardian angel, Attorney General Janet Reno, stood at Mr. Klein's shoulder.

Thus ended the first act in a continuing drama that began in the summer of 1993, when, after the Federal Trade Commission twice failed to vote out a complaint against Microsoft, the Justice Department launched its own investigation of the company's possible antitrust violations. The Department of Justice's intervention in its sister agency's three-year-long inquiry was both unprecedented—in order to avoid unseemly competition the FTC and Justice have since 1948 operated under a liaison agreement that divides the antitrust territory between them—and politically inspired. Anne Bingaman, President Clinton's first assistant attorney general for antitrust, requested the files accumulated during the commission's investigation in response to pressure from Senators Howard Metzenbaum (since retired) and Orrin Hatch, both of whom urged her to take over the Microsoft case.

The substance of the charges of unlawful behavior against Microsoft has been in metamorphosis over the course of the company's protracted encounter with the federal antitrust authorities—and with the 19 states and the District of Columbia that have filed their own antitrust lawsuits against it. At the outset the FTC's attorneys maintained that Microsoft had illegally foreclosed the market for computer operating systems by entering into contracts with manufacturers of personal computers, granting them substantial discounts in return for agreeing to preload Microsoft's own operating system, MS-DOS (later upgraded and marketed as Windows), on all their PCs. Indeed, some of the contracts obligated the manufacturers to pay Microsoft a royalty on every computer processor they shipped even if some other operating system had been installed. The FTC's investigation had centered particularly on the lack of success experienced by DR-DOS, an operating system marketed by Novell, Inc., headquartered in Utah and represented in the U.S. Senate by Orrin Hatch.

When the Justice Department took over the investigation, the focus shifted to Web-browsing software. Reacting to the spectacular growth of the Internet and to consumers' desires for a product that would allow them to navigate

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easily around the information superhighway it spawned, Microsoft developed its Internet Explorer Web browser and formed plans ultimately to integrate it with Windows. Those plans bore fruit with the release of Windows 95, raising the competitive stakes between Microsoft and Netscape, Inc., which marketed its own Web browser, Navigator, as a standalone software product.

Tying that Binds?

Following meetings between James Barksdale, then CEO of Netscape, and Assistant Attorney General Klein, the Justice Department filed suit in federal district court seeking to force Microsoft to offer a version of Windows without Internet Explorer. The Justice Department charged that Microsoft's practice of bundling Internet Explorer with its operating system violated the Clayton Act's proscription on "tying," whereby the sale of one product is conditioned on the purchase of another. By requiring purchasers of Windows to also buy its Web browser, Microsoft, according to the government, had leveraged its market power in operating systems to foreclose Netscape from distributing Navigator. Not only did Microsoft's strategy represent an unlawful restriction on consumer choice, but, given that Internet Explorer was included in Windows at no additional charge, the strategy also may have been intended predatorily to drive Netscape from the browser market.

The district court agreed and ordered Microsoft to offer two versions of Windows, with and without Internet Explorer. But only a month after the Justice Department filed more far-reaching charges of anticompetitive behavior against Microsoft on May 18, 1998, the D.C. Circuit Court of Appeals overturned the lower court's ruling. Wading through mind-numbing details on the question of whether Internet Explorer was truly "integrated" with Windows 95, the appeals court held that because Internet Explorer 3.0 contained features that went beyond browsing capabilities, it did not constitute a separate product within the meaning of the law's anti-tying language; hence, Microsoft's decision to include Internet Explorer in Windows did not violate the terms of a 1995 consent decree in which the company agreed not to bundle computer software applications with its operating system.

And so, by the time the Department of Justice submitted its proposed findings of fact to Judge Jackson, the basis of the government's case against Microsoft had shifted once again. The Justice Department's new theory, ultimately embraced by the judge, is that Microsoft has engaged in a variety of anticompetitive practices—including its decision to incorporate Web-browsing capabilities within Windows—calculated to protect and extend its monopoly power in the market for "Intel-compatible PC operating systems" (about which more below) by erecting and maintaining a so-called applications barrier to entry.

That entry barrier is based on the positive feedback loop between a computer's operating system and the software applications that run on top of it. The greater the number of copies of a particular operating system in use, the more potentially profitable it is for software vendors to write compatible applications (such as word processors, spreadsheets, and tax-preparation and e-mail programs), which after all are why consumers want to buy personal computers in the first place. The more applications written to run on a particular operating system, the greater the demand for that operating system will in turn be. Hence, applications and operating systems are subject to a proverbial "chicken-and-egg" problem. With its large installed base of users—something on the order of 90 percent of new PCs are shipped with Microsoft's operating system—thousands of Windows-compatible software applications are available on the market. Few applications are written for alternative operating systems because few copies of those operating systems are in use, and few alternative operating systems are in use because few software vendors write applications compatible with them.

The threat posed by Netscape's Navigator (and by Sun Microsystems' Java programming language) was not that they competed with Microsoft's Web browser per se, but that they exposed interfaces that might serve as an alternative platform for running network-centric application programs—applications capable of running on Web servers rather than on a computer's hard drive. Navigator and other such "middleware" thus endangered Microsoft's dominance of the operating system market, and according to the Justice Department, the company moved aggressively and unlawfully to quash the competition.

Microsoft was particularly worried that Navigator, which had captured about 80 percent of the browser market (and had "been ported to more than fifteen different operating systems"[1]), would be seen as such an attractive platform for applications by software developers that, in the words of Netscape's co-founder, Marc Andreessen, Windows eventually would be relegated to an unimportant collection of "slightly buggy" device drivers.[2]

The Relevant Antitrust Market

As in any antitrust case, the definition of the market that is relevant for analyzing the competitive effects of Microsoft's business practices is the key issue in Judge Jackson's findings of fact. Drawn narrowly enough, the boundaries of relevant antitrust markets can limit the number of products that ostensibly compete with one another so severely that almost any firm can be determined to possess "market power"—the ability to raise prices above competitive levels. In the case at hand, Judge Jackson chose to define the relevant market as "Intel-compatible PC operating systems," the narrow definition advocated in the government's pleadings.

The curious conclusion produced by the judge's finding on the relevant market definition is that Microsoft does not compete with the very firms it is accused of injuring. Excluded from the market so defined are Netscape and Sun, which, as indicated, market software products that interface with a computer's operating system (and which might also serve as alternative platforms for running application programs); Apple, which markets an operating system (Mac OS) that is incompatible with Intel-based PCs; and the many other companies striving to develop the next ubiquitous applications platform. The only other firms in the "market" are those offering either alternative Intel-compatible operating systems, such as IBM (OS/2) and Be (BeOS), or "cross-platform" operating systems, such as Linux, capable of running on both Intel-based and non-Intel-based PCs.

Judge Jackson defended his decision to define the relevant market in this way by pointing to the high cost consumers face in switching to the available alternatives. For one, unlike Windows, the Mac OS is licensed only for use on Apple's own hardware—the two products are sold as a bundle. The owner of an Intel-compatible PC is therefore required to purchase an Apple machine to take advantage of that substitution possibility. In addition, because it is considerably more expensive at current prices, the Mac OS option places few competitive constraints on the market for Intel-compatible PC operating systems.[3]

The applications barrier to entry provides a second justification for a narrow market definition, according to Judge Jackson. Even if consumers could easily overcome the costs of installing and learning to use an alternative operating system, they would still be deterred from switching because of the relatively small number of application programs written for those operating systems.

Defining the relevant market as including only Intel-compatible PC operating systems leads inescapably to the conclusion that Microsoft enjoys substantial market power. That conclusion is reinforced in Judge Jackson's mind by the testimony of Frederick Warren-Boulton, one of the government's economists, suggesting that, because the price of an operating system represents a small fraction of the total cost of a personal computer, which consists of a central processing unit and peripheral devices such as a keyboard, a monitor, and a printer, consumers are not very sensitive to changes in the price of Windows; that is, Microsoft confronts a demand for its flagship product that is highly inelastic. And since Microsoft *could* raise the price of Windows substantially without inducing large numbers of consumers to switch to alternatives, the company possesses market power.

It is a well-established principle of the neoclassical theory of the firm that a monopolist will never sell at a price where demand is inelastic. That is because a seller facing an inelastic demand can increase its total revenues and profits by reducing output and raising price. Hence, saying that the demand for Windows is inelastic at the current price is the same thing as saying that Microsoft has failed to maximize its profits. Bill Gates has been accused of many things, but making less money when he could have made more is not one of them.

Relevant market definition is supposed to be about the problem of identifying the alternatives to which consumers could turn if confronted with an increase in the price of the product at issue. Judge Jackson's stated concern that there seem to be few good substitutes for Windows available at current prices misses that important point. The key question is not whether there are good substitutes for Windows at the current price, but rather whether substitution possibilities exist in the event that Microsoft attempts to charge a monopoly price. The fact that a substantial number of alternative Intel-compatible PC operating systems are on the market presently—a list that includes, among others, IBM, Oracle, Sun, AT&T, Hewlett Packard, NeXT, Xerox, Wang, Be, Linux, DEC, Psion, 3COM, Geos, and GEM—points to the conclusion that Microsoft's pricing discretion is tightly constrained.[4] Taken together with the assertion of inelastic demand, the observation that the sellers of alternative Intel-compatible PC operating systems collectively now account for only about 10 percent of sales suggests that the current price is the competitive price. In other words, Microsoft sells Windows at a price where demand is inelastic because it thinks its sales would fall dramatically if price were increased.

Microsoft's Contracting Practices

But in any case, Microsoft is not accused of exploiting its market power by raising its prices and profits at consumers' expense. Nor is it charged with acquiring that power by unlawful means. Instead, Judge Jackson contends that the company has used its dominant position in the market for Intel-compatible PC operating systems to force the manufacturers of PC hardware, writers of software applications, Internet access providers, Internet content providers, and other customers and competitors to agree to contractual terms calculated to protect its monopoly by reinforcing the so-called applications barrier to entry. Put differently, Microsoft has forgone profits it could have earned now and in the past to forestall the entry of new software application platforms (or the expansion of sales of existing platforms), thereby preventing the erosion of future profits. By offering discounts, free advertising, access to pre-release ("beta") versions of software, placement on the Windows desktop, and other valuable considerations, Microsoft "beguiled" customers into entering a "special relationship" with the company.[5]

Stripped to its essentials, the government's case against Microsoft is one of unlawful predation. And while the list of the alleged victims of Microsoft's anticompetitive business practices is long, judged by the amount of narrative space devoted to describing how Microsoft attempted to destroy its competition, the case is all about Netscape. According to Judge Jackson, Microsoft employed a variety of tactics to stave off the threat posed by Navigator. That threat, to reiterate, was the prospect that Navigator would expose interfaces to software developers that would eventually weaken the applications barrier to entry by providing an alternative platform for running application programs and, hence, jeopardize the Windows operating system "monopoly."

Among other tactics, beginning with the release of Windows 95, Microsoft integrated Web-browsing functionality within its operating system and adopted a policy of giving subsequent versions of Internet Explorer away for free. It also took steps to exclude Navigator from important distribution channels. Microsoft did so by preventing the hardware manufacturers to which it had licensed Windows from modifying the sequence of screens seen by consumers on first use, including deleting Internet Explorer from the start sequence, and, if it had also been preinstalled, from giving more favorable placement to Navigator's desktop icon on the Windows default screen than given to the Internet

Explorer icon. With similar ends in mind, Microsoft also entered into agreements with Internet access providers, such as America Online, to bundle its browser with their proprietary client software and to endorse and promote it, paying bounties for every subscriber converted from Navigator to Internet Explorer.[6] Microsoft likewise entered into agreements with the Disney Channel and other Internet content providers to promote Internet Explorer in return for favorable placement of their own icons on the Windows default screen.

Such policies, in Judge Jackson's words, "guaranteed the presence of Internet Explorer on every new Windows PC system."[7] Netscape was thereby forced into less desirable distribution channels, such as "carpet bombing" consumers with free disks they must install themselves, a task supposedly daunting to novice computer users.[8] And indeed, Microsoft's browser strategy ultimately paid dividends: "from early 1996 to the late summer of 1998, Navigator's share of all browser usage fell from above seventy percent to around fifty percent, while Internet Explorer's share rose from about five percent to around fifty percent."[9] It is worth noting, however, that Microsoft did not begin taking market share away from Netscape until it had invested considerable resources in improving a product that, at the time of its initial introduction, was widely seen as inferior to that of its rival. In particular, "from 1995 onward, Microsoft spent more than $100 million each year developing Internet Explorer. The firm's management gradually increased the number of developers working on Internet Explorer from five or six in early 1995 to more than one thousand in 1999."[10]

When Internet Explorer 4.0 was released in late 1997, Microsoft had caught up technologically with Netscape, and so, explanations for Internet Explorer's success based on the company's restrictive contractual practices cannot be disentangled easily from those based on technological improvements. There is no doubt, however, that Netscape's own business decisions contributed to its loss of market share.

In September 1996, Microsoft announced the introduction of the "Internet Explorer Access Kit" (IEAK), which allowed Internet access providers conveniently to download Internet Explorer at no charge and to modify certain of its features to create distinctive identities for their services. Indeed, Microsoft allowed Internet access providers to preset the browser's default home page so that customers would be taken directly to the access provider's Website whenever they logged on to the Internet, thereby supplying them with valuable advertising and promotional opportunities. "Netscape, by contrast, refused to allow its [Internet access provider] licensees to move Navigator's home page from Netscape's NetCenter portal site."[11] It was slow to follow Microsoft's lead, continuing to charge Internet access providers between $15 and $20 for every copy of Navigator they distributed, and failing to offer them a tool comparable to Microsoft's access kit. When Netscape finally released a tool kit, known as "Mission Control," with the same capabilities as IEAK in June 1997, it charged $1,995 per copy. Too much, too late. By that time, about 2,500 Internet access providers had executed licensing agreements for the IEAK.[12]

Whatever else may be said about Microsoft's allegedly unlawful contractual practices, it is clear they did not work. Netscape continues to distribute copies of Navigator in droves—primarily by allowing consumers to download the program from its Website—despite Microsoft's attempts to limit its access to important distribution channels. Moreover, although Netscape has been forced by Microsoft's policy of giving Internet Explorer away for free to also charge a zero price for Navigator—the same strategy Netscape had employed initially to build a dominant market share in browsing software—Netscape's continued economic viability was assured when, while the trial was still underway, America Online agreed to purchase the company in a stock transaction worth $10 billion.

In sum, if Microsoft's contractual practices were intended predatorily to drive Netscape from the market, thereby preserving the applications barrier to entry, that strategy failed utterly, as economic theory would predict.[13] A plausible theory of predation requires a reasonable expectation that the predator, once successful in eliminating the competition, will be able to recoup his losses. The ability to recoup, in turn, presupposes that at some point in the future the predator will raise his price above competitive levels. Sustaining an above-competitive price in the future requires the existence of barriers to entry that prevent rivals from undercutting that price, thereby eroding the above-normal profits that make the whole sequence of events pay off.

The difficulty of recouping predatory losses in general, a point that the Supreme Court has recognized increasingly in recent years,[14] is even more manifest in the case at hand. Because no competitor in the "browser wars" has been eliminated, any attempt on Microsoft's part to raise the price of Internet Explorer would quickly be defeated. A zero price for browsers is more plausibly seen, not as predatory, but as competitive. This conclusion follows by recognizing that, like the newspaper business, money is to be made by charging advertisers for the right to access consumers rather than by charging consumers for the right to access the Web.

If it were shown to be sound, of course, Judge Jackson's finding of an applications barrier to entry might provide the basis for a predatory scenario underlying Microsoft's actions. But a careful study of software markets by economists Stan Liebowitz and Stephen Margolis raises doubts about the existence of "network externalities" said to raise barriers to the entry of new competitors.[15] (A "network good," such as a telephone, a fax machine, or a computer operating system, is one whose value increases with the number of units in use.) Examining the evolution of market shares of the sellers of a variety of computer software applications, they report three key findings. First, Microsoft's software applications begin to capture significant shares of total sales only when they garner favorable quality ratings by independent experts. Second, successful entry by Microsoft into software markets brings prices down. Third, there is no evidence of a "tipping point"—a threshold market share that, when reached, allows the dominant seller quickly to gain control of the balance of the market because his product has achieved the status of an industry standard. The market for Web browsers is a case in point: Netscape's 80 percent market share evidently did not deter Microsoft's successful entry. The growing popularity of Linux, a cross-platform operating system freely available for download, casts further doubt on the proposition that entry is hopelessly barred.[16]

Microsoft's Defense and Beyond

If Judge Jackson's prose reads like a carbon copy of the government's proposed findings of fact, Microsoft has no one but itself to blame. Its defense team apparently adopted a strategy of retaining economists who had spent their careers defending antitrust in the hope that, if they questioned the charges against Microsoft, their credibility would be enhanced. That strategy backfired. Forced on the stand to explain at great length why their opinions in the case at hand were so inconsistent with their previous writings, the substance of their testimony got lost.

Microsoft's leading expert witness was MIT Professor Richard Schmalensee, the architect of the infamous "shared monopoly" case brought by the FTC against the nation's leading producers of ready-to-eat breakfast cereals in the early 1970s.[17] That case, which the commission ultimately dismissed "with prejudice," was based on the novel and untested theory that Kellogg, General Foods, and General Mills had deterred the entry of new rivals by adopting a strategy of "brand proliferation," pre-empting scarce grocery store shelf space by taking advantage of every opportunity to introduce new cereal brands and, hence, making it more difficult for new entrants to fill niches in the market. On record in support of the notion that it is somehow less desirable to have consumers' wants satisfied by existing firms than by new entrants, Professor Schamlensee's testimony was immediately suspect. Not surprisingly, except to disparage data relied on by him to calculate usage shares for different brands of Web-browsing software, Judge Jackson ignored Microsoft's experts completely.

The findings of fact leave little room for doubting that Microsoft will be found guilty of using its monopoly of Intel-compatible PC operating systems unlawfully. Moreover, Judge Jackson provides some fairly clear signals about the remedies he has in mind. For one, despite the D.C. Circuit's 1998 decision to the contrary, he seems to think that there is "no technical justification"[18] for Microsoft's refusal "to supply a version of Windows 98 that does not provide the ability to browse the web, to which users could add a browser of their choice."[19] The findings of fact also hint at remedies aimed at undoing Microsoft's restrictions on the ability of computer manufacturers to modify the Windows boot sequence and permitting Internet access providers to promote and distribute Netscape's Navigator.[20] Observers have speculated that in addition to prohibiting Microsoft from imposing certain restrictive contractual terms, Judge Jackson may go so far as to order the company to separate its operating system business from its software applications or declare the operating system an "essential facility," granting access to Windows proprietary code to all who wish it.

Remedies are always an afterthought in antitrust proceedings, and the difficulties of crafting one in this case that will not interfere unduly with Microsoft's ability to innovate are great. Judge Jackson's unexpected appointment of Judge Richard Posner to have a go at mediating a settlement acceptable to Microsoft and the Department of Justice suggests that neither Jackson nor the government has a clear idea about what is to be done. The real tragedy is that Judge Jackson's findings of fact will provide Microsoft's rivals with a legal basis to sue for compensation for the damages caused by its allegedly unlawful behavior. Two such claims have already been filed. These follow-on private antitrust suits promise to entangle Microsoft in litigation for years to come, distracting Bill Gates from doing what he does best, namely putting useful new products in the hands of consumers. Aided and abetted by the Department of Justice, that is what Microsoft's rivals wanted all along and, unfortunately, they seem to have won the first battle.

It is common knowledge that Netscape, Sun Microsystems, and other interested parties lobbied hard to convince the government to battle Microsoft on their behalf, thereby shifting the cost of litigation from shareholders to taxpayers. In the beginning, Microsoft tried to ignore the powerful political forces arrayed against it, hunkering down in Redmond, Washington, to focus on its core businesses. Guess which side prevailed. The moral of the story is that antitrust is not about market efficiency or the welfare of consumers. It is about interest-group politics.[21] As such, antitrust is no different from any other modern public policy process in which the police powers of the state can be mobilized selectively to benefit one group at the expense of others. □

1. Findings of Fact, *United States v. Microsoft Corp.*, Civil No. 98-1232 (TPJ), November 5, 1999, p. 69. Hereinafter referred to as "Findings."

2. Quoted in David S. Evans, "Antitrust on Internet Time: Whatever Happened to the Government's Case in *United States v. Microsoft?*," National Economic Research Associates, September 17, 1999, p. 11.

3. Judge Jackson does say, however, that including the Mac OS in the relevant market would not lead him to alter his conclusions. Findings, p. 21.

4. See Richard B. McKenzie and William F. Shughart II, "Is Microsoft a Monopolist?," *Independent Review*, Fall 1998, pp. 165–97.

5. Findings, p. 252.

6. Ibid., p. 139.

7. Ibid., p. 158.

8. Ibid., p. 147.

9. Ibid., p. 372.

10. Ibid., p. 135.

11. Ibid., p. 249.

12. Ibid., pp. 250–51.

13. Recent evidence casts even more doubt on the logic underlying theories of predation. See John R. Lott, Jr., *Are Predatory Commitments Credible? Who Should the Courts Believe?* (Chicago: University of Chicago Press, 1999).

14. See, for example, *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 113 St. 2578 (1993) (predatory pricing is "rarely tried and even more rarely successful").

15. Stan J. Liebowitz and Stephen E. Margolis, *Winners, Losers and Microsoft: Competition and Antitrust in High Technology* (Oakland, Calif.: Independent Institute, 1999).

16. As the trial was coming to a close, Red Hat, a major distributor of Linux, went public. The company had a market value of $8 billion as of September 10, 1999. Evans, "Antitrust on Internet Time," p. 15.

17. *In the Matter of Kellogg Co. et al.*, FTC Docket No. 8883 (1972). The theory underpinning the case is laid out in Richard L. Schmalensee, "Entry Deterrence in the Ready-to-Eat Cereal Industry," *Bell Journal of Economics and Management Science*, Autumn 1978, pp. 305–27.

18. Findings, p. 177.

19. Ibid., p. 187.

20. Ibid., pp. 218, 247.

21. See, for example, William F. Shughart II, *Antitrust Policy and Interest-Group Politics* (New York: Quorum, 1990) and Fred S. McChesney and William F. Shughart II, eds., *The Causes and Consequences of Antitrust: The Public-Choice Perspective* (Chicago: University of Chicago Press, 1995).

IDEAS ON LIBERTY
APRIL 2000

Cut Taxes, Not the Debt

Last fall's standoff over the budget between the Republican Congress and Democratic President generated a curious by-product: more money to reduce the national debt. Some analysts want to devote future surpluses to the same purpose, perhaps eventually paying off the entire $5.6 trillion national debt.

Eliminating not only the budget deficit but also the national debt is obviously a worthy goal. Interest payments were the second largest federal expenditure in 1999.

Although low interest rates have been reducing this burden, it will remain above $250 billion annually despite expected surpluses throughout the next decade. We all will be paying the price of Washington's past profligacy for years to come.

However, it is more important to provide tax relief to Americans who bear this cost. According to the Tax Foundation, the per capita expense of taxes this year is $10,298; the burden is even heavier in high-tax states such as Connecticut, New Jersey, and New York.

This expenditure dwarfs everything else in people's budgets: shelter ($5,833), health care ($3,829), food ($2,693), transportation ($2,568), recreation ($1,922), and clothing ($1,404). If you separate federal ($7,026) and local ($3,272) levies, taxes still top the list, while taking fourth place as well!

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The rise in taxes has been particularly sharp during the Bush-Clinton administrations. Because of these spendthrifts, every American pays an extra $2,000 to accommodate the steadily expanding federal behemoth.

Of course, increasing incomes in a booming economy have helped mask the impact of higher taxes. But that doesn't make a serious tax cut any less imperative.

Reducing the tax burden would strengthen the economy at a time when some analysts fear an approaching slowdown. With the Federal Reserve hinting at higher interest rates and pessimists predicting the imminent arrival of the stock market bear, let Americans keep more of their incomes. Economists Aldona and Gary Robbins figure that even last year's modest GOP tax cut proposal would have generated enough new economic activity to cover nearly a third of the lost revenue.

Cutting taxes would also encourage private saving. As the Robbinses observed: "Because the increased federal tax burden (running at 20.8 percent of GDP for the current fiscal year) imposes high marginal rates which discourage saving and investment, the current policy of running surpluses will result in less—not more—U.S. saving."

The biggest economic bang for the buck would come from reducing capital gains tax rates, liberalizing IRA and pension rules, and adjusting other business levies. However, reducing tax rates on every working person is even more important because it is the right thing to do. People are paying too much for too little. The budget is larded with immoral income transfers, pork, unnecessary programs, special-interest subsidies, and blatant waste. Washington politicians insult people's intelligence when claiming there's little or no money to give back.

It is particularly important that any tax cut be across-the-board. Even Republicans often fall prey to demagoguery about not giving tax cuts to "the rich." Yet the latest analysis of the Tax Foundation shows that the top 5 percent of taxpayers account for over half of income tax revenues, up sharply from a decade ago. The top 1 percent bear one-third of the burden. The top 50 percent pay 96 percent of all income tax revenues.

Denouncing Debt

However, opponents of tax cuts now routinely play the Social Security card. They say we should pay down the national debt to save Social Security. Having spent years advocating a policy of tax, borrow, and spend, they now denounce the debt they did so much to accumulate.

Indeed, the surpluses only invite Congress to increase outlays, which it has been doing. During the budget fight at the end of last year, both major parties tossed money out the Treasury door with wild abandon. The GOP was often worse, determined to prove that it was as "compassionate" as was the President. The Republican Congress wouldn't even live up to its meaningless promise not to spend the Social Security surplus.

Unfortunately, reports Tom McCluskey, a budget analyst with the National Taxpayers Union Foundation, "Although the new battle cry to 'Save Social Security first' has forced many lawmakers to retreat from backing large budget bills, the data show that a sizeable contingent in Congress has continued to advance spending increases." Although net spending agendas were mercifully down (while the number of spending bills was up) in the 106th Congress, compared to the 105th, legislators were still willing to waste taxpayers' money on all manner of parochial projects.

McCluskey found that 98 members of the House had net spending agendas that would entirely consume the on-budget surplus; if all the bills were enacted the jump would be $1.4 trillion, nearly doubling the federal budget. Writes McCluskey: "for a sizeable number of Members, belonging to the first Congress since 1970 that inherited a budget surplus has served as a green light to spend the entire windfall on new programs."

While it is good that legislators now generally eschew huge spending initiatives, their reliance on what McCluskey terms "policy incrementalism" is probably more insidious. It is far easier for politicians to approve a collection of small outlay increases than massive new programs. Indeed, Congress is steadily moving U.S. health care toward President Clinton's original goal of nationalization through an accumulation of small steps.

The best way to meet the spendthrift temptation is to eliminate the surplus by cutting taxes.

In any case, the debt has nothing to do with Social Security. Because of the demographic tsunami—more elderly, and more of them living longer—by around 2014 the system will be spending more than it takes in.

Cutting the debt won't change that. Social Security is an unsustainable Ponzi scheme that is breaking down as ever more retirees depend on ever fewer workers.

Of course, lower interest payments would make it easier to shift general revenues to Social Security. But cutting the nonessential programs that dominate the budget would achieve the same end. And those programs should be eliminated in any case.

However, the resulting savings shouldn't be poured into Social Security's bottomless pit. By 2070 the annual flood of red ink will be $7 trillion. In fact, between 2010 and 2070 the system is committed to paying out $140 trillion more than it is projected to take in.

Social Security can be "fixed" only by allowing workers to opt out in favor of private investment plans. People would collect better benefits while dropping their claim to a tax-paid retirement.

The federal government expects to collect $22.8 trillion in revenue over the next decade. All this money, and not just the surplus, belongs to the taxpayers, not to the government. Washington should leave it with its rightful owners. □

IDEAS ON LIBERTY
APRIL 2000

Economic Illiteracy

by Paul A. Cleveland

During the fall semester, the first examination given to my principles-of-economics students included this:

> *Discuss the following statement: When an economic function is turned over to the government, social cooperation invariably replaces self-interest as the motivation for human action.*

The proper answer to the question, of course, is that the statement is "false" and that redistributing control over property cannot change the underlying nature of human beings. In truth, "self-interest" remains an adequate term for describing human behavior, and it applies as much to government officials as it does to anyone else. If the demise of the Soviet system taught us anything, it is that communism will not reconstruct humanity and or usher in the "new man" who suddenly becomes only concerned about others.

I had chosen the question because one of the six chapters of our text covered on the exam dealt with the field of Public Choice, which analyzes these matters. I had also spent a significant amount of time in class discussing the essence of human action. I thought that the question was clear cut, and so I naïvely assumed that the majority of the class would easily answer it correctly. That was not to be. Only half the 50 students answered the question more or less correctly. The other half espoused a kind of incoherent Marxist dogma that would have suited the taste of not only Karl himself, but of Lenin, Stalin, and Mao as well.

Students Who Should Know Better

To put the situation into better perspective it is important to understand my institution and the kind of students I teach. Birmingham Southern is a small, private liberal arts college that has gained a reasonable national reputation for quality education. In Alabama the college is considered the premiere school of higher learning of this type. As such, it attracts students of high caliber. Our students generally go on to graduate and professional schools and often do well in their careers. In addition to this, because it is a private college, the students are generally from middle-class or upper-middle-class backgrounds. Therefore, the majority would have received their lower education in some of the better public schools in the state, while a minority would have had private school education.

Given all this, it might be curious that my students did so poorly with the question. More surprising perhaps is that among the students who answered the question correctly, two were from other countries, the former Yugoslavia and China. It is interesting that

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these two young women who have firsthand knowledge of government control over the entire economy were able to discern the falsity of the statement I presented, while those reared in some of the best circumstances the United States has to offer could not.

As I pondered this, I came to a few conclusions. First, there is a real problem in education today. Students seem unwilling to accept a position purely on the basis of rational argument. My knowledge of political economy and the evidence I provided in class were not enough to persuade my students that human nature does not change because the government takes over something. At least half were apparently unwilling to relinquish their socialistic views despite the facts and arguments I had presented. This reminds me of Ben Franklin's statement, "Experience keeps a dear school, but the fool will learn in no other."

The second conclusion is that the government's socialized educational system has done an excellent job of propagandizing students into accepting socialistic dogma. Throughout the classroom presentations there was little debate and almost no discussion that might have allowed us to dispense with the myths of socialism. Yet it would appear that for the students none was necessary, for they felt no need to actually think about the issues themselves.

My final conclusion is that there is much work to be done in this country to teach people the nature and value of human freedom and private initiative. I am determined to step up my own efforts to engage my students in meaningful discourse so that they might see the falsehoods of socialism. Perhaps I am too pessimistic, for half the class did get the question right. But as a teacher, I am compelled to believe that that success rate is too low. □

IDEAS ON LIBERTY
APRIL 2000

The Price of Resistance

Consider this remarkable sentence in the *New York Times* last winter: "Brandishing new data showing that the drug industry earns higher profits and pays lower taxes than most other industries, White House officials say drug companies may bring price controls on themselves if they continue to resist President Clinton's plan to have Medicare provide pharmaceutical benefits." This was said to be the "personal view" of Daniel N. Mendelson, associate director of President Clinton's Office of Management and Budget. Yet Mendelson was speaking for the President.

What does it mean to say that the pharmaceutical companies "resist" President Clinton's plan? If the companies have launched a guerrilla war against the government, the newspapers have missed the story. So I presume the resistance consists of speech, printed materials, and lobbying—all protected by the U.S. Constitution (not to mention the philosophy of natural rights) at last check.

The administration, then, is saying that if the companies continue peacefully to oppose its plan, they will lose their freedom to set the prices of their products. That's a tough choice: the freedom to speak in defense of their freedom or the freedom to control their property. Unfortunately, the companies dropped their opposition. Where was the bellow of protest from the "civil libertarians"?

Ironically, the plan being resisted would bring price controls anyway. Under the proposed Medicare expansion, the federal government would become the buyer of the elderly's prescription drugs. Anyone who thinks that wouldn't give the government the power to set prices hasn't thought about the matter. The feds may not control prices immediately, but when the inevitable price spiral sets in, as the elderly act as if the drugs are free (or cheap), price controls will be the next stage. That's what happened with Medicare. At first the government did not set prices. The system operated on a cost-plus basis. But when prices soared, the government started a series of price-control schemes. It's one reason that doctors are increasingly reluctant to see Medicare patients.

Economic theory and at least 4,000 years of experience with price ceilings lead to one inescapable conclusion: they create shortages. To understand this, we have to begin with the principle that prices in a market are not the result of businessmen's kindness or callousness. While capitalists own their means of production in the moral-legal sense, economically speaking they hold them at the pleasure of consumers. Although business owners typically seek to maximize their revenues, and set prices accordingly, their decisions are subject to the preferences, needs, tastes, and whims of potential buyers, who are constantly being wooed by sellers of competing products. (See my article "Captain Consumer" in *The Freeman,* February 1999.)

Thus entrepreneurs are limited by the competitive process in what they can charge for their products. If the market price for a product is too low to enable an entrepreneur to bid

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the necessary scarce resources (labor, raw materials, and so on) away from other uses, that's a signal that consumers want the resources devoted to other purposes. But if consumers are willing to pay a price that covers the entrepreneur's expenses and yields an attractive profit, they are signaling that the project is worthwhile compared to alternatives. Profits are the rewards the entrepreneur reaps by noticing hitherto unattended-to consumer needs: the higher the profits, the bigger the previous oversight.

If the government imposes a maximum price on a product below what the market would set, producers will make less of it or none at all. Moreover, the quality will suffer, as producers minimize expenses beyond the point they would have minimized them in a free market. (Milton Friedman used to say that under price controls, there's more air in the candy bars.) And entrepreneurs will be discouraged from looking for new profit opportunities in fields where prices are subject to government control. Businessmen will surely not be encouraged to take risks developing cutting-edge products like exotic medicines.

This is not "only a theory." Anyone who lived through the energy shortages of the 1970s has firsthand experience of how a product can disappear when government refuses to let the market set prices.

Market for Medicine

The market for prescription medicines is intrinsically no different from other markets. Entrepreneurs strive for profits by making investments to develop products that consumers believe will satisfy a need. This is complicated by government prescription regulations—a paternalist intervention that should be abolished—but the economics are basically the same. (The President's wish to crack down on Internet sales of medicine shows how technology can help us to ignore government dinosaurs.) There is another complication, however. The Food and Drug Administration's bureaucratic demands greatly increase the cost of bringing drugs to market. Naturally, the companies try to recoup that investment. A genuine concern with the high price of medicine would begin with an examination of the FDA's malign effect on the marketplace.

But, someone will say, people *need* medicine. Unlike food, clothing, and shelter? But even if medicine were unique, it would not change the fact that price ceilings make things *less*, not more, accessible. Motives notwithstanding, the laws of economics can't be repealed.

It is particularly outrageous for the Clinton administration to hold the pharmaceutical industry's high profits and low taxes against it. As noted, if profits are high, it is because the companies are constantly addressing urgent consumer needs and cutting costs. (I leave aside the issue of patents and the returns they make possible. Suffice it to say that the administration favors intellectual property rights in other contexts.) The industry's taxes are lower than in other industries because the tax rules allow credits for research and for taxes paid to foreign governments. If the authorities think it is unfair that the industry pays less in taxes than other industries do, let them lower the taxes of the others. Taxes stifle production.

If the government is really concerned about the price of medical care, it should look to its own complex of policies that stimulate demand and reduce supply. Medicare is a prime culprit but not the only one. The tax-induced system of employer-based health insurance seriously distorts the medical marketplace by hiding prices from consumers. Licensure and control over medical schools restrict the supply of medical services.

We shouldn't overlook the possibility that price controls on medicine may be intended to disrupt the pharmaceutical industry and offer the government new opportunities to intervene. Ever since the Clinton health plan was turned back, advocates of socialized medicine have pursued incremental socialization, knowing that the harm of each measure would provide grounds for the next increment. □

IDEAS ON LIBERTY
APRIL 2000

Economic Growth and Freedom in the Coming Millennium

by Christopher Lingle

There are many reasons to believe that the year 2000 will usher in a period of rising living standards and greater overall freedom. This positive outlook is supported by the experience of emerging economies in Asia and Latin America, as well as the transition economies escaping from the disasters of authoritarian socialism and communism.

What has been learned is that globalization has been the most effective liberalizing process in the history of mankind. Such a claim might cause Karl Marx to roll over in his grave and induce apoplexy in his diehard disciples. But history speaks for itself. International capital flows and greater trade integration over the past three decades have lifted nearly half a billion people out of poverty, mostly in Asia.

Global trade and capital flows are forcing governments to be more accountable to their people, who wish nothing more than to be able to prosper. Where markets are most open, the productive instincts of their people have been unleashed, allowing entrepreneurs to create wealth and new jobs. Despotic governments in Indonesia and much of Latin America have given way to more democratic leadership that is embracing the formula of market economics.

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Skeptics should note that globalization is a phenomenon that empowers people by giving them another voice. In some settings a vote is of little use, especially in one-party states. For some there is the option to migrate, or "vote with their feet." But only the best educated, the healthy, or the wealthy are normally able to emigrate. With fully liberalized financial systems, all citizens can "vote" by moving their savings or capital assets into the most attractive currency or country. As such, global capital provides another way for citizens to communicate their preferences to their leaders.

But some governments, such as in China, seek to introduce market reforms while holding back political reforms. Time will tell whether this is a disastrous course. There are those who insist that China's approach to reform has been more successful than Russia's. But this assessment is likely to be reversed within a decade or perhaps less.

Russia can be expected to make considerably more progress toward prosperity while China begins to lag behind. This is because leaders in Moscow have reached a point where they must begin providing institutional structures to pull out of a deep economic malaise. To become integrated into the global economy Russia must introduce (at last!) private property rights and a system of law to enforce them. Abiding by the rule of law under the eyes of an independent judiciary will provide support for a "contract culture" that is the basis of modern market-based economies.

In the case of China, there are two entrenched "institutions"—the People's Liberation Army and the Communist Party—and these are unlikely to give up their obstructive powers. China's biggest problems are the entrenched inefficiencies and distortions introduced by central planning.

Unrest in China

Heavy industry in China's economy is mostly state-owned and highly inefficient. These factories receive funds from state banks that are disguised as loans. As a result, nonperforming loans are at least one-fourth of all loans. If this continues, there will be a banking crisis and social unrest. However, if the loans cease, there will be a social crisis from the massive numbers of workers who will be made redundant—and social unrest. Avenues of escape from impending social turmoil have been cut off by a decrease in export growth, declining inflows of foreign capital, and a slowdown in economic growth.

Although China's people are likely to suffer, the expansion of economic freedom as the basis of promoting political freedom elsewhere will continue. As there is a shift from centralized or authoritarian economies toward free markets, individuals will react to changing incentives to work and earn profits. These growing private initiatives will stimulate economic growth and raise living standards.

Many emerging economies offer relatively low wages relative to education levels as well as a strong work ethic. (With its high literacy rate, watch Cuba become the Hong Kong of the Caribbean when the chains of Castro's communism are cast off!) An increasingly open global trading system will allow more rapid technology transfers while free capital movements will aid in economic development. As the incomes of the emerging economies rise, they will become a source of export income for more developed economies in North America and Europe. At the same time, they will be able to increase their own savings and provide a domestic source of capital that will also increase efficiency of international markets, driving down the cost of capital.

While there will be adjustment costs, there will be considerably more benefits accruing to most people in most countries. Most of the losers will be workers or owners of previously protected industries whose privileges cost consumers in the form of higher prices and robbed jobs from newcomers to the labor market. It is only just that the few who imposed so many costs on so many should be the ones to bear the greatest burden.

A lesson of globalization is that protectionism is wrong not so much for the economic distortions and technical inefficiencies that it has always caused. Rather, protections for domestic industries are immoral because they steal job opportunities from the young by reducing growth potential and innovation. Future generations will have more hope if there are fewer restrictions on trade and capital flows, for that is what will create more opportunities in their future. □

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IDEAS ON LIBERTY
APRIL 2000

Drifting In and Out of Socialism: The Case of Ireland

by James L. Payne

National economic policy is generally thought to be set through an intellectual battle over social philosophy. Collectivists, with their ideology of greater government control, oppose individualists, with an equally comprehensive theory of limited government—and a nation's level of taxation, regulation, and government ownership is assumed to reflect the relative strength of these contending forces.

This model has tended to fit England and the United States, which have had a recognizable "left" and "right" in their politics. In most countries of the world, however, ideology does not play such a significant role. Politicians and parties are pragmatic, and government interventions have been adopted not to implement an overall philosophy, but through a day-to-day process of accommodation. And the movement in the other direction, toward less state control, is equally pragmatic. The politicians make what they think are reasonable ad hoc adjustments, without reference to theory or philosophy.

Ireland is a good example of a country with this kind of non-ideological politics. It has not had a meaningful left and right. Over the past century it has adopted socialist policies not because parties and leaders were convinced socialists (most of them were said to be "conservatives"), but because such policies were superficially appealing. In recent years, it has moved somewhat away from these policies and toward the principles of the free market. But this shift has not been the result of any party, faction, or pressure group.

So far as I could detect in weeks of searching, there are no prominent Irish think tanks espousing the cause of limited government. There are no politicians with an underlying skepticism of government action, no talk-radio hosts critical of big government, no one who questions government welfare programs on principle. Names like Hayek and Mises, or for that matter, Jefferson, Thoreau, and Paine, are unknown in Ireland. Practically everyone accepts the general notion that government should be comprehensively involved in national life.

Yet despite this overwhelming pro-government sentiment, and despite the lack of anti-government voices, there is a clear drift against government ownership and control in Ireland! This remarkable tendency cries out for explanation, especially since it is not unique. Many countries with a strongly left-leaning public opinion are nevertheless moving away from systems of government control. They haven't reached anything like a genuine limited government, of course, yet the trend is significant.

The Potato Famine and the Guilt of Empire

The roots of pro-government sentiment in Ireland reach back many centuries. As an English colony from the days of Henry VIII,

Contributing editor James Payne recently returned from a stay in Ireland.

Ireland did not have the opportunity to develop strong traditions of self-government and self-reliance. The tendency was to look to the colonial government in England to solve problems. The potato blight and famine of 1845–49 greatly exacerbated that tendency. Although England did send considerable food relief, it was not enough to prevent widespread suffering. For the rest of the century, English elites felt guilty about not having done enough for Ireland, and they instituted numerous relief and assistance schemes that, in their own country, would have been seen as unacceptably intrusive. Their policies included expropriations of lands (which were then practically given away to Irish tenants), and the development of numerous systems of public relief and subsidies. The result was that the Irish developed, as historian Mary Daly puts it, "a strong dependence on government assistance for everything from famine relief to land reform."

After independence in 1921, the new Irish government took the same paternalistic role, especially under the leadership of Eamon de Valera in the period 1932–48. Motivated by nationalistic and anti-British sentiments, de Valera tried to create a self-sufficient Ireland. To that end he jacked up protective tariffs and prohibited foreign ownership of industry. With investors scared off, de Valera and his Fianna Fail party began creating government firms to fill apparent gaps in the economy. Later, as misguided economic policies put increasing pressure on private firms, the government stepped in to take them over when they went bankrupt. By the 1970s the government owned some 100 entities, including a steel company, a peat-processing firm, banks, and the telephone service.

Undoing this centralized, government-directed economy has been a slow, halting process, but the overall trend is now clear. The first steps of liberalization were taken in the 1960s when tariffs were sharply reduced and the prohibitions against foreign firms were lifted. In fact, foreign firms were given tax breaks to set up in Ireland. Crushing tax burdens were somewhat reduced in the 1980s, when the top income tax rate was lowered from 60 to 48 percent. The 1990s have seen a number of government firms turned over to private ownership, including steel, telephones, and the airline company (Aer Lingus). Competition between government firms and private ones has been introduced in a number of sectors, including banking, parcel delivery, bus transportation, radio, and television. Overall, the relative size of the government sector has declined somewhat from its peak about 20 years ago. In 1980, government expenditures were 50.5 percent of GDP; in 1997 they had fallen to 40.3 percent. In the period 1988–98, as a result of privatization and cutbacks in subsidies, employment in government commercial entities fell by 19.6 percent.

The Rise of Analysis

One important explanation for this movement away from government control has been the rise of economic measurement and calculation. Cost-benefit analysis is the nemesis of socialism. Any number of government schemes can look attractive when you don't know the numbers behind them. At first glance, a government firm like Ireland's Bord na Mona—the peat authority—looks like a wise and humane undertaking. It digs up peat, which is used to warm homes and generate electricity, and at the same time gives work to people in areas of high unemployment. It is only after you call in the fellows with the green eyeshades that you discover the waste and harm of such entities. By adding up the (generally unnoticed) costs, they reveal that Bord na Mona can survive only through a huge tax subsidy. If that same amount of money were spent on cheap coal and more useful employment, Ireland would have more jobs and cheaper electricity.

It is only recently that Ireland has developed capabilities to analyze and evaluate government programs. Perhaps the first unit to work in this field was the Irish Economic and Social Research Institute, a nonprofit think tank started in 1960 with help from the Ford Foundation. In 1973 the government set up its own evaluation unit, the National Economic and Social Council, while other analytical units have sprung up in the Department of Finance,

Since 1961, there has been a 50 percent reduction of families living in government housing, and today over 80 percent of Irish housing is owner-occupied.

the Central Bank, and in connection with the universities. The agencies of the European Union, to which Ireland belongs, constitute another source of economic analysis. None of these entities can be classified as ideologically favoring free markets, but their studies of the costs and inefficiencies of government enterprises have had a strong effect in nudging policymakers toward market approaches.

In housing, for example, the introduction of accounting methods and cost-benefit analysis has revolutionized government policy. Earlier, local authorities built and rented housing simply as one of those nice things that government could do to help people. Then analysts began to make economic and budgetary studies of housing programs. These revealed that maintenance and management costs of government housing were so high that the government would come out ahead if it just gave its houses away to the tenants! The findings prompted authorities—always hard-pressed for cash—to institute programs to enable tenants to buy their dwellings on highly favorable terms (usually at 50 percent of their market value). The overall result has been a major decrease in government involvement in housing. Since 1961, there has been a 50 percent reduction of families living in government housing, and today over 80 percent of Irish housing is owner-occupied. This is just one of many instances where the new awareness of economic realities has led politicians toward private solutions.

How Happy a Family?

The second force that seems to be pushing Irish policymakers away from government alternatives is the desire to avoid conflict.

The doctrines of collectivism tend to see a nation as one big happy family, with the government acting as the father, taking "from each according to ability," and giving "to each according to need." Unfortunately, this vision contains two fallacies. First, it assumes that the citizen-children will respect the government-father who is doling out the benefits. Today, this condition of public respect is not met in any country. In Ireland, when people are asked what they think about their politicians, most wriggle their noses and call them "gangsters"—not violent gangsters, they hasten to point out, but thieving ones. (A recent string of corruption scandals involving the highest officials has strongly reinforced this view.) Hence, people do not believe that the officials who determine benefits act with justice or integrity. No matter what the policy decision is, it is viewed with cynicism and hostility.

The second error in the "one big happy family" view is that it overlooks the tendency of human beings to squabble about what they need and deserve. Even in families, children make resentful comparisons: "Johnny's balloon is bigger than mine"; "Ellen gets to stay up later than I do"; and so on. In a national community where people are free to form pressure groups and to air and inflame grievances, social spatting becomes a major problem. When you make government the arbiter of benefits and privileges, the politicians and administrators become the "bad guys" who stand between each group and what it believes it deserves. Naturally, this is a role they do not enjoy, and therefore they seek ways to escape it. One solution is to turn the problem of deciding who gets what over to the free market.

Consider government housing projects. According to socialist ideology, the occupants are supposed to be grateful and content. But real-world beneficiaries turn out to be grasping and impatient. They are upset by inadequate facilities and irritated by poor maintenance. Furthermore, they generally think that their rents, even though subsidized by taxpayers, are too high. Eventually, politicians who thought they would earn adulation and votes by providing public housing realize this involvement is making them objects of abuse. They begin to see the wisdom of moving out of the housing business. Ireland saw a great deal of tenant-government friction in state housing units: angry demonstrations, as well as a prolonged strike by the National Association of Tenants' Organizations in 1973. The politicians' desire to avoid this animosity was, I believe, another important motive for privatizing government housing.

In October 1999, the country saw more social conflict caused by economic centralization. The occasion was perhaps a welfare state's worst nightmare: a nationwide strike of nurses. After all, when government takes over the health-care system, as it largely has in Ireland, it does so in the name of guaranteeing medical care for everyone. When the nurses walked out of the government hospitals around the country, they left unattended children crying in the wards and cancer patients without their chemotherapy. Parents, doctors, and hospital administrators struggled to fill the gaps but with only partial success. In one psychiatric ward, an unattended young woman committed suicide.

The public sided overwhelmingly with the nurses and against the government, which was criticized not only for underpaying the nurses, but also for underfunding the entire health-care system. (One consequence of the funding shortfall is that waiting times for many operations are over two years.) The cabinet members, for their part, had no desire to appear stingy and certainly didn't want the nurses to strike. But they were constrained by the problem of "tit for tat" wage demands. As the employer of many other groups of workers, the government had negotiated a general wage-restraint package with all of them. If it broke the agreement and boosted the pay of the nurses, then, as one columnist explained, "everyone else will be looking for more. . . . Paramedics, junior doctors, teachers, the army, and the guardai [police] have all been circling this dispute waiting to pounce."

The position of paramedics was an especially sore point with the nurses. The nurses believed they should be given the same pay and benefits because they had the same qualifications and responsibility. "We've been doormats for too long," one nurse told a reporter. "Now it's time we got fair recognition for our work." But the paramedics, with a union even bigger than that of the nurses, had had a strike in 1997 to boost their compensation above that of nurses. It was clear that they would not allow nurses to catch up.

In the end, the strike hurt everyone. After eight days, the nurses grudgingly went back to work, accepting a compromise offer from the government. They were both embarrassed and bitter at having been forced to deny the high ideals of their profession—caring for the sick—to make their demands heard. Relations with hospital colleagues deteriorated. The doctors, who had been forced to cover for the nurses, condemned them for leaving patients in the lurch. Opinion polls showed that government leaders had lost support. Calling them "greedy and corrupt," one letter writer to the *Irish Times* concluded, "If patients die, it's the politicians who kill them." The minister of health, Brian Cowan, was especially singled out for criticism. One of the striking nurses' favorite picket-line placards said, "Help Stop Mad Cowan Disease." For the minister, who certainly hoped that a career in politics would bring him approbation if not glory, this could not have been pleasant.

No Solution

In a centralized government health-care system, there is no solution to this problem of strife. The government is always in the position of determining the relative rewards of different groups of employees and deciding which services to give different groups of customers. All these groups will hold it responsible for every shortcoming, real and imagined.

It is significant to note that private hospitals (with 16 percent of all beds) remained open during the strike. Some said this was unfair, that nurses should have struck these hospitals too, so their patients would suffer equally with patients in the government hospitals. But since these hospitals were willing to pay nurses more, the nurses could hardly close them down out of socialist spite. The success of the private hospitals in bypassing the dispute inspired one columnist—Ellis O'Hanion of the *Irish Independent*—to spot the free-market solution to destructive conflict in the health-care industry. "Perhaps it's time," he wrote, "to start exploring the possibility of privatizing the health service in its entirety. This would instantly take all decisions on nurses' pay out of the political arena. Competition between various sectors of a privatized industry for the best staff would ensure that nurses' pay found its natural level."

The politicians are unlikely to take this advice immediately, there being too many socialist shibboleths to be overcome. But gradually the system is likely to head in this direction. As strikes, bickering, funding shortages, and waiting lists make government hospitals increasingly unattractive, both patients and staff will continue to migrate to systems of private care. Politicians are likely to allow this movement, and even facilitate it, as a way of shedding the blame for health-care problems.

There may be no partisans of limited government in Ireland, but that doesn't mean government's role won't be reduced. People don't like to waste resources, and they don't like conflict and bitterness. These pressures would seem to lead, in the long run, to scaling back government systems of economic and social management. □

Economics

The Economic Advantages of a Commitment to Liberty

In my last column I discussed the bias toward excessive government caused by the dead-weight costs of taxation. Because these costs go unseen, while the benefits from government spending are readily apparent, government expands beyond reasonable limits.

Unfortunately, the unseen cost of taxation is only one factor pushing for too much government. Much of the cost of government is in lost liberty—decisions on how we live our lives are increasingly made by government authorities. And just as with the dead-weight costs of taxation, the costs of gradually losing our liberties go largely unseen. On the other hand, benefits (typically temporary and small) from restricting liberty are easily seen. The result is a political bias that steadily erodes our liberty. Pragmatic politics, free of ideological considerations, with each issue decided solely on its perceived costs and benefits, gives free rein to this bias against liberty. Only with a genuine ideological commitment to liberty, one that creates serious obstacles to all proposals for sacrificing it to some public objective, can we halt, and hopefully reverse, the erosion.

The Hidden Cost of Restricting Liberty

All government actions, whether taxing income, restricting imports, controlling prices, regulating businesses, or subsidizing agricultural production, reduce our liberty to some degree. Of course, some restrictions are necessary for maintaining the social order on which other liberties depend. Traffic laws, sanctions against criminal activity, and the requirement to pay enough taxes to defend our borders come to mind. However, beyond some minimum level the loss of liberty begins imposing costs without offsetting social benefits.

But even when a government restriction on liberty imposes large net costs on society, it still creates benefits commonly captured by a relative few. An example is an import restriction, which concentrates benefits on those in the protected industry by restricting consumers from buying from those who offer them the best deal. As discussed in earlier columns, consumers lose far more than those in the protected industry gain. But because the reduction in liberty spreads cost over all consumers, the political process easily overlooks it. Likewise, government regulations that restrict people from going into certain occupations are advertised as necessary to protect consumers from the unqualified. Yet these restrictions reduce the competition faced by existing members of the protected occupation (who lobby for the restrictions), with the benefits they receive more than offset by the costs to those whose freedoms are restricted. But again, the costs are widely spread and largely unnoticed.

The costs of restricting our liberties are easily ignored not only because they are spread widely over the general public, but also

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because they are indirect and delayed. Often the greatest advantage we realize from freedom is its availability to others. For example, only a relatively few people will choose to become entrepreneurs. But most of the benefits from entrepreneurial freedom take the form of better products and lower prices for untold millions of consumers who will never start companies themselves. As F. A. Hayek observed, "The benefits I derive from freedom are thus largely the uses of freedom by others, and mostly of the uses of freedom that I could never avail myself of."[1] So most of those harmed by the erosion of a freedom will notice no additional restriction on their own freedom and remain unaware of the harm they are suffering.

Also, freedom is vitally important because we have no idea how it will be used. No one can confidently predict the advances that will be made in the future if people are free to try things most would never consider trying. Quoting Hayek again, "If we knew how freedom would be used, the case for it would largely disappear."[2] So most of the cost of restricting freedom today will be doing without things we otherwise would have had tomorrow. The cost is not only delayed, but almost impossible to recognize when it does arrive because it comes as the absence of things we never knew we could have had.

Finally, our liberty is seldom lost all at once. Instead, it is nibbled away a little at a time. Supposedly, if you place a frog in a pan of water and heat it up gradually, the frog will remain in the water completely unaware of the increased temperature until it boils to death. Similarly, as our liberties are eroded slowly, one by one, we hardly notice the loss.

Commitment to Liberty

Because we overlook the costs of eroding liberties, the bias in favor of excessive government is more pronounced and harmful than indicated in previous discussions. Even if all the financial costs of expanding government were fully considered, there would still be too much government if the personal costs of restricting our liberties were ignored. Unfortunately, when government proposals are considered, many of the financial costs and almost all the costs of reduced liberty are politically ignored. The minor benefits to a few trump the far greater loss of the liberty by the many in case after case. Seldom does anyone oppose a particular program because it will erode our liberty; and when someone does, he is typically dismissed as an ideological crackpot. But unless we restore a broad and deeply felt ideological commitment to liberty in general, the value of the particular liberties lost to each government expansion will do nothing to retard that expansion, and our liberty will be surely and steadily sacrificed to the special-interest influence of ordinary politics.

Quite apart from the value of liberty as an end in itself, genuine commitment to liberty is essential for sound, long-run economic policy. The importance of freedom to the innovations and technological improvements on which all economic progress depends cannot be overemphasized. Consider that the national income of the U.S. economy is now a little over $8.5 trillion annually. If average economic growth is reduced from 2.5 to 2 percent per year because of liberties eliminated by government action, in 25 years the national income will be $1.81 trillion less per year than it would have been. That amounts to a loss of approximately $6,830 for every American, a loss that almost no one will notice and which would be difficult to connect to the erosion of liberty even if it is noticed. What will be noticed, and appreciated, are the benefits of particular government activities, even though the entire country is far worse off because of many of them.

The advantage of a commitment to liberty, with respect rather than ridicule accorded those who champion it, is that it would replace the political pragmatism of case-by-case considerations with an ideological rule of restraint that would better promote the long-term interests of all. The problem with political pragmatism is that it doesn't work, not if the objective is to serve the general interest. □

1. F. A. Hayek, *The Constitution of Liberty* (Chicago: University of Chicago Press, 1960), p. 32.
2. Ibid., p. 31.

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Food, Famine, and Free Trade

by Jim Peron

For decades population doomsayers have been predicting that massive famines were around the corner. Yet the United Nations Population Fund recently released its report "The State of the World's Population 1999," which says, "The world's population is healthier from infancy through old age than it ever has been."[1] In a press release the United Nations admits that "More people are being fed adequately today than ever before." In fact, "food production grew from the equivalent of 2,300 to 2,700 calories per person" between 1960 and 1991.

The Population Fund says this is because "Malthus's theory [of over-population] was overtaken by quantum leaps in agricultural technology which have kept food production ahead of population growth." In October 1999 the U.N.'s Food and Agriculture Organization said that during the period 1995–97 the raw number of hungry people was 790 million or 13 percent of the world's population. In 1970 the U.N. said that the number was 918 million, or one third of the world's population.[2]

The trends have been in this direction for years, but the doomsayers haven't changed their tune. While their dire predictions are repeatedly wrong, they have offered up new arguments. The grandfather of the population-bomb hysteria, Paul Ehrlich, even came up with a new definition for overpopulation:

> The key to understanding overpopulation is not population density but the numbers of people in an area relative to its resources and the capacity of the environment to sustain human activities; that is, to the area's carrying capacity. When is an area overpopulated? When its population can't be maintained without rapidly depleting nonrenewable resources (or converting renewable resources into nonrenewable ones) and without degrading the capacity of the environment to support the population. In short, if the long-term carrying capacity of an area is clearly being degraded by its current human occupants, that area is overpopulated.

Ehrlich adds, "By this standard the entire planet and virtually every nation is already vastly overpopulated."[3]

Ehrlich says we know an area is overpopulated when it is "rapidly depleting nonrenewable resources." But if a resource is being depleted, the price of the resource, all things constant, will rise. The way we know a resource is being depleted relative to demand is through increasing prices.

Ehrlich understood this at one time. In fact, his famous 1980 wager with the late Julian Simon was based on this fundamental economic principle. Ehrlich picked five resources that he said were being depleted and predict-

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ed that their prices would therefore increase. Simon said they would decline in price and thus, in economic terms, become more bountiful. After ten years every one of Ehrlich's choices had declined in price in real terms.

If, as Ehrlich says, resources are being depleted in virtually every country of the world, the most basic laws of economics have to be false. His conclusion can only be true if the depletion of resources somehow leads to a reduction in price.

Ehrlich also claims that a nation is overpopulated when it isn't self-sufficient. He uses the Netherlands as an example, arguing that since the Dutch import many products and resources, it is wrong to say that "the Netherlands is thriving with a density of 1,031 people per square mile . . . [because this] simply ignores that those 1,031 Dutch people far exceed the carrying capacity of that square mile." Thus, that the Dutch import beans proves that the Netherlands is overpopulated.[4]

Trade and Population

With this argument Ehrlich enters the twilight zone. Ehrlich ignores how the Dutch have access to the world's resources. Were the beans charitable donations given because the growers felt sorry for them? Or did the Dutch exchange something of value for the beans? Ehrlich ignores that trade is a two-way street.

The people of every nation trade with the people of nearly every other nation. We all import some things and export other things. Canadians imports bananas from Panama, and the Panamanians may in return purchase computers built in Canada. Does this mean the Canadians and Panamanians are exceeding the carrying capacities of their countries? Nations are not equally rich in resources just as people are not equally talented. Because of the uneven nature of talent and natural resources, we trade to improve our standard of living.

Nations specialize in much the same way that people do. You may live in a manufacturing community that produces a large number of shoes. It may import grain from communities that have a lot of grain but are short on shoes. According to Ehrlich, this is proof that your community is overpopulated. Thus a tiny farm community that produces enough corn to feed a small nation is considered overpopulated because it doesn't produce enough shoes for a handful of people.

Ehrlich seems to be condemning the division of labor. Yet, as Ludwig von Mises noted, the division of labor turns the self-sufficient man "into the social animal of which Aristotle spoke."[5] Hostility in a society or world with a division of labor (and resources) is more costly than in a world of self-sufficiency. A world that fails to meet Ehrlich's definition of "overpopulation" is a world more likely to go to war. As Mises wrote: "Self-sufficient farmers, who produce on their own farms everything that they and their families need, can make war on one another. But when a village divides into factions, with the smith on one side and the shoemaker on the other, one faction will have to suffer from want of shoes, and the other from want of tools and weapons."[6]

The very process of complex trade relationships that Ehrlich condemns is to a large degree responsible for the decrease in military conflicts. As the trade boundaries expanded people found it increasingly absurd to make war. Where village once made war on village, free trade meant they now benefited from each other's existence. They cooperated and prospered. Trade is a process where we discover the mutually beneficial relationships that exist between all peoples and all nations. The division of labor increases the level of productivity of each individual while encouraging voluntary, peaceful cooperation.

The world that Ehrlich yearns for would be a primitive one. By returning to a self-sufficient society without a division of labor, and thereby not "overpopulated," we would be returning to a time that predates even the dark ages. The mutually beneficial relations between regions and nations would degenerate. The worst kind of tribalism would arise once more.

Opposition to the division of labor and free trade would in fact create the very problems Ehrlich lays at the door of increasing populations: mass starvation.

While we humans are able to mitigate the disastrous cruelties of nature, we are not able to abolish them. We can reduce the death rate but not abolish death. We can increase food production but not abolish droughts or freezes. We are able to handle minor instances of drought or some freezes, but we will still suffer under severe, naturally occurring weather anomalies. In the past when a drought ravished a country the entire populace suffered. The destruction of crops meant mass starvation. Today when a drought hits the American midwest it hurts the farmers' bottom line and may slightly increase food prices for others, but nobody starves. This is so because most Americans are not farmers. The fact that most American people produce something other than food allows them to trade those products for food produced in countries or regions that aren't suffering drought. Because the American people aren't self-sufficient they don't suffer from famine. On the other hand, the bulk of Africans are peasant farmers producing the foods they consume. If drought hits, they starve. They don't have other goods and services to trade for food.

The division of labor coupled with free trade allows us to spread the risk of famine. Free trade is like an insurance policy that pools the risk among many individuals. It seems odd that so many people want coercive, mandatory social insurance and are opposed to this much fairer system. With free trade a nation receives the benefits of social insurance without the drawbacks of a coercive system.

The market solves the problem in several ways. First, it spreads the risk so that no one starves but everyone pays a bit more. The increased prices encourage people to consume less or purchase foods not in short supply. The increased prices also encourage increased production by farmers. The reduction in consumption is a short-term solution; increased production is a long-term solution. Anyone who is truly concerned about the plight of the world's hungry should be in the forefront to encourage the division of labor, free trade, and free markets. But the doomsayers are, in fact, proposing measures that increase the likelihood of famine.

Ehrlich forgets that in the economic realm man responds to incentives. Human behavior is not set in stone, but can go in many directions. When prices rise humans consume less. But because of Ehrlich's contempt for economics he can't understand, or refuses to understand, how economic incentives can change behavior. This is why he says, "overpopulation is defined by the animals that occupy the turf, behaving as they naturally behave, not by a hypothetical group that might be substituted for them."[7]

Sheep will graze a field until it is no longer able to sustain them. As they graze there is no change in the price of grass because sheep don't have a price system. They cannot plan for the future. To Ehrlich human beings are no different from sheep.

It should therefore come as no surprise that Ehrlich has not made one major correct prediction regarding resources, population, famine, and so on. Even psychics have better track records. □

1. "The State of the World's Population 1999" (New York: United Nations Population Fund), p. 19.
2. Associated Press, "Third-World Hunger Slightly Alleviated," *Business Day*, October 15, 1999, p. 2.
3. Paul and Anne Ehrlich, *The Population Explosion* (London: Arrow Books, 1990), p. 38.
4. Ibid., p. 39.
5. Ludwig von Mises, *Liberalism in the Classical Tradition* (Irvington-on-Hudson, N.Y. and San Francisco: Foundation for Economic Education and Cobden Press, 1985), p. 25.
6. Ibid., p. 25.
7. Ehrlich, p. 40.

IDEAS ON LIBERTY
April 2000

Free Trade and Flexible Markets

by Christopher Mayer

International trade plays a critical and often overlooked role in the prosperity of the world's economy. Imprudence on the part of governments can stifle growth and trigger painful unnecessary contractions. The Smoot-Hawley tariff of 1930 was a major cause of the Great Depression. Punishing protective tariff rates precipitated an international trade war that caused U.S. farmers to lose a third of their markets. Agricultural prices plummeted as those farmers were caught with a supply that exceeded domestic demand. Their debts became a tremendous burden. Many farmers went bankrupt. The banks that lent these farmers the money soon followed them into bankruptcy. This started a credit contraction that rippled back east to the banks that had lent money to the midwestern banks.

The Smoot-Hawley tariff was perhaps the most protectionist piece of legislation ever adopted in this country's history. While no such legislation currently appears on the horizon, that tariff should be a lesson for current policymakers, who seem to be forgetting the power of international trade. Witness the well-publicized and escalating trade war between the United States and the European Union, which originated over bananas and continues with the latest tussle occurring over beef. Since trade wars are really fought against oneself, all nations partaking in this nonsense are equally responsible and equally capable of ending the conflict by simply abandoning tariffs altogether. A tariff is, after all, a tax on domestic consumers.

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Ominous Signs

Other evidence of an emerging trade war can be seen in smaller sectors of the economy, like making men's suits. In "Is This How Tariffs Should Work?" *Investor's Business Daily* outlined the loss of jobs in the domestic tailored-clothing industry. The workforce in this industry has been cut in half in just under a decade from 58,000 to 30,000. Why? Because the United States imposed punishing tariffs on imported fabrics, often exceeding 30 percent. Canada smartly dropped its tariffs on imported fabrics entirely, and its suit makers are thriving. They've increased their exports to the United States 250 percent.

Here the shortsightedness of protectionism is evident. In its effort to save jobs in the textile industry, the government harmed domestic producers and consumers. You would think such stark evidence, and the broad-based support for a reduction or elimination of the tariff from suit makers and retailers, would dispose of the matter. Wrong. Instead, there is talk of slapping a big tariff on imported suits.

As *IBD* notes, "That, of course, would be self-defeating. No one wins a trade war. They only make matters worse. When a country fires a shot (a tariff created or increased), the targeted country responds in kind."

A futile, costly, and stupid policy once again seems to be the order of the day. The lessons of free trade need to be continually preached, because it's clear that the policy-makers don't get it.

They would do well to read Frederic Bastiat, who wrote, "Assume, if it amuses you, that foreigners flood our shores with all kinds of useful goods, without asking anything from us; even if our imports are infinite and our exports nothing, I defy you to prove to me that we should be the poorer for it."

Unfortunately, protectionism is among the most durable of economic sophisms. The arguments never change. Yet the lesson of free trade is so easy to learn. It is so basic, so fundamental to the nature of exchange; "so clear, so obvious, so indisputable," Ludwig von Mises wrote, "that its opponents were unable to advance any arguments against it that could not be immediately refuted as completely mistaken and absurd."

Constant Change

In a living, breathing economy, change is perhaps the only constant. Individuals' subjective valuations of goods and services, and of money itself, are like quicksilver. Market prices, therefore, adjust according to the demand for and the supply of a particular good. Prices also respond to the demand for and stock of money. An economy unable to adjust, to reconfigure labor and capital to yield the best results, is an economy likely to be highly unstable and fraught with persistent misallocation.

An example of the benefits of free trade and the virtues of economic flexibility is to be seen in Hickory, North Carolina. Certain traditional sectors of Hickory's economy—namely, the furniture, textile, and chemical industries—have been shrinking for many months as cheaper importers beat out domestic producers for market share. But Hickory is booming, and unemployment is at a 30-year low.

Why? Because of new fiber-optic cable plants, medical centers, semiconductor plants, and satellite manufacturing companies. While some may credit state incentives and education, I see the market economy doing exactly what it should be doing. The south has lost thousands of jobs in traditional industries such as textiles, chemicals, and paper. Those jobs tend to pay low wages and require few skills. But the south could not compete with cheaper foreign labor in these areas. So the capital in these industries migrated to where it would be more efficiently employed and new industries have taken advantage of a relatively well-educated labor force.

What government did *not* do is revealing. If protectionist policies had been followed, these new industries would likely never have come into being, and Hickory, emblematic of economic conditions in the bulk of the south, would have been on the front page for less favorable reasons, like unemployment and stagnation. Tariff protection would have perhaps ensured a longer life for the south's textile mills, but at what cost? Citizens would have been subsidizing textile mills and forgoing the benefits of cheaper textiles and the additional goods created by the new industries. These people would have been worse off. The new industries freely stand on their own merits in the competitive market.

Belief in markets requires some vision and faith. In a sense, what's happening in Hickory is a microcosm of what is going on throughout the country. Our economy is constantly shifting to serve consumers better. Think of how this country has shifted from farming to heavy manufacturing to financial services and technology. And the changes will continue.

Japanese Woes

The trouble in Japan illustrates the same point but in a different way. While Hickory is booming, Japan is mired in a slump of historic proportions. Unemployment is the highest since statistics have been kept—despite Japan's ingrained social pattern of lifetime employment. Or, more accurately, *because* of it. Japan's tale is one of inflexibility and of trying to overlay a matrix of rigidity and stability on a changing complex market economy.

Despite major economic distress, Japanese companies are reluctant to cut workers. This has the effect of choking off the development of new industries and stifling the shifting of workers to where consumers would want them. Instead, they remained trapped in industries that bleed with losses. The difficulty in letting workers go has a flip side: Japanese companies are reluctant to hire new workers.

Flexibility means change and, for some people, a sense of uneasiness. It means that we are not likely to stay in one job for 20 years and that we will have to upgrade our job skills continuously. However, change is inherent in the real world. The societies that have the most flexible economies are equipped to handle their changing needs. They will grow, prosper, and change, while those anchored by political chains or societal bonds will go through periods of struggle and suffering. □

CAPITAL LETTERS

Who Controls the Money?

To the Editor:

"It Just Ain't So!" by Richard Timberlake (December 1999) contains material errors that mislead readers. The Federal Reserve does not, as Professor Timberlake writes, have "monopoly power to increase or decrease the economy's stock of money." It is the banking system (of which the Fed is a component) that has that power. Most money is created by the banks, not the Fed.

Since 1950, of the approximately $6.4 trillion that has been created by the banking system, only about $500 billion was created by the Federal Reserve. People need to understand that the Congress has improperly delegated to the banks a power that the Congress does not have under our Constitution. We have, in effect, a statist monetary system that is at odds with the Constitution. To talk about the Fed having a money-creation monopoly clouds the issue.

Professor Timberlake is equally mistaken when he writes, "Federal Reserve policy is responsible for the quantity of money—cash and bank deposits—that all households and business firms have in their possession at any moment." Without getting into a deep discussion about this, the Federal Reserve is an influencer, not a controller. Its essential function is to stand ready to bail out the banking system if and when it gets into trouble.

Since Professor Timberlake is mistaken in his premises, he is equally mistaken in his conclusion: "By controlling the basic stock of money in the U.S. economy, Fed policy determines the level of prices." Simply put, "It just ain't so." This said, he is correct that the Fed does not control interest rates; it can only influence them.

—LARRY PARKS
Foundation for the Advancement of
Monetary Education
New York, N.Y.

Richard Timberlake responds:

When I wrote the "It Just Ain't So" explaining that the Federal Reserve System—in practice, the Federal Open Market Committee (FOMC)—could not raise interest rates, I could not also take the space to write a textbook on how commercial banks and the Federal Reserve System create money. I have already written that book.

First, the Fed is not "a component of the banking system." The Fed is *the* central bank, and despite the label "bank" is an institution fundamentally different from the banks in the fractional-reserve commercial banking system. The latter consists of some thousands of individual banking firms that operate to make a profit. The industry cannot and does not set policy or deliberately create money. Indeed, commercial bankers are renowned for believing and claiming that they do not create money. All the demand deposits they create are an unintentional by-product of their lending operations. Just as important, they do not initiate the creation of money. Only the Fed's FOMC can and does initiate changes in the monetary base that the commercial banks use to make new loans and investments. The FOMC carries out its policies deliberately, with an avowed policy goal.

Second, Congress has not "delegated powers to the banks." It has delegated unlimited (and unconstitutional) powers of money creation to the Federal Reserve System, which is not "a bank" in any functional sense of the word. It is a governmentally controlled institution that operates primarily for the benefit of the federal government. Only the policy-making central bank part of "the monetary system" is statist. If the Fed and all its trappings were obliterated, the commercial banking system still in existence would have no policymaking powers and no organization to create additional money. The stock of bank-created demand deposits would be fixed.

Third, the Fed's "essential function" is not "to bail out the banking system when it gets in trouble," as Parks alleges. (To assert that the Fed still has this anachronistic function is to admit that the Fed and the commercial banks are indeed different animals.) Far from it. Even though the Fed continues to hold this propaganda goody in front of the media and the public, its essential function is the creation of new base money by monetizing outstanding government securities—securities that the U.S. Treasury has issued and sold previously to finance federal government excesses. From this base-money creation the Fed realizes huge seigniorage profits—about $30 billion per year—for its government owners. The commercial "member" banks also get a pittance, perhaps $1 billion, for their "membership."

I will state my conclusion again in more detail in order to contradict the misinterpretations Parks introduces and to clarify my original statement: "By controlling [increases or decreases in] the basic stock of money in the U.S. economy, Fed policy determines the level of prices [and any change in direction the price level will take]." This statement does not deny that other real factors—production of goods and services, and the public's demand for cash—also influence the price level. Nonetheless, the Fed's control over the stock of money is of a magnitude and a means that can counteract or subordinate these other factors. The one thing lacking in Fed control over the monetary system is its ability to effect changes immediately. In other words, a substantial lag of months and even years exists between the Fed's immediate policy actions and their results on the economy. But that problem is another story.

The conclusion here is that Parks's criticism is a medley of conceptual and factual errors by someone who does not really understand the monetary system.

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What It Takes to Be an Objective Scholar

"It was the facts that changed my mind."
—JULIAN SIMON[1]

During the 1990s, we watched the Dow Jones Industrial Average increase fourfold and Nasdaq stocks tenfold. Yet there were well-known investment advisers—some of them my friends—who were bearish during the entire period, missing out on the greatest bull market in history.[2]

How is this possible? What kind of prejudices would keep an intelligent analyst from missing an overwhelming trend? In the financial business the key to success is a willingness to change your mind when you're wrong. Stubbornness can be financially ruinous. When a market goes against you, you should always ask, "What am I missing?"

Over the years, I've encountered three kinds of investment analysts: those who are always bullish; those who are always bearish; and those whose outlook depends on market conditions. I've found that the third type, the most flexible, are the most successful on Wall Street.

Confessions of a Gold-Bug Technician

A good friend of mine is a technical analyst who searches the movement of prices, volume, and other technical indicators to determine the direction of stocks and commodities. Most financial technicians are free of prejudices and will invest their money wherever they see a positive upward trend, and avoid (or sell short) markets that are seen in a downward trend. But my friend is a gold bug and no matter what the charts show, he somehow interprets them to suggest that gold is ready to reverse its downward trend and head back up. Equally, he always seems to think the stock market has peaked and is headed south. As a result, throughout the entire 1990s, he missed out on the great bull market on Wall Street and lost his shirt chasing gold stocks.

I also see this type of prejudice in the academic world. Some analysts are anti-market no matter what. Take, for example, Lester Brown, president of the Worldwatch Institute in Washington, D.C., who puts out the annual *State of the World* and other alarmist surveys and data. He gathers together all kinds of statistics and graphs showing a decline in our standard of living and the growing threat of population growth, environmental degradation, the spread of the AIDS virus, and so on. For example, despite clear evidence of sharply lower fertility rates in most nations, Brown concludes, "stabilizing population may be the most difficult challenge of all."[3]

Too bad Julian Simon, the late professor of economics at the University of Maryland, is no longer around to dispute Brown and the

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environmental doomsdayers. Simon was as optimistic about the world as Brown is pessimistic. Simon's last survey of world economic conditions, *The State of Humanity*, was published in 1995. That book, along with his *The Ultimate Resource* (and its second edition), came to the exact opposite of Brown's conclusions. "Our species is better off in just about every measurable material way."[4]

Yet Julian Simon was not simply a Pollyanna optimist. He let the facts affect his thinking. In the 1960s, Simon was deeply worried about population and nuclear war, just like Lester Brown, Paul Ehrlich, and their colleagues. But Simon changed his mind after investigating and discovering that "the available empirical data did not support that theory."[5]

Scholars Who See the Light

The best scholars are those willing to change their minds after looking at the data or discovering a new principle. They admit their mistakes when they have been proven wrong. You don't see it happen often, though. Once a scholar has built a reputation around a certain point of view and has published books and articles on his pet theory, it's almost impossible to recant. This propensity applies to scholars across the political spectrum.

We admire those rare intellectuals who are honest enough to admit that their past views were wrong. For example, when New York historian Richard Gid Powers began his history of the anticommunist movement, his attitude was pejorative. He had previously written a highly negative book on J. Edgar Hoover, *Secrecy and Power*. Yet after several years of painstaking research, he changed his mind: "Writing this book radically altered my view of American anticommunism. I began with the idea that anticommunism displayed America at its worst, but I came to see in anticommunism America at its best."[6] That's my kind of scholar. □

1. Julian L. Simon, *The Ultimate Resource 2* (Princeton, N.J.: Princeton University Press, 1996), preface.
2. See the revealing article, "Down and Out on Wall Street," *New York Times*, Money & Business Section, Sunday, December 26, 1999.
3. Lester R. Brown, Gary Gardner, and Brian Halweil, *Beyond Malthus* (New York: Norton, 1999), p. 30.
4. Julian L. Simon, *The State of Humanity* (Cambridge, Mass.: Blackwell, 1995), p. 1.
5. Simon, *The Ultimate Resource 2*, preface.
6. Richard Gid Powers, *Not Without Honor: The History of American Anticommunism* (Free Press, 1996), p. 503.

BOOKS

The Stakeholder Society

by Bruce Ackerman and Anne Alstott

Yale University Press • 1999 • 296 pages • $26.00

Reviewed by Charles W. Baird

This book amounts to nothing more than a new version of how to take wealth from some and give it to others in the name of "social justice." Its principal theme is that Jefferson's proclamation in the Declaration of Independence of equality and freedom of all people cannot be realized in the United States because of the wide disparities in wealth and income that naturally occur in a market economy.

The authors, professors of law at Yale, complain that there can be no true "equality of opportunity" when the children of parents with high incomes have "unjust privileges" of family, environment, and education that enable them to speak "fluent and standard English," attend "elite private schools or a prosperous high school in the suburbs," and be "surrounded with eager guides to the skills of social advancement and the mysteries of college education." Because children of the not-so-wealthy and poor do not have those advantages, Ackerman and Alstott lament, they do not have "equal opportunity."

To address that timeworn complaint, the authors propose to give every American a one-time "stake" of $80,000 on entering college or reaching the age of 21. Subsidies resume later in life with a $670 per month "citizen pension" on reaching 67. The latter handout is supposedly justified because everyone has "a right to a dignified retirement" irrespective of work history and financial preparation. Those welfare measures will, the authors assert, build a strong sense of "community" needed to counteract excessive individualism. Americans, they say, suffer from an "infatuation with individual rights."

Naturally all this largess must be paid for, and the authors advocate two wealth taxes that they call a "trusteeship tax" and a "privilege tax." The "trusteeship tax" would be used to pay for the $80,000 "stakes" and would be raised or lowered enough each year to guarantee that enough money would be in the "stakeholder" fund to pay everyone who becomes "entitled." The "privilege tax" would "require each American to pay a tax based on the degree of privilege that she enjoyed during her childhood." Privilege would be measured by "the amount of money that his parents earn while he is growing up." (Besides their financial egalitarianism, the authors insist on equal treatment for pronouns!)

To keep "too much" wealth from accumulating in any private hands, they also call for a tremendous reduction in the lifetime tax exemption on gifts, from the present $650,000 to $50,000. And to make sure that money doesn't escape their tax net, they advocate a limit of $1,000 per recipient per year for holiday and birthday gifts. Imagine a solemn IRS agent saying, "Grandpa, you can't give Johnny that tricycle—it puts you over the annual gift limit."

Our brave redistributionists issue this stirring cry, "Against the cynicism of the age, we are not embarrassed to announce our message: by the taxes they pay as well as the stakes they receive, Americans should be prepared to reaffirm their common commitment to economic citizenship as an enduring aspect of a revitalized political identity."

So if you had been wondering if leftists still wrote books laying out new plans for society according to their grand visions, the answer is yes. *The Stakeholder Society* reaffirms Hayek's point that the lessons of sound economic reasoning must be relearned in every generation. Absurd plans like this have been advanced many times before and intellectually demolished, but we cannot rest.

Ackerman and Alstott assert that their scheme promotes "social justice," freedom, and respect for private property. However, as Hayek forcefully argued, social justice is a nonsensical mirage. Moreover, freedom does not come from government handouts, but entails the absence of government interference with your life. And respect for private property could hardly be encouraged by the incessant involuntary transfers of wealth that their plan necessitates.

Most of all, the authors are badly confused about equality. They are hung up on the term "equality of opportunity." Jefferson's "equality" in the Declaration is, of course, what Hayek called *isonomia*—equality before the law. Philosopher Robert Nozick called it *process* equality, which he carefully distinguished from *end-state* equality. The authors pursue the latter of those mutually exclusive concepts.

There's a lesson here. Classical liberals sometimes carelessly misrepresent *isonomia* as "equality of opportunity." But given the unavoidable differences in the means available to families as they bring up their children, true equality of opportunity is a chimera. Ackerman and Alstott exploit the ambiguity surrounding equality of opportunity to sell their version of collectivist redistribution while claiming to represent the middle ground between libertarianism and utilitarianism. Classical liberal arguments based on "equal opportunity" are vulnerable to such exploitation. The words we use to express our ideas, as well as the ideas themselves, have consequences. □

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Unpaid Professionals: Commercialism and Conflict in Big-Time College Sports

by Andrew Zimbalist

Princeton University Press • 1999 • 252 pages • $24.00

Reviewed by George C. Leef

Turn on your television set almost any Saturday afternoon from September to March and the chances are pretty good that you will be able to find a college football or basketball game. You'll see a lot of color and excitement. Dazzling athletic feats performed in a state-of-the-art facility before thousands of cheering fans.

That, of course, is the bright face that college sports always wants people to see. There is, however, a darker side that is rarely seen except by those who pierce the glitzy exterior. Andrew Zimbalist, professor of economics at Smith College and a long-time student of college sports, has done exactly that in his new book, *Unpaid Professionals*. It is worth reading even if you are not a sports fan; it may spoil some of the fun if you are.

Among collegiate sports powerhouses, the concept of the "student-athlete" has long been something of a joke. Well back into the 1800s, Zimbalist notes, colleges were using mercenaries to improve their chances of beating rivals, claiming that they were students when in fact they were not. Things are not much different today, except that the pretend students are actually enrolled and soak up money (ultimately taken from taxpayers in most instances) all year long, rather than just on game day. Many take courses with no intellectual content so they can maintain the minimum grade point average and leave college (usually without a diploma) as dull as the day they entered.

People and institutions respond to incentives, and there are big bucks to be had in winning in college sports—at least football and basketball. Schools seldom resist the temptation to build successful teams by letting academic standards slide. Zimbalist writes, "[M]any NCAA schools find the temptations of success too alluring to worry about the rules. Schools cheat. They cheat by arranging to help their prospective athletes pass standardized tests. They cheat by providing illegal payments to their recruits. They cheat by setting up rinky-dink curricula so their athletes can stay qualified. And when one school cheats, others feel compelled to do the same."

There is a lot of evidence that the athletic tail is wagging the academic dog, and Zimbalist provides his readers with interesting facts such as these:

- The University of North Carolina gives more than $3 million in athletic scholarships yearly to around 700 athletes, but only some $600,000 in academic merit scholarships among the rest of its 15,000 students.

• Clemson University paid young black men from Columbia, South Carolina, to be on campus and pretend to be members of a black fraternity so the university would look more appealing to visiting black athletes.

• The president of the University of Oklahoma said in a speech to the state legislature, "I hope to build a university of which our football team can be proud."

Unlike some writers who shed crocodile tears over the supposedly exploited college athlete, Zimbalist doesn't think their plight so bad. "Full scholarship rides, special eating and housing privileges, the right to carry Pell Grants on top of their scholarship, to receive several hundred dollars a year in special needs support, and preferential access to summer jobs are all adequate remuneration. Yes, there are star players who may generate a half-million dollars of revenue or more for their teams, but many of these stars will soon earn millions in the pros and they can leave anytime they like."

Defenders of the sports system often claim that the "big-time" sports of football and basketball generate profits for the rest of the athletic department, but Zimbalist is skeptical. He observes that there is no set of uniform accounting rules for college athletics and the defenders can therefore get away with absurdities like this: The University of Massachusetts basketball team supposedly made a $1.78 million profit in 1997, but examination of its budget shows that the basketball team was charged with none of the cost for, among other things, insurance, maintenance, advertising, utilities, medical expenses, or debt service on the arena in which the team plays its home games. With a conservative cost allocation, Zimbalist thinks that the team actually lost around $1.1 million.

Although the book contains much that supports a free-market critique of the college sports system, the author doesn't explicitly make one. He never mentions the word "taxpayer," even though it's obvious that the collegiate sports mania is heavily subsidized by them. Instead of concern for taxpayers, we get concern for "gender equity" in large doses. There's strong support in the book for a laissez-faire approach whereby college sports would be told, "You survive only as long as you can pay your own way," but Zimbalist's recommendations are rather pallid ones, decidedly not of the Gordian Knot-cutting type.

Still, there is a substantial amount of good in *Unpaid Professionals*. It might have been a home run, but a double isn't bad. □

George Leef is director of the Pope Center for Higher Education Policy at the John Locke Foundation and book review editor of Ideas on Liberty.

Ceasefire! Why Women and Men Must Join Forces to Achieve True Equality

by Cathy Young

Free Press • 1999 • 360 pages • $25.00

Reviewed by Ellen Frankel Paul

Cathy Young has not lost any of the spunk that drove her as a youngster to question the absurdities of daily life in the Soviet Union and impelled her family's immigration to the United States. *Ceasefire!*, much like her first book (*Growing Up in Moscow*) displays an uncanny ability to puncture the shibboleths of a dominant culture, this time the contradictions of radical feminism. In it, she skewers many of the sacred cows of contemporary feminism, while criticizing conservative traditionalists as well. All in all, it is a tour de force.

Once its earlier goals of achieving legal and social equality for women had been largely achieved, feminism took a lurch to the left. Abandoning equal rights, which Young backs fervently, the new incarnation of feminism glorifies women as a class while demonizing men, exaggerates any remaining disadvantages women may experience while ignoring impediments unique to men, and routinely distorts statistics to portray women as victims in desperate plight (and therefore worthy of special political dispensations).

Young amasses evidence aplenty to counter the radicals' "Phony Statistics Hall of Fame." For example, the National Organization for Women claims that many judges and attorneys are still biased against women and therefore that fathers are granted custody 70 percent of the time when they seek it. As she does with each of the radicals' favorite statistics, Young traces that claim back to its origins. She finds three sources: a book by a feminist widely criticized for its sloppy statistics and "penchant for hyperbole," another book that claimed a similar percentage but for *uncontested* cases; and a gender-bias study that actually found that women who filed for sole custody received it 75 percent of the time, as opposed to 44 percent for men. Digging deeper, Young finds data from state studies that clearly display the overwhelming advantage that women enjoy both in contested and uncontested custody cases.

Throughout the book, Young evinces a sympathy for men that radical feminists will find appalling. Rather than being the historical victors in a war between the sexes—the foot-soldiers of the patriarchy that oppresses, rapes, sexually harasses, and underemploys women—Young contends that men are condemned as a sex with little regard for their individual differences or for the impediments that they suffer as men. Men die on average seven years earlier than women, have no choice about engaging in a lifetime of work to support their families, commit suicide four times as often, suffer ten times as many work-related fatalities, receive much harsher prison sentences for identical crimes, and are the only group in society that it is permissible to caricature.

Declining to endorse a nascent men's movement that would champion men's status as victim, Young issues a clarion call for all individuals to be treated as human beings. In a saner age, this admonition might sound trivial, but in ours it is nearly revolutionary. Instead of a National Organization for Women, she envisions a National Organization for Gender Equality. This equal-rights and equal-responsibility movement for both sexes would be built on what she calls (with tongue firmly in cheek, no doubt) a "Twelve Step Program." Among the twelve are such recommendations as: recognize that behaving badly is not a monopoly of the male sex; insist that advocacy groups get the facts straight; acknowledge that both sexes are from earth (not Venus and Mars), with large similarities and smaller differences; presume that fathers are equal parents with mothers despite their different roles; stop treating women as an interest group with claims that are more legitimate than men's.

Although Young's attack is directed mainly at feminist radicals, traditionalist conservatives do not emerge from *Ceasefire!* unscathed. Pro-patriarchy conservatives who revel in the supposed inevitability of male domination or define women principally as sexual creatures are roundly condemned. F. Carolyn Graglia's *Domestic Tranquility: A Brief Against Feminism*, a huge hit among traditionalists for its glorification of women's role as homemaker, mother, and contented sexual soul mate, "rivals any radical feminist tract in shrill extremism and sheer nuttiness." What Young finds most disagreeable in Graglia's vision is that without striving or aspirations of their own, women are less than human. Young embraces a more proactive life for women. Built on serious pursuits outside the family, "it is a life of *doing* and not just *being*." For women who choose to put children above career, she proffers "respect," but doubts that such a choice, if made over an entire lifetime, will lead to the fulfillment Graglia expects. (Editor's note: See Candace Allen's review in the February *Ideas on Liberty*.)

Individualists will find Young's vision appealing. As for traditionalists, *Ceasefire!* is filled with so much evidence and common sense directed against radical feminism, the short chapter attacking traditionalism should be easier to bear. ☐

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The Hayek-Keynes Debate: Lessons for Current Business Cycle Research

by John P. Cochran and Fred R. Glahe

Edwin Mellen Press • 1999 • 200 pages • $89.95

Reviewed by Larry J. Sechrest

Unlike some, this book's title accurately reveals the theme and goal of the text. The authors have set for themselves an admirable task. In a book of only about 200 pages they review the debates that occurred during the 1930s between F. A. Hayek and John Maynard Keynes over the cause of business cycles, explain in detail both to what extent and why these two famous economists disagreed, and then argue that most of the recent work on cycle theory is deficient precisely because it ignores the insights offered by Hayek many years ago. In short, this is not a book designed for the lay reader. It does not inundate the reader with econometrics or differential equations, but it does presuppose a knowledge of economics.

Cochran and Glahe set the stage by noting that today's conventional macroeconomics is flawed by a troubling group of propositions. Macroeconomics asserts that investment and consumption are positively related in the short run and inversely related in the long run, and yet the long run "emerges as a seamless sequence of short runs." This paradox is the legacy of the Keynesian detour taken in the 1930s. Both Keynes and Hayek rejected the classical emphasis on the long run. Indeed, both reasoned within the same broad framework, namely the savings-investment approach used by Swedish economist Knut Wicksell. The Wicksellian view proposes that the key to the puzzle is the process by which ex ante investment can differ from ex ante saving owing to departures of the market rate of interest from the "natural rate" of interest. Keynes argued that the underlying real economic factors, as embodied in the natural rate, need not dominate. The market rate of interest could be maintained indefinitely at a level different from the natural rate. And since he believed that banks could keep the market rate *above* the natural rate, Keynes concluded that the principal problem was too little investment.

Hayek, building on the pioneering work of his mentor, Ludwig von Mises, argued that in the short run, increases in the "money stream" (the stock of money times the rate at which it is spent) would drive the market rate of interest *below* the natural rate and induce an overinvestment in capital goods.

This "malinvestment" could not be sustained in the long run because it represented a production structure that was inconsistent with consumers' time preferences (the ratio of consumer goods to capital goods that they desire). For Hayek, the natural rate of interest, which reflects consumers' time preferences, must eventually win out. All of this is indicative of the crucial fact that Hayek wove together monetary theory and capital theory into a coherent whole. It must be admitted that both Hayek and Keynes were aware that the real world of time, money, and uncertainty required an analytical departure from the pure barter models of classical economics. However, Hayek understood, as did Mises, that capital is heterogeneous, often specific to a particular firm or project, and driven by changes in relative prices. Keynes understood little or none of this. Indeed, he seemed mystified by Hayek's explanation of the interface between money and capital.

The Hayekian approach to cycles differs even from that espoused by other, seemingly like-minded economists, such as the monetarists and New Classicals, in that "the method of analysis is diametrically opposed . . . the key features of Hayek's analysis are absent in models that use the national income concept as a starting point for macroeconomic analysis." Hayek's is a microeconomic explanation of what most economists believe can only be explained in terms of macroeconomic aggregates. Like all Austrians, Hayek was convinced that aggregates or averages cannot be causally related to one another. Only individual actions can be made truly intelligible, so to comprehend business cycles fully economists should focus on relative prices rather than the price level, the structure of production rather than the level of aggregate production, and disequilibrium in the short run as well as equilibrium in the long run.

I found this book to be a very worthwhile addition to the existing literature on business cycles. Although most of the text is devoted to Hayek and Keynes, there are brief but insightful presentations of classical theory, monetarism, real business cycles, and rational expectations. Nevertheless, the authors make it clear why the explanation of cyclical phenomena offered by Hayek and other Austrians is superior to all others. Only the Austrians have successfully combined monetary and capital theory. And if macroeconomics is ever to be meaningful, it must address these "issues in capital theory and the time structure of production."

The next time I teach a university course on business cycles I intend to use this book as the main text. □

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Losing Our Language: How Multicultural Classroom Instruction Is Undermining Our Children's Ability to Read, Write, and Reason

by Sandra Stotsky

Free Press • 1999 • 307 pages • $26.00

Reviewed by Nicholas Stix

Sandra Stotsky, a researcher at the Harvard Graduate School of Education, has for over 20 years studied the cognitive and political (she prefers "civic") consequences of contemporary educational fads, as well as their historical predecessors. *Losing Our Language* argues that during the past 30 years the pedagogical theories and strategies used to teach children English have harmed their cognitive development by supplanting academic goals with social goals and increasingly anti-intellectual methods and materials.

Stotsky reports that contemporary English "language arts" readers misrepresent American history by refusing to tell children about great American leaders, inventors, and scientists because they tended to be white males. Thus children are given to believe that Amelia Earhart invented the airplane, and the only "George Washington" they hear of is George Washington Carver. When presented at all, white males are portrayed as despicable racists. The focus, instead, is on American Indians, blacks, and Hispanics, all of whom are presented as victims.

The editors of these readers, and the professors of education and state education commissars whose recommendations they follow, are concerned primarily with quotas for the number of politically correct readings by writers who are black, Hispanic, Indian, disabled, and so on. The quotas and ideology leave little room for exciting, new children's literature, and since classic children's literature largely comes from the politically suspect pre-1970 "dark ages," it has practically been outlawed.

Stotsky cleverly intuits that the claim of prejudice in classic children's literature (for example, by Robert Louis Stevenson and Rudyard Kipling) is a cover story for the source of multiculturalists' real anger: that the stories are so bloody good! The fantasy, whimsy, and relatively rich vocabulary of the great literature children have traditionally wanted to read creates a special, private world of the imagination.

Stotsky indicts multiculturalists as seeking to imprison children in a regimented, mean little public world. The preachy pseudo-literature they force on children uses vocabulary that is a mix of leaden, abstract nouns; useless foreign terms that are often presented with no guide to pronunciation; confusing pidgin languages such as "Spanglish" and "ebonics"; and little or no vocabulary that children can build on in their future studies. Thus at ages when children's learning should be accelerated, it is actively decelerated. And instructional guides demand that teachers lead small children in discussions of grown-up concerns such as the evils of capitalism and racism.

The impoverished vocabularies are part of a war on English, which the educationists and state education officials who run the textbook-adoption process insist oppresses black and

Hispanic children. Instead of improving the teaching of English for these children, the "solution" is to destroy the English language: "Self-righteous educators have chosen to take out their professed anger at this country's social problems on the English language itself. Unwilling to engage in the hard work of helping all children learn how to read and write, they have spitefully made the English language the object of their seeming frustration because it is so vulnerable, especially in its written form. What is not clear is how these educators can be held accountable for the damage their pedagogical notions are inflicting on a fundamental biological process in human development."

Stotsky observes repeatedly that no scholarship supports the multiculturalists' pedagogical claims. Influential education researchers such as Carl Grant of the University of Wisconsin and James Banks of the University of Washington constantly refer to other "research" that supposedly backs up their own outlandish claims. But no such research exists. Stotsky notes that in contrast to early twentieth-century progressive pedagogues, multiculturalists consider the mere request for factual support proof of racism.

Concluding that dodges by multicultural education professors and teachers are the result of their laziness, unconscious racism, and desire to enhance their own self-esteem at children's expense, Stotsky gives parents advice on how to regain control of their children's education.

This is an exhaustively researched, rigorously argued work. However, in her insistence on maintaining a civil tone, Stotsky has avoided telling the occasionally brutal social history from which this pedagogy derived. The Black Power and New Left movements grew into the apartheid movement of multiculturalism, which mixes notions from communism, national socialism, and caste thinking. Through affirmative action and violent "community control," multiculturalists took over both university schools of education and slum-district public schools. They installed incompetent professors and often functionally illiterate school teachers based on the color of their skin and their degree of hatred, while running off competent educators of all colors. Only then did the pedagogy and teacher guides come along to rationalize the apartheid.

The truth can be a nasty business. □

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IDEAS ON LIBERTY
APRIL 2000

Who May Harm Whom?

Smoking has been one of the hot controversies of our time. Many people find tobacco smoke annoying, smelly, and just plain dirty and unpleasant. Some smokers themselves agree. But today's smoking restrictions, not to mention the attack on smokers and extortion of tobacco companies, could not have been engineered simply on the grounds that tobacco smoke is unpleasant. We needed another reason. So the Environmental Protection Agency (EPA), using bogus science, literally manufactured the finding that secondhand smoke is a class A carcinogen causing death and illness for tens of thousands of nonsmokers. The major news media, along with anti-tobacco zealots, convinced us of the wisdom of the EPA report. They downplayed or ignored findings of outright EPA fraud.[1]

The EPA "proved" that smoke harms other people. Preventing harm to others, especially children, is something most Americans support. Thus all manner of smoking regulations descended upon the nation, including bans in airplanes, airports, restaurants, bars, and workplaces, and even open-air stadiums.

Let's pretend that the EPA's bogus science is legitimate and examine this business about harming others. First, we should acknowledge that we live in a world of harms. The secondhand smoke from my cigarette might harm you. However, your preventing my smoking harms me, since I will have less enjoyment. We cannot say whose harm is more worthy of being avoided because it's impossible to make interpersonal utility comparisons. In other words, there is no scientific way of deciding whose well-being is more important.

The impossibility of interpersonal utility comparisons is applicable to most situations. Suppose a beautiful lady is pursued by Jim and Bob. If Jim wins her hand, Bob is harmed, and if Bob wins her hand, Jim is harmed. We cannot scientifically determine whose harm is more worthy of being avoided.

In a socialistic society, conflicting harms are resolved through government intimidation and coercion. In a free society, conflicting harms are settled through the institution of private property rights. Private property rights are owners' rights to keep, acquire, use, and dispose of their property as they deem fit, so long as they do not violate the property rights of another.

Who Owns the Air?

In a free society, whether smoking harms others or not is irrelevant. The relevant issue is who owns the air? It is clear that if you own it, you have the right to decide how it is used. If you do not want tobacco smoke in your air, that is your right and the government should protect it. By the same token, if I own the air, I also have the right to decide how it is used. If I want to have tobacco smoke in my air, I have every right to do so and the government should protect my property rights just as it protects yours.

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Most people will agree that for all intents and purposes the air in your house belongs to you. That being the case, other people do not have the right to use your air in ways that you do not approve. Similarly, the air in my house belongs to me and other people do not have rights to use my air in ways that I do not approve (like keeping it smoke-free). Most Americans probably agree that people have the right to decide whether smoking is permitted in their own homes, but that is where the agreement ends.

A majority of Americans approve of laws prohibiting smoking in restaurants, bars, airplanes, factories, offices, and other "public" places. But why should their wishes be indulged through force of law? Are those places publicly owned? No. For the most part, they are private property simply doing business with the public. As such, the institution of private property rights should resolve any conflict over smoking. The owner of a restaurant or bar has the right to decide whether smoking is permitted on his premises. Customers have the right to decide the terms on which they patronize the restaurant. If the owner does not permit smoking, then people who wish to smoke during dinner can decide not to go there. Similarly, an employer who wishes to permit smoking in his offices should have the right to do so. People who wish to work in a smoke-free office environment can simply choose some other place of employment where the owner prohibits smoking.

There is absolutely no moral argument for using the power of the state to force a restaurant owner who does not want smoking in his establishment to accommodate smokers. Likewise, there is no moral argument for using the power of the state to force a restaurant owner who permits smoking to prohibit it. This is true for a free society; however, so much of mankind exhibits a generalized contempt for the principles of liberty. We succumb to the temptation of using the state to forcibly impose our preferences on others. In doing so, we establish dangerous precedents that have dire implications for liberty. After all, if health concerns become the reason for violating private property rights and forcibly overruling people's preferences, where does it end? There are people who want high taxes on so-called junk food, with the proceeds used to build hiking and biking paths. There are people who want to regulate caffeine in coffee, sodas, and chocolates. There are people who want to regulate the size of meals in Chinese and Mexican restaurants because they are deemed too large and contribute to the nation's obesity problems.[2]

Health concerns can be used to justify control of a considerable part of our day-to-day lives, from what time we go to bed to whether we exercise. Some might claim that such a concern is overly alarmist and that kind of government control is impossible. But back in the 1960s, when anti-tobacco zealots were simply asking for nonsmoking sections on airplanes, who would have predicted what we have today? Had the zealots revealed their true and complete agenda when they started out, they never would have gotten those first nonsmoking sections. □

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1. In July 1999, U.S. District Court Judge William L. Osteen found reason to nullify the EPA's 1992 report that claimed second-hand smoke to be a class A human carcinogen and cause of lung cancer. He found that the EPA knowingly, willfully, and aggressively put out false and misleading information.

2. Michael Jacobson, director of the Center for Science in the Public Interest, says about large food servings, "It's high time the [restaurant] industry begins to bear some responsibility for its contribution to obesity, heart disease and cancer." Dr. Ronald Griffiths at Johns Hopkins University, concerned about coffee addiction says, "If health risks are well-documented, caffeine could be catapulted in public perception from a pleasant habit to a possibly harmful drug of abuse." Along with Jacobson, he wants the FDA to regulate caffeine content in soda, coffee, tea, and chocolate.