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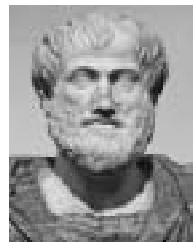
Features

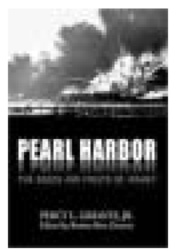
Page 17

Columns



Page 25

Book Reviews



Page 42

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Cover: still photo from "The Fight of the Century," courtesy Emergent Order

Perspective

Elizabeth Warren's Non Sequitur

Elizabeth Warren, who's running for the U.S. Senate in Massachusetts, made quite a splash on the Internet with remarks to supporters in which she said:

> There is nobody in this country who got rich on his own. Nobody. You built a factory out there? Good for you. But I want to be clear: you moved your goods to market on the roads the rest of us paid for; you hired workers the rest of us paid to educate; you were safe in your factory because of police forces and fire forces that the rest of us paid for. You didn't have to worry that marauding bands would come and seize everything at your factory, and hire someone to protect against this, because of the work the rest of us did. Now look, you built a factory and it turned into something terrific, or a great idea? God bless. Keep a big hunk of it. But part of the underlying social contract is you take a hunk of that and pay forward for the next kid who comes along (tinyurl.com/3ewtzut).

Just goes to show, you can start with a valid premise and end up with an invalid conclusion.

She's right, of course. When you live in a society you benefit in countless ways, material and otherwise. The language you speak and think in is a social institution and would be impossible without the presence of others. So is custom, which regulates our interpersonal conduct far more than the edicts of legislatures. Money itself is an organic social institution. Of course today money is fiat paper controlled by government, but even that system has a foundation in the institution described by Carl Menger and Ludwig von Mises.

So we need not deny Warren's premise. Human beings are social animals. Frédéric Bastiat celebrated this fact in *Economic Harmonies*: "I make bold to say that in one day [the average person] consumes more things than he could produce himself in ten centuries."

Warren, then, said nothing startling. But she places what should be a mundane observation in the service of a bad cause: higher taxes. That's a non sequitur.

In today's society great wealth can be made by what Franz Oppenheimer called "the political means" and Bastiat called "legal plunder." That is, many business-people make fortunes from government interventions that obstruct entry into their industries or limit self-employment opportunities, allowing them to earn oligopolistic rents at the expense of consumers and workers. That's a traditional classical-liberal complaint about government and its connivance with business.

But that is not what Warren means. She says nothing about corporate-state privilege. She mentions only tax-financed roads, schools, and police—*three of the worst "services" precisely because they are tax-financed government monopolies*. There's an easy remedy for State-granted privileges: repeal. But like a good corporate-liberal, she prefers regulation to repeal. And as we know, George Stigler's theory of regulatory capture tells us that the rules will tend to be written with the regulated industries in mind, if not with their active participation.

Warren invokes a social contract, but has anyone seen this thing that purportedly obligates you to surrender a "hunk" of what you produce under penalty of violence? Sorry, I don't trust unwritten, open-ended so-called contracts into which any advocate of government power may read conditions ex post. (There is a more reasonable notion of social contract but that must wait for another time.) Moreover, why aren't honest production and exchange of valuable goods counted as payment forward? Just as our living standard is the fruit of previous generations' production, so today's producers help to raise the living standard of the next generations.

Boiled down, then, Warren's argument is that since everyone has paid taxes to provide services without which wealthy people couldn't have made their money, they should pay more. How does that follow? She'd first have to show that they are paying too little now. She only assumes this. That's not good enough. And maybe the services are inferior and cost too much—wouldn't we expect that from a protected monopoly?

She might respond that the deficit shows that too little money is collected in taxes and therefore the wealthiest should pay more. Still not good enough. As she herself intimates in another part of her speech, the George W. Bush years were marked by *unfunded spending.* That sounds like a problem of overspending, not undertaxation. Solution: Cut spending.

⋆ ⋆ ⋆

Unemployment is not letting up. So why is this post-recession economy different from others? Warren Gibson concludes his two-part series on joblessness.

Economists who support the latest Obama administration proposal to create jobs say they can calculate precisely how successful the program would be. But Max Borders says what they do is no better than reading entrails.

When you get right down to it, our well-being is in the hands of a few people in the Federal Reserve System. Why do we tolerate this? John Allison and John Chapman say enough is enough.

Comparative advantage is the principle that everyone stands to make gains from trade. Meaning no disrespect, Richard Fulmer thinks even a caveman can understand this.

Who were the Progressives? Since it was an eclectic group, there is no simple answer. Joseph Stromberg guides us through the labyrinth.

A Supreme Court ruling fueled the debate over whether spending money to promote candidates is protected political speech. Michael Cummins says many people have missed the point.

If we were replacing the eagle or Uncle Sam as a national symbol, what might take its place? Ridgeway Knight Foley, Jr., suggests a picture of a busybody.

Our columnists labored long at their keyboards. Here's what they have to show for it: Lawrence Reed puts in a good word for humility. Burton Folsom places Herbert Hoover's proto-New Deal Reconstruction Finance Corporation under the microscope. Thomas Szasz demonstrates the lethality of government suicide prevention. John Stossel reflects on the government's response to 9/11. Walter Williams debunks alarms about overpopulation. And Steven Horwitz, reading the claim that Keynesian economics isn't about big government, replies, "It Just Ain't So!"

Books coming under inspection look at Pearl Harbor, the financial crisis, statism, and justice.

This being December, our annual index concludes the issue.

—Sheldon Richman
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Wanted: A Healthy Dose of Humility

BY LAWRENCE W. REED

An awful lot of people in this world are really puffed up about themselves. One of the character traits I wish were much more widely practiced these days is good old-fashioned humility.

T. S. Eliot said, "Humility is the most difficult of all virtues to achieve; nothing dies harder than the desire to think well of oneself."

If you're not sure what humility is, these lyrics from an old Mac Davis tune will at least remind you of what it's *not*:

> *Oh Lord it's hard to be humble when you're perfect in every way.*
> *I can't wait to look in the mirror 'cause I get better looking every day.*
> *I guess you could say I'm a loner, a cowboy outlaw tough and proud.*
> *I could have lots of friends if I want to, but then*
> *I wouldn't stand out from the crowd.*
> *Oh Lord, it's hard to be humble!*

I couldn't disagree more with those words. It's not hard to be humble if you stop comparing yourself to others. It's not hard to be humble if your focus is building your own character. It's not hard to be humble if you first come to grips with how little you really know. "The wise person possesses humility. He knows that his small island of knowledge is surrounded by a vast sea of the unknown," noted Harold C. Chase.

One of the greatest teachers and theologians of our day, Pastor Timothy Keller of Redeemer Presbyterian Church in New York City, makes this keen observation: "Until the twentieth century most cultures, including ours, held that having *too high* an opinion of oneself was the root of most of the world's troubles. Misbehavior from drug addiction to cruelty to wars resulted from hubris or pride—a haughtiness of spirit that needed to be deterred or disciplined. The idea that you were bigger or better, or more self-righteous, or somehow immune from the rules that govern others—*the absence of humility*, in other words—gave you license to do unto others what you would never allow them to do unto you."

These days, however, it's a different story. Being humble rubs against what millions have been taught under the banner of "self-esteem." Even as our schools fail to teach us elemental facts and skills, they somehow manage to teach us to feel good in our ignorance. We explain away bad behavior as the result of the guilty feeling bad about themselves. We manufacture excuses for them, form support groups for them, and resist making moral judgments lest we hurt their feelings. We don't demand repentance and self-discipline as much as we pump up their egos.

> Humility doesn't mean thinking less of yourself. It means thinking of yourself *less*.

Don't get me wrong. Humility doesn't mean thinking less of yourself. It means thinking of yourself *less*. It means putting yourself in proper perspective. It means cultivating a healthy sense of your limitations and the vast room you have to grow and improve. It means you don't presume to know more than you do.

Fifty-three years ago this month (December 1958) Leonard Read's essay "I, Pencil" made its debut (tinyurl.com/3pgfdys). Let me summarize it for you here: No one person—repeat, *no one*, no matter how smart or how many degrees follow his name—could create from scratch, entirely by himself, a small, everyday *pencil*, let alone a car or an airplane.

A mere pencil—a simple thing, yet beyond any one

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person's complete comprehension. Think of all that went into it, the countless people and skills assembled miraculously in the marketplace without a single mastermind—indeed, without anyone knowing more than a corner of the whole process. It's impossible not to think of the huge implications of this lesson for the economy and the role of government.

It is in fact a message that humbles the high and mighty. It pricks the inflated egos of those who think they know how to mind everybody else's business. It explains in plain language why central planning of society or an economy is an exercise in arrogance and futility. If I can't make a pencil, holy cow, I'd better be careful about how smart I think I am.

Big Plans, Broken Shells

Maximilian Robespierre blessed the horrific French Revolution with this chilling declaration: "On ne saurait faire une omelette sans casser des oeufs." Translation: "One can't expect to make an omelet without breaking eggs." He worked tirelessly to plan the lives of others and became the architect of the Revolution's bloodiest phase: the Reign of Terror. Robespierre and his guillotine broke eggs by the thousands in a vain effort to impose a utopian society with government planners at the top and everybody else at the bottom.

That French experience is one example in a disturbingly familiar pattern. Call them what you will—socialist, interventionist, collectivist, statist—history is littered with their presumptuous plans for rearranging society to fit their vision of the common good, plans that always fail as they kill or impoverish people in the process. I've said it in this magazine before but I'm happy to say it again: If big government ever earns a final epitaph, it will be, "Here lies a contrivance engineered by know-it-alls who broke eggs with abandon but never, *ever* created an omelet."

None of the Robespierres of the world knew how to make a pencil, yet they wanted to remake entire societies.

None of the Robespierres of the world knew how to make a pencil, yet they wanted to remake entire societies. How utterly preposterous and mournfully tragic!

The destructive acts of pride don't always come from brash and fiery revolutionaries or egotistical tyrants full of pompous and hateful rhetoric. More often they come cloaked in benevolence and disguised as the wisdom of the elders, who have only the best of intentions for the whole community. An outstanding example of this type of hubris is the political philosophy in Plato's *Republic*, in which he maintains, with breathtaking vanity, that the world would be a harmonious and prosperous place if only philosophers like himself were given absolute authority to run it as they saw fit!

We would miss a large implication of Leonard Read's message if we assume it aims only at the tyrants whose names we all know. The lesson of "I, Pencil" is not that error begins when the planners plan big. It begins the moment one tosses humility aside, assumes he knows the unknowable, and employs the force of government to control more and more of other people's lives. That's not just a national disease. It can be very local indeed.

In our midst are people who think that if only they had government power on their side, they could pick tomorrow's winners and losers in the marketplace, set prices or rents where they ought to be, decide which forms of energy should power our homes and cars, and choose which industries should survive and which should die. They make grandiose promises they can't possibly keep without bankrupting us all. They should stop for a few moments and learn a little humility from a lowly writing implement.

So humility, in my book, is pretty important stuff. It may well be the one virtue of strong character that is a precondition of all the others. FEE

Keynesianism Doesn't Mean Bigger Government? It Just Ain't So!

BY STEVEN HORWITZ

The debate over what John Maynard Keynes "really" meant by the theories he put forward in *The General Theory of Employment, Interest, and Money* has been going on almost since it was published in 1936. The release of the second Hayek-Keynes hip-hop video (tinyurl.com/6yjxsrp) brought this debate back to a boil. For example, in a May 2 blog post at *The New Republic*, Jonathan Chait argues that Keynesian fiscal policy is not "an argument for larger government."

Unfortunately Chait misses two important points. First, Keynes's argument for why his view of fiscal policy need not mean a larger government ignores the incentives facing the politicians who must implement it. Those incentives would lead to a larger government. Second, Keynes called for the socialization of investment as part of a broader vision of how to prevent the crises that necessitate stimulus spending in the first place. The result of both arguments is larger government. Thus Chait's claim about Keynes just ain't so.

The problem with Keynes's analysis is that he paid no attention to the real incentives facing politicians.

Chait rightly notes that while Keynes argued that deficit spending was necessary as a stimulus during recessions, he also argued that governments should run surpluses in good times to pay off the debt. Chait concludes: "This policy is perfectly compatible with any level of government and does not require higher aggregate levels of debt than maintaining a regular balanced budget."

Indeed, *in theory* it is compatible, but the problem is that the theory does not comport with reality. Keynesian ideas have ruled fiscal policy for at least 50 years, fewer than five of which had budget surpluses. During this time the debt has gone up to more than $14 trillion and the size of government has expanded enormously. Surely the economy was not in recession all but those few years. Apparently Keynesian policy is *not* compatible with any level of government and *does* seem to necessitate higher levels of aggregate debt.

What Chait overlooks is that regardless of what Keynes *believed* government should do, what it in fact *will* do is another matter. As James Buchanan and Richard Wagner argued in their classic critique of Keynesian fiscal policy, *Democracy in Deficit*, by removing the preexisting moral and institutional constraints on deficit spending as a way to balance the economy, Keynes and the Keynesians unleashed the perverse incentives of the political process into policymaking. The problem with Keynes's analysis is that he paid no attention to the real incentives facing politicians, who now had the green light to deficit-spend in the name of economic stability.

Buchanan and Wagner argued that vote-seeking politicians will always prefer spending to taxing because the former gets them votes and the latter does not. As long as there are no institutional or moral impediments to this (such as a balanced budget amendment or a

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deeply held norm against deficit spending, except during wartime), politicians will always take deficits over surpluses, especially when economists such as Keynes have given them theoretical support. The result is that rather than the offsetting surpluses Chait focuses on, politicians continue to deficit-spend even during periods of economic growth because none wish to raise taxes or cut the flow of government benefits to their prospective voters. The result is exactly what Buchanan and Wagner predicted in 1977: large and increasing deficits and debt, and a growing danger of higher levels of inflation to pay it off.

In addition it's worth observing that government stimulus spending simply does not work. Part of the Keynesian story is that deficit-financed spending will end recessions and generate the growth that will lead to the later surpluses to pay off the deficits. But what if stimulus spending doesn't generate growth, or even prolongs or deepens recessions? In that case deficits beget deficits, debt begets debt, and government grows out of control. When Chait wrote in May unemployment was about 9 percent three and a half years after the recession started and around two years after it officially ended. As I write this two months afterward unemployment is unchanged. Massive stimulus spending is not just the path to larger government but also to permanently low rates of growth, which will only worsen the deficit and debt.

> Keynes's fiscal policy recommendations were part of a larger story calling for the socialization of investment through the State.

What Not To Do

In his article Chait also claims that defenders of Hayek cannot tell us what should be done when an economy is stuck in a recession. That's an unfair charge. First, Hayekians can tell us what *not* to do: engage in large-scale stimulus spending, for the reasons noted. Second, Hayekians do have positive advice: Government should get out of the way so entrepreneurs and others who have a better idea of what to do can try things and see if they work. Chait claims it's a cop-out for Hayekians to criticize Keynesian solutions for relying on government without specifying what the alternative is. The Hayekian perspective is that neither Hayekians nor Keynesians know what to do. That's why we have market competition, which in Hayek's words is a "discovery procedure" that helps us figure out how to revive a moribund economy.

Finally, Chait overlooks the broader context of Keynes's fiscal policy recommendations. These were really only stop-gap measures rather than a long-term solution to what Keynes saw as the chronic tendency of capitalist economies to fall into recession. In his view there would never be enough profitable investment opportunities to match the public's saving. So he proposed a fix for this oversaving/underconsumption problem. That fix was the socialization of investment through the State.

In trying to argue that there's nothing in Keynes to suggest larger government, Chait is correct, but only if he's referring to "fiscal policy" in its narrowest sense and ignoring the political incentives discussed above. But Keynes's fiscal policy analysis was part of a larger story of the instability of capitalism, which requires that government play a more prominent role in allocating money for investment to avoid future recessions. *This* element of fiscal policy *clearly* calls for a bigger government.

The claim that Keynesianism doesn't necessarily imply bigger government and greater debt is shown to be mistaken when we consider the implications of Keynes's argument for countercyclical fiscal policy, the record of Keynesian policy in the last 50 years, and the broader context of his views on fiscal policy in *The General Theory*. FEE

Unemployment: What's To Be Done?

BY WARREN C. GIBSON

In Part 1 (tinyurl.com/3umpdms) I outlined natural unemployment, government-caused unemployment, and the attempts to measure these. We saw how ambiguous and subjective some of the concepts of unemployment are and how the government, specifically the Federal Reserve, is charged with managing it. Now we turn to current conditions and what can be done about them.

There have been huge advances in technology and substantial declines in trade barriers in recent years. While these developments have raised living standards they have been hard on people whose skills were rendered obsolete or uncompetitive. When changes evolve gradually, as when so many people left farming in the last century, the disruption is not so great. Changes are now coming faster and are extending to some high-paid professional jobs. Automated systems can now handle at least the routine aspects of some legal research and medical diagnosis.

Machines replace people but create more productive employment elsewhere.
State Records NSW [flickr]

Time and time again new doors have opened to workers as old doors closed. Machines replace workers, but they raise productivity and produce new employment opportunities. We can expect this pattern to continue for a long time to come. Still, it is within the realm of possibility that robots and computers could take over so much work that the demand for human workers would shrink drastically. But those very machines would mean higher productivity and thus higher living standards.

A great deal of work can be now be done remotely, providing an advantage to areas with low living costs. Substantial outsourcing of such jobs to foreign countries has occurred (though that trend may be reversing as low-cost areas of the United States become competitive and as customer dissatisfaction and problems with managing offshore workers come up). The benefits of outsourcing and other productivity enhancements are spread across all consumers, but the job losses are concentrated among small and sometimes vocal minorities.

Another theoretical point: Unemployment notwithstanding, it is an empirical fact of life that labor is scarce relative to natural resources, as Murray Rothbard explained. Over time, this gap tends to lessen and could theoretically disappear.

Education Is Key

Problems with education are legion, but two in particular bear on unemployment and underemployment. One is the emphasis on college education over vocational training. Everyone should attend college, says President Obama. Really? What about welders, truck drivers, repair people, retail sales people? These skills are in demand, and for many people the jobs may offer good pay and personal satisfaction. Why not attend a trade school or get an apprenticeship rather than a college degree? Compare

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four years in school leading to a bachelor of arts in business and a big student debt versus on-the-job learning.

The second problem is that college administrators and instructors lack incentives to prepare students for good jobs. Schools usually have little to say about the jobs their graduates have gotten or the debt burdens they carry.

Even with all the emphasis on college, by 2020 only about a third of the labor force will be equipped with bachelor's degrees or higher, according to the McKinsey Global Institute (tinyurl.com/6ebjzdd). But the glut of dubious business and social "science" degree-holders will continue while STEM (science, technology, engineering, and math) degree holders will remain scarce.

Among employers surveyed by McKinsey, a majority expect to hire more part-time, temporary, or contract workers. One reason for this trend is mandated and generally very expensive health insurance for full-time employees. But more sophisticated resource-management systems also contribute to this trend, in addition to telecommuting opportunities.

The glut of dubious business and social "science" degree-holders will continue while STEM (science, technology, engineering, and math) degree holders will remain scarce.

Unemployment Figures Are Grim, and Yet . . .

As this is written, the widely followed U-3 measure of unemployment stands at 9.1 percent while the broader U-6 is a whopping 16.2 percent. People are also going longer without work. About 45 percent of those unemployed have been out of work for more than 27 weeks. The number of discouraged workers rose sharply during the recent recession. Speaking of the Great Recession, it officially ended in June 2009, and if we had gotten a recovery along the lines of past recoveries, GDP would be booming by now and unemployment, always the last aspect to recover, would be falling noticeably. Not only is unemployment high, but GDP growth for the first half of 2011 was close to zero. There was talk of a slide back into recession, though this diminished in the fall.

Job losses since the start of the Great Recession number about 7.5 million; three million more people have become discouraged. Total payrolls amount to about 130 million, fewer than in 2000, when the population was about 11 percent lower. Seven people compete for each job opening.

Unemployment varies widely from place to place. The U-3 version varies from 3.2 percent in North Dakota to 12.4 percent in Nevada. Among cities the numbers range from 3.2 percent in Bismarck, North Dakota, to 27.9 percent in Yuma, Arizona. There is also wide variation among job classifications. Nutritionists, welders, and nurses' aides are in short supply, along with computer specialists and engineers.

Aggregate figures always mask important differences. Many employers still find it hard to locate good people. The McKinsey study reports that 40 percent of companies surveyed have had openings for six months, while 64 percent reported positions for which they cannot find qualified applicants, with managers, scientists, and computer engineers topping the list.

Anecdotally, "Now Hiring" signs are not hard to spot. Friends who own businesses tell me they have difficulty filling even a receptionist's job with someone who is reliable, can write a passable letter, or create a simple Excel spreadsheet. Alas these days one cannot assume that a holder of a bachelor's degree in business, for example, has these basic skills.

Recent Government Policy

The Fed has been unable to do anything about unemployment in recent years. The massive doses of money inflation, which tripled the monetary base (currency plus bank reserves) from about 2008 until the present, have not produced any significant price inflation, and unemployment remains stubbornly high. Money inflation has not produced price inflation largely because banks are not lending but instead have accumulated massive amounts of excess reserves—above and beyond the levels mandated by the Fed to back deposit liabilities. (The Fed pays interest on reserves held in the banks' Fed accounts.)

As we have seen, the distinction between U-3 and U-6 hinges on the rather arbitrary classification of some unemployed workers as "discouraged." Alternately, one could simply count the number of work-age people who do not hold jobs. For example, one-fifth of all men of prime working age are not getting up in the morning and heading for a job either because they're officially unemployed or excluded from the labor force.

Labor productivity is way up and with it, corporate profits. This is typical of the early stages of a recovery. Employers realize that they may have gone overboard with hiring during the boom and need to pull back. When they need additional help they usually turn first to temporary workers. Employees work harder with the specter of unemployment looming large. Only later does employers' confidence pick up enough that they're willing to take the risky step of adding permanent hires.

Productivity increases are a good thing in the long run, but by this stage of the recovery employment should be picking up. Why isn't it?

Businesspeople have to predict the future, so they hate uncertainty, especially the kind that comes from government—and there's plenty of that around right now.

What's to Be Done?

Businesspeople have to predict the future, so they hate uncertainty, especially the kind that comes from government—and there's plenty of that around right now. What will Obamacare do to them? Will the Bush tax cuts be allowed to expire next year? Will there be another debt crisis? What will happen to the not-so-almighty dollar? Who will win next year's election? The best way to get the economy on track again is to lessen these vexing uncertainties. Given the performance of the President and Congress in the recent debt ceiling debacle, this seems unlikely to happen before the next election.

Rhetoric matters. By 1937 unemployment had recovered somewhat from its Great Depression peak of 25 percent. But with the failure of the New Deal becoming evident, FDR, needing a scapegoat, turned against businesspeople with new regulations, antitrust action, new taxes, and hostile rhetoric—he called them "economic royalists" at one point. The recovery stalled, unemployment rose, and only the war brought an end to unemployment—good news if you got a job, bad news if it was a job that got you shot at. (But what was being made? Not consumer goods.) President Obama has referred to "fat-cat bankers" but has backed away from inflammatory rhetoric, perhaps because of adult supervision.

Can stimulus programs mitigate unemployment? Sure, they can put people to work, but the projects are politically motivated and do not represent the best use of scarce resources, as market-based projects must try to do. The projects end, the workers disperse, and there has often been little or no lasting benefit. About all we have to show for those programs are massive new debt levels, a weakening dollar, and a feeble economy—and yes, a frightened and angry populace.

The economics profession must lessen its fascination with dubious macroeconomic aggregates. Production of needed and wanted goods and services is what really matters, not just production of any old thing that gets added to GDP. Economists should focus on conditions that generate real jobs, jobs that produce things people really want, not just any activity that draws a subsidized paycheck.

Congress must make serious spending cuts, and proponents should not pretend these won't hurt short-term. Cuts should be immediate, because promises about cuts ten years from now are all but meaningless. Today's Congress has little influence over future officeholders.

The Federal Reserve should be relieved of its unemployment mandate (and the new Consumer Financial Protection Bureau). Its money-creation powers should be reined in, and ultimately it should be abolished. FEE

Scientism and the Great Power Nexus

BY MAX BORDERS

President Obama wants to create jobs. His political life depends on it. So the President recently used the bully pulpit to propose a "jobs" bill that would include heavy spending on infrastructure. Journalists wanted to know what the bill would do. They turned to economists.

These experts, armed with the most sophisticated methods available, gave the journalists what they needed. In turn the journalists—armed with what they uncritically accepted as good information—returned with coffee to their keyboards and reported.

Witness:

> Mark Zandi, chief economist at Moody's Analytics, is frequently the go-to guy for both parties when it comes to analysis of various jobs proposals. So, what did he think of President Obama's speech last night? Here's the report: "The plan would add 2 percentage points to GDP growth next year, add 1.9 million jobs, and cut the unemployment rate by a percentage point." [Brad Plummer, "Ezra Klein's Wonkblog," *Washington Post*, September 9.]

And who are the willing consumers of this information? People looking for reasons to be hopeful. People looking for certainty. Who can blame them? Times are tough.

About as accurate as modern economics.

But this sort of reporting is just *scientism* on display. I'm not alone in thinking this. Economist Russ Roberts, reacting to similar reporting in the *Financial Times,* wrote at Cafe Hayek (September 13): "Really? That's what they found? [The journalist] treats it like a discovery of fact. As in '[Alan] Blinder and Zandi weren't sure of the distance between the earth and the sun but when they measured it, they found it was about 93,000,000 miles.'" (tinyurl.com/5sq44ua)

Roberts knows economists aren't capable of auguring such things. Because when it comes to national-level prediction and forecast, economics has all the reliability of a *Farmer's Almanac.* And that's being charitable.

Certainty for Sale

Here's the problem: People like Mark Zandi belong to a great power nexus that relies on scientism for its very existence. To repeat: People crave certainty. Politicians crave power. So the latter have to provide the former with at least the illusion of certainty to stay in office. But they can't do it alone.

Economists—especially those who tend to get tapped by the media or by Washington elites—are the

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ones willing to strut around on the national stage showing their predictive plumage. Journalists, no experts themselves, report what they're told. (And few try to spot the turkey behind all that peacocking.)

But as readers of this publication know, a nexus of politicians, economists, journalists, special interests, and a desperate lay public can hardly be virtuous. This industry enables peddlers of scientism to hock their wares in a world full of uncertainty. Indeed, a pseudo-certainty creates the circumstances under which great wishes can father great lies.

F. A. Hayek warned us about this, of course, when he said, "It seems to me that this failure of the economists to guide policy more successfully is closely connected with their propensity to imitate as closely as possible the procedures of the brilliantly successful physical sciences—an attempt which in our field may lead to outright error. It is an approach which has come to be described as the "scientistic" attitude. . . ."

Since Hayek, a growing movement of great minds, across disciplines, warns us to clip our wax wings.

Chaos Rules

In 1961 Edward Lorenz discovered the "butterfly effect." Ironically, when he figured out that tiny changes in initial conditions could mean seismic shifts in the rest of a system, he was studying weather and climate. I won't discuss the irony here. Suffice it to say Lorenz is the one who taught us that complex systems—whether the climate, an ecosystem, or an economy—can also be chaotic systems. "I realized," said Lorenz of his then-obscure finding, "that *any* physical system that behaved nonperiodically would be unpredictable."

Although "chaotic" eludes strict definition, the term usually refers to a system that is sensitive to changes in initial conditions, shows order without regularity, and is immune to prediction and forecast.

In his still-vibrant *Chaos* (1989), James Gleick tells Lorenz's story—including the latter's discoveries and the implications of chaos. "Forecasts of economic growth or unemployment were put forward with an implied precision of two or three decimal places," writes Gleick. "Governments and financial institutions paid for such predictions and acted on them, perhaps out of necessity or for want of anything better. . . . But few realized how fragile was the very process of modeling flows on computers, even when the data [were] recognizably trustworthy and the laws were purely physical, as in weather forecasting."

Little has changed.

Aggregates, Agents, and Ants

I think the failure of macroeconomics can be boiled down to this: Macroeconomics deals primarily with aggregates, or macro-level trends. But to be truly accurate the macro level would have to be explained *in terms of the micro*—that is, individual agent behavior. Micro behaviors give rise to macro trends. Another way of putting this is that macro trends are *dependent on* micro behaviors. The trouble is, individual agents interact with—and react to—one another in diverse, complicated ways.

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Similarly, it's impossible to predict exactly what an ant colony will do when confronted with two picnics at equal distances from the colony. In that famous experiment we might be able to predict a single ant's behavior if we have lots of local information about its pheromone secretion algorithms and such. But relative to each food source it would be impossible to predict the behavior of the colony as a whole. Such is life at the edge of chaos.

A Blind Spot

Now of course we have processors that can crunch tons of data. We have a new breed of mathematical wizards in the tradition of Paul Samuelson who can write whole tracts with as many equations as words. And we have whole new constituencies of politicians, pundits, and people ready to believe. So are we finally living in a time when macroeconomics can tell us what we need to know about unemployment in a year—as Newtonian mechanics tells us when Halley's Comet will arrive?

Alas no, says mathematician William Byers. In his excellent *The Blind Spot,* Byers makes an audacious argument for humility in the sciences—both hard and human: "Human beings have a basic need for certainty. Yet since things are ultimately uncertain, we satisfy this need by creating artificial islands of certainty. We create models of reality and then insist that the models are reality. It is not that science, mathematics, and statistics do not provide useful information about the real world. The problem lies in making excessive claims for the validity of these methods and models and believing them to be absolutely certain."

Interestingly, Byers also picks up on the idea of selling certainty. Whether he's talking about the complicated financial instruments that obscured the problems leading to the financial meltdown, or the schematics for all the Keynesian fixes that followed, models are the conduits of pseudo-certainty. "The more complex the package and the more arcane the mathematics, the better," says Byers. "What was being sold was the faith that the complex, *human,* world of economics and finance could be made over in the image of science, could be made objective and predictable."

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Byers goes on to explain that there is a kind of quantification bias at work. That is, if you can describe things in mathematics, you are in some sense speaking the language of nature. But limning the world in numbers has its limits—especially since so many of the important aspects of science are subjective. And so many aspects of nature are, well, uncertain. Numbers, argues Byers, are our attempt to create the illusion of objectivity—where objectivity is thought to be the very stuff of certainty. But "science does great damage when it turns into ideology, when it begins to worship certainty."

The (Other) Freeman

Eminent physicist Freeman Dyson is no libertarian. But his call for humility in science ("Heretical Thoughts about Science and Society," tinyurl.com/yozuja) extends to economics too:

> The politicians and the public expect science to provide answers to the problems. Scientific experts are paid and encouraged to provide answers. The public does not have much use for a scientist who says, "Sorry, but we don't know." The public prefers to listen to scientists who give confident answers to questions and make confident predictions of what will happen as a result of human activities. So it happens that the experts who talk publicly about politically contentious questions tend to speak more clearly than they think. They make confident predictions about the future, and end up believing their own predictions. Their predictions become dogmas which they do not question. The public is led to believe that the fashionable scientific dogmas are true, and it may sometimes happen that they are wrong. That is why heretics who question the dogmas are needed.

So if Dyson is right about the need for heretics, are those skeptical of macroeconomics heretics or "market fundamentalists"?

People who understand markets know they can't do everything under the sun. Yes, markets can and do work wonders. But most truly liberal thinkers start with a particular kind of skepticism:

- *Knowledge is dispersed, not centralized.* Planning or tweaking by central authorities is a fool's errand and results in perverse effects. (Skepticism of grand designs.)
- *Centralized power tends to corrupt people.* Coalitions of interests, bureaucrats, and moralists form to transfer resources from the masses or from competitors to the

pockets of coalition members. (Skepticism of power wielded for the "public good.")

- *Value is not objective but rather subjective.* This not only makes market exchanges possible, but makes it difficult for any central authority to claim it is operating in the name of a universal good. (Skepticism of claims to objective value. [See my "The Relentless Subjectivity of Value," tinyurl.com/3kgpvj9])

I could go on. Suffice it to say that to be a classical liberal is to be a heretic. And for heretics skepticism is a prime virtue. Yes, we tend to admire the market process. But unlike those who prostrate themselves before the golden calf of Aggregate Demand or Government as God, we are skeptics first and foremost.

> Yes, we tend to admire the market process. But unlike those who prostrate themselves before the golden calf of Aggregate Demand or Government as God, we are skeptics first and foremost.

Soothsayers and Charlatans

When it comes to heresy in economics Arnold Kling comes to mind. Writing in *The American* (tinyurl.com/3pzrnyq), he says: "I think that if the press were aware of the intellectual history and lack of scientific standing of the models, it would cease rounding up these usual suspects. Macroeconometrics stands discredited among mainstream academic economists. Applying macroeconometric models to questions of fiscal policy is the equivalent of using pre-Copernican astronomy to launch a satellite or using bleeding to treat an infection."

Kling says economists should be more honest about their limitations. He thinks the Congressional Budget Office, with all its scoring, can do little to predict the effects of various policy scenarios, such as taxing and spending: "The CBO adds value to policymakers by 'scoring' the impact of policies on the budget. However, the 'scoring' of policies in terms of GDP growth or jobs saved is of no value. The CBO should simply refuse to do it, and the consulting firms that purport to provide such estimates should be regarded as the charlatans they are."

An Uncertain Constituency

Though the methods used by these macroeconomists are no more reliable than "soothsaying or entrail-reading," they belong to that great nexus of power, which creates incentives for folks to "step right up" for more of the same elixir.

Sadly there is no competing power nexus. And yet people are growing increasingly suspicious of these nostra. Just as Americans have grown weary of intervention in foreign affairs, they're growing weary of intervention in the economy too. Call it what you like—stimulus bills, jobs plans, back-to-work schemes, or whatever—fiscal interventionism is not producing the desired effect. And people are getting wise to it. In the old days they ran the charlatans out of town. FEE

The First Government Bailouts: The Story of the RFC

BY BURTON FOLSOM, JR.

The idea of using federal money to bail out large failing corporations did not begin with the Bush administration. In the beginning was the RFC, the Reconstruction Finance Corporation, which President Herbert Hoover pretentiously named and bountifully funded during the Great Depression to bail out corporations deemed too big to fail. In 1932 Congress gave the RFC $2 billion—plus much more later—and the power to choose who got the money.

On the surface the idea behind the RFC sounds good. By 1932 the Great Depression had already been devastating. Banks were failing, railroads were going broke, workers had been laid off by the millions. Why not pump cash into some large struggling companies and keep them serving customers and hiring workers? Jobs would be saved, dollars would flow through the economy, and the Great Depression might be halted.

But there were two big problems. First, the $2 billion the RFC would dole out had to come from taxpayers. And they could have used that money instead to buy radios, shirts, gas, or a host of other products that would have put people to work making and selling these items. In other words, shifting capital from workers who earn it to central planners who spend it may not create or even save jobs.

Second, Hoover's whole idea of an RFC assumed that a group of wise men could discern the U.S. economy clearly enough to pick the right banks, railroads, and corporations to resuscitate with the right amount of cash. What we find instead is that when an appointed committee like the RFC is matched with large amounts of money, the results quickly become politicized.

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Thousands of large U.S. companies wanted capital, but only a fraction of them could get it. Rep. Louis McFadden (R, Pa.), himself a bank president, called the RFC "a scheme for taking $500,000,000 of the people's money produced by labor at a cost of toil and suffering and giving it to a supercorporation for the sinister purpose of helping a gang of financial looters to cover up their tracks."

Immediate Politicization

Hoover, a Republican, appointed former Republican Vice President Charles Dawes to head the new RFC. Dawes, however, resigned in June 1932 to care for his bank in Chicago, the Central Republic Bank and Trust Company. Three weeks after his resignation, Dawes won a $90 million loan for his failing bank (it went broke anyway). After that, Atlee Pomerene, the new RFC president, accepted a $12.3 million loan for his Cleveland bank. Joseph Nutt, treasurer of the Republican National Committee, won a $14 million loan for his bank in Cleveland. Republican Senator Phillips Goldsborough of Maryland received a $7.4 million loan for his Baltimore bank. Roy Chapin, Hoover's secretary of commerce, won $13 million for his Detroit bank.

Some Democrats (Pomerene was a former Democratic senator) also finagled loans from the RFC, but the larger point is that choosing who got loans and who didn't was a political process that gave capital to the winners and took more in taxes from everyone else. Funding federal programs was expensive. During 1932,

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for example, the top income earners saw their top tax rate hiked from 25 to 63 percent. Plus Congress that year passed a host of new excise taxes on gas, tires, telephone calls, and movie tickets.

The Other Side's Turn

When Franklin Roosevelt was elected president, he installed a loyal Democrat, Texas banker Jesse Jones, as the new president of the RFC. Jones helped those Roosevelt sent his way—either through RFC loans or by using his influence with others. J. David Stern, for example, edited the *Philadelphia Record,* which backed Roosevelt and other Democrats enthusiastically in the election. Stern, however, almost went bankrupt in the 1930s, so Roosevelt asked Jones to help. Jones used his influence in the banking community to secure $1 million in loans to keep Stern publishing.

Some reporters were sensitive to the RFC money and influence offered by Jones. Walter Trohan, the Washington bureau chief for the *Chicago Tribune,* often interviewed Jones, who according to Trohan would often offer RFC loans and agency-controlled firms to him. "I turned these offers down, because I didn't know anything about such businesses and because I didn't think I would be honest in accepting," Trohan revealed in his book *Political Animals*.

> After WWII, the RFC had lost its economic purpose, but with all those tax dollars on hand it never lost a political purpose.

Others did not have Trohan's scruples. Hall Roosevelt, the President's brother-in-law, used White House telephones to request loans from the RFC. According to Jones, "Two or three loans were made in which it appeared Hall Roosevelt had some kind of interest." At one point the President urged Jones to give Hall the loan he requested because, as Jones wrote in his book, *Fifty Billion Dollars*, "The president wanted to get Hall as far from the White House as possible." Jones also helped FDR's son Elliott escape a $200,000 debt from a failed radio business in Texas.

Defenders of the RFC are quick to cite its many loans and gifts during World War II to big corporations to make weapons and supplies that helped the U.S. government win the war. But even if we assume the right corporations got the right loans and gifts, that still leaves the RFC with no reason to exist after the war. The Great Depression had ended and unemployment had stabilized at under 4 percent in 1946 and 1947, yet the RFC was still aiding corporations.

The Closest Thing to Immortality

True, the RFC had lost its economic purpose, but with all those tax dollars on hand it never lost a political purpose. To repeat what FDR once said about Social Security, the RFC loans "were never a problem of economics. They are politics all the way through." In other words, congressmen eagerly sought RFC money to bring back to corporations in their districts. President Truman noted that "a great many members of Congress had accepted fees for their influence in getting RFC loans for constituents."

Not only were congressmen profiting, but RFC staffers were using these loans to get jobs with the lucky companies. John J. Hagerty, for example, head of the RFC in Boston, endorsed a loan to the Waltham Watch Company. Hagerty soon accepted a job with the company for three times his RFC salary.

In 1953 President Eisenhower ended the reign of the RFC, but not completely. Parts of it reemerged as the Small Business Administration—which began making loans to favored small businesses.

What do we learn from the RFC? First, that government programs are easier to start than stop; second, that those programs will cost more than the originators intended; and third, that federal money becomes politicized very quickly, helping politicians to win votes. FEE

A Return to Gold?

BY JOHN A. ALLISON AND JOHN L. CHAPMAN

"Lenin is said to have declared that the best way to destroy the Capitalist System was to debauch the currency. . . . Lenin was certainly right. There is no subtler, no surer means of overturning the existing basis of society. . . . The process engages all the hidden forces of economic law on the side of destruction, and does it in a manner which not one man in a million is able to diagnose."

— John Maynard Keynes

This summer marked the 40th anniversary of President Richard M. Nixon's decision to sever the U.S. dollar's official link to gold. On August 15, 1971, Nixon took to the airwaves in a national address from the Oval Office to declare that the U.S. Treasury would no longer honor foreigners' demands to redeem dollars for gold. Because the United States was then the last country in the world with a currency defined by gold, it represented a complete and historic decoupling of the globe's currencies—literally the money of the entire world—from the yellow metal.

Central bankers expect to be trusted more than this stuff.
Swiss Banker [Wikipedia]

For the first time in at least 2,700 years, dating to the Lydian coinage in what is now Turkey, gold was used as official money *nowhere* in the world. And for the first time *ever* the world's monetary affairs were defined by a system of politically managed *fiat* currencies—that is, paper money run by governments or their central banks. The story behind Nixon's catastrophic mistake, and the lessons it contains for today, suggest a framework for monetary policy and reforms that will induce strong and sustainable economic growth in the future.

It is important to understand what many current central bankers seem to have forgotten: the seminal importance of *sound* money—dependably valued, honest money whose value is not intentionally manipulated—as an *institution* in a modern exchange economy. Economies grow, and material wealth and welfare advance, through three interconnected phenomena, all of which are crucially supported by a well-functioning monetary unit: 1) efficient use of scarce resources via a system of prices and profit-and-loss, both of which encourage optimizing behavior on the part of all; 2) saving and the accumulation of capital for investment; and 3) the division of labor, specialization, and trade.

Regarding the last phenomenon, we would all be poor, and indeed most of us dead due to starvation, if

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we had to make and produce all our own food, housing, clothing, and other necessities and modern luxuries. As Adam Smith explained in his famous examination of a pin factory, dividing up the metal-straightening, wire-cutting, grinding, pin-head fashioning, and fastening and bundling operations into 18 separate steps increased the productivity of labor in the factory by at least *240-fold*. (This of course dramatically increased productive output and raised workers' real incomes.) And of course for society at large this specialization was not confined to single factories but spread across industries and agriculture: The baker, the butcher, the brewer, and the cobbler could all focus on their productive specialties and produce for a market wherein they could exchange with other specialists for desired goods.

Via economies of scale and scope, then, specialized production and exchange help to create a material horn of plenty for all in a society that's felicitously based on peaceful, harmonious social cooperation. And here's the key: None of this would be possible without a dependable monetary unit that serves as a medium for this exchange. Absent sound money, in fact, a division of labor, with all its specialized knowledge and skills, could hardly be exploited, because barter would mean that, say, a neurosurgeon would have to find a grocer who coincidentally needed brain surgery every time he wanted to obtain food. A barter society is by definition a primitive and poor one.

Similarly, the explosion in human progress in the last three centuries was propelled by the accumulation of capital, the tools, machinery, and other assets that increase per capita output and dramatically increase living standards. And here again, a well-functioning monetary unit facilitates the saving that allows for capital accumulation: Income need not be consumed immediately but can be transferred to others to invest productively in return for future payment streams. Sound money, in short, greatly enhances wealth-creating exchange and transfer of resources *between present and future,* and in doing so often assists in the development of higher output capacity in the future.

There is a third crucial way in which sound money serves to advance civilized human progress: By providing a common denominator for the expression of all exchange prices between goods, money greatly facilitates trade among all parties, thus extending the breadth of markets as far as money's use itself, which in turn *intensifies* the division of labor that increases productive output and per capita incomes. Think about it: Without a monetary unit of account there would be an infinite array of prices for one good against all other goods; for example, the bread-price of shoes, the book-price of apples, and so on. In turn, calculation of profit and loss, on which effective use of scarce resources so critically depends, would be impossible.

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In sum the institutional development and use of money has been an immense human achievement, every bit as important as language, property rights, the rule of law, and entrepreneurship in the advancement of human civilization. And it is important to note that while several commodities were tried as monetary exchange media over the centuries, from fish to cigarettes, the precious metals and especially gold were seen to be most effective, as they are valuable, highly divisible, durable, uniform in composition, easily assayable, transportable, and bear high value-to-bulk, along with being relatively stable in annual supply. In short, in an ever-changing world of imperfection, gold has been found to be a near-perfect, and certainly dependably valued, form of money.

Money, International Trade, and Economic Growth

To understand much about our current economic challenges and what to do to meet them, it is important to understand *why* gold, after several centuries of trial and error, came to be seen as sound money versus paper, other commodities, and even silver. The term *sound money* is especially important to grasp: It is meant to describe a reliable, dependably valued medium of exchange and account, not subject easily to manipulation, which can therefore effectively perform the three functions of money described above, all of which lead to prosperity and an advancing economy. This is critical for a civilized society whose economy is based on monetary exchange, because money is literally one-half of every transaction. So when the value of the monetary unit is volatile—when money becomes more or less *unsound*—it changes the intended terms of trade between parties, especially when that transaction involves exchange between present and future, as in capital investment. This in turn can cause such exchanges to break down or lead to distortions in trade that bring malinvestment of assets and waste of scarce resources.

No better illustration of this can be seen than in the German hyperinflation of 1923. German war reparations mandated by Versailles had so burdened the German economy that the German government took literally to printing the currency known as the *papiermark* in massive quantities. This rapidly depreciated the value of the currency until in the fall of 1923 workers were paid in wheelbarrows of cash twice daily. The velocity of spending skyrocketed, as workers immediately rushed to trade the quickly worthless paper money for anything of tangible value, buying commodities they often did not need. Saving and investment were stunted, price inflation soared out of control, and civil society lurched toward a complete breakdown by the end of 1923, when $1, which had bought 5.21 marks in 1918, now bought 4.2 trillion of them.

At the least, the central bank's mandate included—and seemed to assure—maintenance of the value of the currency.

Seen another way, the German hyperinflation is an example of a "virus" infecting the economy, distorting prices in every transaction, every entrepreneurial investment decision, and the value of every bank account. Every calculation of profit and loss was changed in real terms as well, thus causing resources to be inefficiently used or traded—that is, wasted. While the harm caused by unsound money is usually less than what occurred in 1923 in Germany, it was no less real in a 1970s-style inflation, a 1930s-style deflation, or a 2000s-style housing bubble fueled by falsified interest rates thanks to the Fed's over-creation of money.

Conversely it was sound money, based on the international gold standard, that greatly impelled the fantastic rise in living standards across the nineteenth century in many parts of the globe. Gold as a common medium facilitated dramatic increases in trade and the international division of labor. With a dependably valued international medium of exchange and unit of account, long-term investment could be undertaken, and ever-increasing volumes of mutually profitable trading developed between nations, increasing jobs, output, and living standards dramatically. The century up to 1914 was a golden age of prosperity and harmony among nations, and while not devoid of all war, recessions, or panics, it was comparatively more peaceful and productive than any other period in human history.

The Rise of Central Banking

While the Bank of England was created in 1694, the United States did not get a central bank until the creation of the Federal Reserve System in 1913; by 1935, with the creation of the Bank of Canada, all modern nations had central banks. In theory a central bank, through monopoly banknote issue and effective control of a nation's money supply, serves as a stabilizing influence in an economy by acting as a banker's bank, a lender of last resort providing liquidity in panics, and a regulator of commercial banks and thus governor of their excesses. (However, in a recent exhaustive study, economists George Selgin and William Lastrapes of the University of Georgia and Lawrence White of George Mason University show that recessions were shorter and less severe, inflation and unemployment lower, and economic growth stronger and more durable in the century before 1913 than since the Fed's creation). At the least, the central bank's mandate included—and seemed to assure—maintenance of the value of the currency.

Beginning with World War I, and continuing through the Great Depression and World War II, the links to gold were for the most part effectively severed from most nations' currencies, including the U.S. dollar. In the summer of 1944 economists (led by John Maynard Keynes and Harry Dexter White) met at Bretton Woods, New Hampshire, to design a postwar monetary system conducive to international trade. The resulting mechanism, known as the gold-exchange standard, tried to resurrect the beneficial aspects of the nineteenth century's classical gold standard and lasted until Nixon scrapped it in 1971. In short the Bretton Woods agreement charged the U.S. government with defining the dollar in gold ($35 per ounce) and maintaining convertibility at this rate only with foreign governments and central banks. (Pointedly, there was no similar obligation to *U.S. banks or citizens*; gold had disappeared from circulation in the United States after Franklin Roosevelt's 1933 decree.) In turn all foreign nations were to peg their currencies to the dollar, thereby preserving a regime (however illusory) of fixed exchange rates so as to promote certainty in international exchange and encourage cross-border trade and investment.

By the 1960s this system was beginning to break down on all sides. Foreign governments announced periodic devaluations against the gold-linked dollar to promote exports and allow for domestic government spending, and the United States ramped up "guns-and-butter" federal spending on both the Great Society and the Vietnam War. Inflation slowly crept into the U.S. economy, and gold-redemption requests spiked by the late 1960s at the U.S. Treasury's gold window.

Nixon thus made his fateful decision in the summer of 1971, freeing the government from any redemption obligations. This had two immediate effects: It amounted to an automatic, if stealthy, repudiation of U.S. debt in real terms because it devalued all dollar-denominated assets and currency at once. It also allowed the U.S. government, in concert with a technically independent Federal Reserve, to manage the U.S. money supply for its own political ends indefinitely.

The Predictable Aftermath of 1971

In developing his theory of money and credit a century ago, the great economist Ludwig von Mises explained why a system of fiat currencies was bound to break down: The politicians' urge to inflate the money supply in order to commandeer the resources of the real economy via expanded government spending would prove too great. Further, because the dollar was the de facto reserve currency of the globe post-Nixon (replacing gold itself), any U.S. inflation would encourage other nations' monetary expansions and competitive devaluations in tandem. And indeed, an era of predictable instability has been the result: A trenchant stagflation in the 1970s was followed by banking and S&L crises in the 1980s; Russian, Asian, and Latin American banking crises in the 1980s–90s; overleveraged financial institutions and moral hazard-based bailouts of too-big-to-fail institutions in the 1990s–2000s; and in the last decade or so two Fed-induced bubbles and subsequent crashes. The second of those, based in the housing sector, "went viral" across the world thanks to the huge nominal amount of funds plus leverage of U.S.-based mortgage debt, coupled with the expectation on the part of investors that the U.S. government would guarantee any mortgage-bond losses.

> By increasing the money supply at zero effective cost, central banks encourage government spending and cause interest rates to fall below their natural rate, which induces private investment and a temporary boom.

This instability has starkly proven another tenet of Mises's seminal work: Fiat currencies managed by central banks with a monopoly on note issue, rather than being a source of macro stability, are *themselves the causal agents of repeated boom-and-bust business cycles.* By increasing the money supply at zero effective cost, central banks encourage government spending and cause interest rates to fall below their natural rate, which induces private investment and a temporary boom. But this boom, usually in capital-equipment sectors or long-term durables, is not based on *real* individual and institutional savings. That is, the accumulation of capital is not "backed" by the real resources of society. By definition such a boom is inherently unsustainable and unstable, and must end in a bust and painful retrenchment. The greater and longer the creation of fiat money by the central bank, the harder and longer will be the ensuing recession.

A Path to Reform

The best solution to the myriad problems caused by the Fed's post-Nixon fiat currency management is to return to sound money generated by private markets and intermediated by freely competing banks issuing their own notes. These notes could be backed by any commodity but most likely would involve a return to gold. Banks would compete for customer deposits and loan business on the basis of the soundness of their balance sheets and thus could not over-issue—or else they'd face redemption of their outstanding notes and a potential collapse from a bank-run. Such a system is far more stable than a monopoly central bank without constraints, subject to the inexorable pull of political designs (that is, malfeasance).

> To bring about a sound currency, monetary policy must again become a big political issue—the dominating political issue—in a way it has not been since the presidential election of 1896.

But there are many challenges to developing and implementing such a free-banking system with commodity money; this is the subject of work to be published in the future. Meanwhile a second-best solution would be for the Federal Reserve to cease and desist with any further fiat money creation—in essence, freeze the monetary base where it is, *permanently.* The Fed could then announce an intent to return to full gold convertibility, and any new notes it issued (and used by Fed member banks) would be 100 percent backed by gold. Any maturing securities held as assets on the Fed's balance sheet would be used to purchase gold to build the Fed's reserves. The permanent price of gold would be set over a period of months after the announcement of the new regime, as gold itself and competing currencies traded at new (lower) levels based on the U.S. government's new commitment to dollar stability.

The results of this reform program would be electric and dramatic. Capital investment would soar in the United States, as America became a haven for high-productivity ventures once again. The entire U.S. economy would in effect be recapitalized. While an end to activist Fed monetary policy would raise the short end of the yield curve, over time *real* interest rates would revert to historic low levels due to dollar stability. Such monetary reform implies pro-growth fiscal reforms as well; the U.S. government's profligacy would have to end because fiscal laxity would no longer be supported by an accommodating Fed. A new, sound dollar and a passive Fed would also engender other pro-growth reforms in banking, such as a reduction in or end to deposit insurance and a lower burden of regulations that stunt growth. The banking sector would at once be more competitive, better capitalized, less brittle, and on sounder footing itself.

To bring this about monetary policy must again become a big political issue—*the dominating political issue*—in a way it has not been since the presidential election of 1896, when William Jennings Bryan railed against a "cross of gold." Indeed this can happen if people come to understand that the main culprit of U.S. booms and busts since 1971, and indeed the primary progenitor of the global disaster of 2008—from which we have yet to recover—is the political management of money by the Federal Reserve. Sound money, honest money, besides being a necessary cause of sustainable economic growth itself, is the antidote to the tragically unnecessary torpor of our modern world. FEE

The Family Stone: Cavemen, Trade, and Comparative Advantage

BY RICHARD W. FULMER

Imagine a Stone Age family: Papa Stone, Mama Stone, and their two little pebbles. Suppose that, as befits pre-women's-lib Neanderthals, Papa Stone is initially more competent at every prehistoric survival skill: hunting, fishing, nut-and-berry gathering, fire-building, tool-making. Despite his superior talents, it does not make sense for other family members to sit around waiting for him to do everything. Instead the family is better off if dad does those things that only he can do—hunting perhaps—while the others tackle those tasks that they can do well enough.

In this example Papa Stone has what economists call a "comparative advantage" in hunting while the children have a comparative advantage in collecting firewood. Even though dad can collect firewood more efficiently than the children, the family's opportunity cost in lost game outweighs its benefit from the incremental tinder he could collect were he to forgo hunting in favor of gathering wood.

Once tasks are divided up among the members of the family, each will soon become more adept at his or her work until dad ceases to be the preeminent expert in all things Stone Age. Family productivity will increase and the Stones will become materially better off.

Suppose the members of a neighboring family, the Gravels, are far less capable than the Stones. Despite the disparity in skills, or rather because of it, each family can still gain by trading goods and services—just as the Stones benefitted individually by in effect trading goods and services among themselves. For example, let's say it takes the Gravels two hours to gather a stack of wood and ten hours to capture a rabbit, while it takes the Stones only one hour of labor per stack of wood and three per rabbit. If the Gravels give the Stones four stacks of wood in exchange for one rabbit, they save two hours of labor while the Stones save one.

The exchange creates wealth. Both families gain time they can spend in leisure or in increasing their own material well-being. Note that no trade will occur

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unless each family benefits. Because of the opportunity for gain that trade offers, though, each family has an incentive to discover its comparative advantages with respect to the other and to find those things that can be exchanged to their mutual benefit. Through trial, error, and observation they will quickly learn the ways in which they can best serve each other.

Not only does trade increase the families' wealth, it also makes them more resilient in hard times. If Papa Stone's hunt goes badly today his family may have better luck gathering nuts and berries. If not, the Gravels might have fared better and be willing to exchange some of their harvest for a garment or tool that Mama Stone crafted. The community becomes more resilient as additional families are included in the circle of trade, allowing the realization of economies of scale and a finer division of labor.

Perhaps most important trade brings with it new knowledge and new thoughts. Far more valuable than a tool is the idea of a tool—a rock is just an inert lump until, mixed with knowledge, it becomes a hammer, club, or building block. Without knowledge there are no resources. Throughout history communities on or near trade routes have advanced far more quickly than have isolated peoples. Isolation yields ignorance and ignorance yields not bliss but poverty, disease, and death.

> Unfortunately governments have had a dismal record of picking industry winners and losers.

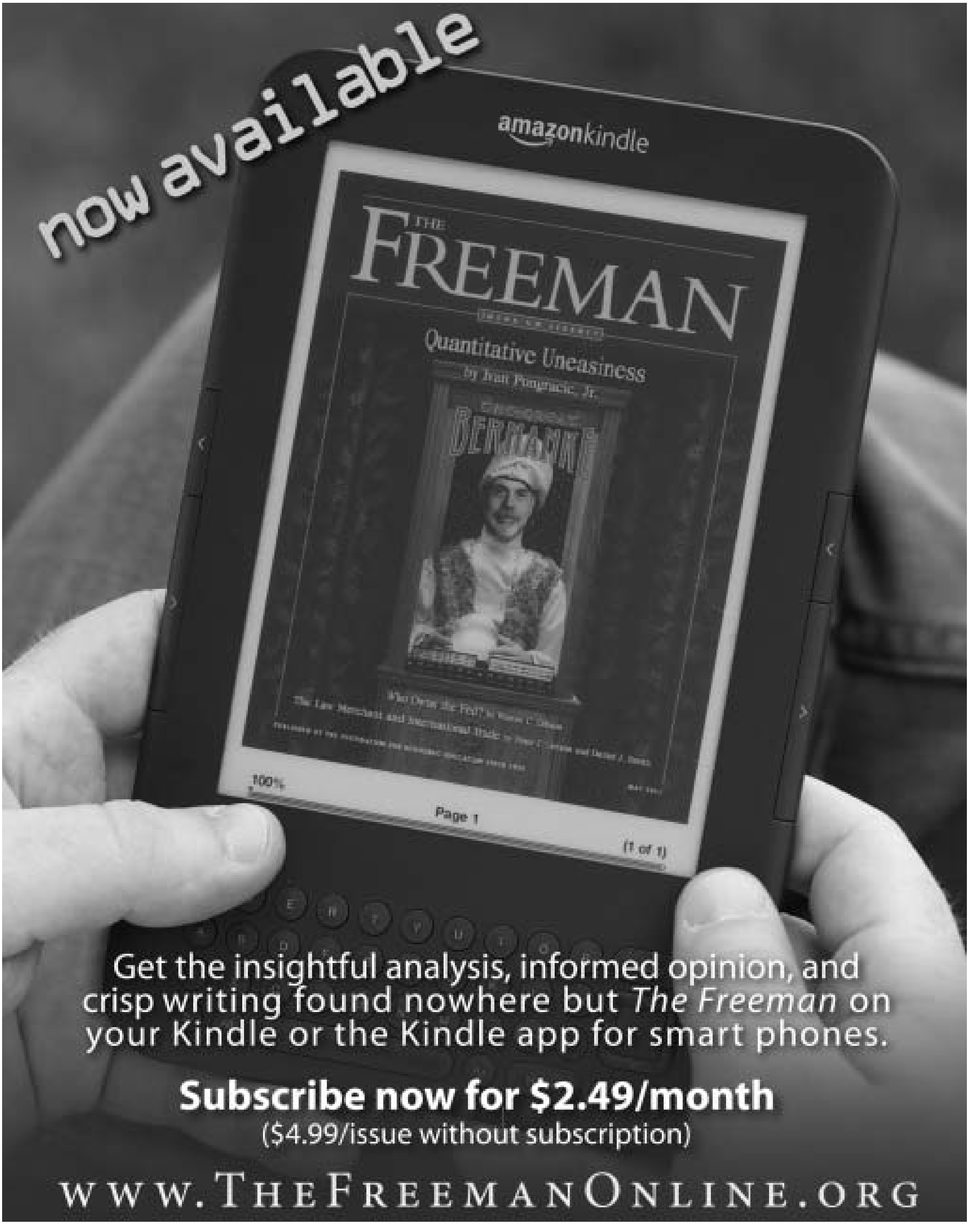
Jumping ahead a few score millennia, suppose that today's Japanese are far more competent at every imaginable task than the citizens of any other country. Despite the disparity of skills, it would not make sense for Japan to produce all of the world's goods while everyone else remains idle. Rather, the Japanese should do those things that only they can do, or for which they are best suited, while others do what they can. After such an international division of labor, people from other countries will become increasingly proficient in their work to the point that the Japanese are no longer the world's experts in everything. People will grow into their niches, world productivity will rise, and poverty will decrease.

Comparative advantage is rooted in differences: differences in skills, culture, interests, location, climate, geology, geography. These differences lead to specialization, which in turn leads to still more differences and still more advantages. Comparative advantage and division of labor are locked in a virtuous cycle of ever-increasing productivity.

Who should determine those tasks for which the Japanese are best suited—to say nothing of the Australians, Brazilians, and Icelanders? Perhaps their respective governments can get together and determine how to best divide up the work. Unfortunately governments have had a dismal record of picking industry winners and losers.

Four decades ago, for example, Japan's vaunted Ministry of International Trade and Industry (MITI) thought that the Japanese were best suited to building ships and actively discouraged the nation's companies from trying to compete with American automobile and electronics firms. Had MITI's view prevailed, the loss to Japan and to the rest of the world would have been incalculable. On the other hand, suppose that the Japanese auto and electronics companies had been mistaken and their attempt to break into American markets had failed miserably. The losses would have been substantial, but they would have been far less than those that would have stemmed from MITI's error. Mistakes made on a small scale are far less costly than those made on a national or international level. They are easier to stop too.

Far better to let individuals, with local knowledge and a stake in the outcome, decide how best to employ their own time, skills, and property. Prices will reveal the comparative advantages these individuals enjoy as they compete with each other in the marketplace. FEE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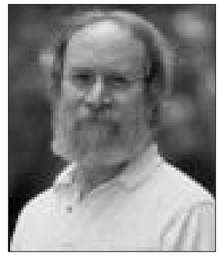
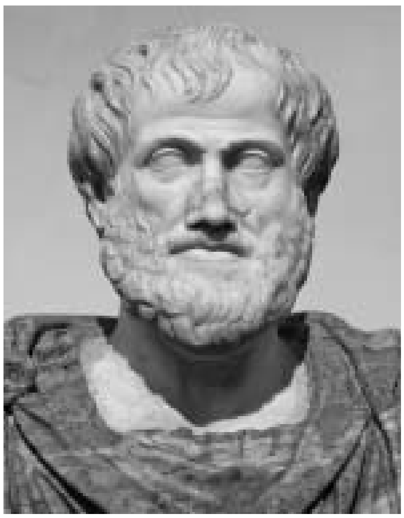


Social Cooperation, Part 2

BY SHELDON RICHMAN

Last month I wrote about Ludwig von Mises's emphasis on social cooperation as the basis of his economic philosophy, particularly in his magnum opus, *Human Action*. I thought I'd follow up with more thoughts on this subject.

Mises was no maverick in this regard. Interest in social cooperation pervades the best classical-liberal and libertarian thought. Paradoxical as it sounds, it is at the heart of the philosophy of individualism. If opponents of the freedom philosophy base their criticism on an atomistic model of the individual, it's largely because too many libertarians overlook their heritage and emphasize that side of the coin to the neglect of the social side.



Liberal thought has never forgotten Aristotle's point that people are inherently social.
Wikipedia

Leading thinkers in the liberal tradition have sought a synthesis of individual and society. In *Social Statics* (1850), Herbert Spencer discussed the "tendency to individuation," which is most pronounced in the human race:

> [The person] is self-conscious; that is, he recognizes his own individuality. . . . [W]hat we call the moral law—the law of equal freedom—is the law under which individuation becomes perfect, and that ability to act up to this law is the final endowment of humanity. . . . The increasing assertion of personal rights is an increasing demand that the external conditions needful to a complete unfolding of the individuality shall be respected. Not only is there now a consciousness of individuality and an intelligence whereby individuality may be preserved, but there is a perception that the sphere of action requisite for due development of the individuality may be claimed, and a correlative desire to claim it. And when the change at present going on is complete—when each possesses an active instinct of freedom, together with an active sympathy—then will all the still existing limitations to individuality, be they governmental restraints or be they the aggressions of men on one another, cease. Then none will be hindered from duly unfolding their natures.

But in the next section Spencer wrote:

> Yet must this higher individuation be joined with the greatest mutual dependence. Paradoxical though the assertion looks, the progress is at once toward complete separateness and complete union. But the separateness is of a kind consistent with the most complex combinations for fulfilling social wants; and the union is of a kind that does not hinder entire development of each personality. Civilization is evolving a state of things and a kind of character in which two apparently conflicting requirements are reconciled.

Thus Spencer foresaw "at once perfect individuation and perfect mutual dependence."

> Just that kind of individuality will be acquired which finds in the most highly organized community the fittest sphere for its manifestation, which finds in each social arrangement a condition answering to some faculty in itself, which could not, in fact, expand at all if otherwise circumstanced. The ultimate man will be one whose private require-

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> ments coincide with public ones. He will be that manner of man who, in spontaneously fulfilling his own nature, incidentally performs the functions of a social unit, and yet is only enabled so to fulfill his own nature by all others doing the like.

For Spencer, to violate the law of equal freedom—"that vital law of the social organism"—is to assault society itself. It sounds as though Spencer is saying that we need society not only for economic exchange and security but something more—because our very nature requires it.

Aristotle

Despite some differences this reminds me of Aristotle. (Fred D. Miller, Jr., finds classical-liberal themes in Aristotle.) In the *Politics* Aristotle states that a *polis* is not merely a collection of individuals seeking gains from trade and safety. It "is a community of families and aggregations of families in well-being, for the sake of a perfect and self-sufficing life. . . . The end of the state [*polis*] is the good life. . . ."

Aristotle famously identified the human being as a social/political animal, a concept inseparable from the capacity to reason, use language, and discourse. In Aristotle's view a human being can live like a human being only in society. We need other people to be fully human because we can't know what we need to know or do what we need to do except through interaction in a community. "For each individual among the many has a share of virtue and prudence," Aristotle writes.

Likewise in the *Nicomachean Ethics* he writes, "For the final and perfect good seems to be self-sufficient. However, we define something as self-sufficient not by reference to the 'self' alone. We do not mean a man who lives his life in isolation, but a man who also lives with parents, children, a wife, and friends and fellow citizens generally, since man is by nature a social and political animal."

The defense of personal liberty is the defense of society.

Endoxa

Auburn University philosopher Roderick T. Long (to whom I am indebted for his discussion of Aristotle in *Reason and Value: Aristotle versus Ayn Rand*) emphasizes Aristotle's view that we can't know very much without help from society. Discussing Aristotle's theory of knowledge and belief, Long notes that for the Greek philosopher *endoxa*, or "reputable beliefs," are critical to the individual. No one builds up her knowledge from scratch on a bedrock foundation. We are born into a particular context and are taught many things, some true and some false. It would be impossible to start over, and fortunately there is no need to. We can begin with the beliefs we have and move forward making adjustments as we find inconsistencies and learn new information. This is necessarily a *social* process. Long writes: "But Aristotle thinks I will have good reasons for including the *endoxa* of others—the collective wisdom of mankind, as it were—among my *endoxa* or *phainomena*. The pursuit of knowledge is a cooperative endeavor, and will be more successful if everyone is allowed to make a contribution."

Aristotle says, "For each man has something personal to contribute toward the truth. . . ." For him, society is not just a *bridge* to the good life, it is *constitutive* of the good life.

I could also invoke Ludwig Wittgenstein (no classical liberal), who drew attention to the intrinsically public nature of language (and hence thought) itself. Wittgenstein, like F. A. Hayek, underscored the communality of rules. "The word 'agreement' and the word 'rule,'" Wittgenstein wrote, "are *related* to one another, they are cousins [like Wittgenstein and Hayek]. If I teach anyone the use of the one word, he learns the use of the other with it."

Only individuals value, choose, and act, of course, but in an important sense the resulting social whole is greater than the sum of its individual parts. Thus the defense of personal liberty is the defense of society. Let's hear liberalism's opponents criticize that. FEE

The Twisted Tree of Progressivism

BY JOSEPH R. STROMBERG

Sorting out the Progressive movement and its constituent ideologies can be difficult in that the very term "progressive" is burdened with contested meanings. Rather than work along lines agreeable to presently out-of-office politicians hoping to regain power by denouncing long-dead Progressives, we begin with some deep background.

One portent of Progressivism is found in the Liberal Republican movement of the 1870s. Prone to Paris Commune panics, distressed by strikes and labor trouble, such reformers as Charles Francis Adams (descended from John Adams), Francis Amasa Walker (Boston laissez-faire economist and Indian manager), and E. L. Godkin (Anglo-Irish editor of *The Nation*) concluded that *efficient*, inexpensive bureaucracy was just the ticket. It could manage questions too important to be left to democratic processes, especially those touching on the lately acquired government-bestowed advantages of big business. ("Efficiency" had a great future before it.) This movement was urban, basically eastern, and closely connected with economic elites (Nancy Cohen, *Reconstruction of American Liberalism*).

Progressivism has so many different sources, it's hardly possible to use the term "progressive" meaningfully.

Another tributary into Progressivism—populism—began in opposition to all the above. Populists stated the case for tariff- and debt-ridden farmers in the South and the West. Their key innovation, or deviation from the Jeffersonian-Jacksonian tradition, was the belief that "the powers of government . . . should be expanded," as their 1892 platform put it. How far this idea actually reached depended on the particular populist, but this new approach brought some of them closer, in method anyway, to the later Progressive movement.

A third source of Progressivism was a university-based intellectual movement whose leading figures included Justice Oliver Wendell Holmes, philosopher John Dewey, economist Thorstein Veblen, and historians James Harvey Robinson and Charles A. Beard. What united them was historicism and cultural organicism (Morton White, *Social Thought in America*). The ferment amounted to "a pragmatic revolt against formalism, abstraction and deductive methodology in the social sciences" (Wallace Mendelson, *Capitalism, Democracy, and the Supreme Court*). Darwinism, variously read, and scientism were among their weaponry.

A vaguer force was post-millennial Protestant reform, originally based in Greater New England, but now of national scope. Kicked off center-stage by science, many Protestant clergymen engaged social causes in a distinctly Progressive spirit. All these tendencies, plus an ingrained American penchant toward panic, pointed toward a busy future.

These forces (and perhaps others) converged on certain economic, social, and political problems stemming from America's rapid industrial growth: the Gilded Age's blatant corruption and subsidies (embodied in the

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railroads, their origins, and practices), labor strife, urban poverty, economic concentration, and financial manipulation. (Subtext: no stone unturned, no child left alone, no person unregistered, and no physical entity unregulated.) (See my October *Freeman* article, "The Gilded Age: A Modest Revision," tinyurl.com/3ocd5ke.)

Progressives were fierce critics of federal courts, which they saw as the bulwark of big business. (This was never exactly untrue.) Their foremost concern was how to sustain the new industrial order while conserving American values and institutions. As they saw it, the main alternatives were: 1) restore competition by various means, including antitrust laws, or 2) accept and closely regulate an economy of large corporations. These conflicting visions constituted a serious fault line within Progressivism.

East versus West Approximates Hamilton versus Jefferson

New Republic editor Herbert Croly tried to bridge the Progressives' divide by setting Hamiltonian means alongside Jeffersonian ends—a "synthesis" that could not survive the slightest clash with real life. Taking "Jeffersonian" as answering roughly to Plan I (restore competition) and "Hamiltonian" as answering to Plan II (accept and regulate big corporations), we can spot the rough geographical outlines of what were (as much of the literature suggests) two quite different forms of Progressivism.

Self-identified Progressives were concentrated in the GOP. Eastern Progressives proposed to regulate big corporate businesses, whose rise they viewed as inevitable. Thus for the eastern wing of the Republican Party "the problem was not how to remedy the evils of the new finance capitalism. [It was] how to manage the discontent it aroused, particularly in the once-docile middle class." The eastern Progressive icon, Theodore Roosevelt, "wished to see the American people governed by a liberal oligarchy; he did not want them governing themselves." By contrast, western Progressives tended to see "big business as an artificial menace to self-government, not merely aided but made possible by a whole system of special privilege" (Walter Karp, *Politics of War*). This means, in effect, that westerners thought some of the damage could be undone. Western Progressivism owed more to populism; it was "more rural and sectional than nationwide" and "represents, in a sense, the roots of modern American isolationism. [It was] less pacifistic and isolationist than it was nationalist," but "opposed to imperialism or colonialism or militarism." Such Progressives rejected American imperial initiatives precisely because of their apparent connections to Wall Street and the British Empire (Richard Hofstadter, *The Age of Reform*).

Eastern Progressives proposed to regulate big corporate businesses, whose rise they viewed as inevitable. Western Progressives tended to see "big business as an artificial menace to self-government, not merely aided but made possible by a whole system of special privilege."

Given this political geography, there was considerable overlap between farm spokesmen and these "populist" Progressives. Historian Elizabeth Sanders writes that the farm bloc pursued specific reforms through *statutory* regulations enacted by Congress and enforceable in the courts, and not through expert commissions and administrative bureaucracies. To that extent, then, they were antibureaucratic. The more developed parts of the Midwest and Pacific coast fell midway between populism and eastern Progressivism, while peripheral western zones and much of the South remained essentially populist.

Further: "[I]t was the periphery that furnished most of the opposition, in both parties, to Wilson's preparedness efforts, for in this momentous sense . . . the agrarians were *not statists*: far more than other sections, the periphery opposed war, standing armies, and imperialism" (Sanders, *Roots of Reform*, italics added). Certainly, these positions ought to count on the antistatist side of the ledger, unless war, militarism, and empire are *not* causes and instruments of aggravated statism. (President Wilson's ruthless purge after 1917 of antiwar Democrats has long obscured the antiwar aspects of populism in the South. See Anthony Gaughan, "Woodrow Wilson and the Rise of Militant Interventionism in the South," *Journal of Southern History*, November 1999.)

It was not just farmers with whom quasi-Jeffersonian western Progressives identified. Senator William Borah (R., Id.) saw himself as a defender of small business and carried on a two-front war against large corporations and state bureaucracies. A noninterventionist foreign policy completed the package. And somewhat jarringly perhaps, Georgism was the default economic position of many Progressives. This makes sense, however, because Henry George's reform program, like that of the farm bloc, rejected administrative solutions. (Ransom E. Noble, "Henry George and the Progressive Movement," *American Journal of Economics and Sociology*, April 1949.)

Creeping American Statism

There are attempts from time to time to father American statism on Progressivism. This will hardly do. First, union-nationalist theorists like John W. Burgess and Orestes Brownson reveled in the vastness of national sovereignty after 1865. In cases like *In re Neagle* (1890), the U.S. Supreme Court theorized abstrusely on national sovereignty per square foot. At the level of ideas there was quite a lot of statism about. Second, as legal historian William Novak writes, a steadily rising curve of interfering ("statist") state and federal legislation runs from the 1870s into the 1920s. This upward trend was across-the-board and predated Progressivism. ("The Legal Origins of the Modern American State," in Austin Sarat et al., *Looking Back at Law's Century*.)

There are attempts from time to time to father American statism on Progressivism. This will hardly do.

Here is one example. After the biggest western landgrabbers crowded small farmers onto marginal lands, especially in California (see my "The American Land Question," *Freeman*, July/August 2009, tinyurl.com/n374pl), the cry went up for federal engineers to build colossal dams in the arid West to help small farmers become competitive. These projects reinvented ancient hydraulic despotism, coupling it rhetorically with a Jeffersonian end. (Donald Worcester, *Rivers of Empire*). Here Veblen's favorite social class, the engineers, did wondrous works and overcame nature itself over many decades. It was impressive—but hardly chargeable to Progressivism.

Progressivism, Law, and State

Eastern, urban Progressives were committed to efficiency, expertise, regulatory bureaucracy, and scientism. Their program was effectively a political phase of corporate liberalism, of which Teddy Roosevelt, an artificial westerner, and Woodrow Wilson, an ex-southerner, offered somewhat different brands. (Wilson's corporate liberalism did not wear the Progressive label.)

An important point of historical controversy concerns the relation of big business to Progressive legislation. Gabriel Kolko has argued that many key statutes were prepared by big-business lawyers and contained provisions intended to cartelize industries by restricting competition and discouraging new entrants. Sanders counters that the resistance of the farm bloc and organized labor sometimes kept business from getting exactly what it wanted (Kolko, *Triumph of Conservatism*; Sanders, 179–182).

The related "capture" thesis holds that, whatever the intention of legislators, the businesses to be regulated will eventually dominate the relevant bureaucracy. American socialist William J. Ghent commented that regulatory bodies were "Irresponsible to both the people and the people's officials" and "peculiarly liable to the influence of the Big Men" (*Our Benevolent Feudalism*). In private, businessmen themselves agreed with Ghent.

To the extent that eastern Progressives were able, between 1900 and 1916, to control legislative agendas nationally and in the states, they unleashed the reign of bureaucratic tidy-mindedness. In southern states legislatures fine-tuned racial segregation and classification (George M. Frederickson, *White Supremacy: A Comparative Study in American and South African History*). In a cross-section of states, legislatures blessed the pseudoscience of eugenics and provided for sterilization of unwanted classes. At the federal level Justice Holmes helped out by finding such laws constitutional. (See Edward Black, *War Against the Weak*.)

There was also what we might call "departicipation"—a trend that reflected upper- and middle-class WASP panic about the working classes, immigrants, and "unassimilable" races. Instances of departicipation included judicial rules narrowing legal standing, increasing top-down control over juries, and eroding common-law concepts; voter disenfranchisement North and South; city manager regimes with at-large voting in city elections and standing armies of police; and finally, detailed task-management in the workplace, or Taylorism. (On the last, see Kevin A. Carson in the September 2011 *Freeman*, tinyurl.com/43zmc8w).

In foreign affairs many eastern, corporate-liberal Progressives favored forceful American expansion into overseas markets. If this required empire—and even war to secure the deal—they were up for it.

Progressivism: A Partial Defense

Murray Rothbard famously called World War I the "fulfillment of Progressivism," a substantially true assertion, if eastern Progressivism is meant. (It was.) One would not wish to defend those Progressives. They gave us the War Industries Board, Prohibition, and much else besides. (Perhaps any war party would have given us some of those.) The war witnessed John Dewey's endorsement of *force* as the royal road to progress and Randolph Bourne's daring escape from Dewey's instrumentalism and liberal practicality (White, *Social Thought in America*).

Even western Progressives were a bit mixed. Some pursued bureaucratic solutions at the state level. But on national issues of war and peace, and on the question of empire, western Progressives like Senators Borah and Robert LaFollette (R., Wi.), and U.S. Rep. Jeannette Rankin (R., Mt.) earned their keep. One suspects this is why contemporary conservatives prefer to jam all Progressives into a single category to be dismissed as statist at home and naive abroad—the better to flog their own impossible program of freedom at home and empire abroad.

One suspects contemporary conservatives prefer to jam all Progressives into a single category to flog their own impossible program of freedom at home and empire abroad.

Progressivism and the New Deal

Progressivism as an outwardly unified (but internally divided) movement effectively ended in the 1920s. American politics limped along, bereft of real ideas. This is normal. Then the Great Depression called forth the New Deal. The ensuing leap into governmental problem-solving wasted the memory of the former days—Novak's previous 70 years of creeping statism. It would be easy, but inexact, to say that the New Deal continued and consolidated Progressivism—but which one? The first New Deal adopted a rather eastern Progressive program of corporatism and cartelization modeled on World War I legislation. Here was the test of Croly's Hamilton-Jefferson synthesis, and it drove many relatively Jeffersonian Progressives out of the New Deal. The administration's later (partial) retreat from corporatism did not bring them back (Otis Graham, *Old Progressives and the New Deal*).

The argument that equates Progressivism with the New Deal and the New Deal with fascism is also misleading. A little care is needed. Certain New Deal economic policies had definite structural resemblances to those of fascist Italy. The New Deal laid *part* of the groundwork for a uniquely American fascism, but did not finish the job. More building blocks would be needed. (Anyway, an exceptional people like Americans deserve an exceptional form of fascism—nicer, bigger, better, more efficient, and so on.)

John T. Flynn was one of those Jeffersonian Progressives who turned his back on the New Deal. He also helped launch comparisons between New Deal and fascist *economic* policy. But more important, he tried to discover what would be required for a completed exercise in American fascism. In *As We Go Marching* (1944), he developed a set of criteria. Measured by those, America was still only potentially fascist. It might be different in the long run. We didn't have to take the same branch at every fork in the road. But we might.

Living in the Long Run

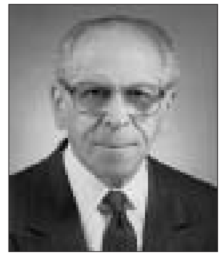
Flynn's checklist for realized fascism was as follows: perpetual public debt, autarchy, socialization of investment, bureaucratic supervision of society, public-works militarism, overseas empire, executive dictatorship, and the institutional changes to make them all work together. Seventy-some years later, we are well along. Flynn was wrong of course about autarchy in the short run. He did not anticipate that one imperial State could become strong enough to force its economic rules on most of the world, while preaching about "free trade."

Progressivism cannot take the blame for every bad thing that came along after it was dead.

Flynn was right, however, about what would hold American fascism together: executive power effectively above the law. (Shelley called monarchy the knot that tied the robber's bundle.) Long ago, tidy-minded eastern Progressives championed executive power but did not perfect it. Other hands—"liberal" and "conservative"—did that. Today important "conservatives" and Chicago-tinged theorists proclaim executive supremacy a universal blessing. (See, for example, Eric Posner and Adrian Vermeule, *The Executive Unbound*.)

American Progressives, Sinners, and Republicans

So here we are, trying to find some shade under the twisted tree of Progressivism. There is a little, and if the tree is twisted, that is partly because so many have made it into various things it was not, while imposing a false unity on it. Some of it *was* bad; but Progressivism cannot take the blame for every bad thing that came along after it was dead. An awful lot's happened since then, and there is a lot of blame to go around. One could wish for a happier ending. FEE



Imprisoning Innocents

BY THOMAS SZASZ

We often engage in behaviors that endanger ourselves and are protected from such actions by warnings—instinctual or those issued by parents, priests, politicians, and physicians. The penalty for ignoring most warnings is the consequence of our actions. In only a few exceptions—"suicidal ideation" or "threat" being one—are we punished for such actions by agents of the State.

Although suicide is legal, failed suicide or communicating the intention to commit suicide is not. Each is a violation of mental health laws, punished by coercions called "hospitalization" and "treatment." In my recent book, *Suicide Prohibition: The Shame of Medicine* (Syracuse University Press), I examine this modern phenomenon and illustrate it with many examples. Here I add a few more typical vignettes.

On February 11 KTLA TV in Los Angeles reported that little Jack Dorman, a 6-year-old child in San Pedro, California, "was pulled out of his elementary school classroom after he sketched a drawing of zombies and stick figures and wrote that he wanted to die." Against the express wishes of his mother, he was incarcerated in a psychiatric hospital. Why? Because in the eyes of the mental health establishment and the school system, he was, prima facie, guilty of the thought crime of "dangerousness to self."

Jack's father, a soldier, was being deployed to Iraq. His mother, Syndi, said her son "was simply upset" because he missed his father and that the school's treatment of her son "was right up there with my worst nightmare."

Before taking Jack to the insane asylum by ambulance, the school authorities notified Mrs. Dorman of their decision. She objected, according to the television report, explaining that he "suffers from separation anxiety and has seen a therapist in the past. On the day he drew the disturbing picture, he was upset that he couldn't stay home with his family [and she added] that she would immediately take her son to see his own therapist."

Nevertheless school officials "called a Los Angeles County psychiatric mobile response team. They determined Jack needed to be committed to a 72-hour psychiatric hold at a local hospital. . . . Los Angeles Unified School District Superintendent Ramon Cortines released a statement, saying, 'When any student indicates a desire to take his or her own life, the LAUSD is required to follow strict protocols to ensure the safety of the student. . . . The safety of LAUSD students is paramount. We did the right thing here.'"

This is medical sadism masquerading as suicide prevention. Worse, it is educational entrapment masquerading as compassionate concern for "kids." From kindergarten on American children are routinely given crayons and encouraged to "express themselves." Often their drawings are interpreted as if they were the productions of potentially dangerous persons providing "psychiatric insights" into their "minds." Thus children are diagnosed as mentally ill, ejected from school, incarcerated in insane asylums, and drugged. They as well as their parents are victims of legal-psychiatric entrapment, an outcome due in part to the fact that many Americans—parents especially—have eagerly entrapped themselves in the psychiatric protection racket.

After 48 hours, little Jack was allowed to go home. Not surprisingly, he now has a bona fide mental illness, "school phobia": "He's afraid they are going to take him away again," says his mother.

When Suicide Prohibition Promotes Suicide

Prohibitions tend to promote the very things prohibitionists ostensibly seek to prevent. Suicide prohi-

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bition is no exception. When the result is unqualified evil, as it often is, we insist on misinterpreting the causal sequence, as the following story illustrates.

In February the Everly Funeral Homes in Fairfax, Virginia, placed the following notice on its website: "Mr. Nicholas L. 'Nick' Stuban, age 15, of Fairfax, VA, passed away on January 20, 2011. . . . In lieu of flowers, the family requests donations in Nick's memory to any organization dealing with Teen Depression and Suicide Prevention."

Nick Stuban was a popular football player at W. T. Woodson High School in Fairfax County. He was a good student, well behaved, and well liked by teachers. He did not "pass away." He killed himself. Why? Because of a set of events set in motion by punishment for buying a capsule of a legal substance, JWH-018, a synthetic compound with marijuana-like properties.

On November 3, 2010, Nick was suspended from school. For almost three months he was banned from attending weekly Boy Scout meetings, driver's education sessions, and all sports events. "He felt stigmatized and grew isolated. . . . [T]he teen rumor mill produced exaggerated versions of why he'd been suspended. Some friendships slipped away. His sense of accumulating unfairness rose," one news report stated. This was not the only trauma Nick had to cope with. His mother, disabled by amyotrophic lateral sclerosis, was dependent on a mechanical ventilator and cared for by her husband, nurses, and Nick.

On November 16, Nick and his parents—his mother in a ventilator-equipped wheelchair, attended by a nurse—participated in a hearing on the charges against him. They followed the advice of a Woodson administrator who warned against bringing in an attorney "because it might create a confrontational climate." The hearing was worse than confrontational; it was inquisitorial. The hearing officer said to Nick: "You haven't really given us a good reason why you did this, and we suspect you were really looking to buy something else." "Why don't you believe me?" Nick asked, according to his father.

The board ruled against Nick, assigning him to another school. "By then, Nick's descent had begun," a newspaper reported. "His father recalls he was quiet, head down when he went to see his new high school." On December 30 Steve Stuban walked into his son's bedroom and saw a plastic bag of marijuana. He now realized that Nick's "disciplinary experience had inadvertently encouraged the behavior it was designed to discourage. 'Nick was looking to pot to ease his pain,' said Sandy Stuban." Desperate, Nick sent a text message to a friend saying he wanted to take his life. "After a tense night, when he wandered off and police searched for him, his family took him to a mental health clinic. He was admitted to a psychiatric hospital." A week later, diagnosed with depression, Nick was released. The psychiatrists told the parents "they didn't think Nick would harm himself." They advised counseling, which he started, and prescribed an antidepressant, which he took.

In the hands of the educational and mental health establishments, this could be a kid's ticket to a psychiatric hospital.
Zeimusu [Wikipedia]

Were the Stubans unaware that the alliance between the educational system and the mental health establishment was responsible for their predicament? Or did they realize it but deny this frightful insight? We do not know. What we do know is that they bought into Nick's psychiatric degradation disguised as scientific mental health practice and suicide prevention.

On January 5, 2011, Nick killed himself. He left a note for his parents in which he referred to "life's unfairness." Poor Nick was too young to recognize that, more than unfairness, his mistreatment was a manifestation of the malice lurking in the hearts of all too many unhappy educational and mental health professionals. FEE

Money Is Not Speech

BY MICHAEL CUMMINS

"The Supreme Court said that money equals speech!"

Proponents of campaign finance regulation have thrown this trope around freely since 2010's landmark Supreme Court ruling in *Citizens United v. Federal Elections Commission*. Fortunately, the Court never actually made such an absurd equation. It would be hard to take the Court seriously if it had.

But the phrase is not just a throwaway idiom. For those who push the idea to the public that the Court has ruled as such—opinion leaders who should (and maybe do) know better—the phrase serves to caricature the Court's reasoning on campaign finance issues vis-à-vis the First Amendment. And the last thing America needs is to misunderstand the Court when it is actually doing its job: protecting constitutional freedoms from a meddlesome Congress.

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The widespread mischaracterization likely stems from an earlier widespread mischaracterization, that of the ruling in *Buckley v. Valeo* (1976). *Buckley* overturned restrictions on independent political spending by citizens and associations, and on candidates' personal spending. A shocking number of scholarly texts and newspaper citations assert that in *Buckley* the Court ruled that "money is a form of speech." (Even Wikipedia's open-source entry for *Buckley* claimed this at the time of writing.)

In *Citizens United* the Court went beyond Buckley, ruling that the federal government may not limit corporate or union spending on independent political expression. The ruling is consonant with the text of the First Amendment's Free Speech Clause, "Congress shall make no law . . . abridging the freedom of speech." Note that the clause concerns itself solely with its subject—Congress. The nature of the speaker—individual, group, or corporation—was apparently of no matter to the framers.

But putting aside the merits of the Court's ruling, what relationship does it cast between money and speech?

Though reams of learned text have been devoted to the topic, most economists agree on the very basics of what money is. It is credit for service rendered. Even when we purchase a *good*, all we pay for is the service of the raw materials having been located, gathered, altered, combined, and then brought to a location convenient to us. If I have a dollar, then I have made a sacrifice (assuming it was not a gift or loot . . . and I'm not a banker!). I expect to be able to use that dollar to induce another person to make a sacrifice on my behalf. Services can exist independently of money, as in a barter system or when we perform a service directly for ourselves. But every service we receive, however it may come to us, requires a sacrifice from *someone* for its performance.

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Consider the interplay of money, service, and sacrifice in the hypothetical case of a young idealist who wishes to exercise his right to free speech.

Speech Isn't Free

He considers walking to the town square to regale passersby with his opinions. But he instead decides to take funds from his paycheck to buy a bus ticket. The result of either plan would be the same. His fellow citizens are treated to his well-reasoned proclamations. So do the two dollars he pays for his bus ticket have any nominal connection to the speech he engages in? Would anyone say that the two-dollar fare "equals" his speech?

The idealist's original plan—to walk to town—would by no means have been cost-free. Depending on what he does for a living, it might even have cost more than the bus fare. He would have had to exert himself—at his job or in his garden—to procure the extra food needed to fuel his walk, sacrificing other services he might have enjoyed with those energy resources. Had he eaten just his usual amount before leaving his house, then the energy he consumed walking could have been used instead to, say, mow his lawn. Or perhaps he would have mowed his neighbor's lawn . . . for ten dollars.

There is absolutely no cost-free way to express political beliefs to our fellow citizens. And the cost involved is the means to a completely distinct end.

The point is that there is absolutely no cost-free way to express political beliefs to our fellow citizens. And the cost involved is the means to a completely distinct end.

Certainly, the money that corporations use to effect political expression is of a much larger scale than that involved in the foregoing example. But though some will balk at the notion, it really is just a difference in degree, not in kind. And even if one believes the scale of spending matters when it comes to political expression, "money" cannot be equated with "speech" in any analysis.

Poll Taxes

But money is the operational equivalent of resources, and to regulate the expenditure of resources for political expression is to regulate the expression itself. It brings to mind Jim Crow-era poll taxes. Racist state legislators claimed that they were not violating the Fifteenth Amendment with such fees, because poll taxes were not an actual prohibition on voting. For decades the Supreme Court bought this argument, failing to recognize that interference with the necessary means of voting is tantamount to disfranchisement.

So, much as they might try to fool themselves and others, proponents of campaign finance limitations are opponents of free speech. In many ways, their concerns are understandable—corporate power in today's America is daunting. But instead of tinkering with fundamental rights, perhaps they should strive instead to hold the federal government to its constitutionally limited functions. With few governmental goodies to be had, and few onerous regulations to fear, corporate America would undoubtedly regard massive political expenditures as a massive waste of money. FEE

The Age of the Busybody

BY RIDGWAY KNIGHT FOLEY, JR.

Busybodies. In an earlier, gentler time, every neighborhood had one. Predominantly but not exclusively female in those days, the local busybody was recognized with ease. Although the verb was mercifully unknown, she micromanaged all PTA meetings, gatherings, sales, and affairs whether or not she was chairman or even occupied a seat on the governing board. She notified all neighbors about the proper means and methods of raising their children, managing their households, and directing their spouses. Since she knew more about everything than anyone else, she offered unsolicited commands disguised as suggestions to the community grocer, the resident pharmacist, and the sales managers at the five-and-dime, variety, shoe, and apparel stores. In essence, she minded everyone else's business.

One other trait of the busybodies stood tall for all thoughtful folks to perceive: They were far too busy minding the business of all within their fiefdoms to mind their own business, to care for their own children, and to manage their own households.

Times are no longer simple and gentle and safe, but the busybody has not only survived but also prospered, become fruitful, and filled every crevice and cranny of the nation. Fifty years ago my father insightfully titled his speech to a San Francisco business gathering as I have this article. He observed that in the years following World War II, busybodydom had flourished like an obnoxious weed, threatening to crowd out the air and light of individual ideas and purposeful personal action, and in this manner destroy the nurture encouraged by stable and essential decisions. The past decades verified Jack Foley's observation and warning and, unfortunately, we reside today in times dominated by throngs of busybodies.

Rules and regulations, orders and directives, all kinds and kindred of commands direct almost every avenue of our daily lives. Virtually all these directives emanate from busybodies and almost all of them are, or may be, enforced by the power of law; that is, the noncomplying person suffers a penalty, usually loss of liberty or property, occasionally the loss of his life. Our lives today are ruled by force writ large, a force that usually commands far less efficacious outcomes than would result from the free actions flowing from purposive and creative individual conduct.

> Unfortunately, we reside today in times dominated by throngs of busybodies.

When we consider legally compelled directives, we blandly think of the tripartite governmental structure of the federal government and the similar political construction of the several states, and we see in theory a legislative branch that enacts laws, an executive who administers those laws, and a judiciary that interprets rules and issues orders based on and about those laws. Myopically we do not see the whole regulatory blight that afflicts us because we overlook several obscured but essential components of law-making. Without limitation, consider the following busybody regulators.

Legislate and Delegate

First, state and federal legislators seldom enact detailed statutory law. Most often they pass broad

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policy statements and "delegate" detailed rule-making and enforcement powers to an administrative bureaucracy. The critical characteristic of this rule-making and law-enforcing apparatus is that it is unelected, usually unknown, and fundamentally untouchable and ungovernable. While the legislator theoretically oversees the detailed conduct of the administrator, in fact oversight is nonexistent in almost all instances. Hence the common retort to those who disagree with overwhelming and strangling legislation that "you can reject the legislators at the next election" is a sham and a chimera. Legislators come and go, normally after enhancing their own wealth remarkably, but the unelected bureaucratic rule-makers and rule-enforcers remain for a lifetime, ordinarily protected by compulsory civil service "safeguards" and most assuredly made wealthy by huge and untouchable pensions and other emoluments of the office.

Legislators come and go, normally after enhancing their own wealth remarkably, but the unelected bureaucratic rule-makers and rule-enforcers remain for a lifetime.

Second, concentration on legislators obscures the rule-making and enforcement/enhancement of the executive. In federal terms the president often creates very real and effective restraints on individual rights and conduct by use of executive orders; to make matters worse, these orders are usually hidden from common view and secreted under some sort of "national security" or "rule of necessity" rubric. They may be printed and published but often remain cloaked in secrecy. Many governors possess and use similar powers.

Third, it is all too easy to overlook or forget the myriad municipal and quasi-municipal corporations that regulate the fiber of our lives. Busybodies abound and prosper in local improvement districts, school districts, sewer districts, government-owned and -operated utilities, park and recreation districts, and a Mongol horde of other quasigovernmental entities in addition to the more obvious and long-recognized city and county governments. Each and every one of these institutions possesses and exercises the power to enact and enforce rules that compel or constrain individual human behavior and, more odious, many of these rules are produced in the shadows and are difficult to locate until enforcement suddenly becomes an issue.

Fourth, the day of the judge as a limited dispute-decider has long passed. To a greater or lesser degree, federal, state, and local judges make regulatory law by purporting to "interpret" legislation in a manner not dissimilar to the rule-making and enforcement-enhancing activities of the administrative apparatus. Once again, many members of the judiciary serve for lengthy terms or for life and are seldom sanctioned by the voting public.

Root Causes

A search beneath the surface of this calamitous condition reveals at least two elemental causes. Reining in the busybody requires a brief analysis of each, neither of which is easily recognized nor fully appreciated.

To begin, people are inclined to be busybodies. No one should overlook or deny the infinite variety in human behavior; nonetheless permit some generalizations to illustrate my greater point. We humans tend to egotism, an ingrained belief that we can perceive a condition and prescribe a proper conclusion, and do so much more accurately and appropriately than any other person. In addition we tend to judge ourselves much less harshly than we do others, meaning we are more forgiving of our own mistakes than of the errors of our fellow man.

Busybodydom results from the conceit and concatenation of these everyday human traits. It causes perfectly ordinary—that is, flawed—persons to see what they perceive as a problem requiring a solution and to decide on the proper process by which to resolve the problem. More than that it encourages the observer to believe that his is the only suitable method and disposition, and it compels him to seek out others to join him in foreclosing any alternative process or solution by the force of law.

Rules and Orders

Second, one must appreciate the essential and elemental differences in types of legal commands, one of which encourages the current State's incipient tendency toward busybodyness. Legal philosophers commonly divide legal commands into two categories: rules and orders. Such philosophers may disagree that rules and orders comprise the sum of human law, but these general categories illustrate the larger point of this essay.

In simple terms rules refer to statutory or regulatory enactments by legislatures and other similar governing bodies, which seek to identify a situation or condition, command by force of law an express outcome in all such and similar contexts, and prohibit and penalize any alternative individual or group action or outcome. On the other hand, orders simply refer to the legally enforceable decision by an arbiter of a dispute chosen by specified individuals or entities.

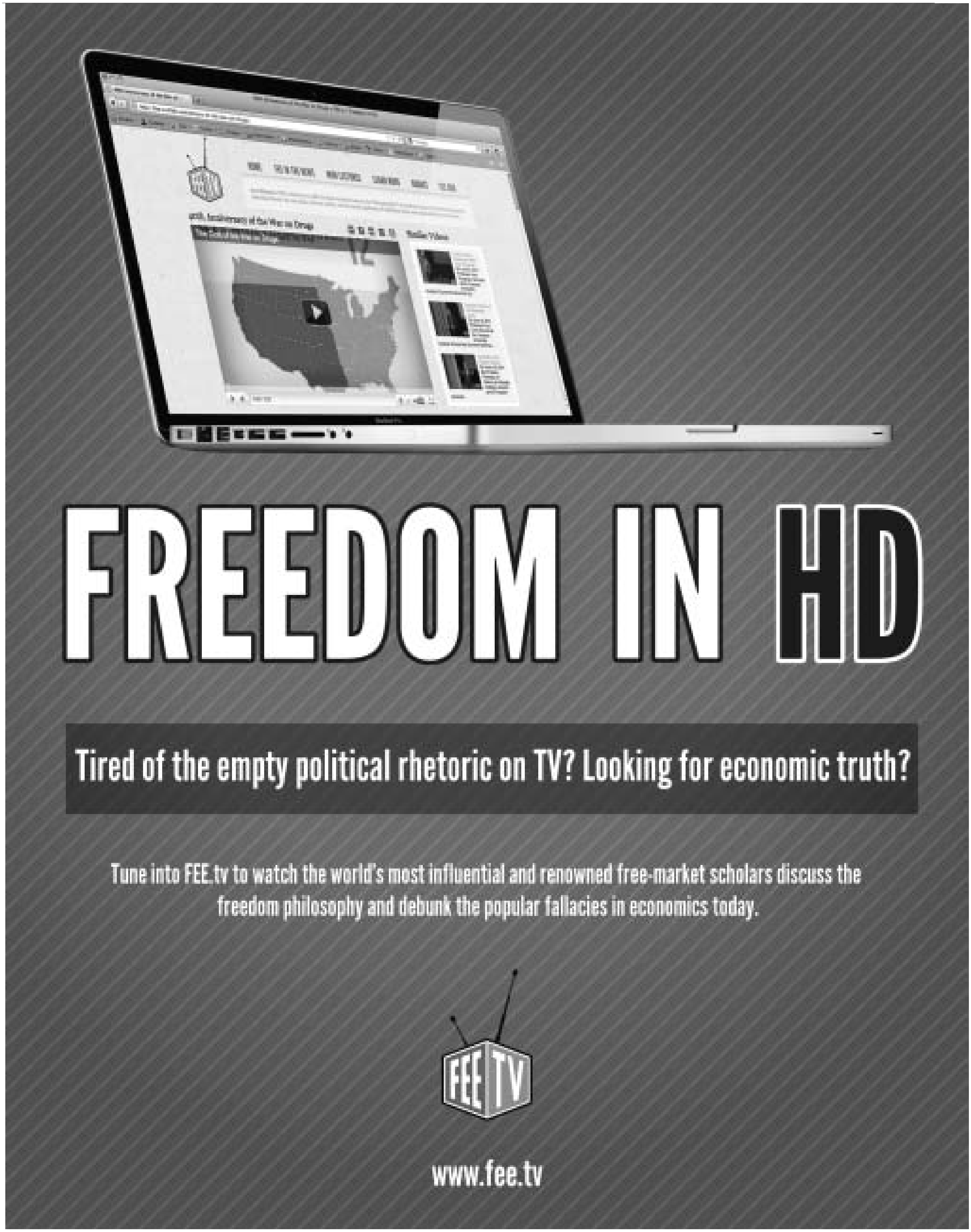
Even given the blurry line between rules and orders, appreciated only by the jurisprudential philosopher, this primary distinction illustrates one of the reasons that modern busybodies truncate human choice and inhibit productive individual action. Rule-making attempts to foresee most or all human interactions and to prescribe in advance all legally acceptable outcomes. Ordering conduct differs because it uses (or should use) the force of law only in a more limited fashion, purporting to decide a particular dispute between identified human beings or groups, and designing an outcome limited to those persons and others in direct relationship with them. The more limited the legal intrusion, the more open-textured the law. Orders tend to restrict creative human behavior less than do rules because orders arise in single instances (although English and American courts do tend to decide like cases in a similar manner under doctrines labeled by the quaint Norman-French-Latin phrases *res judicata* and *stare decisis*), where 1) discrete and specific facts can be assessed and evaluated and 2) only the individuals directly or closely affected (all of whom generally are able to participate in the proceeding) are governed and legally limited by the outcome.

Rules, to the contrary, attempt to forecast and prescribe limited permissible outcomes for all persons in all cases without the benefit of individual factual evidence and express relevant participation. Yet human beings are limited in their ability to forecast correctly; indeed we have trouble even figuring out how history has produced our current conditions. As a result, rulemaking tends to stymie human action and the improvement of civilization by foreclosing individual choice.

In fact the beauty of the traditional Anglo-American common law lies in its primary reliance on orders and its reluctance to employ an abundance of rules. The open legal texture enabled creative individuals to compose new and untried outcomes that, in a given number of instances, resulted in a much better life not only for the persons directly affected but also for a multitude of other beneficiaries. Thus individual conceit and the surfeit of rules join and promote a more closed society. Consider the result: an obvious diminution of human freedom and restraint on free individual action to solve problems. Empirically, the busybody inhibits the improvement of the general human condition. Why does that happen? Simply because each competent actor is more able to make better decisions affecting his person and his future than is any other individual. Free and purposive human beings effect better results when they have something personal at stake, and no person is sufficiently foresighted and wise to recognize all aspects of a problem and all possible outcomes.

> Rule-making tends to stagnate human action and the improvement of civilization by foreclosing individual choice.

Further, the age of the busybody contains a moral component and induces a moral decline of the individual. One grows by choosing, by selecting between alternatives, and by enduring the burdens of his poor choices as well as enjoying the benefits of his better selections. The busybody foreordains decisions by rule of law and in so doing diminishes the choice-making opportunities and growth available to his fellow members of society. In this fashion the busybody stunts individual growth and deprives the larger society of the benefits of unfettered productive and constructive human action. FEE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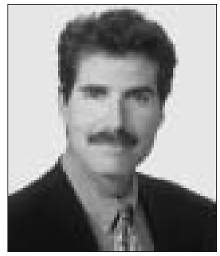

Ten Years After

BY JOHN STOSSEL

After 9/11 the U.S. Congress created the Department of Homeland Security and the Transportation Security Administration (TSA). America went to war, overtly and covertly, in several countries. Nearly $8 trillion was spent on what is called "security," Chris Hellman of the National Priorities Project estimates.

Was it worth it?

Yes, in many ways, says author Ann Coulter. No, says *Reason* magazine editor Matt Welch.

"There's no reason at all that the bureaucratization of security is going to make us any more safe," Welch said. "All we have to do is go on an airplane . . . to see that there's a difference between security and security theater, between federalizing a problem and actually solving the problem."

Coulter thinks the government got lots of things right.

"Whatever liberals screamed bloody murder about was very important on the war on terrorism," she said. "I think Iraq was a crucial part . . . ." Welch dissented.

"We're on the verge of bankruptcy. . . . We are at the sort of tipping point of imperial overstretch."

Imperial overstretch? Welch has a point. Politicians talk about tight budgets, but *National Defense Magazine* recently ran this headline: "Homeland Security Market Is Vibrant Despite Budget Concerns." I fear this is the military-industrial complex President Eisenhower warned us about. Military contractors collude with politicians to keep the money flowing.

I blame the politicians. The contractors just do what they're supposed to do. The politicians are supposed to spend our money well. They don't.

After 9/11 the Senate voted 100 to zero to federalize airport security. Then-Sen. Tom Daschle said, "You can't professionalize if you don't federalize."

Nonsense. Before the TSA was created private contractors paid airport inspectors not much more than minimum wage. They weren't very good. Now we spend five times as much, and they're still not very good.

Today even the TSA knows that private security is better. In one of its own tests its screeners in Los Angeles missed 75 percent of the explosives planted by inspectors. In San Francisco, one of the few cities allowed to have privately managed security, screeners missed 20 percent.

> Before the TSA was created private contractors paid airport inspectors not much more than minimum wage. They weren't very good. Now we spend five times as much, and they're still not very good.

In a reasonable world the government would disband the TSA and move to a private competitive system.

But we live in a Big Government world.

The Health of the State

Randolph Bourne, who opposed U.S. entry into World War I, said, "War is the health of the state." He meant that in war, government grows in power and prestige—and freedom shrinks. As *Freeman* columnist Robert Higgs of the Independent Institute documents in *Crisis and Leviathan*, government never recedes to its prewar dimensions.

Shortly after September 11, Sen. Charles Schumer declared that the "era of a shrinking federal government

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is over." This was more nonsense. The government hadn't been shrinking. But for politicians like Schumer 9/11 was an excuse to take more power. Price was no object.

I can't tell you what Homeland Security does with your money. Much of its spending is secret. Certainly much is wasted. The department made a big fuss over its color-coded airport security system, then scrapped it because it provided "little practical information." The department spent billions on things like special boats to protect a lake in Nebraska, all-terrain vehicles for a small town in Tennessee and 70 security cameras for a remote Alaskan village.

That's what politicians do. Members of Congress say, "You want my vote? You'd better give my district some cash." And when people are scared, they let bureaucrats spend.

This played into Osama bin Laden's hands. In one videotaped message he talked about "bleeding America to the point of bankruptcy."

The attacks on 9/11 were largely a failure of government. Our so-called "intelligence agencies" knew nothing about the plot. The Immigration and Naturalization Service, charged with keeping track of foreigners who overstay their visas, did not pay attention to the 19 hijackers. And as Rep. Ron Paul points out, history did not begin on September 11. Part of the failure was America's interventionist foreign policy, which needlessly made enemies.

The attacks on 9/11 were largely a failure of government.

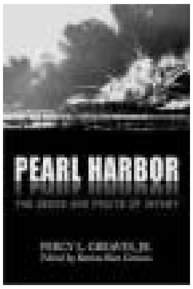
So government failed on 9/11, and yet the politicians' answer to failure is always the same: Give us more money and power. And we do. When will we learn? FEE

Book Reviews

Pearl Harbor: The Seeds and Fruits of Infamy

by Percy L. Greaves, Jr., edited by Bettina Bien Greaves
Ludwig von Mises Institute • 2010 • 937 pages • $24.00

Reviewed by Jim Powell



For decades the prevailing view among historians has been that because the American people were too stubborn and stupid to concern themselves with foreign wars, President Franklin Roosevelt had to lie for a noble cause—namely, waging war against imperialist Japan and Nazi Germany.

Seldom have historians asked themselves why Americans would want to stay out of foreign wars. In 1940 Americans knew that the last time the subject came up was during the 1916 election, when President Woodrow Wilson vowed to keep America out of World War I. He won the election and the following year persuaded Congress to enter what he claimed was "the war to end all wars" so he could "make the world safe for democracy." Instead the peace treaty triggered the bitter nationalist reaction that generated political support for Adolf Hitler's totalitarian movement. Clearly those who wanted America to enter foreign wars were utterly unable to anticipate the horrifying consequences. Thus in 1940-41 many Americans wanted nothing to do with the wars in Europe and Asia.

FDR figured that if he could provoke the Japanese to attack the United States, the American public would support a declaration of war against Japan. Since Japan was allied with Germany, a war with Japan would bring America into the war against Germany. FDR was anxious to help his beleaguered British friends, even though most Americans wanted to remain at peace.

Pearl Harbor: The Seeds and Fruits of Infamy is a suspenseful detective story of that behind-the-scenes political scheming. The initial draft of the book was written by Percy L. Greaves, Jr., who served as chief of staff to the Republicans on the Joint Congressional Committee, which investigated Pearl Harbor in 1945-46. Greaves combed through countless documents and interviewed all the major (and many minor) figures involved. He continued to investigate for many years afterward, finding key pieces of evidence overlooked by everyone else. After he died in 1984, his wife, longtime FEE staffer Bettina Bien Greaves, spent more than two decades turning the manuscript into a monumental scholarly achievement.

Pearl Harbor is among the most provocative mysteries in American history. In Greaves's account FDR appears as the grand puppeteer manipulating events—even when this meant sacrificing American lives. While the Japanese bombing is almost universally described as an outrageous surprise attack, the book presents considerable evidence that it wasn't much of a surprise to FDR. Although he probably didn't know for sure where or when the Japanese would attack, he had many reasons to expect they would, and Pearl Harbor was a good bet to be the target.

As the book documents, in January 1940 the U.S. government began blocking exports to Japan, including strategic minerals, iron, steel scrap, and petroleum products like gasoline. Since the Japanese weren't willing to abandon their ambitions for conquest in Asia, it should not have been surprising that they would attempt to retaliate against the United States. In fact, when questioned by his wife, Eleanor, about his economic policies toward Japan, Roosevelt admitted that they were driving the two countries toward conflict.

Moreover, in 1940 American cryptographers cracked the top Japanese diplomatic code—known as "Purple"—used to transmit messages. That enabled U.S. officials to learn a great deal about what the Japanese government was planning. Much of the intrigue and suspense in the book involves the interception and decoding of Japanese diplomatic messages. The research done by Percy Greaves demolishes the idea, long cultivated by FDR's followers, that the attack on Pearl Harbor took the President and his military advisers completely by surprise.

What had FDR and his advisers known—and when? After reading the book it seems beyond question that the administration knew late on December 6 that a Japanese attack was imminent, with Pearl Harbor a likely target, and yet no one took immediate action to warn the endangered base. The two Hawaiian commanders, Admiral Husband Kimmel and General Walter Short, were scapegoated to hide the administration's incompetence and duplicity. After rigging a hasty "investigation" that declared Kimmel and Short derelict in their duty, the military engaged in a cover-up. Evidence was tampered with. Officers were pressured to have convenient "memory lapses" under questioning from counsel for Kimmel and Short. Army Chief of Staff General George Marshall (famed for the postwar Marshall Plan) comes off looking especially bad in the book's recounting of events.

The book has two important lessons for today. One is that using duplicity to enter foreign wars is likely to backfire with terrible consequences for the ordinary people of a nation. The other is that politicians will stop at almost nothing to make themselves appear great and heroic. I recommend this book highly.

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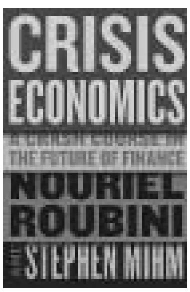
Crisis Economics: A Crash Course in the Future of Finance

by Nouriel Roubini and Stephen Mihm

Penguin • 2010/2011 • 368 pages • $27.95 hardcover; 17.00 paperback

Reviewed by George Selgin



Nouriel Roubini and Stephen Mihm's book on the great subprime crisis gets off to a good start by dismissing as a red herring the "tired" argument attributing the boom to "greed" and focusing instead on "changes in the structure of incentives . . . that channeled greed in new and dangerous directions." These included programs aimed at increasing poorer persons' access to mortgages, the growing moral hazard connected to "too-big-too-fail" (TBTF), and the Fed's post-2001 easy-money policy. Greenspan, they write, "muted the effects of one bubble's collapse by inflating an entirely new one," while the "Greenspan put"—a policy of letting asset bubbles inflate while promising to rescue firms that suffer when they burst—"created moral hazard on a grand scale."

The authors' criticisms of the Fed's response to the crisis are no less trenchant. "In its rush to prop up the financial system," they observe, the Fed rescued insolvent financial institutions, exposing taxpayers to losses on toxic assets while helping to "sow the seeds of bigger bubbles and even more destructive crises."

But although Roubini and Mihm draw attention to some ways in which the government contributed to the crisis, they go seriously wrong in claiming that the boom "was primarily underwritten not by Fannie Mae and Freddie Mac but by private mortgage lenders like Countrywide": Although Fannie and Freddie didn't *originate* any subprime loans, they bought and (implicitly) guaranteed plenty of them, including a very large share of Countrywide's Community Reinvestment Act (CRA) "Best Practice" loans. What Fannie and Freddie didn't buy other lenders did, to meet their own CRA requirements. Such facts undermine Roubini and Mihm's conclusion that "the significance of government intervention was dwarfed by the significance of government inaction."

Roubini and Mihm's reform proposals also fail to properly weigh government policy's contribution to the crisis. They start well again by insisting on the need to restore to financial services "the creative destruction that Schumpeter saw as essential for capitalism's long-term health." Although Lehman Brothers' failure revealed the shortcomings of ordinary bankruptcy as a means for resolving large and heavily leveraged financial firms, Roubini and Mihm note how those shortcomings could be avoided by means of "living wills" or by splitting ailing firms into "good" and "bad" parts, so that the latter might be declared bankrupt without raising Cain.

But some of Roubini and Mihm's other proposals appear useless at best, including their endorsement of a "beefed-up" Glass-Steagall that would forcibly break up enterprises that become too big to fail, with its implicit suggestion that Gramm-Leach-Bliley contributed to the crisis. In fact that 1999 "repeal" of Glass-Steagall merely allowed commercial banks to affiliate with investment banks and played no important part in the insolvency of Lehman Brothers and other independent broker-dealers that was at the heart of the crisis.

A beefed-up Glass-Steagall Act might of course spin a much tighter web of firewalls than the original did. But as Roubini and Mihm themselves suggest, many TBTF firms exist only thanks to "heavy helpings of government largess," including guarantees and actual bailouts, and could be left to break up naturally once improved bankruptcy procedures are in place. Perversities in executive compensation might likewise vanish on their own once imprudent decisions lead to bankruptcy rather than bailouts.

The most disappointing part of *Crisis Economics* is the second chapter's hackneyed history of thought. Here Adam Smith is portrayed as a Walras-Debreu *manqué* who blinked at capitalism's "vulnerabilities," while Marx is credited with the "hugely important insight" that crises are "part and parcel of capitalism"—as if he'd predicted occasional financial panics rather than a steady decline in firm profits. The incomprehensible parts of the *General Theory* are treated, per usual, as proof of Keynes's genius rather than of his being, well, incomprehensible. Finally and most disappointingly, by confusing the Mises-Hayek view of the business cycle with Schumpeter's notion of creative destruction, Roubini and Mihm overlook the one theory of crises that best fits the housing boom-bust story.

Crisis Economics' occasional references to the Great Depression must also be taken with a pinch of salt. It wasn't Hoover but FDR who, in February 1933, stood by while "thousands of banks" went under; and it was growth in the money stock rather than fiscal stimulus that fueled the post-1933 recovery. The deflation of 1937–38 was mainly caused not by FDR's belated attempt to balance the federal budget but by the Fed's doubling of bank reserve requirements. Finally, corrected statistics show that World War II brought further stagnation rather than sustained recovery.

In short this "crash course in the future of finance" has both strengths and weaknesses. Although it contains much useful information about the subprime debacle, it understates the government's contribution to the crisis, and although it suggests some desirable reforms, it suggests others that could prove counterproductive. Readers looking for straight A's are advised to cram with caution. FEE

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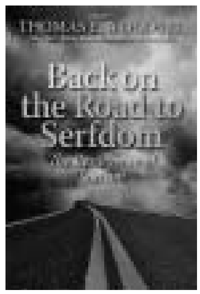
Back on the Road to Serfdom: The Resurgence of Statism

edited by Thomas E. Woods, Jr.
ISI Books • 2010 • 368 pages • $29.95

Reviewed by George Leef



Since the housing bubble burst in 2007, America's social and economic troubles have mounted rapidly. Unemployment remains high, saving and investment low. The federal government is desperate to suck in enough money to pay its enormous tab for welfare and warfare a bit longer. Our politics have become increasingly vicious. About two-thirds of the people say that the country is on the wrong track.

The great battle is to persuade those people that our ills are rooted in statism—that is, reliance on government to do things that should be left to voluntary action. Back in the 1930s most Americans also thought the country was on the wrong track, but unfortunately they blundered into the wrong conclusion—that a great expansion of government power was what we needed. The challenge today is to convince them that government is the problem, not the solution.

Among the most stalwart opponents of big government and its apologists is historian Thomas Woods. His 2009 book *Meltdown* explained why the housing bubble and its aftermath were caused entirely by politics, not the free market. With this book he and his essayists indict statism generally and argue strongly in favor of radical depoliticization. In his introduction Woods identifies a key element in our national malaise: "The more functions the state usurps from civil society, the more the institutions of civil society atrophy. Once supplanted by coercive government, the tasks the people used to perform on a voluntary basis come to be viewed as impossible for society to manage in the absence of government. . . . The spiritless population comes in turn to look for political solutions even to the most trivial problems."

The book consists of ten essays. In the first, Brian Domitrovic gives a useful history of the growth of the American State over the last two centuries. Carey Roberts follows it with an essay showing the continuing damage we suffer due to the statist thinking of Alexander Hamilton. Swedish economist Per Bylund then demolishes the notion, so often uttered by advocates of the welfare state, that Sweden proves how effective the "third way" (a welfare state neither capitalist nor socialist) can be.

Those three essays establish a solid framework for thinking about the impact of government interference with society's spontaneous order. Woods next places Anthony Mueller's essay exploring the true causes of the recent financial crisis, offering a corrective to the desperate scapegoating we've gotten from the politicians responsible for it. Mueller's essay is followed by one by Mark Brandly, who reasserts the case for free trade and the international division of labor, which is under attack by statists who would have us believe that free trade hurts workers in poor countries. Dane Stangler next shows how entrepreneurship is threatened by the ever-encroaching power of government and how foolish it is to think that the State can perform the entrepreneurial function.

Journalist Tim Carney contributes the next essay, eviscerating one of the great myths of modern life: that big business is opposed to big government. The truth, Carney shows, is that big business is extremely cozy with both "liberal" and conservative politicians. As a result America's economy is steadily drifting toward a syndicalist system dominated by politically favored firms.

Two essays deal with the interface between religion and the politicized society. Gerard Casey examines the traditional hostility many Christian clerics have toward capitalism and finds that it is without any foundation in the Bible. John Larrivee also evaluates the religious arguments against the free market. In his view those arguments are not only naive but ultimately undermine both faith and civil society.

In the book's final essay Paul Cantor shows how government intervention in culture, specifically television, substitutes bureaucratic directives for the spontaneous origins of true culture. If you ever wondered why the boat on the series *Gilligan's Island* was named "Minnow" you'll find out by reading Cantor's essay.

These are all splendid pieces, but I am especially drawn to Per Bylund's. In it he demonstrates the truth of Hayek's argument that socialism destroys the foundation for prosperity by gradually changing the character of the people. Bylund observes that young Swedish adults today are far different in their outlook from their grandparents. Whereas Swedes had once been known for their solid work ethic, after many years of the welfare state and its numerous entitlements, it is largely gone. Young Swedes are known for taking as much time off as they can while collecting as much as possible in government benefits. The nation's standard of living is falling and must continue to do so.

I have just one tiny quibble with the book's title. When were we ever *off* the road to serfdom? FEE

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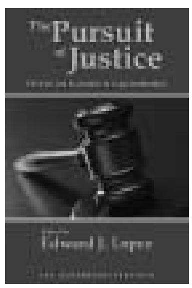
The Pursuit of Justice: Law and Economics of Legal Institutions

edited by Edward J. López
Palgrave Macmillan • 2010 • 316 pages • $30.00 paperback; $90.00 hardcover

Reviewed by Michael DeBow



Public Choice analysis is the application of economic reasoning—principally the idea that human action is primarily self-interested—to questions drawn from politics and government. It was famously described by James Buchanan as "politics without romance." To date most Public Choice research has focused on the behavior of political actors. Less attention has been paid to the behavior of (arguably) less political figures, such as judges, juries, prosecutors, and police. As a result Public

Choice has delivered on the promise of "politics without romance" but has not done as much to show us "law without romance." *The Pursuit of Justice* addresses this shortcoming by demonstrating how Public Choice theory can help us better understand our law and legal institutions.

In his introductory essay editor Edward López states the core idea advanced in the book: "[I]f we want to understand why the legal system sometimes fails to perform up to our ideals and expectations we must analyze the incentives available to actors in the legal arena and the institutions that set the 'rules of the game.'" This focus raises the question of whether Public Choice analysis differs from the "economic analysis of law" advanced by Ronald Coase, Richard Posner, and others. López maintains that while "there is little fundamental difference between" the two on methodological grounds, there seems to be a difference "in the character of the reforms they recommend." According to López, Public Choice emphasizes constraining political actors while the economic analysis of law emphasizes "arranging institutions to minimize transactions costs."

Benjamin Barton's chapter on the "lawyer-judge hypothesis"—which might be the marquee contribution to this volume—argues that "if there is a clear advantage or disadvantage to the legal profession in any given question of law, judges will choose the route that benefits the profession as a whole." Barton offers a number of examples drawn from numerous areas of the law that support the hypothesis. Charles Keckler's outline of recent changes in the *cy pres* doctrine that enable judges to award unclaimed funds from class actions to "law related entities such as law schools" fits squarely within this analysis.

The other nonquantitative contributions deal with more familiar topics. Nicholas Curott and Edward Stringham do a nice job retelling the story of Anglo-Saxon law as a spontaneous order that focused on victim compensation and how it was replaced by a centralizing Norman legal order after 1066. Ilya Somin takes dead aim at the use of eminent domain by local governments bent on "economic development," and John Bratland argues that "just compensation" in cases of government takings fails as an ethical matter. Adam Summers recounts the case against government licensure of lawyers and argues for market-based alternatives.

Three chapters that use numerical data and summary statistics all include suggestions for reform. Roger Koppl offers a strong critique of the current use of forensic science in criminal justice administration. Government-run forensic laboratories make mistakes in testing crime scene evidence—television dramas to the contrary notwithstanding. Testing at multiple labs simultaneously would reduce the number of mistakes, but money for multiple testing is unlikely to be sought by the law enforcement bureaucrats who handle the laboratories' budget requests—in part because the bureaucrats are likely more interested in maximizing the number of convictions than in the disinterested pursuit of truth. Koppl argues for triplicate testing of fingerprint evidence on the grounds of cost savings; his most conservative estimate is that \$9 million in extra testing would save taxpayers \$61 million in prison costs by "eliminating over 98 percent of the false felony convictions" caused by errors in fingerprint analysis.

Jeffrey Hammond explains class-action litigation as a vehicle for rent extraction, using the government lawsuits against the tobacco companies as a strong example.

The book's three chapters that use regression analysis all find fault with the election of judges at the state level. Russell Sobel, Matt Ryan, and Joshua Hall suggest nonpartisan elections as an alternative. They also relate overly aggressive prosecutions to the election of public prosecutors. Adrianna Cordis finds that judicial elections contribute to government corruption, but does note a 2008 article by Alt and Lassen that finds the contrary to be true. Aleksandar Tomic and Jahn Hakes explain judicial sentencing of criminals as a function of whether the judges face political pressure. While all three papers will doubtless enter the long-running debate over state judicial selection, they are unlikely to provide a knockout punch to the supporters of judicial elections.

In all, this book is an excellent contribution to the Public Choice literature. FEE

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Population Control Nonsense

BY WALTER E. WILLIAMS

According to an *American Dream* article, "Al Gore, Agenda 21 And Population Control," there are too many of us and it has a negative impact on the earth (tinyurl.com/63em794). Here's what the United Nations Population Fund said in its annual State of the World Population Report for 2009, "Facing a Changing World: Women, Population and Climate": "Each birth results not only in the emissions attributable to that person in his or her lifetime, but also the emissions of all his or her descendants. Hence, the emissions savings from intended or planned births multiply with time. . . . No human is genuinely 'carbon neutral,' especially when all greenhouse gases are figured into the equation. Therefore, everyone is part of the problem, so everyone must be part of the solution in some way. . . . Strong family planning programmes are in the interests of all countries for greenhouse-gas concerns as well as for broader welfare concerns."

Thomas Friedman agrees in his *New York Times* column "The Earth is Full" (June 8, 2008), in which he says, "[P]opulation growth and global warming push up food prices, which leads to political instability, which leads to higher oil prices, which leads to higher food prices, and so on in a vicious circle."

In his article "What Nobody Wants to Hear, But Everyone Needs to Know," University of Texas at Austin biology professor Eric R. Pianka wrote, "I do not bear any ill will toward people. However, I am convinced that the world, including *all humanity*, WOULD clearly be much better off without so many of us (tinyurl.com/6jlzysu)."

However, there is absolutely no relationship between high populations, disaster, and poverty. Population-control advocates might consider the Democratic Republic of Congo's meager 75 people per square mile to be ideal while Hong Kong's 6,500 people per square mile is problematic. Yet Hong Kong's citizens enjoy a per capita income of $43,000 while the Democratic Republic of Congo, one of the world's poorest countries, has a per capita income of $300. It's no anomaly. Some of the world's poorest countries have the lowest population densities.

Planet earth is loaded with room. We could put the world's entire population into the United States, yielding a density of 1,713 people per square mile. That's far lower than what now exists in all major U.S. cities. The entire U.S. population could move to Texas, and each family of four would enjoy more than 2.1 acres of land. Likewise, if the entire world's population moved to Texas, California, Colorado, and Pennsylvania, each family of four would enjoy a bit over two acres. Nobody's suggesting that the entire earth's population be put in the United States or that the entire U.S. population move to Texas. I cite these figures to help put the matter into perspective.

> If the entire world's population moved to Texas, California, Colorado, and Pennsylvania, each family of four would enjoy a bit over two acres.

Let's look at some other population density evidence. Before the collapse of the Soviet Union, West Germany had a higher population density than East Germany. The same is true of South Korea versus North Korea; Taiwan, Hong Kong, and Singapore versus China; the United States versus the Soviet Union; and Japan versus India. Despite more crowding, West Germany, South Korea, Taiwan, Hong Kong, Singapore,

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the United States, and Japan experienced far greater economic growth, higher standards of living, and greater access to resources than their counterparts with lower population densities. By the way, Hong Kong has virtually no agriculture sector, but its citizens eat well.

One wonders why anyone listens to doomsayers who have been consistently wrong in their predictions—not a little off, but way off. Professor Paul Ehrlich, author of the 1968 bestseller *The Population Bomb*, predicted major food shortages in the United States and that by "the 1970s . . . hundreds of millions of people are going to starve to death." Ehrlich forecasted the starvation of 65 million Americans between 1980 and 1989 and a decline in U.S. population to 22.6 million by 1999. He saw England in more desperate straits: "If I were a gambler, I would take even money that England will not exist in the year 2000."

What are called overpopulation problems result from socialistic government practices that reduce the capacity of people to educate, clothe, house, and feed themselves.

Expert Poverty

By a considerable measure, poverty in underdeveloped nations is directly attributable to their leaders heeding the advice of western "experts." Nobel laureate and Swedish economist Gunnar Myrdal said (1956), "The special advisors to underdeveloped countries who have taken the time and trouble to acquaint themselves with the problem . . . all recommend central planning as the first condition of progress." In 1957 Stanford University economist Paul A. Baran advised, "The establishment of a socialist planned economy is an essential, indeed indispensable, condition for the attainment of economic and social progress in underdeveloped countries."

Topping off this bad advice, underdeveloped countries sent their brightest to the London School of Economics, Berkeley, Harvard, and Yale to be taught socialist nonsense about economic growth. Nobel laureate economist Paul Samuelson taught them that underdeveloped countries "cannot get their heads above water because their production is so low that they can spare nothing for capital formation by which the standard of living could be raised." Economist Ranger Nurkse describes the "vicious circle of poverty" as the basic cause of the underdevelopment of poor countries. According to him, a country is poor because it is poor. On its face this theory is ludicrous. If it had validity, all mankind would still be cave dwellers because we all were poor at one time and poverty is inescapable.

Population controllers have a Malthusian vision of the world that sees population growth outpacing the means for people to care for themselves. Mankind's ingenuity has proven the Malthusians dead wrong. As a result we can grow increasingly larger quantities of food on less and less land. The energy used to produce food, per dollar of GDP, has been in steep decline. We're getting more with less, and that applies to most other inputs we use for goods and services.

Ponder the following question: Why is it that mankind today enjoys cell phones, computers, and airplanes but did not when King Louis XIV was alive? After all the necessary physical resources to make cell phones, computers, and airplanes have always been around, even when cavemen walked the earth. There is only one reason we enjoy these goodies today but did not in past eras. It's the growth in human knowledge, ingenuity, and specialization and trade—coupled with personal liberty and private property rights—that led to industrialization and betterment. In other words human beings are immensely valuable resources.

What are called overpopulation problems result from socialistic government practices that reduce the capacity of people to educate, clothe, house, and feed themselves. Underdeveloped nations are rife with farm controls, export and import restrictions, restrictive licensing, price controls, plus gross human rights violations that encourage their most productive people to emigrate and stifle the productivity of those who remain. The true antipoverty lesson for poor nations is that the most promising route out of poverty to greater wealth is personal liberty and its main ingredient, limited government. FEE

INDEX: THE FREEMAN: IDEAS ON LIBERTY VOLUME 61 JANUARY–DECEMBER 2011

Prepared by Michael Nolan, with the assistance of Linda Newton

NOTE: In page references, the number preceding the colon designates the month, the numbers following refer to the pages. For example, 1/2:47–48 refers to pages 47–48 of the January–February issue. Articles have at least three entries—author, title, and subject—except in cases when the title and subject coincide. Books reviewed are listed alphabetically by author on page 56.

A

B

C

G

H

I

J

K

L

M

N

O

P

Q

R

S

T

U

V

W

Y

BOOKS

(Reviewer's name in parentheses)