Intervention Explains Economic Success? It Just Ain't So!

BY JUDE BLANCHETTE

On the first day of an introductory statistics class a student is likely to learn the maxim "correlation isn't causation." Simply put, the correlation (a statistical relationship) between two variables doesn't mean that one caused the other. That the sun rises when roosters crow does not mean that roosters cause the sun to rise. To prove causation, one must employ a theory.

Economist Jeff Madrick, in his January 20 *New York Times* article, "Is Less Government Better for Business? Not if History Provides a Guide," has handed a Statistics 101 class a good example of the erroneous conclusions that can be reached when correlation is confused with causation.

"Going back in time, every successful capitalist economy in the world has had an active partnership between government and business," Madrick writes. "Even when the United States government was small in the nineteenth century, it built canals, subsidized the railroads, made private ownership of land accessible, and developed a widely envied public education system." One can see where Madrick is leading us: It is the active partnership between government and business that creates capitalist prosperity.

What Madrick misses is that the mere incidence of government intervention in the economy throughout U.S. history is not enough to prove that it helped create our prosperity. Perhaps *more* economic growth would have occurred *without* the intervention. To verify his assertion Madrick must construct a theory. "Government increases prosperity because it corrects 'market failures' " would be one example of an explanatory theory (albeit an incorrect one).

To see how the absence of a theoretical base can lead to confusion, consider the following "historical" statements:

- Every successful capitalist economy in the world has had the presence of airborne diseases.
- Every successful capitalist economy in the world has had rotten food.
- Every successful capitalist economy in the world has had dirty water.

We can see that it would be preposterous to claim that airborne disease, rotten food, or dirty water created the wealth we enjoy today. They were all negative occurrences that most likely hindered, not encouraged, economic growth. And so it is with government intervention in the U.S. economy.

To further bolster his case, Madrick attacks the *Index of Economic Freedom*, published by the Heritage Foundation and *Wall Street Journal*, which correlates prosperity with economic freedom. Contra this survey, he cites the World Economic Forum's "Global Competitiveness Report." According to Madrick, "The forum's growth competitive index is based heavily on an opinion survey of business executives, as well as measures of technological sophistication and other factors." The report finds that Norway, Sweden, and Finland all rank high in competitiveness, and, Madrick concludes, even though they have "high taxes and generous welfare systems, [they] are considered by business executives among the 10 most competitive nations. Why? Because they use their government spending to improve education, for example."

Madrick may hope his readers won't track down the report and read it for themselves. While it is true that Norway ranks first (incidentally, the United States is second), active government management of the economy is not the reason. Rather, the executive summary notes, Norway has "low levels of corruption," "widespread

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respect for contracts and the rule of law," and a private sector that shows "a proclivity for adopting new technologies, and nurtures a culture of innovation." Finland "has been running budget surpluses." This is not exactly intellectual ammunition for government planners.

It is also important to note that an opinion survey of business executives is not necessarily a guide to sound policy. Unfortunately, business and government often work actively together to the detriment of the economy. Government handouts have seduced business leaders into becoming wards of the state.

In his enthusiasm for this survey Madrick also seems at odds with the article's publisher, the *New York Times*, and others who commonly assert that we should fear a global "race to the bottom," that is, countries attempting to attract business by cutting back government services. But here we have Madrick asserting that business leaders prefer, not low taxes, loose environmental regulations, and pro-business labor laws, but precisely the opposite.

No matter what some executives might indicate in a survey, the proper role of government is to secure property rights. Once individuals are safe in their persons and possessions, their entrepreneurial ability knows few boundaries. The constant search for new and better ways to serve the consumer is at the heart of our economic growth. Yet once a government oversteps this limited role it becomes a threat to prosperity, not its progenitor. Ludwig von Mises makes much the same point: "gasoline is a very useful liquid, useful for many purposes, but I would nevertheless not drink gasoline because I think that would not be the right use for it."

Almost every example of government's positive influence on the economy that Madrick employs is fallacious. He exhorts politicians to do for college education what they did 100 years ago for primary education: make it "free." If 2 trillion in tax dollars were spent subsidizing college education, Madrick writes, "imagine the gains in new ideas, in superior labor force and in productivity in general."

But there's no direct correlation between a college degree and "new ideas" or a "superior labor force." As *Forbes* magazine reports: "Fifty-eight members of The Forbes 400 [a list of the wealthiest Americans] either avoided college or ditched it partway through. These 58—almost 15% of the total—have an average net worth of $4.8 billion. This is 167% greater than the average net worth of the 400, which is $1.8 billion. It is more than twice the average net worth of those 400 members who attended Ivy League colleges." I doubt that new ideas are lacking in this group.

College Graduates Earn More?

This brings us to another incidence of the correlation-causation fallacy. The argument is often made that a college degree causes increased income. The statistic often bandied about by college administrators (and parents) is that college graduates earn 77 percent more than high-school graduates. This is misleading. While it is true that the majority of high earners went to college, it doesn't necessarily follow that a high income is the effect of a college degree. Smart and ambitious people (like Bill Gates) tend to do well no matter what level of education they have, and because bright individuals who graduate from college go on to earn high incomes (which they most likely would have done anyway), the graduate-income statistic trends upwards.

Madrick saves the best for last: "If our politicians realize that the purpose of government is to adapt to, and even promote, change, they may at last deal successfully with the nation's problems." His teleocratic, or ends-oriented, view of government presumes knowledge on the part of politicians that they have never demonstrated before and raises many questions, most of which F. A. Hayek dealt with in *The Road to Serfdom*. Exactly who decides which changes are to be promoted and which are to be stunted? Does the promotion of change come at the expense of property rights and liberty? How much power do we grant the government to bring about this change?

Using "change" as the organizing principle of government action is an old notion. As long as men have held power, they have sought to justify its use, and "adapting to and promoting change," being so abstract, fits just about anything.

In contradistinction to political change, consider the change and innovation one sees in the marketplace. Unlike any overarching plan for change that the federal government might pursue (which necessarily excludes all other competing plans), the market economy allows each and every one of us to identify and, individually or collectively, pursue goals. Change, to be individually meaningful, must be personal.