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The Keynesian Abyss

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Perhaps the greatest modern champion of central economic planning was the twentieth-century English economist John Maynard Keynes. Keynes advocated the idea that the government should play a large, active role in the economy. Among the consequences of Keynes' economic theories, whether intended or unintended, is the fact that Western economies today are characterized by large, central governments, central banks, and massive debts.

Government policies based on Keynesian theories and the institution of central banking form a nexus of central economic planning. Control of the central planning process is a winner-take-all proposition for businesses. In the U.S., the result is an unholy alliance of the U.S. federal government, the Federal Reserve (along with the largest U.S. banks), and the largest U.S. corporations. The logical chain beginning with Keynes' fundamental idea that government, supported by a central bank, should play a large and active role in the economy sets the stage for a centrally planned economy and ultimately produces a corporate state.

The U.S. economy is locked in a downward spiral of economic decline. By growing in size, and by engaging in ever-larger economic interventions, the U.S. federal government became itself a material cause of the recession that began in 2007. By attempting to grow the economy through monetary expansion, the Federal Reserve destroyed savings and fueled a series of disastrous economic bubbles, culminating in the housing bubble.

Following Keynesian economic theories, the policy response of the U.S. federal government to the recession that began in 2007 and of the financial crisis that began in 2008 was to expand the government further and at a more rapid pace. In other words, some of the root causes of the economic imbalances that led to the recession and financial crisis (the relative size of the government and the resulting economic distortions) were compounded. As a consequence, the so-called "double dip recession" in the U.S. that began in the second half of 2011 will be longer and ultimately more severe than the economic downturn of 2007–2009.

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Leviathan: The Size of the State

Government encroachment on the private sector, like a self-fulfilling prophecy, often magnifies the reasons why government intervention was originally believed to be necessary. For example, when the U.S. federal government became involved in education through federally guaranteed student loans, the result was

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that the cost of a college education rose toward the limit of what students could borrow and repay during their careers simply because the loans were guaranteed by the government. The guarantees produced more and riskier loans, larger loans, and higher education costs.

When the U.S. federal government promoted home ownership for minorities and the poor, mortgage loan guarantees resulted in higher home prices and contributed to the sub-prime lending debacle where banks originated loans to unqualified borrowers in order to sell them to government sponsored entities (GSEs), i.e., to Fannie Mae and Freddie Mac, and to investors as collateralized debt obligations (CDOs) and other mortgage backed securities (MBS).

Governments redistribute wealth and manipulate economic activity through taxes, subsidies, guarantees, regulations and so forth, but they do not produce new wealth. Government spending unavoidably favors businesses with close ties to the government over those that are taxed but that do not benefit. Government programs that overlap the private sector divert economic resources to businesses that have the favor of politicians minus the cost of government, thus producing economic distortions and a net loss of wealth for society.

How the Government Destroys Jobs

While politicians extol the theoretical benefits of ever more government control of the economy, e.g., through increased regulation, from the standpoint of individual entrepreneurs, businesses and private investors, the government is a nuisance, an impediment to wealth creation, and the source of countless costs and risks. The larger the government becomes relative to the size of the economy, the more it tends to discourage economic activity. Although roughly 70 percent of U.S. jobs are created by small businesses, ranging from family owned businesses to high technology startups, the burden of government falls disproportionately on them because they have fewer resources with which to administer and to demonstrate compliance with government regulations.

When large companies are audited or investigated by any of several government agencies, their accounting, legal, and compliance departments are well equipped to deal with such matters. However, when a small company faces the same hurdles or seeks government permits, licenses or certifications, its operations are directly impacted and the associated accounting, legal, and regulatory compliance costs can cause the business to lose money or to fail. In the event of an audit or investigation, small business owners in the U.S. generally seek to comply immediately and often pay fines or penalties without contest in order to end the government's interference. While large companies can afford to dispute the government, small businesses face the equivalent of extortion.

As a practical matter, small businesses in the U.S. are permitted to operate at the sole discretion of government bureaucrats that can effectively shut down small businesses without any evidence of wrongdoing. Setting aside the fact that small business owners live in constant and well-justified fear of their own government, the result is a stifling of economic activity and a net loss of jobs. For example, traditional small businesses in the U.S., i.e., sole proprietorships, increasingly avoid hiring employees.

Free-market competition and the inherent uncertainty of economic conditions provide ample risk for startup businesses. A disproportionately large government relative to the size of the economy damages economic activity and discourages investment in new businesses. The

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aggregate overhead of government regulations and regulatory compliance, along with taxes and potential penalties, e.g., the 2010 Patient Protection and Affordable Care Act ("Obama-care"), increases business costs, amplifies business risks, and further increases the burden of regulatory compliance. The result of systematically increasing the costs and risks of doing business—in lock step with the size of government—is to reduce the rate of business formation and to encourage investors to look elsewhere to find returns.

If the U.S. government, currently almost 45 percent of GDP, desired to create jobs, the correct policy would be to greatly reduce the countless regulations, taxes, and fees that encumber small businesses. The path to job creation is for the government to reduce job destruction.

Central banks, such as the Federal Reserve, are examples of central economic planning, i.e., they control the money supply and exercise centralized control over the value and cost of money through interest rates, bank reserve ratios, monetary inflation and by other means. The Federal Reserve engages in central planning for the benefit of banks. Like the U.S. federal government, the Federal Reserve, through monetary mechanisms, distorts spending and investment patterns, redistributes wealth and preempts the financial and economic decisions of households, individual entrepreneurs, businesses and private investors.

Keynes and The Corporate State

The U.S. economy is anything but a free market today. In fact, the U.S. government increasingly resembles an oligarchy in which the oligarchs are large corporations, i.e., a "corporatocracy." Thus, the illegitimate offspring of the grand government envisaged by Keynes and the institution of central banking is a corporate state.

Without a large government, businesses have little incentive to influence it, but with the government (local, state, and federal) representing nearly half of the U.S. economy, influencing the government is a mission-critical objective for every company. The size of government implied by Keynesian economics provides motive and opportunity but only the largest corporations have the means to succeed.

The goals of businesses seeking to influence the government include winning government business, mandating consumption of products and services (from child car seats to health insurance), avoiding taxes, guaranteeing profits, creating regulatory loopholes, protecting markets, eliminating competition, socializing losses, and so forth.

The influence of Wall Street over Washington D.C. through political campaign contributions, corporate lobbyists, and revolving doors (where the same individuals alternate between closely linked private sector jobs and government posts) is almost absolute. Lobbyists are intimately involved in writing legislation that is often rubber-stamped by the U.S. Congress, i.e., passed without reading or meaningful debate. The largest corporations support political candidates through campaign contributions and by funding political action committees that, among other things, use corporate public relations tools for political purposes, i.e., propaganda. Key government posts are consistently held by individuals with clear conflicts of interest, and the existence of such conflicts is routinely ignored.

The current reality of the United States is that the largest corporations have hijacked the Keynesian central planning powers of the federal

government and have used these powers to encourage ever larger and more direct interventions in the economy for their own benefit, as well as laws and regulations that serve as a barrier to free-market competition. U.S. regulators, such as the Securities and Exchange Commission (SEC), Commodities and Futures Trading Commission (CFTC) and the Food and Drug Administration (FDA), appear to have been captured by the industries they are intended to regulate. Government regulators selectively enforce regulations, often against small businesses and growing companies, such as organic dairy farmers, protecting the interests of the largest corporations from small businesses, free-market competition, and consumer choice.

The largest U.S. corporations (including oil companies like ExxonMobil and Chevron; drug companies like Johnson & Johnson, Pfizer, and GlaxoSmithKline; agribusiness companies like Archer Daniels Midland, which are heavily subsidized by the U.S. federal government; agricultural biotechnology companies like Monsanto; military contractors like Lockheed Martin, Northrop Grumman, Boeing, Raytheon, and General Dynamics; and banks like Bank of America, J.P. Morgan Chase, Citigroup, Wells Fargo, Goldman Sachs, and Morgan Stanley) have not only been the beneficiaries of government expansion, deficit spending,and central economic planning, but, considering political campaign funding practices, have become the de facto oligarchs of America.

Sliding Into the Keynesian Abyss

The decline of the U.S. economy is the logical outcome of Keynesian economics, which enshrines central economic planning and embraces central banking. The unholy alliance of the federal government, the Federal Reserve, and Wall Street has all but eliminated capitalism and has transformed the United States from a burgeoning free-market economy into a failing corporate state.

The U.S. federal government, the Federal Reserve, and Wall Street each played a role in the progression from central economic planning and central banking to a corporate state. Politicians used Keynesian economics to justify big government, a welfare state, and budget deficits. The Federal Reserve sought to grow the economy through monetary expansion, thereby crippling it. At the same time, Wall Street sought higher profits through influence over the government. The resulting corporate state undermined capitalism and the free market in the United States and produced a downward spiral of economic decline from which there is no escape without fundamental reforms. ■

Inside:

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