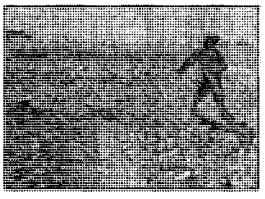
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Ideas On Liberty

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Cover: Detail from *The Sower* by Vincent van Gogh

PERSPECTIVE

Pragmatic Collectivism

Do we individualists exaggerate when we condemn our ideological opponents as collectivists? That word isn't merely a term of abuse. It is a spot-on label for the political philosophy of those who would give government a prominent economic and social role. The philosophy holds that society (or some other group) is superior to the expendable individuals who comprise it and that government should act on its behalf. Government carries out the social will, which has little or nothing to do with the will of persons, since that only reflects narrow self-interest.

Collectivism can be detected in certain views on property and wealth. While much variation is possible, today's pragmatic collectivists are willing to permit a semblance of private property, until it clashes with their lofty aspirations. Few people today favor outright and total collectivization of the means of production. But all collectivists are ready to summon the constabulary when a nominal property owner does something they don't like. Ultimately, all property belongs to the collective.

You can spot a good collectivist by his choice of words. Recently, former New York Governor Mario Cuomo, the quintessential pragmatic collectivist, was defending President Clinton against his critics who favor impeachment or resignation. Cuomo said that although Clinton had done wrong, he's doing a good job as president. "The job of the president is to run the United States of America," Cuomo said. Not just the *government*, mind you. The whole United States.

A few minutes later he pressed his point: Who cares that we can't believe the President on a certain personal matter? The important thing is that "we do believe he knows what to do with the wealth of this country."

That's collectivism.

* * *

There is no longer a legal entitlement to welfare, and almost everyone now acknowledges that America's long experience with handouts for the poor was a failure. James Payne explains why the $5 trillion war on poverty had no chance of success.

State and local governments spend a significant amount of cash trying to get doctors to set up practices in rural areas. Is this a good idea? William Pike says it's not only unnecessary, it's especially bad for the residents of those areas.

The government's offensive against tobacco is well known. But as Aaron Lukas reminds us, the feds for over 30 years have waged a war against one particular kind of tobacco: the kind grown and rolled into cigars in Cuba.

Can the arts flourish under capitalism when writers, painters, and composers have to worry about mundane things like making a living? Critics of the market have long answered no. A new book by economist Tyler Cowen, excerpted herein, says the arts can and do flourish in such circumstances.

A new move is afoot to amend the U.S. Constitution to permit prohibition of the burning of the American flag. Andrew Cohen surveys the standard arguments pro and con before asking the overlooked question: whose flag is it?

Advocates of quotas, set-asides, and other government-mandated discrimination don't seem to realize that those measures assume that the targeted groups can't succeed on their own in the free market. Burton Folsom says history disputes that assumption and offers two cases of entrepreneurial determination to prove his point.

When the government required air bags in all automobiles some years ago, the regulators and "consumer advocates" said the mandate would save lives. They didn't say it would also take lives—but that's what happened. Loren Lomasky takes a philosophical look at this episode of Government Knows Best.

The publication in Japanese of *Libertarianism: A Primer* gave David Boaz the opportunity to contemplate the universality of liberty in a new introduction to that edition of his book. We are pleased to reprint it here.

There are two ways to provide goods: the market (consent) and the government (coercion). Hugh Macaulay compares the two methods in his mission to discover which is superior.

For many years the Swiss had no rivals among watchmakers. Then along came the quartz revolution in timekeeping. The entrepreneurial Swiss were down, but they didn't give up. Anthony Young has the story.

Government is often petitioned to compensate individuals and groups for injuries inflicted at the hands of bureaucrats and politicians. But as Karen Selick points out, whenever a victim is compensated, a whole new set of victims is created.

In this month's columns, Lawrence Reed sets the record straight on America's "overconsumption," Doug Bandow sees hope for education in the growing private scholarship movement, Dwight Lee argues that laws against profiteering during natural disasters are a form of censorship, Mark Skousen takes a look at financial markets, and Walter Williams takes a fresh look at the War Between the States. To Robert Kuttner's complaint that the world economy suffers from "market worship," Russell Roberts says, It Just Ain't So!

Our reviewers dissect books on John D. Rockefeller, radical legal philosophy, natural law, democracy, environmental entrepreneurship, and the twentieth-century battle between capitalism and socialism.

—SHELDON RICHMAN

THE FREEMAN
Ideas On Liberty

Market Worship? It Just Ain't So!

As we approach the millennium, the pace of economic change quickens. Consumers have always wanted better products at lower prices. But in today's economy, the market delivers "better and cheaper" more quickly than at any time in human history. The time between product improvements gets shorter and shorter. Competition drives prices lower.

It's a wonderful time to be a consumer. For entrepreneurs and business leaders, it is feast and famine at the same time. The opportunities are unprecedented, but the risks are formidable. Even Bill Gates doesn't sleep well. Today's genius can be out of business tomorrow because of technological advances we cannot dream of. New business starts are at extraordinary levels, but more of these ventures fail than succeed. Competition is fiercer and more unforgiving than ever before.

Two fundamental forces drive the pace of economic change. The first is technological innovation, particularly in handling and disseminating information. Computers get more powerful, smaller, and cheaper. The Internet expands the reach of customers in ways that are just beginning to be explored. And in traditional markets such as retailing, the application of information technology pushes prices down and pressures those who do not keep pace.

The second fundamental force driving change is the increasing accessibility of global markets. The increase in international opportunity means new markets for products and workers and greater economies of scale.

We like the wealth and opportunity that come from technological change and globalization. Alas, there is no free lunch. Innovation displaces established firms. A factory opens in Malaysia and one in the United States closes. Financial markets in Asia swirl with rumor and speculation affecting our markets as well. Russia teeters on the edge, it seems, of chaos.

Who is in charge here? The desire to take control, to improve the system via some "third way" is always tempting. Chaos and uncertainty are never pleasant. The natural response is to try and hold back the forces of innovation or reduce the sway of global markets. After all, are these not the cause of the confusion?

"Market Worship"

In a recent piece in the *Washington Post*, economics writer Robert Kuttner blames the chaos on a naïve worship of free markets. He blames speculators for the problems of Asia. He blames the United States for encouraging capitalism in Russia then failing to help out when capitalism fails. Kuttner is not alone. Numerous commentators see the current state of world markets as an indictment of capitalism and free markets.

Yet much of the chaos comes from previous government attempts to meddle with the system or control it. In Asia, government tinkering with capital markets is endemic. Special interests get favors, and markets react. Speculation is not the cause of Asia's economic problems; it's the result. Government policy cannot stand in a vacuum; speculation is the market's judgement of the wisdom of the policymakers.

In Russia, policymakers have partially dismantled socialism without putting property rights in place to allow markets to work. You cannot buy and sell land freely. Banks cannot

enforce mortgages, so home equity cannot be converted into capital for new businesses. The tax code is capricious. Too many people still work in government-controlled firms where wages are determined by politics rather than market forces.

Many of the current problems in Asia and elsewhere come from the government's inexorable urge to cushion the hardship that results from bad economic decisions. We see the same problems in the United States. We implicitly bailed out banks that made bad investments in Mexico. And we had the Federal Reserve pressuring private investment banks to bail out the Long-Term Capital hedge fund lest it fail. These maneuvers only encourage future investors to take more risk unwarranted by potential returns.

Security Through Protectionism?

But what about the changes in the marketplace that are due not to poor public policy but to the market forces of innovation and global competition? As we get wealthier, it is natural that we think of ways to reduce risk and uncertainty. One way is to limit the role of global competition via protectionism in its many forms. Or to soften the blows of competition, we can support businesses that fail in the marketplace. Should the government intervene to reduce the chaos that comes with competition?

The simple answer is that competition and free markets make us rich, which surely beats the alternative. But wealth creation is not the only reason for allowing free markets to work their magic. Free markets maximize the menu of opportunities available to us as individuals. Whenever I speak to high school students or college freshmen, I like to ask them whether they want the same careers as their parents. Inevitably, only a few want to pursue the careers of either of their parents. The next generation has its own skills and dreams. The incredibly vibrant marketplace that we live in today allows it to live out those dreams.

Dealing with the menu of opportunity presented by free markets is a challenge. It means preparing for those opportunities by investing in knowledge and skills. It means embracing some opportunities and forgoing others. It means living with the consequences of our decisions. The marketplace is not kind to all people at all times. But coping with the challenge of opportunity is what allows us to feel fully alive.

There are two ways to cope with the uncertainty that comes along with economic opportunity. One is to lobby the government for special treatment to insulate your industry, your job, your lifestyle from market forces. Whenever this is an option, men and women divert energy and resources from the world's business and instead devote their skills to influencing government. This diminishes the human enterprise. Using government to protect one industry always means punishing another.

It is far better to prepare for the economic adventure that lies before us by investing in skills and knowledge that can be used in the increasingly competitive marketplace. Coping with the market's challenge enhances the lives we lead and, through our efforts, the lives of others.

—Russell Roberts
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Why the War on Poverty Failed

by James L. Payne

Well, it's now official: the war on poverty was a costly, tragic mistake. Ordinary people have suspected that for decades, of course, but we had to wait for the *New York Times* to decide this news was fit to print—which it finally did on February 9, 1998. In a front-page story on poverty in rural Kentucky, Michael Janofsky detailed the failure of this effort in the one region that was supposed to be the centerpiece of reform. "Federal and state agencies have plowed billions of dollars into Appalachia," he wrote, yet the area "looks much as it did 30 years ago, when President Lyndon B. Johnson declared a war on poverty, taking special aim at the rural decay."[1]

Janofsky visited Owsley County, Kentucky, and found a poverty rate of over 46 percent, with over half the adults illiterate and half unemployed. "Feelings of hopelessness have become so deeply entrenched," he reported, "that many residents have long forsaken any expectation of bettering themselves." For years, the government has been trying to treat the despair with welfare programs: two-thirds of the inhabitants receive federal assistance, including food stamps, AFDC, and SSI disability payments. This, it now appears, is part of the area's problems.

"The war on poverty was the worst thing that ever happened to Appalachia," Janofsky quotes one resident as saying. "It gave people a way to get by without having to do any work." Local officials told him that "many parents urge their children to try to go to special education classes at school as a way to prove they are eligible for [SSI] disability benefits." (The senior class at the local high school picked as its motto, "I came, I slept, I graduated.")

Why did the war on poverty fail? What was wrong with the programs under which the nation spent over $5 trillion attempting to solve the problems of the poor, only to come up empty? It's an important question to ask in these days of welfare reform. The first step toward a sound policy ought to be to identify the errors of the past.

Perhaps the best way to answer the question is to take a close look at the book that inspired the war on poverty, Michael Harrington's *The Other America*, published in 1962. (Harrington died in 1989.) Possibly the most influential policy book in history, *The Other America* was cited again and again by the politicians, activists, and administrators who set up welfare programs in the 1960s. In it we find the fallacies that sent reformers down dark and tangled paths into today's social tragedies.

Curing Poverty Through Algebra

Though social workers and welfare administrators embraced Harrington's account, neither he nor they realized how distinctive, even

James Payne is the author of Overcoming Welfare: Expecting More from the Poor and from Ourselves *(Basic Books, 1998).*

bizarre, was the theory of poverty that it contained. Harrington's premise was that poverty is a purely economic problem: the needy simply lack the material resources to lead productive, happy lives. Supply these resources, the theory runs, and you will have solved the problem of poverty. "The means are at hand," declared Harrington, "to fulfill the age-old dream: poverty can now be abolished."[2] This theme was repeated up and down the welfare establishment. Sargent Shriver, the administration's leading anti-poverty warrior, told Congress that the nation had "both the resources and the know-how to eliminate grinding poverty in the United States." President Lyndon Johnson echoed the claim. "For the first time in our history," he declared, "it is possible to conquer poverty."

To most people, these claims seemed incredibly naïve. While the state of neediness we call poverty does involve a lack of material resources, it also involves a mass of psychological and moral problems, including weak motivation, lack of trust in others, ignorance, irresponsibility, self-destructiveness, short-sightedness, alcoholism, drug addiction, promiscuity, and violence. To say that all these behavioral and psychological problems can be "abolished" seems a denial of the common-sense Biblical teaching that the poor will always be with us.

Abolishing poverty did not seem farfetched to the activists, however. Indeed, one book from that era boldly challenged the Biblical wisdom with its title: *The Poor Ye Need Not Have With You.* This 1970 volume was written by Robert Levine, who had served in the Office of Economic Opportunity, the federal government's anti-poverty agency. His book was also supported by the Ford Foundation and the Urban Institute, two principal backers of the war on poverty. Levine adhered to the simple materialistic view of poverty. "Even a quick look can convince us that poverty as it is currently defined in the United States is a completely solvable problem," he wrote. "If we were to provide every last poor family and individual in the United States with enough income to bring them above the level of poverty, the required outlay would be less than $10 billion a year."[3] In this perspective, curing poverty was simple algebra: add government's x dollars to the poor's y dollars and the result would be the end to poverty.

It was a perspective that led to intolerance. Since poverty was so simple to remedy—the activists reasoned—it was unethical not to act. "In a nation with a technology that could provide every citizen with a decent life," Harrington thundered, "it is an outrage and a scandal that there should be such social misery."[4] For the activists, welfare programs did not involve complex relationships and intractable problems about which honest people could disagree. They were simple moral imperatives, and anyone who opposed them was seen as selfish and insensitive. (This dogmatic view has by no means disappeared from so-called liberal circles.)

The Ideology of Handouts

The simple economic theory of poverty led to a single underlying principle for welfare programs. Since the needy just lacked goods and services to become productive members of the community, it followed that all you had to do was give them these things. You didn't have to see that they stopped engaging in the behavior that plunged them into neediness. You didn't have to ask them to apply themselves, or to work, or to save, or to stop using drugs, or to stop having babies they couldn't support, or to make any other kind of effort to improve themselves. In other words, the welfare programs the war-on-poverty activists designed embodied something-for-nothing giving, or what we usually call "handouts."

The handout feature characterized not only the programs that gave away cash and material resources like food and housing; it was also incorporated in programs that provided training, education, and rehabilitation. Recipients did not have to make any significant sacrifice to be admitted to them, and they did not have to make any significant effort to stay in them. Swept up by the rhetoric of the day, program organizers simply assumed that all that recipients needed was "opportunity," especially the opportunity to learn a trade and to get a job.

Alas, this was mainly untrue. One of the first things the needy lack is motivation; that

is, they lack the ability to sacrifice and to discipline themselves, to defer present gratification for future benefit. Most of the recipients in the anti-poverty training and education programs were poorly motivated, and their lack of commitment meant that they couldn't make good use of the opportunities put before them. Worse, they dragged down the morale of teachers and those recipients prepared to apply themselves. What were administrators to do? If they required a strong commitment to the task of self-improvement, this would mean turning away most of the applicants—and watching their welfare empires collapse. Not surprisingly, officials were inclined to relax standards and let education and training programs become giveaways.

For example, in the early 1980s, the Manpower Development Research Corporation (MDRC) ran a number of "supported work" programs for disadvantaged youths financed by the federal government. The aim, as an MDRC vice-president told a Senate subcommittee, was a program "for instilling positive work habits and attitudes."[5] To implement this goal, attendance standards were announced: no more than three unexcused absences or five unexcused latenesses in the first ten weeks of training class. Reporter Ken Auletta attended one of these courses in New York City and discovered that even these modest rules were not being applied. Students were allowed to come and go as they wished, even to sleep or read the newspaper in class.[6] The trainer in charge explained that if the rules were applied, "we'd lose just about everyone in the class."[7] The overall effect of this indulgent approach in job training programs has been to "train" participants in irresponsibility: they learn that the world will keep rewarding them even when they don't live up to their obligations.

Head Start is another case where the giveaway approach has undermined the effectiveness of the program. The original idea behind Head Start was to give poverty-level preschoolers social and educational enrichment that would help them succeed in school. Since the children are in class only a few hours a week, it is vital that anything learned be reinforced at home by parents. That means, as Head Start's own promoters insist, that parent participation is crucial to the success of early intervention.[8] Logically, then, parental involvement should be required as a condition of the program. Unfortunately, the idea of a requirement goes against the agency's handout principle. "Head Start cannot threaten to dismiss a child for non-performance of either parent or child," says one pamphlet extolling the program. "It can only offer to help."[9]

This indulgent approach has meant that most parents have no significant involvement with the Head Start program, and for them and their children it is little more than a babysitting service. In the Head Start office in Sandpoint, Idaho, I asked a teacher how often parents volunteered to be in the classroom with their children. "We'd *like* them to come in once a month," she replied. The emphasis she put on "like" indicated that she understood even this minuscule level of parental involvement was an unrealistic hope. I happened to see the roll and time sheet for one class: it showed that not one parent of the 18 children had volunteered in the entire month.

The Healthy Way to Give

In adopting the handout approach for their programs, the war-on-poverty activists failed to notice—or failed to care—that they were ignoring over a century of theory and experience in the social welfare field. Charity leaders of the nineteenth century had lived with the poor and had analyzed the effects of different kinds of aid. They discovered that almsgiving—that is, something for nothing—actually hurt the poor. First, it weakened them by undermining their motivation to improve themselves. If you kept giving a man food when he was hungry, you undermined his incentive to look for a way to feed himself. Second, handouts encouraged self-destructive vices by softening the natural penalties for irresponsible and socially harmful behavior. If you gave a man coal who had wasted his money on drink, you encouraged him to drink away next month's coal money, too. Finally, the nineteenth-century experts argued, handouts were self-defeating. People became

dependent on them, and new recipients were attracted to them. So this type of aid could never reduce the size of the needy population. With handouts, the more you gave, the more you had to give.

The correct way to help the needy, they said, was to expect something of recipients in return for what was given them. Instead of giving poor people what they needed, the charity leaders organized programs that enabled the needy to supply their own wants. They weren't given money, but were counseled to find employment; they weren't given apartments, but were rented, at cost, healthy dwellings managed by charities; they weren't given food, but learned to grow their own food at garden clubs developed for that purpose. The great English charity leader Octavia Hill, who worked all her life among the poor, summed up the nineteenth-century social workers' position on handouts: "I proclaim that I myself have no belief whatever in the poor being one atom richer or better for the alms that reach them, that they are very distinctly worse, and that I give literally no such alms myself."[10]

Failing in the Field

The war-on-poverty activists not only ignored the lessons of the past on the subject of handouts; they also ignored their own experience with the poor. The case of Harrington himself is especially revealing.

In the early 1950s Harrington worked at the St. Joseph's House of Hospitality, a shelter for the homeless in New York's Bowery district. The philosophy of the shelter was pure handout. Beds, food, and clothing were given out, as Harrington proudly reported, on a "first come, first served" basis. The shelter didn't require anything in return: not small amounts of money, not work, not any effort at self-improvement. In *The Other America* Harrington described at length the tragic lives of the alcoholics served by the shelter, the degradation, exposure, disease, theft, and violence that made up their lives. Yet he didn't report having any strategy to uplift them, and didn't report rehabilitating a single one. Though he became friendly with some of the street alcoholics, he never saw his friendship as a platform for mentoring them, as a way of guiding them to recovery. He simply watched these suffering men go in and out of their drunks, and gave them handouts as they went along. Summarizing his experience, he concluded that alcoholic poverty was not an economic problem but "deeply a matter of personality." In a revealing aside, he added, "One hardly knows where to begin."[11]

For someone so ready to hector others about how easily poverty could be "abolished," Harrington was astonishingly unreflective about his own performance. His failure as a social worker among the homeless never led him to question his handout approach, and his personal knowledge that poverty was *not* an economic problem never shook his ideological conviction that it was. The rest, as they say, is history. The man who "hardly knew where to begin" in treating the problems of poverty—and who failed when he tried—became the guru for a massive array of government handout programs that, as even the *New York Times* now concedes, only deepened the culture of poverty.

The Road Back to Common Sense

In the 1996 welfare reform, the nation began to undo the damage caused by the war on poverty's misguided approach. Most lawmakers finally grasped the point that handout programs are harmful and self-defeating. They began to see that welfare programs need requirements, that recipients have to be asked to take steps toward self-improvement and self-sufficiency.

It has not been easy to implement this concept, however. Lawmakers have yet to discover that government agencies are ill-suited to carry out the subtle task of personal uplift. This mission requires helpers who become personally involved in the lives of their clients. It requires that helpers be mentors who project healthy values. It also requires treating each client as an individual, subject to a different set of expectations and rewards. All this runs against the grain in government, where the pressures of law and regulation

push agencies toward behaving in an impersonal, value-free, and uniform manner. In the long run, this leads to handout programs, because handouts are impersonal, value-free, and uniform.

The nineteenth-century charity leaders were familiar with the drawbacks of government assistance. Mary Richmond, one of the founders of American social work, condemned public relief in no uncertain terms: "The most experienced charity workers regard it as a source of demoralization both to the poor and the charitable. No public agency can supply the devoted, friendly, and intensely personal relation so necessary in charity. It can supply the gift, but it cannot supply the giver, for the giver is a compulsory tax rate."[12]

The 1996 welfare reform was therefore just a first step in undoing the harmful anti-poverty policies of the 1960s. It did introduce the idea that handouts are wrong. But it missed the deeper point that, in the long run, government agencies aren't very good at anything but handouts. It remains for future generations to lay the government programs entirely aside and to promote the personal, voluntary arrangements that make for truly effective social assistance. □

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2. Michael Harrington, *The Other America: Poverty in the United States* (New York: Macmillan, 1969 [1962]), p. 174.
3. Robert A. Levine, *The Poor Ye Need Not Have With You: Lessons from the War on Poverty* (Cambridge, Mass.: M.I.T. Press, 1970), p. 6.
4. Harrington, p. 17.
5. Quoted in Ken Auletta, *The Underclass* (New York: Random House, 1983), p. 23.
6. Ibid., pp. 57, 120, 121, 122.
7. Ibid., p. 65.
8. Edward Zigler, Sally J. Styfco, and Elizabeth Gilman, "The National Head Start Program for Disadvantaged Preschoolers," in Zigler and Styfco, eds., *Head Start and Beyond: A National Plan for Extended Childhood Intervention* (New Haven: Yale University Press, 1993), p. 4.
9. Tim Nolan, *What Really Makes Head Start Work?* (Milwaukee: Institute for Innovation in Human Services, 1991), p. 8.
10. Octavia Hill, *The Befriending Leader: Social Assistance without Dependency*, ed. James L. Payne (Sandpoint, Idaho: Lytton Publishing Co., 1997), p. 57.
11. Harrington, p. 94.
12. Mary E. Richmond, *Friendly Visiting Among the Poor: A Handbook for Charity Workers* (Montclair, N.J.: Patterson Smith: 1969 [1899]), pp. 151–52.

The Foundations of Morality

by Henry Hazlitt



In this impressive work Hazlitt explores the proper foundation of morality. It would give the game away to reveal his conclusion, but suffice it to say that Hazlitt conducts a detailed and scholarly inquiry into the many possibilities.

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Recruiting Rural Physicians: Small-Town Socialism

by William E. Pike

As the supreme defender of the status quo, the state often feels a necessity to react whenever a broad market or social change is taking place. Lawmakers and bureaucrats are rarely satisfied to let new trends work themselves out for the public good in a free-market society. Such has certainly been the case with health care in America over the last decade.

Through the 1980s and into the 1990s, as health-care costs grew, society saw a shift in provider demographics. Two conflicting things occurred during this period. First, rising physician salaries in specialties such as radiology and anesthesiology drew more and more medical students away from traditional general practice. Second, managed care became increasingly prominent. Managed care, of course, relies on general practitioners, or primary care physicians, as gatekeepers between patients and more expensive specialized care.

As the ranks of primary care physicians grew smaller, such doctors began to get lucrative offers from large urban managed care organizations. These trends left an obvious void—a shortage of rural primary care physicians. A survey of medical school seniors taken in 1979 showed that only 59 percent preferred a large or moderate city practice. By 1989 that number had grown to 80 percent.[1]

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Government Response

Local, state, and federal government agencies moved to check this shortage by spending tax dollars and manipulating the market. Now most states maintain some sort of program, at a cost of millions of dollars a year, to recruit and retain rural physicians. Politically, such programs are easily defended as absolutely necessary, in the words of Tennessee's rural health office, "to improve and enhance the accessibility, availability, and affordability of quality health care." Few voters, and certainly few legislators, are willing to argue with such a mission. However, are such agencies really efficient in the face of free-market alternatives?

How do government agencies recruit physicians for rural communities? The foremost device is money. Many states lure doctors to rural practice by paying all or part of the cost of their medical education. In some cases the state contracts with new physicians to work in a rural area for a specific amount of time in return for payment of debts at the end of that service. In other, less effective programs, students sign agreements promising to work in a rural area after completion of medical school, which the state pays for in the meantime. Obviously, this arrangement is prone to exploitation by students who, their education paid for and degrees in hand, decide not to practice rural medicine, or at least not to fulfill their entire obligation. In either case, citizens pay heavily.

Other recruitment methods also exist. States have sponsored programs to interest rural high school students in medical careers. They have also set up residency training programs in rural hospitals to give medical students the chance to experience rural life firsthand. Some of these programs have succeeded in bringing doctors to rural areas. In 1971 the University of Minnesota opened the Rural Physician Associate Program, a nine-month elective available to third-year medical students. According to the university, "Students live and train in non-metropolitan communities under the supervision of family practice and other physicians called preceptors." Over 800 medical students have participated, and of those, 65 percent now practice in rural areas. Eighty-two percent of the participants chose primary care.[2]

In addition, state-sponsored recruitment agencies attempt to lure practicing physicians to rural hospitals and communities. For instance, Oregon sponsors the Healthcare Experts for Rural Oregon (HERO) program, which works with rural communities to attract compatible physicians, offering bonuses such as a state income tax credit of $5,000 for up to ten years.

Is State Recruitment Necessary?

Government-sponsored recruitment is certainly a departure from free-market principles. However, it is not the kind of government intervention that is likely to draw much criticism. The state would respond that it is fulfilling its proper role by helping rural communities find the physicians they need for quality care. The subject isn't quite that simple, however, and the outcomes aren't always so rosy.

The emphasis placed on recruiting physicians helps contribute to a dangerous culture of dependence among residents of rural areas. Rural communities come to see themselves as "charity cases," unworthy of having a physician except at the start of his career and not able to support or attract a physician without state help. That culture subverts the free-market principle of voluntary exchange for *mutual* benefit that rules other aspects of our economy, urban and rural. Consider the advice of one publication written as a guide for those working in the field of rural physician recruitment:

> Develop a recruitment fund with donations from the hospital, businesses, and community events, e.g., cake sales and high school car washes. Be prepared to spend several years of hard work developing the fund.
>
> Consider developing a community finance plan to help new doctors purchase equipment or repay their educational debts.[3]

Imagine a community accepting such advice for the recruitment of bankers or lawyers. It wouldn't happen. We do not hear of severe shortages of bankers or lawyers in rural America, not because there are necessarily too many of them, but because the free market offers a place for practitioners of these professions in small towns as well as in large cities. Advocates of state-sponsored rural physician recruitment are bound to argue that physicians cannot be compared to bankers or lawyers. But in fact, none can exist without the others. All three, along with grocers, custodians, restaurateurs, teachers, carpenters, and a host of other workers and entrepreneurs are intertwined into any local economy, and none should be singled out for special treatment. When special treatment is accorded to one occupation, the population is bound to suffer through both the cost and quality of the service offered. Lopsided dependence is no base on which to build any segment of an economy.

Just as government interference creates a culture of dependence among rural residents, it also creates a culture of transience in the rural health-care community. In the free market, physicians take up practice in a community because they want to live there and because they feel that good opportunities exist for them. Some are bound to move on, but many will stay and pursue their dreams. When physicians are lured to a community through state loan repayments, tax breaks, and other perks, a sense of transience is almost expected. One North Carolina study

found that 19 percent of newly recruited rural physicians planned to leave, even when they first arrived. Fewer than half planned to stay.[4] Though some physicians will remain in an area for a long time, others will move on to still greener pastures when their obligations are fulfilled or when they realize that their personalities and dreams do not fit the community in which they were placed. Such transience is detrimental to quality health care in small communities and merely perpetuates the recruitment problem by opening up a vacancy not long after it has been filled.

Market Alternatives

Nevertheless, primary care physicians are few and far between in much of rural America, and access to medical care there is often a real problem. But this situation must not drive us to conclude that free-market solutions don't exist. Indeed, trends that have drawn so much discussion over the past decade may be reversing themselves. The growth of managed care organizations, which drew so many general practitioners to urban areas over the last several years, is slowing. Profits are shrinking. Consumers are clamoring for more choice.[5] The shortage of primary care physicians nationwide may very well be turning into a surplus, as medical students realize where their best opportunities for work might be in the future.[6] Some of these physicians will turn to rural communities on their own, realizing that markets there are open.

In the meantime, rural hospitals and communities should be encouraged to use private recruiting agents or cooperative recruiting efforts, rather than state-supported recruiting mechanisms. Such efforts are more realistic and efficient—and more satisfying in matching a doctor to a community.

In short, we must be careful not to pass off any state-sponsored program as helpful or even as harmless without a full analysis of the free-market alternatives. Though wide-ranging government health-care initiatives, such as the 1993 Clinton plan, are likely to raise the eyebrows of voters, few people will even notice something as seemingly innocuous as government-sponsored rural physician recruitment. On its surface that mission, like so many others, seems to be a proper use of tax dollars, a beneficial action on behalf of those with little political or economic power. Yet it is in exactly such cases that citizens lose freedom and independence to the state, a trend that is hard to reverse. □

1. Victoria D. Weisfeld, ed., *Rural Health Challenges in the 1990s*, (Princeton: Robert Wood Johnson Foundation, November 1993), p. 57.

2. University of Minnesota, *Rural Physician Associate Program.* Http://www.rpap.umn.edu/. May 7, 1997.

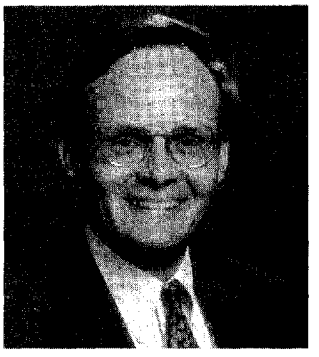
3. *Plugging the Leaks in Health Care: Harnessing Economic Opportunity in Rural America.* Center for the New West. December 1992, p. K3.

4. Sari Teplin and Christine Kushner, *Physician Life and Practice in Underserved Communities: Strategies for Recruitment and Retention*, University of North Carolina Rural Health Research Program, March 1994, p. 8.

5. Center for Studying Health System Change, *Issue Brief*, Washington, D.C., May 1998.

6. "Survey shows surplus of primary care physicians." CNN Interactive, U.S. News Story page, http://www.cnn.com/US/9804/13/doctor.shortage.ap/. April 13, 1998.





The Poverty of the United Nations

Twenty years ago, a United Nations report listed the United States as consuming 115,540 kilowatt-hours of energy per person per year. At the same time, each person in the tiny central African nation of Burundi was using up just 120 kilowatt-hours. My guess is that today, the average American is still consuming about a thousand times as much energy as the average Burundian. It's also a safe bet that the "experts" at the United Nations want Americans to feel just as guilty about the disparity today as 20 years ago.

Is this something about which Americans should flog themselves in unremitting guilt? Does Burundi use less energy because America uses too much? Is world energy a fixed pie, with America greedily hogging more than its quota at the expense of the Burundis of the planet? Would Burundi be better off if America impoverished itself? Questions like these were answered definitively by free-market economists decades ago, but like a nagging mother-in-law, the questions just never go away.

You've heard this international class warfare stuff before, from many sources besides the United Nations. A few years ago, the mantra of the international statist community—repeated endlessly in the media—was this: "Americans are only 6 percent of the world's population but they consume 40 percent of the world's energy." Greed was supposed to be the explanation for this disparity, and the solution offered was for America to spread its wealth in foreign-aid gifts to the less fortunate countries of the world.

Energy, of course, wasn't (and still isn't) the only thing of which America consumes more than its share of global population. We also eat more than 6 percent of the world's potato chips and broccoli. We enjoy more than 6 percent of the world's indoor plumbing, hearing aids, and baseballs. We operate more than 6 percent of the world's cars, trucks, hang gliders, tricycles, and skateboards. We listen to more than 6 percent of all lectures and read more than 6 percent of the world's books. And we probably put up with more than our share of nonsense too.

The fact is that Americans *consume* more because Americans *produce* more. That's right—more than 6 percent of the world's potato chips, baseballs, skateboards, and countless other things. If we didn't first produce, we wouldn't have it to consume or to trade for what we really wanted. How can such an elementary point, such a basic principle of life and economics, be lost on anyone who doesn't have to sign his name with an "X"?

Unfortunately, the U.N. is at it again. Last September it issued a document called "The Human Development Report 1998." The richest fifth of the world's nations, declares the report, accounts for 86 percent of private consumption. Never mind the inherently dubious nature of adding up "private consumption" in almost 200 different countries.

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The report is yet another lamentation about how the rich have it and the poor don't: the richest fifth purchase nine times as much meat, have access to nearly 50 times as many telephones, and use more than 80 times the paper products and motorized vehicles than the poorest fifth. While two billion people worldwide supposedly go without schools and toilets, self-indulgent Americans are painting themselves with $8 billion in cosmetics and Europeans are feasting on $11 billion in ice cream. To reduce these horrid inequalities, the report recommends that "consumption levels among the poor" be increased to "basic" levels.

Think about that. The poor nations don't consume much now, and the U.N. tells us that the answer is for them to consume more. How are the poor nations to get more? Change their ways? *Produce* more, perhaps? If the U.N. thinks that poor nations' low productivity is at fault here, there's little sign of it. As the *New York Times* revealed, "the report only skirts the issue of what role the poorest nations themselves play in this predicament."

The sad fact is that in those poor countries like Burundi, indigenous political and cultural barriers to production constitute the overwhelming if not exclusive source of poverty. Routinely, the chronically destitute nations of the world are the ones that make war on private property, keep out foreign investment, impose viciously punitive taxes and regulations, spend inordinate sums on the military, squander resources on corruption and public works boondoggles, and in general, penalize or even kill anybody with enough spunk to start a business. These nations don't consume much because, as a result of these barriers, they don't produce much. It's as simple as that. And it's no coincidence that reports to the contrary come forth from a world body in which the ranks of the benighted are legion.

What poor nations need to do is to create the enlightened political and cultural conditions whereby capital investment and the resulting production are encouraged instead of suppressed. This is not new information. It's the same formula by which America emerged from the status of 13 poor backwater colonies to the wealthiest nation on the globe. With a relatively free economy, America has shown the world how to go from Model T's to space shuttles in less time than most peoples have taken to get from dirt paths to gravel roads. Other countries from England to Hong Kong can boast similar accomplishments as well, and for similar reasons.

It is no disgrace that Americans consume 40 percent of the world's energy, or whatever the number may really be. Rather, it is a tribute to our ingenuity, creativity, and enterprise. We've put our God-given abilities to work within a system that even with all its government intervention is still infinitely more hospitable to production than Burundi's. If we restricted our energy consumption to just 6 percent of the total world supply, our lives would be shorter, less healthy, and a lot more painful. There would be fewer of us, and not by choice. The rest of the world would be worse off too because poor people cannot materially do much to help other poor people through trade.

People who are interested in ending poverty and really solving economic problems would do well to read Adam Smith's *The Wealth of Nations* and ignore any report that comes out of the United Nations. □

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THE FREEMAN
Ideas On Liberty

The Other Tobacco War

by Aaron Lukas

The U.S. Customs Service recently mounted a major offensive in the federal government's latest brainchild: the war on Cuban cigars. Agents swept through exclusive Manhattan clubs and restaurants, arresting managers and patrons alike. Once again, law-abiding New Yorkers are free to stroll down Park Avenue without fear of encountering a contraband Cohiba.

News reports evoked images of grim-faced, Prohibition-era G-men busting up speakeasies: "[Agents] searched the upscale restaurant Patroon and arrested its cigar room manager Alex Hasbany," reported the Reuters news wire. "The restaurant's owner, Kenneth Aretsky, former president of New York's famous '21 Club' surrendered to authorities on Thursday."

Good thing Aretsky went peacefully—gun battles in expensive restaurants were all the rage in the days of cigar-smoking crime boss Al Capone, but are passé today.

Federal prosecutors reported seizing several hundred thousand dollars' worth of the prized stogies. At least nine people were arrested, including the head of U.S. securities at Chase Securities, Inc., a unit of Chase Manhattan Bank.

All of this suggests the question: doesn't customs have anything useful to do?

The raids were conducted under the auspices of the Trading with the Enemy Act, which grants presidents the authority to prohibit the import of property from specified foreign countries. Federal law has banned most imports from Cuba since July 8, 1963, shortly after President John F. Kennedy ordered press secretary Pierre Salinger to go out and buy as many of his favorite H. Upmann Petit Coronas as possible.

Sanctions Codified

In 1996 the Helms-Burton Act codified many of the unilateral economic sanctions against Cuba that the United States had maintained under the Trading with the Enemy Act. It also added noxious new provisions, such as extraterritorial boycotts of foreign companies that do business in Cuba.

Such laws offer massive potential for abuse because enforcement is nearly impossible. Prominent businessmen have been nabbed, but how many members of Congress have occasionally indulged in a fine Havana Montecristo or Cohiba Esplendidos? Don't expect to see agents raiding Capitol Hill offices anytime soon.

Besides, is Cuba really our enemy? With the collapse of the Soviet Union and the subsequent end of subsidies to Cuba in the early 1990s, the Cuban security threat virtually ceased to exist. Now we isolate Cuba not to enhance security, but to "help" the Cuban people.

It's difficult to see how commando raids on American citizens will promote freedom

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abroad. In any case, it's bad policy. Our government was established to protect the life, liberty, and property of the people of the United States. We shouldn't allow our rights to be compromised, even for seemingly noble goals. The example of a free and prosperous America is a more powerful force for change than any embargo will ever be.

Nevertheless, Customs has dramatically stepped up its enforcement efforts against Cuban cigars. The agency reported confiscating $3.1 million worth last year alone, in 3,700 separate seizures. As is the case with illegal narcotics, prices will rise and more smuggling will occur; oppression in Cuba will continue, however, just as it has during nearly four decades of U.S. isolation.

Sadly, the cigar sting is only the most recent embarrassment in America's failed policy toward Cuba. Ongoing U.S. antagonism is a major reason that Castro remains so firmly in power, despite the Cuban economy's deterioration.

If Congress and the Clinton administration are serious about encouraging liberalization, they should allow Americans to trade freely with Cuba. The Cuban embargo—and the cigar wars—should be consigned to the ash heap of history. □

It's Time to Privatize Social Security

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THE FREEMAN
Ideas On Liberty

Artistic Freedom Requires Economic Freedom

by Tyler Cowen

Psychological motivations, though a driving force behind many great artworks, do not operate in a vacuum, independent of external constraints. Economic circumstances influence the ability of artists to express their aesthetic aspirations. Specifically, artistic independence requires financial independence and a strong commercial market. Beethoven wrote: "I am not out to be a musical usurer as you think, who writes only to become rich, by no means! Yet, I love an independent life, and this I cannot have without a small income."

Capitalism generates the wealth that enables individuals to support themselves through art. The artistic professions, a relatively recent development in human history, flourish with economic growth. Increasing levels of wealth and comfort have freed creative individuals from tiresome physical labor and have supplied them with the means to pursue their flights of fancy. Wealthy societies usually consume the greatest quantities of non-pecuniary enjoyments. The ability of wealth to fulfill our basic physical needs elevates our goals and our interest in the aesthetic. In accord with this mechanism, the number of individuals who can support themselves as full-time creators has risen steadily for centuries.

Perhaps ironically, the market economy increases the independence of the artist from the immediate demands of the culture-consuming public. Capitalism funds alternative sources of financial support, allowing artists to invest in skills, undertake long-term projects, pursue the internal logic of their chosen genre or niche, and develop their marketing abilities. A commercial society is a prosperous and comfortable society, and offers a rich variety of niches in which artists can find the means to satisfy their creative desires.

Many artists cannot make a living from their craft, and require external sources of financial support. Contrary to many other commentators, I do not interpret this as a sign of market failure. Art markets sometimes fail to recognize the merits of great creators, but a wealthy economy, taken as a whole, is more robust to that kind of failure in judgment than is a poor economy. A wealthy economy gives artists a greater number of other sources of potential financial support.

Private foundations, universities, bequests from wealthy relatives, and ordinary jobs, that bane of the artistic impulse, all have supported budding creators. Jane Austen lived from the wealth of her family, T. S. Eliot worked in Lloyd's bank, James Joyce taught languages, Paul Gauguin accumulated a financial cushion through his work as a stockbroker, Charles Ives was an insurance executive, Vincent van Gogh received support from his

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brother, William Faulkner worked in a power plant and later as a Hollywood screenwriter, and Philip Glass drove a taxi in New York City. William Carlos Williams worked as a physician in Rutherford, New Jersey, and wrote poetry between the visits of his patients.

Wallace Stevens, the American poet, pursued a full-time career in the insurance industry. "He was a very imaginative claims man," noted one former colleague. When offered an endowed chair to teach and write poetry at Harvard University, Stevens declined. He preferred insurance work to lecturing and did not wish to sacrifice his position in the firm. At one point a coworker accused Stevens of working on his poetry during company time. He replied: "I'm thinking about surety problems Saturdays and Sundays when I'm strolling through Elizabeth Park, so it all evens out."

Parents and elderly relations have financed many an anti-establishment cultural revolution. Most of the leading French artists of the nineteenth century lived off family funds—usually generated by mercantile activity—for at least part of their careers. The list includes Delacroix, Corot, Courbet, Seurat, Degas, Manet, Monet, Cézanne, Toulouse-Lautrec, and Moreau. French writers Charles Baudelaire, Paul Verlaine, and Gustave Flaubert went even further in their anti-establishment attitudes, again at their parents' expense.

Even the most seclusive artists sometimes rely furtively on capitalist wealth. Marcel Proust sequestered himself in a cork-lined room to write, covering himself in blankets and venturing outside no more than 15 minutes a day. Yet he relied on his family's wealth, obtained through the Parisian stock exchange. Paul Gauguin left the French art world for the tropical island of Tahiti, knowing that his pictures would appreciate in value in his absence, allowing for a triumphal return. Gauguin never ceased his tireless self-promotion, and during his Pacific stays he constantly monitored the value of his pictures in France.

Wealth and financial security give artists the scope to reject societal values. The bohemian, the avant-garde, and the nihilist are all products of capitalism. They have pursued forms of liberty and inventiveness that are unique to the modern world.

Pecuniary Incentives

Many artists reject the bohemian lifestyle and pursue profits. The artists of the Italian Renaissance were businessmen first and foremost. They produced for profit, wrote commercial contracts, and did not hesitate to walk away from a job if the remuneration was not sufficient. Renaissance sculptor Benvenuto Cellini, in his autobiography, remarked, "You poor idiots, I'm a poor goldsmith, and I work for anyone who pays me."

Bach, Mozart, Haydn, and Beethoven were all obsessed with earning money through their art, as a reading of their letters reveals. Mozart even wrote: "Believe me, my sole purpose is to make as much money as possible; for after good health it is the best thing to have." When accepting an Academy Award in 1972, Charlie Chaplin remarked: "I went into the business for money and the art grew out of it. If people are disillusioned by that remark, I can't help it. It's the truth." The massive pecuniary rewards available to the most successful creators encourage many individuals to try their hand at entering the market.

Profits signal where the artist finds the largest and most enthusiastic audience. British "punk violinist" Nigel Kennedy has written: "I think if you're playing music or doing art you can in some way measure the amount of communication you are achieving by how much money it is bringing in for you and for those around you." Creators desiring to communicate a message to others thus pay heed to market earnings, even if they have little intrinsic interest in material riches. The millions earned by Prince and Bruce Springsteen indicate how successfully they have spread their influence.

Beethoven cared about money as a means of helping others. When approached by a friend in need, he sometimes composed for money: "I have only to sit down at my desk and in a short time help for him is forthcoming." Money, as a general medium of exchange, serves many different ends, not just greedy or materialistic ones.

Funding Artistic Materials

Artists who chase profits are not always accumulating wealth for its own sake. An artist's income allows him or her to purchase the necessary materials for artistic creation. Budding sculptors must pay for bronze, aluminum, and stone. Writers wish to travel for ideas and background, and musicians need studio time. J. S. Bach used his outside income, obtained from playing at weddings and funerals, to buy himself out of his commitment to teach Latin, so that he would have more time to compose. Robert Townsend produced the hit film *Hollywood Shuffle* by selling the use of his credit cards to his friends. Money is a means to the ends of creative expression and artistic communication.

Capitalist wealth supports the accouterments of artistic production. Elizabethan theaters, the venues for Shakespeare's plays, were run for profit and funded from ticket receipts. For the first time in English history, the theater employed full-time professional actors, production companies, and playwrights. Buildings were designed specifically for dramatic productions. Shakespeare, who wrote for money, earned a good living as an actor and playwright.

Pianos, violins, synthesizers, and mixers have all been falling in price, relative to general inflation, since their invention. With the advent of the home camcorder, even rudimentary movie-making equipment is now widely available. Photography blossomed in the late nineteenth century with technological innovations. Equipment fell drastically in price and developing pictures became much easier. Photographers suddenly were able to work with hand cameras, and no longer needed to process pictures immediately after they were taken. Photographic equipment no longer weighed 50 to 70 pounds, and the expense of maintaining a traveling darkroom was removed.

Falling prices for materials have made the arts affordable to millions of enthusiasts and would-be professionals. In previous eras, even paper was costly, limiting the development of both writing and drawing skills to relatively well-off families. Vincent van Gogh, an ascetic loner who ignored public taste, could not have managed his very poor lifestyle at an earlier time in history. His nonconformism was possible because technological progress had lowered the costs of paints and canvas and enabled him to persist as an artist.

Female artists, like Berthe Morisot and Mary Cassatt, also took advantage of falling materials costs to move into the market. In the late nineteenth century women suddenly could paint in their spare time without having to spend exorbitant sums on materials. Artistic willpower became more important than external financial support. This shift gave victims of discrimination greater access to the art world. The presence of women in the visual arts, literature, and music has risen steadily as capitalism has advanced.

Falling costs of materials help explain why art has been able to move away from popular taste in the twentieth century. In the early history of art, paint and materials were very expensive; artists were constrained by the need to generate immediate commissions and sales. When these costs fell, artists could aim more at innovation and personal expression, and less at pleasing buyers and critics. Modern art became possible. The impressionists did not require immediate acceptance from the French Salon, and the abstract expressionists could continue even when Peggy Guggenheim was their only buyer.

The artist's own health and well-being, a form of "human capital," provides an especially important asset. Modernity has improved the health and lengthened the lives of artists. John Keats would not have died at age 26 of tuberculosis with access to modern medicine. Paula Modersohn-Becker, one of the most talented painters Germany has produced, died from complications following childbirth, at the age of 31. Mozart, Schubert, Emily Brontë, and many others who never even made their start also count as medical tragedies who would have survived in the modern era. The ability of a wealthy society to support life for greater numbers of people, compared to premodern societies, has provided significant stimulus to both the supply and demand sides of art markets.

Most advances in health and life expectancy have come quite recently. In the United

States of 1855, one of the wealthiest and healthiest countries in the world at that time, a newly born male child could expect no more than 39 years of life. Yet many of the greatest composers, writers, and painters peak well after their fortieth year.

Birth control technologies, generally available only for the last few decades, have given female creators greater control over their lives and domestic conditions. Most of the renowned female painters of the past, for various intentional or accidental reasons, had either few children or no children at all. Childbearing responsibilities kept most women out of the art world. Today, budding female artists can exercise far greater control over whether and when they wish to have children. The increasing prominence of women in music, literature, and the visual arts provides one of the most compelling arguments for cultural optimism. For much of human history, at least half of the human race has been shut out from many prominent artistic forms, and women are only beginning to redress the balance.

Do the Arts Lag in Productivity?

William Baumol and William Bowen, two economists who have analyzed the performing arts, believe that economic growth imposes a "cost disease" on artistic production. They claim that rising productivity causes the arts to increase in relative cost, as a share of national income. The arts supposedly do not enjoy the benefits of technical progress to equal degree. It took 40 minutes to produce a Mozart string quartet in 1780, and still takes 40 minutes today. As wages rise in the economy, the relative cost of supporting the arts will increase, according to this hypothesis.

Contrary to Baumol and Bowen, the evidence suggests that the arts benefit greatly from technological progress. The printing press, innovations in paper production, and now the World Wide Web have increased the availability of the written word. The French impressionists drew their new colors from innovations in the chemical industry. Recording and radio, both capital technologies, have improved the productivity of the symphony orchestra. Symphonic productions now reach millions of listeners more easily than ever before. These technological improvements are not once-and-for-all events that only postpone the onset of the cost disease. Rather, technological progress benefits the arts in an ongoing and cumulative fashion.

The cost disease argument neglects other beneficial aspects of economic growth. The arts benefit more from technological advances than it may at first appear. Production of a symphonic concert, for instance, involves more than sitting an orchestra in a room and having them play Shostakovich. The players must discover each other's existence, maintain their health and mental composure, arrange transportation for rehearsals and concerts, and receive quality feedback from critics and teachers. In each of these regards the modern world vastly surpasses the productivity of earlier times, largely because of technological advances.

Mechanisms in Support of Artistic Diversity

Well-developed markets support cultural diversity. A quick walk through any compact disc or book superstore belies the view that today's musical and literary tastes are becoming increasingly homogeneous. Retail outlets use product selection and diversity as primary strategies for bringing consumers through the door. Even items that do not turn a direct profit will help attract business and store visits, thereby supporting the ability of the business to offer a wide variety of products.

The available variety of artistic products should come as no surprise. Adam Smith emphasized that the division of labor, and thus the degree of specialization, is limited by the extent of the market. In the case of art, a large market lowers the costs of creative pursuits and makes market niches easier to find. In the contrary case of a single patron, the artist must meet the tastes of that patron or earn no income.

Growing markets in music, literature, and the fine arts have moved creators away from dependence on patronage. A patron, as

opposed to a customer, supports an artist with his or her own money, without necessarily purchasing the artistic output. Samuel Johnson, writing in the eighteenth century, referred to a patron as "a wretch who supports with insolence, and is paid with flattery." Even Johnson, however, did not believe that patrons were intrinsically bad; the problem arises only when artists are completely dependent upon a single patron. Patronage relationships, which today stand at an all-time high, have become more beneficial to artistic creativity over time. The size and diversity of modern funding sources gives artists bargaining power to create space for their creative freedom.

Growth of the market has liberated artists, not only from the patron, but also from the potential tyranny of mainstream market taste. Unlike in the eighteenth century, today's books need not top the bestseller list to remunerate their authors handsomely. Artists who believe that they know better than the crowd can indulge their own tastes and lead fashion. Today it is easier than ever before to make a living by marketing to an artistic niche and rejecting mainstream taste.

In the realm of culture, market mechanisms do more than simply give consumers what they want. Markets give producers the greatest latitude to educate their audiences. Art consists of a continual dialogue between producer and consumer; this dialogue helps both parties decide what they want. The market incentive to conclude a profitable sale simultaneously provides an incentive to engage consumers and producers in a process of want refinement. Economic growth increases our ability to develop sophisticated and specialized tastes. □

Payola and Cultural Diversity

The payola scandals provided a dramatic episode in the clash of musical worlds. Independent record companies frequently used payola to promote rock and roll on American radio. Payola occurs when a disc jockey is paid by record companies or music publishers to play certain recordings. This practice, usually considered scandalous, in fact helped new musicians gain airplay. Payola combated conformism and racism in the music business. Nonetheless rock and roll opponents succeeded in making payola a dirty word akin to bribery or money laundering.

The first documented instances of payola date from England in the 1860s. The publishers of sheet music paid vaudeville artists to sing and popularize their songs. Payment of these fees was a normal marketing procedure for publishers and a significant source of income for performers; payola occasioned no political scandal. Prior to the payola scandals, payola had been an accepted and legal business practice used to promote new products for many decades. In the case of rhythm and blues, the independents lacked the reputations and marketing power to place their artists through name alone, and were forced to rely on payola.

Chuck Berry's "Maybellene," his first hit and still one of his most popular songs, was given initial airplay because of payola. Leonard Chess of Chess Records (Berry's record company) went to well-known disc jockey Alan Freed with a large catalog of material. Chess offered Freed partial songwriting credits on any song of his choice, provided that he would play and promote the song. Freed now had a stronger incentive to pick the best song and to promote it. After listening to hundreds of recordings, Freed picked "Maybellene." Berry became a star, and the Freed estate continues to receive royalties (check your record label). When record companies believed they had a sure-fire hit by an unknown singer, they used payola to buy air-time for the record.

Payola does not differ from the ordinary purchase of advertising time. Instead of hearing a jingle, we hear a song. The song itself, and the performer, is being advertised. Outlawing payola kept radio stations from advertising music, the commodity of greatest interest to their audiences.

Payola also encouraged disc jockeys, the individuals who knew most about music, to discover new talent. The station owners were not as well informed as the disc jockeys and did not have the same ground-level contacts in the musical world, especially for rock and roll. The proliferation of independent record companies made new stars harder to find, increasing the importance of disc jockey middlemen. If a disc jockey found a new star, the disc jockey would receive some of the benefits in the form of payola income.

Payola income decreased disc jockey favoritism and racial discrimination. When disc jockeys receive additional income from playing the more popular product, they are less inclined to indulge their own personal and racial biases, and more inclined to heed the wishes of consumers. The value of giving airplay to a good song, and thus its payola value, is usually higher than the value of promoting a bad song. Record companies were not interested in paying to procure airtime for likely duds.

Critics of payola argued (correctly) that payola gave a special boost to rock and roll. Outlawing payola increases the importance of advertisements as a source of radio station income. The radio station will play music to attract listeners who purchase advertised products—middle-class and upper-class Americans. When payola is legal, the desire to increase payola income encourages the station to attract listeners who will buy *records*. Payola gave record buyers—the young, the die-hard music fans, and the followers of rock and roll—greater influence over station programming.

The payola scandals were part of the ASCAP [American Society of Composers, Authors, and Publishers] campaign against BMI [Broadcast Music Incorporated] and rock music. After an ASCAP antitrust suit against BMI failed, the music publishers sought another legal weapon to use against their competitor. ASCAP also wished to strike out against the disc jockeys who had neglected to promote their music. In late 1959, ASCAP persuaded Congress to launch an investigation of payola for rock and roll, rhythm and blues, and soul music.

The discriminatory nature of the payola hearings belies their origins. Responding to ASCAP pressure, the House Committee examined payola for rock and roll only, not payola for classical music. The government came down much more heavily on "black payola" than "white payola." Alan Freed, the deejay who pushed gritty rock and roll and raucous black music, was prosecuted and found his entire career ruined. Dick Clark, of American Bandstand fame, used payola to promote more respectable forms of white pop. Clark's "violations" were more striking but he was left with his career and media empire intact.

At the end of the Committee hearings, Congress outlawed payola, with a jail term of up to one year and a $10,000 fine for convicted offenders. Earlier, the Federal Communications Commission had threatened to suspend the license of any radio station found guilty of accepting payola. Amazingly, when the payola hearings started, payola was not in violation of any Federal law. The investigations were primarily a witch hunt directed against particular kinds of music that did not meet with universal approval.

—TYLER COWEN

THE FREEMAN
Ideas On Liberty

Flags, Flames, and Property

by Andrew I. Cohen

A constitutional amendment that would forbid the desecration of American flags is again percolating in the nation's capital. As of this writing, the immediate prospects for passage look bleak. But this amendment has a way of never fully going away. Many opponents of the measure trot out free speech arguments. And although concerns about free expression are important, these traditional arguments miss a more central political principle that the amendment and resulting laws against flag burning would jeopardize: property rights. The amendment would undermine key liberties for which the flag stands.

Arguments for Flag Desecration Laws

Those who uphold laws against flag desecration typically speak of the important values that the flag symbolizes. They claim that legally allowing flag burning is tantamount to rejecting the freedoms that the flag represents. They say it is vital that we express our respect for human freedom by institutionalizing penalties against those who would defile the national symbol.

Permitting flag burning, the amendment's proponents continue, sends the wrong message to America's youth, America's voters, and observers abroad. When the young see protesters publicly burning a flag with impunity, they may believe that American freedoms are cheap. They may then think that the nation's commitment to uphold those freedoms is fleeting. Permitting flag burning may also undermine a key basis for community among America's voters. With protesters burning flags, voters may lose a vision of shared citizenship and be less committed to the American ideal. Flag burning is also supposedly a slap in the face to all Americans who suffered in wartime to secure freedoms for everyone. Lastly, foreign observers who see Americans burning their own flag may be less inclined to support America's international policies aimed at securing freedom. Advocates fear that foreigners will think: if Americans cannot take their own freedoms seriously, then we need not take seriously the moral reasoning they present to the world.

The Free Speech Argument Against Flag Desecration Laws

People who burn flags intend to send a message by doing so. This is what makes flag burning a form of expression. Some flag burners take offense at various American foreign policy measures. (Recall the nightly news broadcasts last summer showing Sudanese burning American flags in Khartoum after the United States bombed what it deemed a suspicious pharmaceutical factory.) Some individuals may burn flags as a way of saying America is not true to its own values.

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Others simply despise American ideals and set the flag aflame. In any case, people who burn flags do so deliberately in order to send a public message of protest.

The First Amendment to the Constitution reads, "Congress shall make no law . . . abridging the freedom of speech." Constitutional scholars and legal theorists have long argued over the meaning of this amendment. There is, however, a rough consensus on two ideas: (1) the amendment protects peaceful expression, popular or unpopular, but (2) the Framers clearly did not intend for it to license any and all forms of expression. Consequently, room has been made for laws against libel, slander, and obscenity. Contrary to hyperbolic op-eds railing against flaming protests, burning a flag is not "obscene." At worst, it is despicable. At best, it is a valuable form of political speech.

The First Amendment protects freedom of speech, which in turn protects the liberty to say wrong-headed, bigoted, stupid, vicious things. Such protection is crucial; otherwise freedom of speech would reduce to the empty freedom to say only the right, the true, and the good. That would present a disturbing practical difficulty: some bureaucrat would have to decide what is permissible speech, because in today's pluralistic society, there is little consensus on many aspects of the right, the true, and the good. Freedom of speech, however, is the freedom to say what one wishes without having to solicit the permission of anyone first.

Freedom of speech guarantees a healthy, open marketplace of ideas. More fundamentally, it includes the freedom to say things that others might not like. Those who are offended should respond with reasoned arguments of their own and not by passing a law. If individuals were only free to say things that others liked, public and private discussions would be banal, stilted, and oppressed. A law against flag burning forbids a form of expression simply because others do not like the message. Government exists, however, to protect individual rights. It should not protect citizens from being offended. We can stipulate that many acts of flag burning are offensive. Simply being offensive, however, does not violate individual rights.

The Property Rights Argument Against Flag Burning

The free speech argument against the proposed amendment is powerful; people must be free to offend if free speech is to count for anything. There is, however, one time when flag burning should be against the law: when it's someone else's flag.

Suppose you own a flag. Suppose that Chris takes your flag without your consent and sets it on fire in the public square. What Chris has done ought to be forbidden (and punished) not because he burned a flag, but because he burned *your* flag. Chris ought to be held accountable just as if he had taken a sledgehammer to your concrete garden gnomes without your permission. He destroyed your property.

People who debate the flag issue often lose sight of this important fact: you cannot burn "the American flag" because there is no such thing as "the American flag." There are only *flags*. The "American flag" is an idea that cannot be burned. A particular flag, however, can be burned. Whether it is permissible to do so turns on whose flag it is.

Being a material object, a flag usually comes into the world attached to someone as property. A law against flag burning would forbid you from disposing of your property as you see fit. Let us assume that burning your flag does not pose a threat to public safety (that is, you don't ignite and toss it into an unsuspecting crowd). In that case, when you burn *your* flag, your actions are not importantly different from taking *your* paper and *your* ink to print up pamphlets that say anything (or even nothing) at all. The pamphlets are *your* property, and so too is your flag. Passers-by can take your message or leave it.

To forbid flag burning is to forbid you from disposing of your property in ways that offend others. But property rights protect freedom of action for which one need not solicit the permission of others. A right to *your flag* guarantees a right to burn it, stomp on it, spit on it, or turn it into underwear if you so choose. Your flag is your property. If someone does not like what you do with your property, he should not lock you up; he should persuade

you to change your ways or he should have nothing to do with you. Consider the absurdity of having rights to use your property only in ways others find acceptable.

Permissible Flag Burning and Some Problems

When a flag becomes old and tattered, there is a prescribed way to dispose of it. Part of the process involves burning it. If flag burning were forbidden, presumably it would not be just any flag burning that would be illegal. It would only be flag-burning-while-thinking-nasty-thoughts-about-the-flag. If persons are to be punished not for what they do, but for what they *think*, we will have marched a long way from the freedoms on which this nation was founded, and headed dangerously closer to tyranny.

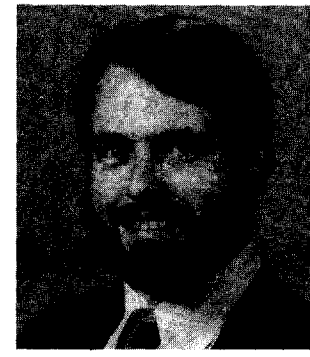
There are further difficulties with laws against flag burning. We all know what an American flag is supposed to look like. It has 50 stars and 13 stripes, all arranged in a certain pattern. Suppose, however, you were to sew a piece of fabric that looked just like a current American flag, except that it had *49* stars or 50 *six*-sided stars (instead of five-sided stars), or *white* stripes on the very top and very bottom (instead of red), or a blue field that was only *six* stripes high (instead of seven). Strictly speaking, those pieces of fabric would not be American flags. They would be imperfect approximations of American flags. Would a law against flag burning forbid the desecration of any piece of fabric that even *looked like* an American flag? What if one takes a big piece of white paper and writes in big boldface letters, "THIS IS AN AMERICAN FLAG," and sets it on fire? Perhaps the courts would rule that any act *intended* to make onlookers believe that one was burning an American flag would be covered by the amendment. Once again, however, the government would be getting into the business of punishing people for having bad thoughts. This is not the mark of a government in a free society.

What the Flag Means

The flag is a symbol of American values such as self-determination and freedom from oppression. Throughout our history, members of the armed services suffered on behalf of freedom, not on behalf of a piece of fabric. They did not put their lives on the line so that busybodies and bureaucrats could tell us what we can or cannot say and what we can or cannot do with our property.

No doubt, flag burners are often quite vicious, detestable persons whose contempt for American values deserves *our* contempt. But the law should not forbid all vicious conduct. We can privately refuse to have anything to do with such persons. We can hold them up to public scorn. We might display our patriotism to counter the flag-burning demonstration. Such acts would help solidify the shared citizenship that flag-burning amendment advocates so often invoke. Those informal responses would also help send the message that some matters are best left to private individuals and the free choices they make. Those who take freedom seriously are civilized enough to put flag burners in their place without beating them up or locking them up.

Supporters of laws to punish people who destroy a flag betray their belief that the values the flag symbolizes cannot prevail on their own merits. They seem to think that freedom demands government-mandated respect. But American ideals are sturdy enough to await voluntary respect. Let us repudiate flag burners and persuade (not force) individuals to respect the flag. We must not, however, cheapen the freedoms the flag represents with an amendment that would restrict individual rights. □



Public Failure, Private Response

President Bill Clinton has called for a "national crusade" on education. Naturally, that means spending more money: he would have Washington hire teachers and build schools. Many states, flush with cash, also plan to spend more.

But the problem of education is monopoly, not money. Average SAT scores dropped from 980 to 899 between 1963 and 1992, while real per-pupil spending rose 160 percent. In fact, real spending per pupil has risen 40 percent a decade since World War II.

The past decade of "reforms" has changed nothing. The 1994 National Assessment of Education Progress (NAEP) test found that 36 percent of fourth graders, 39 percent of eighth graders, and 57 percent of 12th graders failed to meet basic history standards. In most other subjects students perform poorly, and, incredibly, do worse the longer they stay in school. Last year the journal *Education Week* called America's public schools "rife with mediocrity," reporting that "there is no state in which at least half the students perform at the 'proficient' level or above." It refused to give the states grades based on their NAEP results, since "all would have failed."

International comparisons tell an equally dismal story, with American students scoring below foreign kids in almost every subject. The latest survey, the Third International Mathematics and Science Study, ranked America 19th out of 21 countries in math, surpassing only Cyprus and South Africa. (No Asian nations, whose students typically do well, participated.)

While suburban schools have problems, city schools are in crisis. The Carnegie Foundation declared a decade ago: "The failure to educate adequately urban children is a shortcoming of such magnitude that many people have simply written off city schools as little more than human storehouses to keep young people off the streets."

Half of urban kids typically fail to graduate. The diplomas for students who do graduate have the value of Czarist bonds. As of 1997, reports the NAEP, only 40 percent of fourth- and eighth-graders in urban schools score at the basic level for math, reading, and science.

Of course, the educational establishment's mantra remains "more money." But the public schools are doomed to mediocrity. Admitted the late Albert Shanker, head of the American Federation of Teachers: "It's no surprise that our school system doesn't improve; it more resembles the communist economy than our own market economy."

What education needs is more competition. Private schools cost about half as much as public ones and achieve significantly better results.

Alas, serious reform has been blocked by the educational establishment, or "the Blob," as William Bennett calls it, which is more concerned about protecting interest groups

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pigging out at the educational trough than children who are drowning in it. The very people who require the poor to send their kids to dangerous schools exercise choice. Members of city school boards routinely send their children to private institutions. Public school teachers are four times as likely as other parents with comparable incomes to send their children to private schools.

A growing number of supporters of educational choice have launched a flanking maneuver around the special interests: private scholarships. Roughly three dozen private scholarship programs currently serve some 20,000 students nationwide. Another 42,000 students are on waiting lists.

Pat Rooney, chairman of the Golden Rule Insurance Company, helped spark this movement in 1991 by establishing the Educational Choice Charitable Trust (CHOICE) in Indianapolis, which in 1997 offered 1,094 scholarships of up to $800 to low-income families. The latest initiative came last April, when the Children's Educational Opportunity Foundation announced a ten-year, $50 million program for children in San Antonio's Edgewood district. The goal is to provide a scholarship for every one of the nearly 14,000 students, more than half of whom live below the poverty line.

In 1997, the School Choice Scholarships Foundation, a group of foundations, philanthropists, and Wall Street firms, offered 1,300 scholarships worth $1,400 each, to be distributed by lottery: 22,700 kids applied. The decade-old Student Sponsor Partnerships provides full tuition for more than 900 students to attend parochial schools, and Operation Exodus offers 100 scholarships for students in New York and other states. The New York Catholic Archdiocese's Inner-City Scholarship Fund helps subsidize a network of schools that educate largely poor students.

The District of Columbia's Washington Scholarship Fund began in 1993 by aiding 36 students in 12 schools. In late 1997 entrepreneurs Ted Forstmann and John Walton set aside $6 million for an additional 1,000 scholarships to pay half of annual tuition up to $1,700. An incredible 7,573 students, one in every six who is eligible, and one-tenth of the entire D.C. student population, applied.

The Children's Educational Opportunities (CEO) Foundation of Southern California supported 799 kids in Los Angeles and Orange counties; 5,000 more were on waiting lists. The Los Angeles Archdiocese Education Foundation has been awarding scholarships for its parochial schools since 1988. The Pacific Research Institute of San Francisco plans to award 100 scholarships of $2,000 each this year.

Chicago has four separate private programs. One, the FOCUS Fund (Family Options for Children Urban Scholarship Fund), offered 30 noncompetitive scholarships for any private school last fall. The Daniel Murphy Scholarship Foundation works with 36 schools and has provided 80 scholarships this year. Link Unlimited, in operation since 1966, provides 230 scholarships for Catholic schools. The Big Shoulders Fund works with inner-city parochial schools and awards nearly $1 million in scholarships annually.

There are other programs in Atlanta, Austin, Baltimore, Battle Creek, Bridgeport, Buffalo, Chicago, Dallas, Dayton, Denver, Detroit, Grand Rapids, Houston, Jackson (Mississippi), Jersey City, Knoxville, Little Rock, Midland (Texas), Milwaukee, Newark, Oakland, Oklahoma City, Orlando, Philadelphia, Phoenix, Pittsburgh, San Antonio, Schenectady, Seattle, and Washington Heights (New York). The opportunities for further expansion are obviously enormous. In fact, CEO America, headquartered in Bentonville, Arkansas, assists people and organizations interested in setting up their own programs.

Such private programs offer a glimmer of hope to children and families trapped in a failing public monopoly. Political reform remains important, but advocates of children need not wait for politicians to act. Indeed, developing successful private scholarship programs will not only help struggling students; it will also make real political change more likely. Instead of pouring their money and energy into failing public schools—as did publisher Walter Annenberg with $500 million in 1993—businessmen, foundations, and philanthropists should develop alternative private educational options. □

Elijah McCoy and Berry Gordy: Ingenuity Overcomes

by Burton Folsom

Part of the tragedy of affirmative action is its implied premise that intended beneficiaries can't succeed in business unless government grants them special privileges. But history shows that when people have the freedom to succeed, remarkable entrepreneurs and innovators emerge. Two examples separated by a century—Elijah McCoy and Berry Gordy—show how black innovators changed American life before the existence of affirmative action.

Railroads were one of the greatest inventions of the nineteenth century. One man who was indispensable in helping the railroads run efficiently and on time was Elijah McCoy. He was born in 1843 in Canada, where his parents had fled from Kentucky to escape slavery. In Canada, the McCoys learned that individual freedom and training in the marketplace were keys to opening opportunities for blacks.

On reaching manhood, Elijah McCoy went to Scotland for training in mechanical engineering. When it came time to apply his industrial skills, the Civil War had ended and blacks were legally free. McCoy came back to the United States and settled in Ypsilanti, Michigan, where he began working for the Michigan Central Railroad.

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Determined to Achieve

Despite his training, McCoy was offered the lowly job of locomotive fireman. He accepted it with a determination to show the railroad that he could accomplish more.

He immediately applied his skills to a major problem: the dangerous overheating of locomotives. Trains had to stop regularly so that their engines could be oiled to reduce friction. If trains stopped infrequently, the overheating could damage parts or start fires. If they stopped too often, freight and passengers would be delayed. McCoy invented a lubricating cup that oiled engine parts as the train was moving. He secured a patent for it in 1872 and steadily improved it.

Others tried to imitate McCoy's invention, but he kept ahead of them with his superior engineering skills. His standard of quality was so high that the cup became known as "the real McCoy," which many believe to be the origin of the famous phrase.

The invention helped the Michigan Central run safer and quicker across the state. It was also put to use in stationary engines and even in steamship engines. The grateful management of the Michigan Central promoted McCoy and honored him as a teacher and innovator for the railroad.

McCoy showed remarkable creative energy during the next 50 years. He received 51 more patents, mostly for lubricating devices. Not even old age dimmed his creative light. When



COURTESY: STATE ARCHIVES OF MICHIGAN

Elijah McCoy

he was 77, he patented an improved airbrake lubricator; when he was 80, he patented a vehicle wheel tire. He founded the Elijah McCoy Manufacturing Company in Detroit in 1920 to make and sell his inventions.

Elijah McCoy was one of many black Americans who after the Civil War improved the American workplace and showed skeptical whites what free, enterprising blacks could accomplish. In the late 1950s, 30 years after his death, another black American from Detroit, Berry Gordy, was using the free market to transform American music.

The Motown Sound

Forty years ago, many blacks enjoyed rhythm and blues music, but it was routinely unprofitable and often performed in shabby venues. Berry Gordy, a songwriter and assembly-line worker, had a vision of taking black-inspired music out of the slums and giving it broad, national appeal as a respectable art form. In 1959, Gordy borrowed $800 from his family and risked it to start Motown Record Corporation, named for the "motor town" of Detroit.

Once in business, Gordy hustled musical talent from the streets of the city and pinched pennies to survive. He set up a used two-track recorder in his small house at 2648 West Grand Boulevard that became Motown headquarters. His father did the plastering and repairs, and his sister did the bookkeeping. His vocal studio was in the hallway, and his echo chamber was the downstairs bathroom. "We had to post a guard outside the door," Gordy says, "to make sure no one flushed the toilet while we were recording."

The fact that Gordy started Motown out of his home is more than a quaint historical footnote. Doing that today in Detroit's residential areas would violate the city's repressive ban on home-based businesses—a sad comment on how stifling Detroit's regulations and taxes have become since the 1950s.

Gordy's success is sometimes ascribed to his knack for writing and producing hit songs. But there was more than that. As actor Sidney Poitier observed, "Berry Gordy . . . set out to make music for all people, whatever their color or place of origin." In doing so, Gordy made black music—the Motown sound—part of the mainstream popular culture in America.

What an achievement! Gordy had white teens all over America humming the catchy tunes of the Four Tops, the Miracles, and the Temptations. After that he promoted a flurry of black stars including Diana Ross, Michael Jackson, and Stevie Wonder. Gordy so much wanted their music, and that of other Motown singers, to reach the larger white audience in America that the sign on his headquarters read, "Hitsville, U.S.A."

The impact of Gordy's remarkable achievement is worth pondering. At one level, he created more opportunities for blacks everywhere in the music business—production, nightclubs, recording, and marketing. Beyond that, in an era of racial tensions, Gordy's music bonded blacks and whites. In 1964 and 1965, some whites attacked blacks in Oxford, Mississippi, and Selma, Alabama. But during this time, many white fans everywhere were making number-one hits for Gordy out of the first three songs by the Supremes: "Where Did Our Love Go?," "Baby Love," and "Come See About Me."

The Motown sound became mainstream American music not by law or force, but by choice. It was clever entrepreneurship, not affirmative action, that persuaded whites to integrate black musicians into their record

collections. Gordy used well-crafted songs to capture not just first place on *Billboard*'s Top 100, but the number two and three slots as well for the whole last month of 1968.

America's system of private enterprise gave Gordy the chance to air his records on radio stations and have them compete for sales in record stores all over America. But when Gordy tried to expand the Motown sound into England, he found government standing in his way. The government stations, especially the British Broadcasting Company, refused to play Motown records and give Gordy the chance that private enterprise gave him in the United States. "Because we couldn't get our records on the government stations," Gordy said, "our earliest airplay had come from *Radio Veronica* and *Radio Caroline,* 'pirate ships' anchored a few miles off the coasts of England and Holland."

The Motown music broadcast from those pirate ships captivated British listeners. Soon the demand for Gordy's records swamped record stores from Liverpool to London and forced the bureaucrats to permit the music to be heard on government stations. When Radio Free Europe and The Voice of America began playing Gordy's records, his empire penetrated the Iron Curtain and truly became an international force.

Success, Gordy explains to this day, starts with a dream. "That's what's wrong with people," Gordy said when he started Motown. "They give up their dreams too soon. I'm never going to give up mine." And because he didn't give up, black Americans have more opportunities today and American music has changed forever.

Throughout much of American history, black entrepreneurs and innovators have been objects of discrimination. But, as the stories of Elijah McCoy and Berry Gordy suggest, the remedy for discrimination in the past is not reverse discrimination in the present, but the freedom to invent, create, and produce in a free market. □

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THE FREEMAN
Ideas On Liberty

Sudden Impact: The Collision of Ethics and Air Bag Mandates

by Loren E. Lomasky

A John Elway forward pass travels toward its receiver at over 70 miles per hour; Randy Johnson's fastball darts from his hand at over 90 miles per hour; Pete Sampras's serve booms across the net at 120 miles per hour. Unless you know how to play the game, you're advised to stay safely away. But should you find yourself in even a minor fender-bender, you may be on the receiving end of an air bag deploying at up to 200 miles per hour.

For most people most of the time, impact with an air bag is benign compared to what they would have hurtled against had they been traveling unprotected. Although the air bag affords less protection than the seat belt, the air bag is, on balance, a wonderful safeguard. Since 1990 over 3,500 lives have been saved and numerous injuries averted, the National Highway Transportation Safety Administration says.

But the air bag's benefactions do not come free of cost. Although deployment usually produces nothing worse than soon-healed bruises, a significant minority fares worse: over 120 people have been killed by air bag impact, almost always in low-speed accidents from which they otherwise would have walked away.

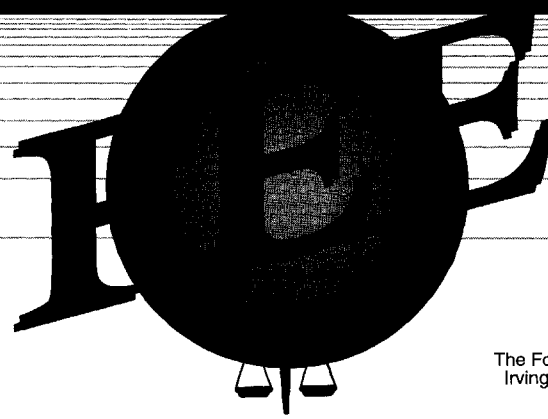
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Any fatality is cause for regret of course, but realism compels us to acknowledge that few valuable interventions come altogether without cost. People die on operating tables during routine surgery, drown while enjoying an invigorating swim, get hit by lightning while out on a golf course. We can and should try to minimize the occurrence of such tragic outcomes, but as Milton Friedman famously observes, there is no such thing as a free lunch. Air bags save on the order of 30 lives for each one lost. It would seem on first blush that this lopsided ratio is an eloquent testimonial to the regulatory regime that mandated them in all new vehicles. Few public safety measures, we might say, can claim so enviable a record of success.

Identifiable Victims

Complicating the appraisal, however, is the fact that air bag fatalities do not occur at random. Most victims of air bags are children (66 of the fatalities since 1990), typically infants or toddlers traveling in the front seat either unbuckled or strapped into child carriers. The air bag is most forceful as it leaves the dashboard, and carriers, especially backwards-facing ones for infants, bring their occupants closer to the point of explosion. Already vulnerable because of their small size, being in a forward location heightens their risk. Otherwise innocuous collisions produce crushed skulls, even a reported decapitation in an Idaho parking lot. Also at considerable risk

NOTES FROM



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January 1999

The Grateful Pedestrian

Yesterday evening I drove to a nearby restaurant. On my way I passed several strolling pedestrians. *I did not kill a single one!*

Please note that I possessed near-absolute ability to do so. A quick and easy flick of my wrist on the steering wheel at almost any time on my drive would have meant certain death for numerous pedestrians. But I refrained from running them over.

******

The above account is true.

Suppose now that you were one of these pedestrians and I solicit from you expressions of gratitude for my not running you over. How would you react? Not only would you be indignant at my solicitation, you'd think me to be demented. And properly so. I would be insanely brazen to seek your gratitude for my not bulldozing you with my car.

And yet politicians routinely seek—and receive—praise for actions that differ in no fundamental way from the actions of drivers who avoid running down innocent pedestrians.

We are bombarded by news reports and campaign ads boasting of how this president or that governor "created" so-many-million new jobs or is responsible for whatever amount of economic growth has occurred during his or her term of office. Such claims are preposterous. They are on a moral and intellectual par with my claim that I deserve credit for not killing pedestrians with my car.

No politician creates jobs or prosperity. Jobs and prosperity are created by entrepreneurs and business firms whenever the economy is sufficiently free of government meddling. For government to avoid meddling—that is, for government to keep taxes low and to steer clear of regulating voluntary exchange—is indeed desirable. But to avoid interfering with voluntary exchange is not at all actually to create whatever jobs and prosperity emerge from voluntary exchange. To insist otherwise would be no different from my insisting that I, as a driver who did not run over Ms. Jones as she walked back from the supermarket, am responsible for the tasty dinner she cooked that evening for her family.

If a car is careening out of control onto a pedestrian walkway, anyone who leaps into the car to stop it is a genuine hero. This person *does* deserve applause and gratitude (while, incidentally, the persons who either intentionally or carelessly caused the car to be out of control deserve condemnation and, perhaps, jail time). But even this hero does not take credit for all that is created and produced by those who would have otherwise been killed.

Whenever that rarest of creatures—an honorable elected official—actually manages to loosen some part of government's grip on us, that person merits bona fide acclaim. Even he, however, doesn't deserve credit for whatever economic growth and cultural flourishing follow. Such credit properly belongs to the countless people who create, innovate, take risks, save, and work hard to produce what consumers want.

The idea that government deserves credit for all of the benefits produced by freedom is a special case of the pernicious deification of government. When deified, government is mistakenly seen as responsible for all that happens in society.

A distressingly large number of writers contend that what looks like government's refusal to intervene is really just a different form of government intervention. I offer here only two examples. One is left-wing economist Warren Samuels who, in a 1995 issue of *Critical Review*, wrote that deregulation is simply government regulation carried out by enforcing private property rights rather than by enforcing bureaucratic edicts. When the economy is deregulated, what Samuels sees is that "[o]ne system or structure of (nominally private) coercive power is substituted for another by the very institution, government, which helped establish and/or reinforce the first one." According to Samuels, only the unsophisticated believe that when government deregulates it thereby reduces its sway over the economy.

This view isn't confined to left-wingers. Louis Hacker, in an otherwise fine essay appearing in F. A. Hayek's edited volume *Capitalism and the Historians*, insists that "the idea of laissez faire is a fiction. For the state, by negative action—that is, by refusing to adopt certain policies—can affect economic events just as significantly as when intervention occurs." Well, yes—in the same way that I, by not running my car over pedestrians, can affect events just as significantly as if I *do* kill pedestrians.

Only in the most base materialist sense are Samuels and Hacker correct: insofar as government possesses power to restrict commerce and suffocate industry with its regulations, any self-restraint by government in its zeal to regulate can be said to "affect economic events." But such sophistry sneakily erects as the benchmark for evaluating government activity the maximum possible destruction that government could possibly inflict. If the actual amount of destruction caused by government falls short of what government *could* have caused, then government is credited with producing all that it refrained from destroying. Using such a benchmark is lunacy.

The Soviet military *could* have annihilated the United States population with an atomic attack at almost any time during the cold war. Should we then credit the Soviet military for our current prosperity and our very lives? Does it really make sense to speak of the Soviet military as having "affected economic events" by not launching a nuclear strike against America? If so, then why not also credit the decision by the British military not to launch a nuclear attack against us as a cause of our prosperity?

Refraining from interfering in other people's affairs is simply the right thing for everyone, including government, to do. Our praise is properly reserved for people who heroically help others whom they have no duty to help, while our condemnation is properly reserved for people who intrude uninvited into others' lives. (By the way, to heroically help another person is to do so voluntarily and with your own resources and effort. You're no hero if you are coerced into giving aid to another; you're a slave. Likewise, you're no hero if you coercively confiscate the resources or efforts of third parties to help others; you're a thug.)

Until someone convinces me that I deserve a ticker-tape parade every time that I don't run down a pedestrian with my car, I will find intolerable the misbegotten gratitude and applause that politicians receive for not destroying even more of our liberties and wealth than they currently ravage.



Donald J. Boudreaux
President

January Book Sale

Henry Hazlitt was uniquely gifted and uniquely generous. His intellectual gifts are clearly evident in his many newspaper columns and magazine articles — and in his books. Much like Frederic Bastiat, the great 19th-century French journalist, Hazlitt had a special talent for explaining economic principles in an easy-to-understand and informative style. But Hazlitt should be remembered for his generosity also. A member of FEE's Board of Trustees from 1946 until his death in 1993, Hazlitt bequeathed both his personal library and a portion of his estate to the Foundation. He was a very special friend of FEE, and a very special friend of freedom. This month, we recommend Hazlitt's fine works for your consideration.

The Conquest of Poverty — "The history of poverty is almost the history of mankind." The key word in the sentence is "almost." Thanks to capitalism, poverty isn't the whole story of humankind. What this book does is to demonstrate the incredible capacity of free markets and free people to overcome the affiliction of want. Hazlitt unearths historical examples of poverty programs, debunks myths of the welfare state, and talks about why socialism just won't work. He ends with a refreshingly direct suggestion for curing poverty: "[b]asically each individual — or at least each family — must solve its own problem of poverty." Individuals acting responsibly within a market economy — this is the secret to ending human want.

Paper, 240 pages $16.95 **Sale: $7.00**

The Failure of the "New Economics" — Think Keynesianism is dead? Think again — Asian nations outlaw "dangerous speculation" while American steel manufacturers take out full-page ads calling for mercantilist policies. Sadly, the ghost of Keynes lives. Keynes's magnum opus, *General Theory of Employment, Interest and Money*, is thoroughly analyzed and, well, destroyed in this insightful and prescient book. Hazlitt exposes the many confusions in Keynes's work and dissects Keynesian theories of consumption, interest, and capital. Arguing throughout that no important doctrines in *General Theory* are both true and original, Hazlitt does a masterful job of knocking Keynes off his pedestal. Excellent ammunition to counter the intellectually challenged proponents of the welfare state.

Paper, 458 pages $ 16.95 **Sale: $7.00**

The Critics of Keynesian Economics — Another of Hazlitt's provocative excursions into macroeconomic theory. This edited volume collects twenty-two essays that take the ideas of Keynesian economics to task. Among the writers represented in this work: Frank Knight, F.A. Hayek, L. Albert Hahn, Ludwig von Mises, and W.H. Hutt. Hazlitt also provides readers with Say's Law (which Keynes refuted) and John Stuart Mill on consumption. This anthology is a most helpful research tool and resource for advocates of limited government and free markets.

Cloth, 427 pages $24.95 **Sale: $7.00**

The Wisdom of Henry Hazlitt — This unique collection includes tributes to Hazlitt from Mises as well as FEE Trustees Bettina Bien Greaves and Edmund Opitz. The book captures Hazlitt's insights about the marvels of free markets, the problems of poverty and how these problems are exacerbated by welfare-state policies, and the need to remain vigilant in the defense of individual liberty and voluntary exchange. This engaging grouping of Hazlitt articles provides an excellent introduction to Hazlitt's philosophy.

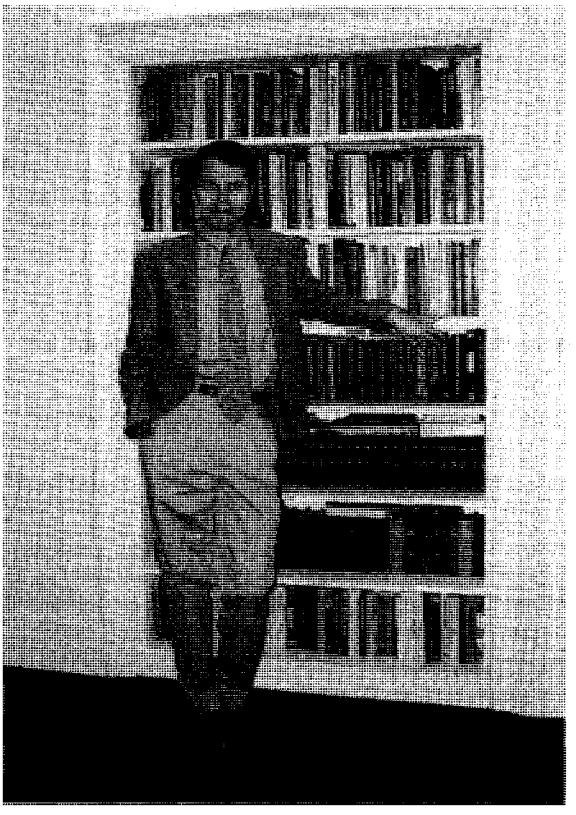
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A Special Message from the President

Help FEE Meet the Challenge . . .

A rare opportunity for your support to multiply!



In November it was my privilege to announce that FEE had received a major new challenge grant from two anonymous contributors.

If FEE raises $150,000 in new money (gifts received and deposited by March 31, 1999), these supporters will give FEE an additional $100,000.

Put another way, if we meet this challenge every three dollars you help us to raise will yield an additional two dollars!

"New money" is any money from people who have never before given to FEE, as well as contributions by existing donors above the level of their last contribution.

With your help, we can meet this challenge and do more than ever to bring liberty to life in 1999.

Don Boudreaux

Donald J. Boudreaux
President

Contributions can be made by telephoning (800) 452-3518 and using your Visa, MasterCard, American Express, or Discover Card, or by using the reply envelope included in this issue. For those who have recently contributed, a heartfelt thanks from the entire FEE staff and Board of Trustees.

are the very old, the very frail, and short drivers who seat themselves close to the steering column. For them the air bag is not a friendly bodyguard but potentially a weapon that maims and kills.

By requiring manufacturers to install air bags in all new cars, the federal government is, then, not simply mandating a policy that confers substantial benefits on the population at large, albeit tempered by occasional harms. Rather, governmental policy deliberately and knowingly enhances the safety of one identifiable group of citizens at the expense of another. It literally has redistributed expected life years between these two classes.

Last fall, the government sought to address this problem in its characteristic way. Instead of permitting freedom of choice so people can select safety features tailored to their own circumstances, it proposed fine-tuning the rules to take into account that small and unbelted bodies may be in the seats. The auto industry fears the newly mandated air bags will be as dangerous as the first generation of bags that threatened children and small, frail adults. Even if this attempt at central planning of technology works, it won't take effect until 2006. (Earlier, the government tried to address the danger by allowing qualifying citizens to have a disabling switch installed.)

Some observers find troubling all governmental edicts designed to protect people against themselves, to force them "for their own good" to act in ways they less prefer or that attempt to engineer compliance by subsidizing officially approved behavior and laying taxes and other penalties on that which is disapproved. For one who takes the free society seriously, this sort of governmental paternalism is odious. I confess I am troubled by these incursions on individual choice. If people wish to drive around in their cars unbelted or dispense with helmets while motorcycling, choose to smoke cigarettes or consume slabs of marbled beef followed by gooey chocolate desserts, I may regard their decisions as imprudent. But if those engaging in these behaviors are competent adults I do not see that I—or anyone—enjoys the prerogative of constraining them to do otherwise.

One need not be a dyed-in-the-wool opponent of paternal government to be disturbed by regulations that protect us from ourselves. That's because they contravene broadly shared moral principles that address the acceptability of forced tradeoffs across persons and that govern the relationship between a liberal government and its citizens.

Ends in Themselves

There is no more fundamental principle of ethics than the proposition that human beings are special. Each person manifests a uniqueness that confers a dignity that no mere thing possesses. They are not interchangeable components of a social whole who may be plugged in and plugged out like chips in a computer. In the Western tradition of moral reflection, this understanding has been expressed in many forms. One is the theory of basic human rights that establish zones of limited sovereignty within which individuals may act without interference so long as they respect the similar liberty of others. Another is the traditional natural-law doctrine which insists that no otherwise good state of affairs can be pursued if doing so requires acting with injustice toward another human being. Yet another version is the Hippocratic Oath's insistence, "First, do no harm." But this moral insight was perhaps best expressed by the German philosopher Immanuel Kant when he insisted that human beings, whether oneself or another, are not to be used as mere means for someone's projects but rather must always be treated as *ends in themselves*. Although it is not altogether certain what this dictum comes to, there are clear cases of its application to which there is general assent. They spotlight what is morally distinctive about persons. Let me offer a few simple examples.

Although it is entirely reasonable to take apart one auto to salvage parts that will restore five other vehicles to operability, it is strictly impermissible to mine one healthy person's body for organs that could be transplanted to save five other individuals. Similarly, it is unacceptable to frame an innocent person in a kangaroo court so as to mollify the mob milling ominously about. Fraud and deceit evince a willingness to manipulate the

beliefs and desires of others so as to render them instruments for one's own designs; assault and rape run roughshod over the essential embodiedness of persons; theft is the action of treating someone as a resource one may freely plunder for one's own ends; murder is literally the obliteration of personhood. Using others as mere means achieves its most fully developed institutional form in the practice of slavery.

It seems hard to avoid the conclusion that insofar as current air bag policy knowingly advances the life prospects of one group of citizens at the expense of another, it violates this most fundamental of moral precepts. It also puts in jeopardy the bedrock principle of liberal democratic government, *political neutrality*. Briefly, this is the requirement that the state not take sides concerning the projects and pursuits of its citizens. Individuals acting in their private capacity are free, of course, to be passionately partisan with regard to their religious creeds, ideological convictions, aesthetic tastes, and conceptions of the good life; the state, though, is not permitted to anoint winners and losers in these disputations. Rather, its role is to be the fair and impartial enforcer of the rules under which individuals operate, an umpire rather than a player in the game.

If air bags were options that car buyers could select if they desired, but forgo if their individual circumstances so dictated, then no class of individuals would be forced to be the unwitting instruments of others' ends; the government would not be acting with partiality toward some at the expense of others. Note that even those who qualify for the disabling switch are nevertheless financially penalized by the mandate. Do we really believe it acceptable for the government to penalize those who wish to safeguard the health and lives of their loved ones?

Protection for the Imprudent

As noted at the outset, air bags burst out at speeds of up to 200 miles per hour. If they were less forceful they would still adequately protect motorists who are belted in, but those who neglect to use seat belts will sometimes suffer injuries that high-speed air bag deployment could have obviated. There is, then, a tradeoff implicit in the regulation as it stands: it affords greater protection to the lazy and imprudent at the expense of babies and others. Make no mistake about it; there is nothing in the technology that renders this tradeoff unavoidable, and the government says it's now interested in air bags with adjustable deployment speeds. But today's dangerous air bag was deliberately engineered through governmental mandates.

If all air bags could be disabled via a standard switch, then foolish or unwise drivers might forgo protection that they would be better off having. To protect them against themselves, parents are impeded in their efforts to better protect their children. Can anyone reasonably deny that these examples of regulatory partiality are morally bizarre?

One response that the National Highway Traffic Safety Administration has offered in the wake of revelations about air bag injuries and fatalities is that children under 13 should not, whether in car seats or otherwise, be placed in the front seat. The intended implication is that children are not so much the victims of air bags as they are of parental malfeasance.

The point is, to an extent, well taken. To assign credit or blame to regulators does not absolve parents of responsibility. However, this response hardly gets the regulators off the moral hook. First, it does not address the issue of other vulnerable populations such as short drivers and the elderly. Second, it sometimes is impossible or impracticable to place all child passengers in the back seat. And third, it is in tension with a regulatory structure that is predicated on the assumption that individuals are not competent enough to be left to make their own choices. At the very least, then, it is a piece of bad faith to downplay the enormity of the human costs air bags impose by protesting that they would be lower if people were generally more provident.

Unrealistic Demand?

What will the regulators say in defense of their position? They might argue that to impose on social policy the condition that it

produce only winners and no losers is unrealistically idealistic, indeed unworldly. Virtually nothing could traverse so high a barrier. For example, polio vaccination has mostly eliminated in this country what was once a deadly scourge. Yet each year some individuals come down with polio, in almost every instance from the vaccine itself. Should we allow the return of polio epidemics rather than accede to these very occasional instances of harm due to inoculation?

That objection misfires because the analogy on which it rests breaks down. To be sure, some individuals who are vaccinated would have been better off had they not received the vaccine. However, we cannot tell in advance which ones they are. For each person getting the vaccine, the ex ante probability of a polio-free life is augmented. Probabilities are not certainties, so ex post some will find that they have pulled the short straw and are worse off. That's too bad for those who lose, but it does not falsify the proposition that for all players it was a good bet to take.

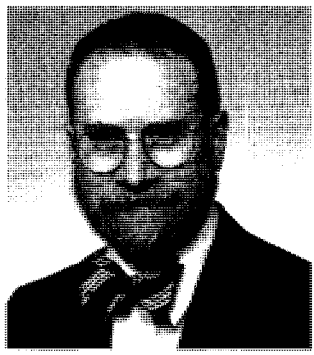
Such is not the case, however, with air bags. Babies and small adults are placed in jeopardy so that those older and larger can be afforded greater protection. The regulators know this now, and the record indicates that they knew it back in the late '70s when air bag regulations were initially being promulgated. So a closer analogy would be to a world in which vaccine is produced by knowingly and deliberately inflicting some with full-blown polio so that their tissues can be harvested and used to confer immunity on others. Would we regard that as acceptable social policy?

Regulation's Opportunity Costs

There are numerous other grounds for questioning the federal government's air bag mandates. Insistence on universal employment of this one safety device precludes experimentation that might generate better alternative safety measures. If cars are made more expensive by the requirement that they carry air bags, then car owners will have less money available to spend on other safety-enhancing measures. (The new generation of bags might add as much as $160 to the car's price.) For example, they may not be able to afford to get their vehicles serviced as often as they otherwise could. Perhaps they will be forced to drive around longer in older, relatively unsafe automobiles rather than purchase newer, relatively safe ones. Or with the money freed up by not purchasing an air bag, consumers could purchase larger vehicles that better withstand crashes. (At least they could if the government did not discourage manufacture of big cars that burn more gas than little cars. This is yet another irony transfixed like a hapless fly in the regulatory web.) It is also the case that individuals differ in the strength of their needs and desires for enhanced safety. Someone who drives defensively and who routinely uses his seat and shoulder belts may quite reasonably judge that the increment of safety afforded at the margin by an air bag does not justify its cost.

These grounds for opposing mandatory air bags commonly pop up in the policy debate. Each is essentially based on an economic way of thinking that bids us to be aware not only of the benefits that we procure through our expenditures but also their associated costs. In calling these reasons economic I do not mean thereby to disparage them. To the contrary: such efficiency considerations are central to rational policy-making. However, they often spawn a response to the effect that issues of public safety transcend dollars-and-cents calculations. Life is too precious, it will be said, to be stuffed into Procrustean cost-benefit computations; morality ought to trump mere monetary considerations.

I could not agree more. This discussion has insisted that morality does indeed matter. It has, however, seriously called into question whether federal bureaucrats and so-called consumer advocates genuinely do occupy the moral high ground. The fact that air bags on balance save lives does not necessarily secure for them this position. There are other criteria that must be met, criteria such as treating individuals as ends in themselves and not bending the technology of governance to the service of some classes of citizens at the expense of others. It is simply unacceptable to save lives by knowingly forfeiting others. □



The Art of Plunder

When the *Washington Post* recently honored Sidney Yates, 89, on the occasion of his retirement, the headline emphasized that he "Made His Mark on the Arts."

Is Sidney Yates a composer? Musician? Painter? Poet? Writer?

None of the above.

He was a congressman.

Don't laugh. In Washington, you can make your mark on the arts by chairing the subcommittee that oversees appropriations for the national endowments of the arts and humanities. From that vantage point, Yates, as he himself modestly put it, "help[ed] the arts and the humanities be the pride of the country."

After 24 terms in the U.S. House of Representatives (no advocate of term limits he!), the Illinois Democrat gave up his office. His retirement was taken as a blow to American culture because he has been, according to the *Post*, such a "fierce defender of the arts." His claim to that title lies in his unflagging belief that the taxpayers should be forced to finance artistic activity—and jailed if they refuse. (Okay, the second part is never pronounced in polite company; but we all know the score.)

For Yates, the greatest threat to American art came in the 1980s when Republicans talked about cutting the funding of the endowments. There were even murmurs of abolition. "Talked" is the operative word here. They didn't *do* anything. (A treatise on Republican dismantling of the welfare state would be titled *Human Inaction*.) The jeopardy to the endowments subsided largely because wealthy old-line Republicans feared losing the prestige they get from sitting on boards of symphony orchestras and community cultural organizations that receive federal grants.

In the silly world of Washington, if you favor forcing the taxpayers to finance artists (including those whom they find repulsive), you are a champion of the arts. If you oppose compulsion, you are an enemy of the arts, not to mention of free speech and all other forms of civilization. By any objective standard, that is of course nonsense. What do tax subsidies have to do with the artistic vitality of the American people? As for freedom of speech, forcing people to finance expression that they wouldn't voluntarily support surely violates the First Amendment.

To hear the inside-the-beltway crowd tell it, you'd think that before the endowments were set up in the mid-1960s, America was a cultural tundra. It takes prodigious oversight to believe that. You'd have ignore such innovations as jazz, the Broadway musical, modern dance, rhythm and blues, rock and roll, bluegrass, several schools of painting, and lots of fiction and poetry. Somehow, the originators of those minor contributions managed to get along without state beneficence. Many art forms that are today considered mainstream were so on the edge in their early days that the arts bureaucrats probably wouldn't have lowered their noses long enough to notice them. Have government subsidies produced anything approaching the greatness of the unsubsidized American arts and letters? Besides,

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Sheldon Richman is editor of The Freeman.

"performance art," the delight of lovers of chocolate and gore everywhere, it is hard to think of anything.

Great and good art doesn't need help from the government. (Even a lot of bad art thrives without subsidy.) The freedom of citizens *not* to support art is not only consistent with cultural vitality, it is the key to it. How odd that the so-called champions of the arts have so little confidence that they would flourish if the taxpayers were not harnessed in their service.

Those champions are caught in their own hopeless contradiction, however: while they insist that without taxpayer support America would turn philistine, they simultaneously insist that the amount government spends is minuscule, surely too little for the troglodytes to furrow their eyebrow ridges over. Truth to tell, taxpayer support is a tiny percentage of the federal budget. But in a $1.7 tee-rillion budget, that's true of lots of things. The subsidies are also a small percentage of what Americans spend privately on the arts.

So why the fuss?

To begin with, there is the little matter of principle. Imagine if someone proposed a small subsidy to religious institutions—no more than 64 cents per man, woman, and child—the price of two stamps before the latest postal increase. Would the quasi-socialists who are mistaken for liberals accept the argument that the amount of the subsidy is too small to bother about? One suspects that they would invoke the principle of church-state separation regardless of the paucity of the alms. When it comes to *their* pet projects, a similar commitment to principle is scorned. As Mayor Daley once said, there are times when it is necessary to rise above principle.

The endowments' backers resolve the aforementioned contradiction by pointing out that the money provides leverage to summon forth big private donations. It's the multiplier effect. The prestige of taxpayer largess apparently so impresses arts patrons, they can't help but write checks. If so, that's an excellent reason to abolish the endowments with dispatch. If bureaucrats are able to channel not just taxpayer money but also private benefactions to their favorite artistic causes, that is more power than a free society should tolerate. Of all places, the United States should not be proud that the government aspires to pick cultural winners. You'd think that people who were regarded as competent to pick their political officeholders would also be able to allocate their own income when it comes to the arts.

What the advocates of subsidy don't appreciate is that culture, like language, is a spontaneous and undesigned institution. No central planner is required or desirable. Government subsidy designed to nudge private patrons in one direction or another is a step toward centralization that arts lovers should deplore. The color of government is mediocrity; why would we want it anywhere near the arts?

Throughout history the arts have flourished when artists were at liberty to offer their products to the broad or narrow market of their choosing and when art consumers were at liberty to accept or reject those products.

Artistic freedom is for both buyer and producer. The endowments must go. □

THE FREEMAN
Ideas On Liberty

Libertarianism in Japan

by David Boaz

The publication of a primer on libertarianism in Japan is another sign of two heartening developments: the continuing process of the world's people being drawn closer together, and the worldwide spread of the ideas of peace and freedom at the end of a century of war and statism.

Americans, and especially American libertarians, find much to admire in the Japanese people: their strong families, their commitment to education, their strong sense of individual responsibility, their peaceful and democratic society, and their productive entrepreneurship that has given the world so much material progress over the past 50 years. The Japanese can take much pride in their economic success, and they certainly don't deserve the criticism they have received from protectionists in the United States and Europe who don't want to compete in a global economy.

But recent economic problems in Japan and its Asian neighbors indicate that there are problems with the region's economic policies. An economy largely based on private property, individual initiative, and free markets has been hampered by too much state allocation of capital and too much of what Americans call "crony capitalism." These policy mistakes have led to the need for currency reform (mostly in Asian countries other than Japan) and deregulation of financial services. Also, Japanese consumers have not always reaped the benefits of economic growth, and deregulation of retailing—particularly a repeal of the laws that impede the opening of large discount stores—might allow them to achieve standards of living commensurate with their productivity. But none of this should obscure the real achievement of the Japanese in dramatically increasing their living standard in scarcely a generation through productive enterprise in a system based on low taxes, free trade, and the rule of law.

The libertarian philosophy has much to offer Japan as we move into a global millennium. But an obvious question may occur to Japanese readers: Are these just American ideas, or at most Western ideas? Do they have any relevance to the people of Japan and Asia?

Universal Values

Some Asian leaders have criticized liberalism and proposed "Asian values" as an alternative. Singapore's leader, Lee Kuan Yew, has said that his country does not "need the kind of free-for-all libertarianism that we see in America." But the values of individual rights, limited government, and free markets are universal values. The principles of science are universal, even though so much of the discovery of those scientific principles took place in the West. No one would argue today that mathematics and physics are "Western" ideas or that Asians cannot participate in the scien-

David Boaz is executive vice president of the Cato Institute. This is adapted from the preface for the Japanese edition of his book Libertarianism: A Primer.

tific enterprise. Liberalism, now known as libertarianism, developed in the West, but it speaks to all people.

But Westerners steeped in the ideas of John Locke and Adam Smith can learn much from Asians who study the traditions of Confucius and Lao-Tzu. Lao-Tzu, who wrote that "without law or compulsion, men would dwell in harmony" and who taught that harmony can emerge from competition, may well have been the world's first libertarian. A similar concept can be found in Zen.

Today the Asian emphasis on strong families and personal responsibility fits better with libertarian political philosophy than does the unfortunate trend in Europe and the United States toward personal irresponsibility, a sense of entitlement, and reliance on the state. Indeed, Japan and America have more to learn from each other than either of us has to learn from the failing welfare states of Europe or the statist model of France.

Libertarianism is sometimes perceived as a radical philosophy, even in its American home. But in fact it is the fundamental philosophy of the modern world: liberty, equality, enterprise, the rule of law, constitutional government. These ideas have become so commonplace that we forget how radical they were at one time. Libertarians want to apply those principles more consistently than do the adherents of other ideologies. But few people in the modern world would want to reject libertarian ideas wholesale.

Liberalize to Prosper

The largest trends in the world reflect libertarian values. Communism is virtually gone, and few people still defend state socialism. Eastern Europe is struggling to achieve societies based on property rights, markets, and the rule of law. Honest observers throughout the developed world understand that the middle-class welfare states are unsustainable and will have to be radically reformed. The information revolution is empowering individuals and small groups and undermining the authority of centralized power.

Perhaps most importantly, the increasing globalization of the world economy means that countries that want to prosper will have to adopt a decentralized, deregulated, market-oriented economic model. You can't avoid world markets in the 21st century; or if you do, you will be left out of the phenomenal economic growth that global markets and technological development will deliver.

So one reason that Japanese readers should be interested in libertarianism is very simple and practical: these are the ideas that drive the modern world, and you need to know about them. The other reason is that libertarianism offers to every country the promise of peace, economic growth, and social harmony. I hope Japanese readers will join American libertarians in working to restrain state power and liberate individuals, families, associations, and enterprises. □

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THE FREEMAN
Ideas On Liberty

Can Government Deliver the Goods?

by Hugh Macaulay

Students in their first course in economics learn that every country faces three problems that it must resolve. What goods will be produced? How will it produce these goods? And, who will get the goods produced? Since the questions deal with economic matters, it is usually assumed that markets will determine the answers. But political forces in government can also provide results.

Milton Friedman has observed that every country answers some aspects of each question through market forces and other aspects through the political system. The proportions vary greatly from country to country. At one extreme would be the old Soviet Union and the People's Republic of China under Mao Zedong. At the other extreme would be the British colony of Hong Kong and the United States before the Great Depression. In between are all shades. Cuba, Sweden, Germany, the United Kingdom, the United States today, Chile, and Taiwan lie along the line moving from more government control to more market control.

What can we say about these two systems for answering the above questions? Each system must have some advantages, for each is used, though in widely varying proportions. The close relation is shown by the early reference to economics as "political economy."

To examine the results we can expect from using each of these systems, we will first look at some broad, general forces that operate in each system. Then we will use the fundamental principles of demand and supply to predict outcomes and evaluate results. We hope that from these considerations, the strengths and weaknesses of each system will be apparent and each individual will be better able to make wiser choices in answering the basic questions cited above.

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Deciding with Votes Versus Deciding with Money

In 1959 Gary Becker, at that time a young professor at the University of Chicago and later a Nobel laureate in economics, compared the two ways of producing and allocating goods. He noted that a person could take his money, go into the market, and choose the goods he wished to obtain. That action would determine what goods were produced, how they were produced, and who got them. Similarly, a person could take her vote, go to the polls, cast it for the politician who favors having government order the production of goods she liked, made the way she preferred, and distributed to the people she thought most deserving. The two systems seemed mirror images of each other. But are there features that make one superior to the other? Becker cited several areas where the two systems differ. We shall discuss three of them.

First, when a person votes for a representative, that person elected will serve for two, four, or six years and cannot be replaced until the term ends. A person may have voted for

Bill Clinton, who promised in 1992 to reduce taxes, but in the following year raised them markedly. But Mr. Clinton had three more years to serve and could not be removed for abandoning his tax-cut promise.

In a market, however, you may enter a Safeway grocery store, based on its promise of quality products, good service, or a large inventory. If Safeway fails to deliver to your satisfaction, you may fire it then and there. You need never patronize it again. Market goods can change rapidly. Government goods change slowly. Not only can the politician remain in office and with power after his services are no longer desired, but the bureaucrat who administers the laws usually has, in effect, a lifetime appointment. An example of a service tied to long tenure is the provision of justice. It should be swift and sure. Instead, it is interminably slow and often random. Federal judges have lifetime tenure. Improving the delivery of justice will take decades, if it can be done at all. Professional arbitrators, however, can be replaced swiftly and their services reflect this condition.

Second, *Consumer Reports* has long complained about the "bundling" of features on automobiles. In order to get the car with the color and power you want, you may have to buy other equipment that you do not want. The product should be "unbundled," says the magazine, so the consumer would receive and pay for only the features desired.

When the voter helps elect a mayor, senator, or other official, that officeholder will represent the voter on a large number of issues. The voter may like her congressman's position on the minimum wage, but vigorously oppose his position on most-favored-nation treatment for China. A congressman will represent his constituents on about a thousand pieces of legislation during his two-year term. Many constituents, even those who actively favored him, will support his position on some of these bills but strongly oppose him on others. The congressman is a bundled good, and the voter will be forced to pay for many results she does not want. Dwight Lee has used a Safeway grocery analogy: the consumer enters the store and is confronted with a full grocery cart containing some goods she wants and some she does not. Her choice is the cart or nothing. In government she must take the representative's bundle; she cannot choose nothing.

In markets, one is not forced to buy all goods from only one supplier. Sears or Wal-Mart will not be the single source of all goods for any consumer. You can vote for only one congressman who will provide you with thousands of rules affecting what is produced, how it is made, and who gets the goods, but in markets you can vote for hundreds, if not thousands, of suppliers of private goods. Even in the purchase of food, the consumer may buy bread at one store, meat at another, and vegetables at a third. In markets a consumer is seldom forced to pay for a good he does not want or that is produced in a way he does not like; in government purchases, he often is.

Rational Ignorance

A third difference between government and market provision of goods involves what economists call rational ignorance. This can be either costly or costless.

Because the Congress will take action on over a thousand bills during a given session, the typical voter cannot be informed on each and every bill. In fact, he will be completely ignorant about almost all of these bills. This does not imply a lack of interest in government, laziness, or an inability to understand the bills presented. Rather, the voter is rationally ignorant about these proposals, for he has his own life to lead, family to care for, job to pursue, church to attend, sports team to enjoy and support, and a thousand other things to occupy his time and attention. There is little left over to be spent on these peripheral political issues, many of which may not interest him. Further, even should he pause and study any issue and try to urge his representative to vote on it intelligently, his voice is likely to be lost among those of the thousands of others also affected. He will be ignorant of 99 percent of all items that come before the Congress, legislature, council, or district governing body, and rationally so. This ignorance is costly to him, but removing it is even more expensive. He is destined to be a loser

on most of these government-provided items.

In the typical voter's purchases and work in private markets, he will also be rationally ignorant about almost all products offered. But these will be products he will not purchase and will not pay for. Most of us are rationally ignorant about the features and cost of yachts, for example. The price system determines how they are produced, and we need not be concerned about others who spend their own money for this product, for we will not spend our money on it. This form of rational ignorance is not costly to the individual.

The late Mancur Olson was an early expositor of a fundamental rule of political action. Every law, rule, or regulation by government helps some group and imposes costs on others. A proposal is likely to become law if it concentrates the benefits in the hands of a few people so that each enjoys a sizable gain; at the same time it spreads the costs over a large population, so each loser bears only a small absolute expense. The gainers, then, have a strong incentive to support the proposal, while the losers have little reason to oppose it actively. They are better off remaining rationally ignorant, spending their time on matters more important to themselves. When government allocates resources, rational ignorance not only creates inefficiency, it also encourages small groups, often called special interests, to press for allocating more and more goods in this manner. In effect, inefficiency breeds even more inefficiency.

Many people think that the government should provide "public goods," so named because many people automatically benefit from them if any one person does. Examples are neighborhood attractiveness, fireworks displays, water quality, and radio broadcasts. Still, many economists argue that markets can provide these goods more efficiently than government can.

When we rely on government, even when democratically elected, to provide the goods we want, produced the way we want, and allocated to the people we want to receive them, we will get fewer of the goods we want, more of the goods we do not want, and will encourage the increased use of this inefficient system. Markets overcome these weaknesses.

Demand and Supply of Goods Under Each System

Economists turn to the concepts of demand and supply to make sense of the allocation of scarce goods. These powerful tools will help us examine our questions in a different light and give us significant insights.

We know that people want lots of units of many goods and services, but they cannot have all they want. The concept of demand tells us a person will take more of a good the less expensive it is and that he will demand each good until he gets about the same happiness from the last dollar he spends on the last unit of each good. If he buys a $20 shirt and a $2 pair of socks, he should get about ten times as much satisfaction from the new shirt as from the additional pair of socks. He is then getting about the same happiness from the last dollar spent on each of these goods.

When we answer our three questions using the concept of demand, we know each consumer will look at the many goods out there and their prices, and decide which goods will bring him the greatest happiness from the dollars he spends on them. He knows why he does not buy some goods he likes and why he does not buy more units of some of the goods he does purchase. The goods are not worth the price. By following these rules of demand, he will be as happy as is possible with his income.

When government produces or allocates goods, it usually provides them at a low or zero price. Schools, police protection, justice in the courts, clean air and water, Medicaid, occupational safety, and welfare payments are all seen as virtually free goods. Many other goods are subsidized, such as public transportation, public housing, and Medicare. When the price of a good is low, or even zero, consumers will want more of it than they would voluntarily have bought at its cost of production. Think how much more food, clothing, and shelter you would buy if they were 50 percent cheaper, or free.

As a consequence of government provision, too much of the good will be produced. That means we will have to give up other more valuable goods to get these less valuable units of the subsidized or free good. Production of government-provided goods will draw scarce resources away from the production of things people would have bought. Remember the fundamental economic rule: there is no free lunch, or even a cheap, subsidized, lunch. It just appears free or cheap. We give up beer, tires, and encyclopedias that are more valuable than what we get in cleaner air, higher SAT scores, or better housing for the poor. In fact, added expenditures on these last three items have often given us dirtier air, lower SAT scores, and fewer housing units for the poor. Federal laws requiring scrubbers on electric utility generating facilities also allowed the use of higher sulfur-content coal so that dirtier air resulted. Despite annual increases in real expenditures per student in recent years, the SAT scores fell throughout the 1970s and 1980s. The early urban renewal program displaced poor residents and built units that only middle-income residents could afford.

But when the government-provided goods do supply some benefit, even if small, we might think, "Well, at least the recipients will be happier." Strangely, they are far more likely to be dissatisfied with what they have received. First, the extra units of the good are not worth much to them. For example, there is far more dissatisfaction with "free," but actually expensive public schools than with cheaper private schools for which consumers pay directly. Similarly, "free" public highways are the subject of frequent complaints because of potholes and delays, while toll roads are seldom criticized. More money spent on either education or highways is likely to be even less productive than the earlier spending.

Second, recipients will be unhappy because government will not provide them with all the goods they are willing to buy at the low prices. People are more likely to be unhappy over receiving public housing and public transportation than over not getting expensive housing and Lincoln Town Cars. Price sends the wrong signal for the first two goods and the right signal for the latter two. Recall the widespread public dissatisfaction during the 1974 OPEC boycott when government set gasoline prices below market levels but could not provide all the gasoline people were willing to buy.

Government provision of goods generally creates wasteful consumption and consumer dissatisfaction, a doubly bad result. Market provision leaves consumers happy with what they got and a clear understanding of why they do not want more units that are not worth their cost.

The concept of supply tells economists that if demanders will pay a higher price for a good, more units will be produced. Further, this price must cover the cost of the land, labor, and capital needed to turn out these units. If demanders will not pay for the good, it will not be produced. Waste will be avoided. Firms that produce goods that people do not want will go bankrupt. This is how markets avoid wasteful activities.

Markets also promote efficiency. People who learn to provide a better or less expensive good make profits. We call them Ray Kroc or Bill Gates. Markets provide a strong incentive to supply only goods people want badly enough to pay their cost of production. The producers of government-provided goods, however, almost never face bankruptcy. The mail may be late, children may learn little in public schools, Medicare fraud may cost billions, job-training programs may leave participants worse off, but rarely are such programs declared a failure or abandoned. There are at least two features that help explain these supply results.

First, those who produce these failed products have little incentive to improve them. The person who produces a better oil-drill bit, Internet browser, or wash-and-wear fabric can make millions from the improvement. Incentives for government employees or administrators to improve government programs are almost nonexistent. No incentive, no improvement.

Second, the incentives facing government workers, in fact, encourage the production of bad products. Schools can get bigger budgets if their students are failing. The judiciary can

get more funds if its cases take longer. The police can increase funding if there is more crime in schools and on the streets. In terms of a supply curve, we are not getting more units of schooling provided at a higher price; we are shifting the supply curve for education upward and getting less education at the same price, or equal education at a higher price. This condition applies to almost all government-produced goods. Failure pays.

Government or Market

Governments can provide goods or markets can do the job. The two systems appear similar, but they are very different. The general problems of slow response of government because of political tenure, the bunching of decisions made by government officials, and costly rational ignorance by voters all argue for abandoning this inefficient system.

When government provides goods, people will demand too much of less valuable goods and become unhappy because they were not provided more and better products. Government agencies producing goods have little incentive to become efficient and significant incentives to turn out failed products. They also need not fear a prospect of bankruptcy or competition.

Markets, on the other hand, change quickly, allow for many producers, and do not burden those who are ignorant of goods they do not buy. Further, consumers will demand only those goods that benefit them most and suppliers will become efficient or go bankrupt. We often choose government as our preferred provider on the basis of emotion. If we can substitute understanding for emotion, we may become healthier and we will certainly become wealthier as we become wiser. □

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THE FREEMAN
Ideas On Liberty

Markets in Time: The Rise, Fall, and Revival of Swiss Watchmaking

by Anthony Young

For more than 300 years, watchmaking has been Switzerland's most identifiable industry. The country's geography and political non-involvement have permitted Swiss watchmakers to survive revolutions, wars, and depressions. Yet there was something the industry almost did not survive: technological change.

Swiss watchmaking grew out of clock making as the ability to make smaller mechanical movements evolved in the seventeenth century. Both innovation and craftsmanship flourished in the eighteenth century. Some firms established back then are still making watches today, including Blancpain (1735), Vacheron Constantin (1755), and Perrelet (1777). For every Blancpain or Perrelet, however, there are many smaller, lesser-known companies in Switzerland. Close to 500 companies in Switzerland manufacture watches, watch movements, and parts.

The mass production of the Industrial Revolution reduced costs, but there has always remained the cherished element of handwork in a Swiss watch. In 1793, Isaac and David Benguerel along with Julien and François Humbert-Droz established the first watch movement-blank factory in Fontainemelon, hard against the Neuchâtel mountains. (A movement-blank is an unfinished, but difficult-to-make watch movement.) This region of Switzerland became a magnet for the watch parts industry. Companies specializing in cylinder, pin lever, and jeweled-lever mechanical movements made possible the establishment of small watch companies that did not have to manufacture every part of the movement themselves.

The twentieth century has had the most profound effect on Swiss watch companies. Two world wars and the Depression in between reduced the demand for Swiss watches, but the industry always recovered. The postwar economies of the world eagerly sought Swiss pocket watches and wristwatches, from inexpensive mass-produced hand-wound watches to self-winding, or automatic movement, watches. By 1974, exports of Swiss mechanical watches and movements had risen to 84 million units.

In this euphoric and seemingly irreversible climate, a quiet revolution was brewing in Switzerland. It was a revolution mostly of its own making, and it would shake the Swiss watch industry to its very foundations.

The Quartz Revolution

Work on an electrical watch began in the 1950s. Development of both the electromechanical movement and the battery to

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power it had to progress concurrently. In 1954, Swiss engineer Max Hetzel developed an electronic wristwatch using an electrically charged tuning fork powered by a 1.35 volt battery. The tuning fork resonated at precisely 360 Hz and powered the hands of the watch through an electro-mechanical gear train. This watch went on to become the famous Accutron by Bulova, which was introduced to the market in 1960. It used a proprietary design that was not adopted by the watch industry. However, the Accutron was beaten to the market by the American-made Hamilton 500, which appeared in 1957; this was the first battery-driven watch in production.

In 1962, a research center, the Centre Electronique Horloger (CEH), was established in Neuchâtel to develop a Swiss-made quartz wristwatch. Why quartz? An electrically charged quartz crystal has the ability to achieve stunning accuracy in a watch mechanism. Research and development took five years, but the center succeeded in reducing the size of the components to fit into a watch case.

The Japanese, however, were also hard at work on an electronic watch and had the financial footing to conduct their own research and development of quartz technology. The Japanese were no strangers to watchmaking. Citizen and Seiko are much older companies than many realize. The first Japanese watch plant was built in Seikosha near Tokyo in 1892, at first making wall clocks. Pocket watches and wristwatches followed. An earthquake in Tokyo destroyed the Seikosha plant in 1923, but it was rebuilt. In 1924, this factory introduced the Seiko brand name. The Citizen Watch Company had its roots in the Shokosha Watch Research Laboratory founded in 1918. The Citizen name was adopted in 1930. All watches produced at these two companies were mechanical until the 1960s, when work was begun on an electronic watch.

The Swiss Neuchâtel Observatory, which was responsible for certifying mechanical watch chronometers for accuracy, held a competition in 1968. Swiss and Japanese watches competed. The Swiss entrants swept the first ten places and the CEH was awarded the Prix du Centenaire. As a result, Japan, with a long-range commitment to consumer electronic products, threw its industrial might behind quartz watch development and production. Seiko was the first company to bring an analog quartz watch to the market, the Seiko Quartz Astron, introduced in 1969. The Swiss, however, were not far behind. The Ebauches SA Beta 21 quartz watch appeared in 1970.

Swiss Slowdown

Swiss companies, steeped in the mechanical tradition, were slow to embrace quartz technology. Mechanical movements had proven their durability and reliability for centuries. This reluctance of the Swiss to adopt quartz technology initially cost them dearly. Exports of Swiss mechanical watches plummeted from 40 million in 1973 to only three million ten years later. While some Swiss watch companies did manufacture quartz watches, Japan and Hong Kong dominated the quartz segment and decimated the Swiss industry. Many small- to medium-sized watch companies in Switzerland closed their doors by the end of the 1970s. The number of workers in the industry plunged from nearly 90,000 in 1970 to 47,000 by 1980.

In 1979, the management of the Swiss ASUAG group (Société Générale de l'Horlogerie Suisse SA) embarked on an ambitious plan to produce its own inexpensive line of quartz watches to counter the Far East juggernaut. To produce an accurate, rugged, and water-resistant watch for less than 50 Swiss francs demanded a paradigm shift in thinking regarding materials, manufacturing, and marketing. The micro-molding of plastic parts, reduction in the number of parts in the quartz movement, and ultrasonic welding were but a few of the cutting-edge technologies applied to the program.

This revolutionary watch line, known as Swatch, was launched in March 1983. The inexpensive watch, offered in myriad styles and colors, took the consumer world by storm. In less than two years, more than 2.5 million Swatches were sold. The Swatch was a phenomenon that put Swiss watches back

on consumers' wrists. As the brand went from victory to victory and sales passed 10 million, it had a profound effect on the Swiss watch industry as a whole and the world's perception of the industry.

The technological fallout of the Swatch permitted the Swiss watch companies to market quartz watches in virtually all price ranges. But quartz was not necessarily the answer for every Swiss watch company. Many companies felt honor-bound by their tradition of making mechanical watches, while others were simply leery of quartz for the long term. As the quartz movement took hold among Swiss watchmakers, articles appeared in watch journals proclaiming that the end of the mechanical movement was in sight. Witnessing the dramatic decline of mechanical watches exported during the 1970s and early 1980s, some pundits stated it was inevitable the mechanical movement would go the way of the horse-drawn carriage. This worried many watch companies; demise of the product would entail scrapping millions of dollars in precision machine tools, investing in the new technology, and retraining a very skilled work force.

Oris—One Company's Response

One of the many watch companies facing the quartz/mechanical dilemma was Oris. Located in the picturesque town of Holstein southeast of Basel, this company had been making watches since 1904. Its founders, Paul Cattin and Georges Christian, chose Oris as the name of their company after a valley near Holstein; the word Oris was formed from the Celtic-Roman word *aurisa*, meaning river. In a crowded industry, Oris has more than a few innovations to its credit. In 1938 the company introduced the pointer calendar, with the days of the month running the circumference of the watch face and the day indicated by a needle-type hand; the seconds were shown on a small dial at six o'clock. During World War II, Oris produced watches with oversized winding crowns to permit Allied bomber crews to synchronize watches with gloves on in the bitter cold environment at 30,000 feet. In 1952, the company introduced a watch line with an automatic (self-winding) movement. Oris received full chronometer certification from the Neuchâtel Observatory in 1968 for its calibre 652 movement.

Oris had survived and prospered for more than half a century making mechanical watches. Nevertheless, it led electronic watch development on several fronts in the 1960s. It was in a small group of companies, including Rolex, that contracted with a Swiss state institute to research and develop an electronic watch. It also became a member of the ASUAG group.

Oris was one of the first Swiss companies to sell an LCD (liquid crystal display) watch and did so for a number of years until Casio virtually took over this market. It had vast experience with mechanical movements, having manufactured cylinder, pin and lever, and jeweled-lever mechanical watches. Its work force was skilled in the fabrication and assembly of such watches, and there was a certain romance to a mechanical movement. Moreover, quartz, while certainly accurate, had a problem mechanical watches didn't have: dead batteries. In most first-generation quartz watches, the batteries typically lasted only a year and obtaining a replacement could be difficult if not impossible in many places. Thus mechanical watches would remain in the Oris catalog. At the same time, the company did not want to ignore what could be a large market for quartz watches. The company took the prudent course of adding quartz watches to its line.

Oris was not convinced that the dire predictions of some industry observers regarding the mechanical watch would come true. The decision to manufacture watches with both types of movements was a cautious one, as Oris waited to see which way the winds would blow. Many watch companies embraced the quartz movement totally and never looked back. Other companies remained faithful to the mechanical movement. During the 1980s, Oris was part of the SMH group of watch companies, which included Omega, Tissot, Mido, and other brands. But Rolf Portmann, who had joined Oris during the 1950s and later steered the company through troubled

waters over the next three decades, orchestrated a management buyout, and Oris was once again an independent watch company.

The market for quartz watches became crowded in the 1980s. The Pacific Rim countries were churning out literally hundreds of millions of quartz watches a year, and many Swiss companies were making them. How could Oris distinguish itself in such a saturated market? The management concluded it was hard to convey through advertising that its watches were unique. So the company decided to focus all its design, manufacturing, and sales efforts on mechanical watches.

Oris chose to lure buyers by extolling the beauty and virtues inherent in the mechanical movement, which had always been the essence of watchmaking. Many Oris models are fitted with a glass back with a screw-down case to show off the handcrafted movement inside—a feature of many other mechanical watch companies. The company has published a series of booklets describing the history of timekeeping, Oris milestones, detailed descriptions of each step in the manufacture of an Oris watch, and a lexicon of the components and functions of the mechanical watch. In so doing, the company is linking itself to Switzerland's rich watchmaking past, building on its own successful history, and making it possible for the watch fancier to wear a piece of that history on his wrist. The company took what, at first, appeared to be a market liability and turned it into a market asset, proving it could compete with the high-tech quartz movement, no matter where it's made.

The Swiss Comeback

In looking at the history of Swiss watchmaking over the last 30 years, it's clear that if the industry had not responded to the electronic revolution that was coming, it would not be in the healthy state it is today. Initially, the



Swatch revolutionized Swiss watchmaking in the 1980s.

industry was slow to embrace quartz technology, but many companies eventually realized it was the key to their survival and to the industry as a whole. In 1997, Swiss production of finished watches was 33 million pieces, with 30 million being quartz analog, and the rest mechanical. This is a far cry from the glory days of the 1970s, but there is a silver lining. Over half the value of the more than 500 million watches sold worldwide (roughly 80 percent being made in Hong Kong and China) is generated by the Swiss watch industry, totaling more than eight billion Swiss francs. Interestingly, while mechanical watches account for only ten percent of annual Swiss production, they generate nearly half of that total. Even Swatch has introduced watches with mechanical automatic movements. On the face of each one of these watches are the two words that make them the most sought-after in the world: Swiss Made. □

Economics



Censoring Pleas for Help

Ask people if they favor government censorship and the response will be a nearly unanimous *no!* Yet if you ask the same people if they favor government price controls, the response will be much more mixed. Ask them if the government should control prices to prevent "price gouging" after natural disasters, and the response will be a nearly unanimous *yes!*

These responses reflect an unfortunate ignorance of how markets allow us to communicate with one another. Once market prices are recognized as a means of communication, we have another powerful way of understanding why government price controls, which I have discussed previously, are a particularly harmful form of censorship. And the harm is greatest in the times of natural disasters because the victims are desperate to communicate their need for help.

The communication permitted by market exchange and the resulting prices creates a remarkable degree of social cooperation. There are no better examples of the benefits of this communication and cooperation than natural disasters. The victims need not only the assistance of people outside the disaster area, but also the cooperation of one another if they are to recover as soon and completely as possible. Unfortunately, when natural disasters strike, governments are most likely to outlaw the price signals that make this cooperation possible—and to do so with the support of public opinion.

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After a natural disaster, prices generally increase sharply for labor, construction materials, electric generators, and a host of other products needed for recovery and comfort. The common explanation for these price increases is that unscrupulous suppliers are profiteering at the victims' expense. Suppliers may be profiting, but not at the expense of the victims. Those whose homes are damaged and lives disrupted are victims of the natural disaster, not of those who supply them with needed goods and services afterward. High prices are better explained as the best way for victims to communicate their need for help to those who are most able to provide it. High prices also insure that pleas for help will be met with a quick and effective response.

Sending Lumber to Miami

I heard an interesting example of such a response when I was giving a talk in Ohio in 1992, not long after Hurricane Andrew ripped through southern Florida. I had mentioned the storm and its aftermath to illustrate the importance of price communication, and a gentleman in the audience told a story about his son, a building contractor outside Cleveland who had started building the house he and his wife had dreamed of for years. The foundation had been laid and the lumber was being delivered as Andrew hit Miami. With the news of the disaster, he decided against using the lumber himself and (despite his wife's opposition) shipped it to Miami instead. Why? Because the news he found most compelling came in

the form of high prices for lumber, informing him that the demand for his lumber was greater in Miami than in Cleveland.

Was the Cleveland contractor an unscrupulous profiteer? Hardly. He did far more good for the victims of Hurricane Andrew than those who sat around expressing contempt for price "gougers." True, a few people helped the hurricane victims by sending supplies to Miami for free. Certainly these people should be commended. But their help was insignificant compared to the help given by suppliers from all over the country (indeed, the world) who responded to higher prices by providing more of the things Andrew's victims indicated (through higher prices) they most desperately needed.

Those who express contempt for people who sell products to natural-disaster victims at high prices should look closer to home for someone to criticize. Their criticism (born of economic ignorance) and the public opinion they inflame frequently provoke price controls, which muzzle those crying out for help. The Atlanta *Journal-Constitution* pointed out last April that Georgia has a "price gouging" law that forbids suppliers from charging "one penny more than they charged the day before the disaster struck." This law was favorably mentioned, with no hint of irony, in an article reporting that building contractors and construction supplies from several states had poured into Atlanta immediately after it suffered massive tornado damage. Can anyone seriously believe that this help would have poured in from far away if the "price gouging" law had been perfectly enforced, or that the help was not reduced by the enforcement that had occurred? (Penalties for price gouging in Georgia range from one to ten years in prison and fines of $5,000.)

The Electric Shaver

Victims of natural disasters need to communicate with one another also. Market prices are the only practical method. Everyone in the stricken area will value the products being made available, but people will want those products to go to those they believe can put them to the best use. Price controls prevent this from happening by censoring communication among victims.

A friend of mine who lived in Charleston, South Carolina, when Hurricane Hugo hit in 1989 saw firsthand the harm done by this censorship. Electricity was out for several days in my friend's area, and so lots of people were anxious to get gas-powered electric generators. Unfortunately, the local hardware store had only two and was unable to get more because of price controls. But there was another problem with the price controls—one that actually benefited my friend's family, though at great cost to others. Because his father was a good friend of the local hardware-store owner, he got one of the electric generators at the controlled price. The store owner couldn't legally sell the generator to anyone else at a higher price, so why not let his buddy have it? My friend's father was delighted because he could continue to shave with his electric shaver. Unfortunately, grocery stores in town required electricity desperately to prevent thousands of dollars' worth of food from spoiling. Without price controls, one of those stores would have offered a higher price for the generator, effectively communicating (on behalf of customers) that it had a more urgent use for it than my friend's father had. One person would have had to suffer the inconvenience of lathering up to shave, but hundreds of his neighbors would have persuaded him, through a high price for the generator, that their desire for fresh food should take precedence. Of course, without price controls, all the stores and my friend's father (had he still wanted one) would have quickly secured electric generators because they would have been able to communicate with suppliers outside the disaster area.

Natural disasters provide a particularly vivid example of the harm done by price controls. Unfortunately, governments do not need natural disasters to justify undermining social cooperation and destroying wealth by dictating prices. Governments have a long history of imposing price controls on a wide range of goods and services. And they will continue to do so until it becomes widely recognized that such controls are a particularly pernicious form of censorship. □

THE FREEMAN
Ideas On Liberty

Let's Pierce the Government Veil

by Karen Selick

ONTARIO, CANADA—Although multiple births are becoming almost commonplace in the 1990s, quintuplets were considered a miracle in 1934 when the Dionne sisters were born in a small northern Ontario town. Their father, a poor farmer with five other children in the family to feed, soon discovered that his five baby girls might bring in some extra income during those tough Depression times. He accepted an invitation to exhibit the girls at the World's Fair. Hastily, the province of Ontario stepped in and made the quintuplets wards of the province, ostensibly to protect them. They were taken away from their parents and deposited in a hospital-compound that was soon transformed into a virtual theme park called "Quintland."

Quintland became a tourist attraction, drawing millions of curious visitors who were permitted to gaze through one-way glass at the five little girls during three daily "showings" over nine-and-a-half years. The quints themselves earned unknown amounts through endorsements. A trust fund was set up for them. When they turned 21, it contained $800,000, which was paid out to them over the next 20 years.

In early 1998, at the age of 63, the three surviving quintuplets, now virtually destitute, alleged that their trust fund should have contained a lot more than the $800,000 they had received. They claimed that the trust had been mismanaged and that money had been pilfered. They demanded compensation from the province of Ontario.

The province denied any legal responsibility, but nevertheless offered to pay them a pension of $2,000 per month each for the rest of their lives. At a press conference, they rejected this offer with the words, "We want justice, not charity." One couldn't help admiring the spirit with which those words were uttered.

However, a few weeks later, the sisters accepted the province's offer of a $4 million lump sum, without seeming to realize that what they got was precisely what they wanted to avoid—charity, not justice. Or maybe something worse.

Justice would have consisted in identifying the individuals responsible for misappropriating their trust money and making those people pay compensation, either out of their ill-gotten gains or their other resources. Instead, the money will come out of the pockets of Ontario taxpayers.

Whose Responsibility?

Many of those now being asked to foot the bill hadn't even been born back in the days when the quints were being put on display or when their trust funds were being dissipated. Others were mere children themselves, too young to vote the government out of office even if they had been aware of the misdeeds taking place. Still others were residents of other provinces or foreign countries and did

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not immigrate to Ontario until later. Among those who resided in Ontario at the time, many had voted against the government then in power. Others, who may have voted for that government initially, would never have sanctioned such actions if it had been in their power to stop them later.

Add up all these segments of the taxpaying population and you will undoubtedly find that the overwhelming majority of the people who will now have to bear the burden of this compensation claim are innocent of even the tiniest share of blame for the offenses. Forcing them to pay will not be righting a wrong. It will just be shifting the wrong from one group of victims to another. But the new victims, the taxpayers, will be so numerous that the injury to each will be diffuse and easy to ignore.

The number of people claiming compensation for government misdeeds in recent years is astonishing. A search through the Canadian Press database reveals literally dozens of unrelated claims. Clearly, many Canadians have suffered physical, emotional, and financial injury at the hands of the state.

If they all receive compensation out of tax money, we'll witness the ludicrous spectacle of victims compensating other victims. Japanese Canadians who suffered internment and expropriation during World War II will be paying compensation to recipients of HIV- and hepatitis-tainted blood, who in turn will compensate David Milgaard for the years he spent in prison after his erroneous murder conviction. Milgaard will pay sexual assault victims at government reform schools, who will pay the victims of Alberta's eugenics laws (sterilized against their will on the mere suspicion of mental inferiority), who will reimburse the Chinese immigrants of the 1920s for the racist head-tax imposed on them, and so on ad infinitum. The same chain of injustice can be found of course in the United States.

Collective Blame

This absurdity has its roots in the acceptance of collective responsibility for misdeeds that were conceived and implemented, as all human action is, by specific individuals. The government is not "us." It is rather a tiny subset of individuals chosen from among us. These people are expected to know right from wrong. Their job is to enact and implement a system of laws that protects the rights of citizens. If they choose instead to exercise the coercive powers of government to violate the rights of citizens, it is they, not innocent bystanders, who should be held accountable—first, for not doing their jobs properly and second, for the harm they've caused.

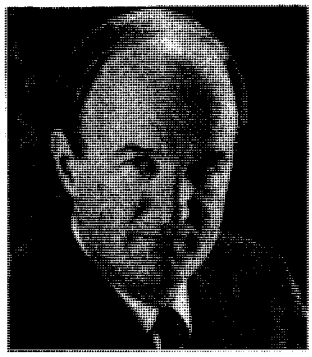
We've had it backwards for centuries. We've allowed successive bands of so-called statesmen to occupy our legislatures, inflict or at least preside over one injustice after another, and then walk away free of all responsibility for the damage they've done. Meanwhile, they bask in praise for having served society, pension checks swelling their bank balances. The worst that ever happens to them, no matter how badly they've harmed their country or their countrymen, is that they don't get re-elected.

It's about time we rethought this. Corporate law has been allowing us to "pierce the corporate veil" for years in order to hold corporate directors responsible for company actions. Why not pierce the government veil? Why not trace the financial liability for genuine government wrongdoing back to the individuals who actually formed the government at the time of the transgression?

If making politicians pay for their blunders would discourage people from seeking public office, or from doing much while in office, so much the better. This might be the shock treatment they need to make them realize they are there primarily as guardians of our liberty, not meddlers in our lives.

The easier we make it for people to collect compensation by taking it out of the common pot so that the new victims won't notice, the more such claims we will encourage. The more we discourage individual responsibility among our elected representatives and their employees by shifting the cost of their malfeasance to the taxpayers, the more such violations of rights we can expect to occur. □

THE FREEMAN
Ideas On Liberty
JANUARY 1999



Are Financial Markets Inherently Unstable?

> "There is an urgent need to recognize that financial markets, far from trending towards equilibrium, are inherently unstable."
>
> —GEORGE SOROS[1]

In the aftermath of the collapse of emerging economies in Asia, eastern Europe, and Latin America, many prominent economists and speculators, from Paul Krugman to George Soros, have called for government intervention in financial markets. Recommended policies include monetary inflation and currency controls. The foundation of such state interference is the belief that free markets in general, and financial markets in particular, are inherently unstable and require strict government regulation.

The fathers of this thesis are the British economist John Maynard Keynes and his principal heir, Hyman P. Minsky, who devised a "financial instability hypothesis." Minsky, a Harvard-taught economist, wrote many books and articles during his academic career of nearly 50 years, most of which he spent at Washington University in St. Louis. He died in 1996.

According to Minsky, Keynes's general theory of the economy was really a financial theory of uncertainty and expectations. According to this thesis, the capitalist economy is primarily ruled by Wall Street, which is fundamentally fragile and destabilizing owing to excessive debt, lax government rules, and businessmen's "animal spirits" and "waves of irrational psychology." (Conservative economist Allan H. Meltzer of Carnegie Mellon University makes the same point.[2])

In the Keynes-Minsky model, full employment in an unregulated market economy is not a natural equilibrium point, but a transitory moment in a business cycle. Euphoric expectations lead to an overleveraged condition where the rate of credit expansion exceeds the rate of profit in the economy. Eventually, the boom turns into a debt deflation and depression.

Long-Run Damage by Government Intervention

To stabilize the business cycle, Keynesians favor big-government capitalism where central banks and the International Monetary Fund play major roles as lenders of last resort. Keynes advocated the "socialization of investment" and taxes on short-term trading.[3] However, Minsky rightly pointed out that interventionist policies validate the existing fragile financial structure and allow the problems to deepen. He warned that "Once borrowers and lenders recognize that the downside instability of profits has decreased

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there will be an increase in the willingness and ability of business and bankers to debt-finance."[4] Larger and more frequent interventions become necessary to fend off debt deflations and recessions.

Minsky correctly criticized neo-classical economics for largely minimizing the impact that financial markets can have on economies: "The neo-classical synthesis became the economics of capitalism without capitalists, capital assets, and financial markets."[5]

My only problem with Minsky is that he mistakenly blames the market itself for its instability.

Mises's Non-Neutrality Thesis

To understand the root cause of financial and economic instability, we need to go back to Ludwig von Mises's "non-neutrality" thesis in his breakthrough work *The Theory of Money and Credit*. Mises pointed out that monetary intervention (easy money policies and artificial lowering of interest rates) is the principal source of uncertainty, false expectations, and excessive debt-leverage in the economy and on Wall Street. Under a stable monetary system, a laissez-faire economy would suffer occasional financial mishaps, bankruptcies, and down-days on Wall Street, but there would be no systematic "cluster of errors" that currently characterize today's global economy.[6]

Fortunately, most economists now recognize that government's monetary and fiscal policies are the main source of economic and financial instability in the world today. In fact, more and more college textbooks teach up front that the economy is relatively stable at full employment; this is known as the "long-term growth model." The short-term Keynesian model is taught at the end of the textbooks, where government intervention is recognized as a destabilizing factor in the economy and the chief cause of the boom-bust cycle. See Roy Ruffin and Paul Gregory's *Principles of Economics* and N. Gregory Mankiw's *Economics*.

Maybe George Soros needs to take a refresher course from these textbooks. □

1. George Soros, remarks before the House Banking Committee Hearing on International Economic Turmoil, September 15, 1998.

2. Allan H. Meltzer, *Keynes's Monetary Theory: A Different Interpretation* (Cambridge: Cambridge University Press, 1968).

3. John Maynard Keynes, *The General Theory of Employment, Money and Interest* (London: Macmillan, 1936), chapter 12, "The State of Long-Term Expectation." See also my article, "Keynes as a Speculator: A Critique of Keynesian Investment Theory," *Dissent on Keynes* (New York: Praeger, 1992), pp. 161–69.

4. Hyman P. Minsky, *Stabilizing an Unstable Economy* (New Haven: Yale University Press, 1986), p. 213.

5. Ibid., p. 120. For a favorable review of Minsky's work, see Robert Pollin, "The Relevance of Hyman Minsky," *Challenge* (March/April 1997), pp. 75–94.

6. Ludwig von Mises, *The Theory of Money and Credit* (Indianapolis: Liberty Classics, 1981 [1934]). See especially Murray Rothbard's excellent foreword in this edition.

Skousen on Samuelson at the AEA

The annual meetings of the American Economic Association (AEA) convene in New York City, January 3–5, 1999.

Freeman columnist Mark Skousen will be chairing and participating in an AEA session titled "Fifty Years of Paul Samuelson's *Economics*" on Monday, January 4, at 8:00 a.m. in the Trianon Ballroom at the New York Hilton. Other participants include Greg Mankiw of Harvard, Alan Blinder of Princeton University, and *Freeman* Contributing Editor Peter Boettke of George Mason University.

For complete information on registration, check AEA's Web site, www.vanderbilt.edu/AEA.

FEE will host a get-together for participants and friends Monday evening at the Hilton. For further information, contact Janette Brown at FEE—(914) 591-7230.

BOOKS

Titan: The Life of John D. Rockefeller, Sr.
by Ron Chernow
Random House • 1998 • 774 pages • $30.00

Reviewed by D.T. Armentano

For me, this is the image that sticks: John D. Rockefeller, president of Standard Oil, age 57, in bicycle suit and goggles, racing around the University of Chicago campus in 1897, harried administrators in tow, with students on the sidewalk chanting: "Rah, Rah, Rah, Rockefeller, he's the feller." Priceless.

He was indeed "the feller," as this scintillating retelling of his life and times by Ron Chernow aptly demonstrates. Chernow must surely be one of the few historians who can really write. That a 774-page book about a businessman born in 1839 can be a wonderful page-turner in the late 1990s says a lot about Chernow's literary talents—and about the object of his attention, John D. Rockefeller.

Chernow's early hunch was that the Rockefeller legend was "exhausted" and that he should skip the project. We can rejoice that he did not. For here, finally, is an intelligent and insightful account of the most important industrialist of his time, of his personal and family life, his religious beliefs, his massive philanthropy, and the company he created. This important revisionist account of the man and the myth is about as good as we are likely to get.

Who was John D. Rockefeller? Chernow shows that he was, above all else, a man who held fast to certain core values throughout his life. His early Baptist religious training shaped his lifelong attitudes toward the importance of hard work and charitable giving. Rockefeller threw himself into both without reservation. "Get money and give money" was his double-entry bookkeeping for reconciling capitalism and Christianity. His church work and other charitable causes were never an apology for his commercial success. Readers of this magazine can be grateful that he sank many millions into creating the University of Chicago.

Despite great wealth, Rockefeller was always economical, some would say miserly, in his own affairs. He reviewed every household bill and often "patrolled the hallways turning off gaslights." The titan and his family owned several residences, but there were no racehorses, no decadent parties, no yachts, no extravagant traveling or gaudy personal trinkets. When Cettie, his beloved wife of 50 years, died in 1915, her most costly items of clothing were a seal coat and muff valued at $135. Rockefeller gave away hundreds of millions of dollars to his children and to selected causes (including medical research and black schooling). When he died, his own personal estate (which had been devastated by the 1929 crash) stood at a "mere" $26 million.

Chernow labors mightily to set Standard's commercial accomplishments reasonably straight. He identifies correctly the factors that account for the early growth of the firm (entrepreneurship, economies of scale, technological innovation) and its ability to maintain market leadership. He also identifies correctly the changing market conditions at the turn of the century that eroded Standard's market share prior to the antitrust suits. Indeed, Chernow even admits that the subsequent legal actions may have been "superfluous."

But there are problems with some of his economic and legal analysis. Lacking a correct (Austrian) theory of monopoly, Chernow is unnecessarily bothered by Standard's "predatory" pricing and by the "rebates" it was able to wring consistently from the railroads. Also, he constantly refers to Standard as a "monopoly" even though there were always rivals in domestic refining (147 in 1911), and even though most markets were legally open to entry.

The greatest disappointment in *Titan* is Chernow's virtual non-treatment of the classic antitrust decisions that broke up Standard. While the book builds to this climax, the Circuit Court (1909) and Supreme Court (1911) decisions are tossed off in less than two pages! Readers are not told that the Circuit Court never made any legal judgment on

Standard's business practices or economic performance. Instead, it decided the case on the more narrow issue of whether Standard Oil of New Jersey was a "trust" or "combination" in restraint of trade. Under the legal precedents, it was. Guilty; divestiture ordered. And while the Supreme Court announced that dominant firms should be judged by a "rule of reason," it never applied that rule to the evidence in the case.

These are not dry academic points. They are crucially important to any overall evaluation of the firm in the marketplace and to an understanding of any appropriate "monopoly" policy. Unfortunately, Chernow misses it all very badly. Still this is a blockbuster book that every student (and professor) of business history would do well to study carefully. □

D.T. Armentano, professor emeritus of economics at the University of Hartford, is the author of Antitrust and Monopoly: Anatomy of a Policy Failure.

The Great Betrayal: How American Sovereignty and Social Justice Are Being Sacrificed to the Gods of the Global Economy

by Patrick Buchanan

Little Brown & Company • 1998 • 320 pages • $22.95

Reviewed by James Bovard

Patrick Buchanan has given America one of the most eloquent theological tracts of recent decades. Unfortunately, when Buchanan, a two-time presidential candidate, takes his theological views into economic areas, the result is a recipe for poverty, conflict, and subjugation.

The subtitle of Buchanan's book is "How American Sovereignty and Social Justice Are Being Sacrificed to the Gods of the Global Economy." Buchanan seems obsessed with demons—denouncing economist Frederic Bastiat as "heretical," denouncing elites for betraying America, denouncing foreigners at every opportunity. He seems far more interested in the proliferation of enemies than with the simple mechanics of economic exchange.

In a chapter entitled "Anatomy of a Murder," Buchanan uses the American auto industry as the consummate example of the evils of American trade policy. He declares: "The U.S. auto industry can justifiably claim to have been a victim of abuse, neglect, and abandonment by the government of the United States." The one lesson from this chapter is that no industry can be held responsible for its own incompetence and abuse of loyal customers.

He begins by declaring that Volkswagen Beetles were the first foreign auto to get significant market share in the United States—and then stresses Hitler's role in creating the Volkswagen corporation and the fact that the company (like many German corporations) relied on slave labor from concentration camps during World War II. Readers are left with the impression that all Volkswagens are forever tainted by this Original Sin and that anyone who bought a Beetle or any foreign car was morally inferior to people who bought American-made cars.

One issue Buchanan did not find space for is quality and reliability. *Consumer Reports* in the early-to-mid-1980s repeatedly flogged the Big Three American automakers for the high rate of defects in their new cars—at a time when Japanese companies had far better quality control. Buchanan, like other protectionists, ignores how foreign competition improves the quality of domestic products.

Among other notions of unfair trade, Buchanan claims that foreigners unfairly benefit because they are not forced to comply with the same regulations and pay the same taxes that American companies face. He has shifted from his earlier beliefs that government must slash the burden of regulations and taxes on American citizens and American businesses—and is now on a holy crusade to "level the playing field" by imposing more taxes and burdens on foreign businesses. The fact that many European companies face heavier tax and regulatory burdens than do U.S. companies somehow never gets mentioned. Even were that not so, why should foreign companies be considered cheaters if their nations' tax systems are not as idiotic as is the U.S. Internal Revenue Code?

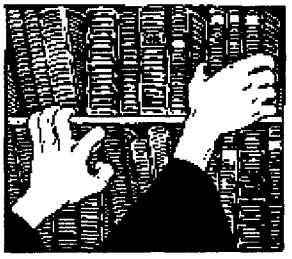
Buchanan's program is nothing new. American protectionists have always found some moral pretext to damn imports. In the 1820s, protectionists proclaimed that trade between England and America could not be fair because England was advanced and America was comparatively backward. In the 1870s, protectionists announced that trade between America and Latin America could not be fair because America was comparatively rich while Latin American countries were poor. In the 1880s, protectionists warned that trade could not be fair if the interest rate among the trading nations differed by more than 2 percent.

In practice, fair trade means protectionism. Yet every trade barrier undermines the productivity of capital and labor throughout the economy. A 1979 Treasury Department study estimated that trade barriers routinely cost American consumers eight to ten times as much as they benefit American producers. A 1984 Federal Trade Commission study estimated that tariffs cost the American economy $81 for every $1 of adjustment costs saved. According to the Institute for International Economics, trade barriers are costing American consumers $70 billion a year—equal to over $1,000 per family.

The myth of fair trade is that politicians and bureaucrats are fairer than markets and that prosperity is best achieved by arbitrary political manipulation, rather than by each individual pursuing his own interest. But government cannot make trade more fair by making it less free.

Should Pat Buchanan have dictatorial power over what other Americans are permitted to buy from 96 percent of the world's population? This is the question by which his doctrine must be judged.

James Bovard is the author of The Fair Trade Fraud.



Politics By Principle, Not Interest: Towards Nondiscriminatory Democracy

by James M. Buchanan and Roger D. Congleton

Cambridge University Press • 1998 • 191 pages • $49.95

Reviewed by William H. Peterson

Said Plato: "Morality determines politics." Which raises a question 2,500 years later for Nobel laureate James Buchanan and fellow economist Roger Congleton: Does politics determine morality?

Their answer in an era of no-holds-barred welfare state politics is, in the main, yes. They argue that the very logic of majoritarianism inevitably leads to unequal treatment and discrimination by the state. Coalitions push the interests of their members at the expense of others. Politics and "takings" become virtually synonymous.

Unprincipled politics? The charge is not new. Ambrose Bierce defined politics as "the conduct of public affairs for private advantage." Oscar Wilde saw democracy as the "bludgeoning of the people by the people for the people." Yet America seems to cling to politics over character. The high approval ratings of scandal-ridden President Clinton come to mind.

A kind of political amorality marks our times. Politics becomes a secondhand religion, an odd mixture of opportunism, apathy, cynicism, relativism, and deception. It sinks into a contest over spoils, plundering many to benefit a few, all via political spin and tax coercion.

Buchanan's insights into this unholy process helped him win the 1986 Nobel Prize in economics, long after he and colleague Gordon Tullock forged the Public Choice school with their 1962 book, *The Calculus of Consent.* Their theory holds that self-interest guides voters and officials in their public as well as private choices, and that government naturally caters to powerful "rent-seeking" groups.

"Rent" in public choice jargon means a special grant: in a sense, a sale of a government favor enabling the beneficiary to prosper

more than it otherwise could. Note, for example, that the domestic price of wholesale sugar is about twice the world price. It remains at that high level because the federal government protects some three-quarters of the market for high-cost domestic growers, with the remaining quarter allotted by quotas to low-cost foreign producers. The domestic growers' gain comes at the expense of sugar consumers—virtually everyone getting clipped for but a few pennies a day.

Why does politics generate programs of such dubious morality? Public choice theorists explain that the rent-seekers are well informed about and fight hard for programs that give them large gains. The costs, on the other hand, are widely diffused among a great number of consumers who know little or nothing about the government's policy and have little incentive to oppose it. The political deck is stacked in favor of those who prefer to wheedle their profits out of government "rent" rather than honest trade.

Buchanan and Congleton point up the economic facts of life. No free lunch ever—the state can give only what it first takes. Most voters are too busy with life's exigencies to cope with the daily maze of politics, or as the public choicers put it, voters are "rationally ignorant." However, they will pursue their perceived self-interest, join pressure groups in an attempt to get their cut of the state's booty, and generally vote for the candidate or party that promises them the most.

The cure? The authors prescribe relimiting the state: Get it back to equal treatment of all. Restore to constitutional vitality the Ninth Amendment: "The enumeration in the Constitution of certain rights shall not be construed to deny or disparage others retained by the people." In short, Buchanan and Congleton want to stop the state *constitutionally* from treating different persons and groups differently.

That would knock rent-seeking for a loop. It would reform election campaigns by getting at the root of the problem—power. It would add up to freer trade, saner environmental controls, greater freedom for American entrepreneurs. It would also lead to faster economic growth, less discrimination, less state waste, and lower taxes.

But, Catch-22: Can guts for such basic change be found in today's jaded electorate? How many Americans want to do in Santa Claus by setting up a real barrier to the free-spending, vote-buying state? The need to put the constitutional brakes on runaway government is clear. How do we get there from here? That question awaits an answer.

As Voltaire wrote some 250 years ago: "The art of government is to take from some to give to others." It is this dark art that James Buchanan and Roger Congleton seek to undo. □

William Peterson, a Heritage Foundation adjunct scholar, is Distinguished Lundy Professor Emeritus of Business Philosophy at Campbell University in North Carolina.

Written on the Heart:
The Case for Natural Law

by J. Budziszewski

InterVarsity Press • 1997 • 252 pages • $15.99

Reviewed by Robert Batemarco

The canard that free-market economists are so narrowly focused on economic concerns that they miss the big picture seems as indestructible as it is indefensible. It was Ludwig von Mises, after all, who said that one cannot be a good economist if he is only an economist. Indeed, there are things higher than economics that do have a bearing on how an economic system should be properly ordered. *Written on the Heart* spells out what those higher things are and why they justify economic freedom.

This book, however, was not written primarily to shed light on the best way to fashion an economy. It is, rather, a primer on natural law philosophy. It discusses the main tenets of three seminal thinkers in this tradition: Aristotle, Aquinas, and Locke. After comparing the views of the three, the author then examines the utilitarian position of John Stuart Mill, which helped move moral philosophy away from natural law thinking.

Just what does natural law philosophy have to say about the proper role of government?

Aristotle's teaching that government exists to make men virtuous looks like an invitation to an overbearing state. However, the author, a philosophy professor at the University of Texas, shows that Aquinas qualified this somewhat, contending that the state should not seek to extirpate all vices but "only the more grievous vices, from which it is possible for the majority to abstain, and chiefly those that are to the hurt of others." This formulation still leaves much to be desired. To most people, for instance, the drinking of alcoholic beverages would scarcely qualify as a "grievous vice," but unfortunately the author, showing more courage than wisdom, denies that Prohibition was an instance in which banning a vice did more harm than good. This will hardly help to promote natural law thinking.

Just how far short of the standards set by natural law thinking current legislative practice falls is clearly demonstrated by Aquinas's definition of law as "an ordinance of practical reason, for the common good, made by those who have care of the community, and promulgated or made known." With so many legislative enactments serving special interests rather than the common good, and so few such measures fully understood even by the legislators who vote on them, the amount of twentieth-century American legislation that meets all these criteria would probably fit in a volume not much larger than one issue of *The Freeman*.

Budziszewski's discussion of Locke revolves around the seventeenth-century philosopher's criteria for justice in the appropriation of goods from their original state of nature and his notion of inalienable rights. It follows from these Lockean concepts that since the natural right to keep justly acquired property is inalienable, redistributive taxation is theft, regardless of how large a majority favors it. That argument will shock many, but it is one that needs to be made.

Budziszewski's critique of the utilitarian challenge to natural law is very pointed. He finds utilitarianism devoid of any notion of right and wrong that is not tantamount to expediency. Moreover, he maintains that the foundation of utilitarian ethics is feeling rather than reason. Thus the widespread acceptance of utilitarianism has imbued the twentieth century with ethical relativism and the exalting of emotions over reason. The price, counted in lives and liberties lost in wars, concentration camps, and bureaucratic tyranny, has been high indeed.

The book is avowedly Christian. It is laced with numerous references to scripture and to Christian writers such as C.S. Lewis. Whether or not the reader shares Budziszewski's belief in God, he would be hard pressed to deny that natural law thinking is a mighty obstacle to the belief that earthly rulers are entitled to wield god-like powers. The acceptance of natural law, he writes, implies that "Earthly rulers are on a leash. They cannot make deeds wrong simply by prohibiting them, nor can they make them right simply by calling them constitutional rights."

Beautifully said. Unless that point is taken to heart, however, the 21st century may turn out as bad as the twentieth. □

Robert Batemarco is director of analytics at a marketing research firm in New York City and teaches economics at Marymount College in Tarrytown, New York.

The Commanding Heights: The Battle Between Government and the Marketplace That Is Remaking the World

by Daniel Yergin and Joseph Stanislaw

Simon and Schuster • 1998 • 352 pages • $26.00

Reviewed by David L. Littmann

The danger in telling a good story is often the sacrifice of key facts, thereby distorting the reader's understanding of reality. In *The Commanding Heights*, authors Daniel Yergin and Joseph Stanislaw describe the epic twentieth-century conflict between socialists and market advocates. This is an extremely worthy story, but the telling, although quite informative, has some serious gaps and weak analysis. We might say that it comes up one sandwich short of a picnic.

The book's title is lifted from a saying of Lenin's, that socialists must aim at seizing the "commanding heights" of a nation's economy

if they are to succeed in their plans. Yergin and Stanislaw embark on an ambitious journey to describe the eight-decade-long, worldwide struggle among economists and politicians with conflicting visions about government's role in the economic and social life of their citizens.

One admirable accomplishment of the book is its tracing of the forces and individuals most centrally involved in the rise and fall of socialist policies around the globe. The authors have painstakingly developed the key names and ideas associated with the drama. Their history of each nation's sorry experience with socialism is excellent. The anecdotes and damaging quotations from now-discredited proponents of socialism alone make the read worthwhile.

The greatest strength of *The Commanding Heights* is its comprehensive portrayal of socialism's ascendency—the road to serfdom, as F.A. Hayek put it. Yergin and Stanislaw reveal an amazingly consistent pattern of political connivance and the distressing ease with which professional politicians and their coterie of "economic advisers" systematically capitalize on fear and gullibility among the masses to replace freedom and property rights with central planning and bureaucracy. The authors illustrate how eagerly totalitarians have—and in the future, will—pounce on every economic crisis as an opportunity to grasp more power.

But there are significant weaknesses in the book stemming from the authors' deficient background in economics. This deficiency leads them to repeat familiar misconceptions about the free market, such as blaming it for the Great Depression. Readers are bombarded by "market failures" as the reasons for the subsequent rise of the central planners, but if the authors had looked more closely, they would have found that government intervention was responsible for all the economic shocks of the century.

Among the precursors of the crises exploited by the socialists are stifling taxes, trade restrictions, intervention in agricultural markets, counterproductive regulations, and perverse monetary and credit policies. The authors, however, accept the conventional, but unprofessional wisdom propounded by the propaganda organs of socialism that whenever something goes wrong, it's a market failure for which the visionaries have a remedy. Consequently, the average reader is apt to blithely accept "market failure" rather than government meddling as the beginning of the government's rise to the commanding heights.

The errors do not end there. Yergin and Stanislaw fail to distinguish between money and credit, and they totally miss the origins of the $200 billion savings and loan disaster. Those and other mistakes undermine the book.

Their understanding of inflation, for example, is weak. Inflation is always and everywhere a monetary phenomenon. Printing money faster than the growth of real output leads to an increase in the overall average price level. Yergin and Stanislaw, however, write as if increases in particular prices—oil, in this case—were the cause of inflation. Worse yet, they fail to examine the terrible policy blunders committed in Washington in an effort to "solve" the so-called energy crisis. Looking down from the commanding heights, our central planners gave us price controls, rationing schemes and, thanks to the Federal Reserve, torrents of new money and true inflation. Many important lessons can be learned from a study of the "energy crisis" of the 1970s, but the reader will have to learn them elsewhere.

The plentiful sins of omission and commission could have been avoided if the authors had talked less with the likes of Felix Rohatyn and had consulted more with, say, Walter Williams. Alas, they didn't.

Read this book for its generally good history, but beware of its poor economic analysis. □

David L. Littmann is senior vice president and chief economist of Comerica Bank, Detroit, Michigan.



Beyond All Reason: The Radical Assault on Truth in American Law

by Daniel A. Farber and Suzanna Sherry

Oxford University Press • 1997 • 195 pages • $25.00

Reviewed by Lauren S. Bain

In *Beyond All Reason,* Daniel Farber and Suzanna Sherry identify a serious threat to our legal system—the assault on the idea that the law should seek and then respond to the truth. Unfortunately, they pull their punches and fail to deliver a knockout blow to this lurking menace.

Much has been written about the farrago of bizarre ideas that goes under the name of "multiculturalism." Among the stranger notions advanced by the multiculturalists is that reality is a social construct. There is no objective truth; instead, each person or group constructs his own reality. Women, for example, supposedly have their own "way of knowing," and those who dispute this idea must be a part of the "dominant power structure" and therefore beneath response. Decades ago, Ludwig von Mises destroyed the claims of what he referred to as "polylogism," but bad ideas have a way of coming back, dressed up in some fancy new language. That is exactly the case here.

Law professors Farber and Sherry see the multiculturalist assault on truth as undermining the very foundations of our system of law. They write, "Critiques of truth, merit and legal reasoning are all tightly intertwined. It is difficult to defend merit if the concept of truth is open-ended. . . . [I]t is difficult to defend truth if the merit of an analysis or argument is wholly subjective. And without either merit or truth, how could judicial reasoning hope to stand?" Well said. They have identified one of the most pernicious tendencies of multiculturalism—its hostility to reason.

Consider, for example, the "indeterminacy thesis" advanced by the "critical legal studies" movement. Professor Mark Tushnet, a proponent of this thesis, explains, "Critique is all there is. . . . A competent adjudicator can square a decision in favor of either side in any given lawsuit with the existing body of legal rules." But the consequences of adopting indeterminacy are devastating. As Farber and Sherry write, "If the indeterminacy thesis is correct, then it is unclear how legal arguments ever have any persuasive effect, because all arguments are equally sound." Why bother with argumentation at all; we might as well flip a coin.

The authors go to considerable lengths to deconstruct two crucial tenets of multiculturalist theory: first, that reality is socially constructed, and second, that all constructs of reality merit equal deference in the marketplace of ideas, including the legal system. They are particularly effective in obliterating the "alternative ways of knowing" supposition that the multiculturalists use as a battering ram against the idea embedded in the legal system that the truth excludes all incompatible ideas. This is the backbone of the book and it is strong.

Unfortunately, our avowedly "centrist" authors weaken their effort by trying to pacify the multiculturalists. "We don't mean that all the work of these scholars is worthless," they write. They then proceed to validate their multiculturalist colleagues' "other work" by resort to the non-judgmental multiculturalist trait of presuming merit where no evidence of merit exists. The reader looks in vain for any sound argument from the authors in favor of multiculturalist theorizing, in law or elsewhere.

At one point, Farber and Sherry go so far as to attempt an intellectual rescue of the people whose ideas they have shown to be a menace in the law, saying that the multiculturalists are only guilty of employing wild and sometimes inane slogans as a means of getting across their ideas. But if the ideas behind the slogans are bad ones, what does it matter how they promote them?

At another turn, the authors, attempting to chart a "middle" course, take a completely gratuitous swipe at the free-market camp: "Radical multiculturalists favor ideas relating to the social construction of reality, just as conservative scholars have latched onto other ideas about free markets." These law professors probably know almost nothing about the

vast extent of free-market scholarship (that they insist on labeling it "conservative" is a tip off), but are happy to dismiss it in the same breath as they dismiss the idea that reality is merely a "social construct."

Their unwillingness to come down hard on the multiculturalists (who are leftist allies, if rather embarrassing ones) and their pandering attacks on freedom advocates undermine what might have been a truly useful book. Like the proverbial road to hell, *Beyond All Reason* is paved with good intentions. Farber and Sherry smoke out and then wound some of the multiculturalist dragons, but it will have to fall to more courageous writers to slay them. □

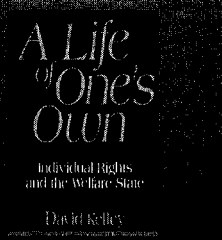
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"A brilliant mix of theory and practice, this is a book you will share with your friends."

— Randy E. Barnett, Boston University School of Law

The welfare state rests on the assumption that people have the right to food, shelter, health care, retirement income, and other goods provided by the government. David Kelley examines the historical origins of that assumption, which, he shows, is deeply flawed. Welfare "rights," he argues, are incompatible with freedom, justice, and true benevolence, and they have damaged the genuine welfare of those who can least afford to become dependent on the government.





"By explaining the tradition of liberty rights and the economic system of capitalism that accompanies it, Kelley shows 'welfare' rights to be both an ethical and an economic sham. Kelley argues that individualism is at odds with neither morality nor community. This is a clearly written work that appeals to common sense."

—Douglas B. Rasmussen
Professor of Philosophy
St. John's University

"Anyone interested in the moral legitimacy of the welfare state must deal with the arguments of this book."

—Ellen Frankel Paul
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Social Philosophy and Policy

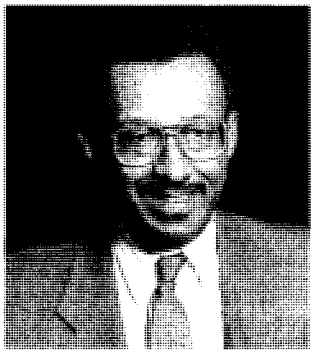
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History



The Civil War's Tragic Legacy

The Civil War produced at least two important outcomes. First, although it was not President Lincoln's intent, it freed slaves in the Confederate States. Second, it settled the question of whether states could secede from the Union. The causes of and the issues surrounding America's most costly war in terms of battlefield casualties are still controversial. Even its name—the Civil War—is in dispute, and plausibly so.

A civil war is a struggle between two or more factions for control of the central government. Modern examples are the conflicts in Lebanon, Liberia, and Angola. In 1861, Jefferson Davis, the president of the Confederate States, no more wanted to take over Washington, D.C., than George Washington wanted to take over London in 1776. The Confederate States were fighting for independence from the Union. Whatever one's sentiments, the conflict is more accurately characterized as a war for Southern independence; in the South, you frequently hear it called the War of Northern Aggression.

Unrestrained Government

History books most often say the war was fought to free the slaves. But that idea is brought into serious question by Abraham Lincoln's repeated disclaimer: "I have no purpose, directly or indirectly, to interfere with the institution of slavery in the states where it exists. I believe I have no lawful right to do so, and I have no inclination to do so." The real causes had more to do with problems similar to those the nation faces today—a federal government that has escaped the limits of the Constitution.

John C. Calhoun expressed that concern in his famous Fort Hill Address of July 26, 1831, when he was Andrew Jackson's vice president. Calhoun, who later became a senator from South Carolina, said, "Stripped of all its covering, the naked question is, whether ours is a federal or consolidated government; a constitutional or absolute one; a government resting solidly on the basis of the sovereignty of the States, or on the unrestrained will of a majority; a form of government, as in all other unlimited ones, in which injustice, violence, and force must ultimately prevail."

Calhoun, like Jefferson, feared Washington, D.C.'s usurpation of powers constitutionally held by the people and the states ("consolidation"). For example, of the tariffs enacted to protect Northern manufacturers, Calhoun said that "an undue proportion of the burden of taxation has been imposed on the South, and an undue proportion of its proceeds appropriated to the North."

Import duties extracted far more from the South than from the North, and Southerners complained of having to pay either high prices for northern-made goods or high tariffs on foreign-made goods. They also complained about federal laws not dissimilar

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to the Navigation Acts that helped bring on the War for Independence.

The Nullification Doctrine

A precursor to the War Between the States came in 1832 when South Carolina called a convention to nullify the tariff acts of 1828 and 1832. Branded "the tariff of abominations," the duties were multiples of previous duties. The convention declared them unconstitutional and authorized the governor to resist federal efforts to collect them. After reaching the brink of armed conflict with Washington, a settlement to reduce the tariffs in steps—the Great Compromise of 1833—was reached.

South Carolinians believed there was precedence for the nullification of unconstitutional federal laws. Both Jefferson and James Madison suggested the doctrine in 1798. It was used to nullify federal laws in Georgia, Alabama, Pennsylvania, and the New England states. The reasoning was that the federal government was created by, and hence was the agent of, the states.

When Congress threatened to raise tariffs to unprecedented levels and the Republican Lincoln was elected president, a special South Carolina convention unanimously adopted an Ordinance of Secession and a "Declaration of Causes" stating that "We assert that fourteen of the States have deliberately refused for years past to fulfill their constitutional obligations. . . . Thus the constitutional compact has been deliberately broken and disregarded by the non-slaveholding States; and the consequence follows that South Carolina is released from her obligation. . . ." Continuing, the Declaration, asserted, "We, therefore, the people of South Carolina, by our delegates in Convention assembled, appealing to the Supreme Judge of the world for the rectitude of our intentions, have solemnly declared that the Union heretofore existing between this State and the other States of North America is dissolved, and that the State of South Carolina has resumed her position among the nations of the world, as a separate and independent state, with full power to levy war, conclude peace, contract alliances, establish commerce, and to do all other acts and things which independent States may of right do." The next year war started when South Carolinians fired on Fort Sumter, an island in the harbor of Charleston, South Carolina.

The principal-agent relationship between the states and federal government was not an idea invented by South Carolina in 1860; it was taken for granted. At Virginia's convention to ratify the U.S. Constitution, the delegates said, "We delegates of the people of Virginia . . . do in the name and on the behalf of the people of Virginia, declare and make known, that the powers granted under the Constitution being derived from the people of the United States, may be resumed by them whensoever the same shall be perverted to their injury or oppression, and that every power not granted thereby remains with them, and at their will."

The clear and key message was: the people of Virginia, through their delegates, entered a contractual agreement with the several other sovereign states and created the federal government as their agent. When the federal government violates their grant of power, the people of Virginia have the right to take back the power and fire their agent.

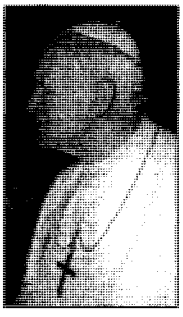
In light of the outcome of the War Between the States, the federal government can do anything it wishes and the states have little or no recourse. A derelict U.S. Supreme Court refuses to do its duty of interpreting both the letter and spirit of the Constitution. That has translated into the 70,000 federal regulations and mandates that controls the lives of our citizens. It also translates into interpretation of the "commerce" and "welfare" clauses of our Constitution in ways the framers could not have possibly envisioned. Today, it is difficult to think of one elected official with the statesman's foresight of a Jefferson, Madison, or Calhoun who can articulate the dangers to liberty presented by a run-amok government. The prospects for liberty thus appear dim. The supreme tragedy is that if liberty dies in America, it is destined to die everywhere. □

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February 1999 Vol. 49, No. 2

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PERSPECTIVE

Monster

Rule No. 1 for slaying the Hydra: *slay* it.

Don't just cut off one—or even a few—of its heads. That's not good enough: the head might grow back. Kill it *dead.* How many times do we need to be taught that lesson before we learn it?

During the presidency of Ronald Reagan the Department of Justice ended the long, unjust, and wasteful antitrust case against IBM. Moreover, antitrust prosecutions dropped significantly. This happened because Reagan's team included an antitrust staff heavily influenced by Chicago-school critics of antitrust theory and practice. Having sipped from the cups of Yale Brozen and then Robert Bork (whose *Antitrust Paradox* made a deep impression), the staff understood that the history of antitrust prosecution was mostly a history of government's going to bat to save weak competitors from consumer-pleasing companies. It was about protectionism, not monopoly.

But the Justice Department people did not object to antitrust in principle. So while they abstained from interfering with mergers and other activity that previously would have summoned the government's wrath, they did not seek repeal of the government's authority to prosecute companies for peaceful activity. The Hydra was sedated, not slain. When the Clinton team replaced the Reagan team, the Hydra awoke. Ask Bill Gates.

Agriculture is another example of reforming the Hydra. A couple of years ago congressional Republicans boasted that they had put the appalling system of farm subsidies on a seven-year track to oblivion. They sappily called their bill the Freedom to Farm Act. But in the last session, with farmers' incomes off and the election bearing down, the GOP-run Congress did a one-eighty. Farm subsidies were nearly doubled. The head grew back.

In the 1970s the rock group Steppenwolf performed an intelligent song about America and its government called "Monster." The chorus was, "There's a monster on the loose. It has our heads in a noose." Regardless of

good intentions, most members of Congress who pay homage to the free market don't understand that you can't phase out a monster over seven years. If you try, you deserve to get bitten. But the rest of us don't.

* * *

Most people seem to believe that if the government were not regulating safety in air travel, airplanes would routinely fall out of the sky. Eric Nolte, a commercial airline pilot, shows that this belief betrays a woeful failure to understand how a free economy works.

What to do with a piece of property should be a fairly straightforward matter. But when the property is a decommissioned government-operated military airport, the simple becomes the hopelessly complicated, as Tibor Machan demonstrates.

The European Union. The new euro currency. What is going on in Europe? Norman Barry compares the ominous process of Eurocentralization with the American constitutional experience.

Pope John Paul II's trip to Cuba last year was remarkable in many ways. One of them had to do with what the Pope said about family and education in Castro's paradise. David Boaz says America's education establishment should have been listening.

President Clinton says "save Social Security first." But should it be saved at all? The intrinsically flawed pay-as-you-go transfer program is given a thorough going-over by Harry Dolan.

Trust in government is at an all-time low. Those who lament this state of affairs chide the people for their wariness. But Dwight Lee and Jeff Clark argue that government is only getting what it deserves.

The 1998 winner of the Nobel Prize in economics is an Indian-born economist who favors government intervention to improve the lot of the people. Barun Mitra contends that India has had enough of that already.

Ludwig von Mises is reputed to have said that government is the only institution that can take a useful commodity like paper, slap some ink on it, and make it worthless. But that paper is imposed on us with the magic words "legal tender." D. Alexander Moseley wonders if it is time to banish those words.

The Big Corporation is the bogeyman of every socialist and lesser interventionist. But not to worry, writes Max More, because the market process and technology favor decentralization and competition.

Beware cost-benefit analyses for government programs. As Karen Selick points out, they stand on a foundation of quicksand: namely, the erroneous principle that one person's costs can be compared to another's benefits.

The University of Wisconsin was once a bastion of free speech. Then Donna Shalala, the future secretary of health and human services, took over. Jon Sanders says it's been downhill ever since.

He was a nineteenth-century American individualist who battled for free speech and the right of women to be as free as men. At age 75 he was sentenced to a year at hard labor for his trouble. Wendy McElroy chronicles the life of Moses Harman.

Our intrepid columnists, Lawrence Reed, Doug Bandow, Dwight Lee, Mark Skousen, and Charles Baird, take on government airports, the folly of alliances, business honesty, Amartya Sen, and the International Labor Organization. George Selgin looks at the case for a worldwide central bank and implores, "It Just Ain't So!"

Book reviews this month scrutinize urban education, taxation, early black entrepreneurs, the costs of war, enviro-capitalism, anti-science, and economics and the law.

—SHELDON RICHMAN

THE FREEMAN
Ideas On Liberty

We Need a Global Fed?

It Just Ain't So!

Some economic pundits see every instance of economic disorder as proof of the defects of capitalism and of the need for more extensive government regulation of the economy. It never seems to cross their minds that government regulations might even *destabilize* markets. A recent example of such thinking comes from Jeffrey E. Garten, dean of Yale's School of Management, who in the September 23, 1998, *New York Times*, urged creation of a global central bank to stabilize the world economy.

Garten begins with a summary of U.S. financial history that would make any economic historian blush. From the Civil War to the 1930s, Garten writes, the American economy "was an uncontrollable Darwinian process" marked by frequent booms and busts and "countless bank failures." Then, to every right-thinking citizen's vast relief, the federal government stepped in, creating the Securities and Exchange Commission, the Federal Deposit Insurance Corporation, and "most important, the Federal Reserve." The "harsh, invisible hand of Adam Smith" was thus moderated, and the business cycle brought under control.

So America's financial system was unregulated before 1930? It just ain't so! In truth, Civil War legislation nearly wiped out the antebellum state banking industry, setting up new national banks that were forced to back their notes with government bonds. Eligible bond collateral became increasingly scarce during the last quarter of the nineteenth century. Over the course of any year, such banks were prevented from meeting seasonal peaks in currency demands. The result was an inelastic stock of national bank currency, which gave rise to serious "currency shortages" in 1884, 1893, and 1907. Government regulation thus played a key role in the "destructive business cycles" that Mr. Garten so unhesitatingly blames on the invisible hand.

In addition to setting unnatural limits to the stock of currency, the government also prohibited national banks from setting up branch networks. This resulted in the proliferation of thousands of under-diversified and failure-prone banks. In Canada, where chartered banks were free to issue notes and to branch nationwide, bank failures were few and far between, and not a single bank failed during the Great Depression. In the United States, by contrast, several thousand banks failed during the 1930s alone, and almost all of them were "unit" banks lacking any branches.

Canada, it should be noted, established a central bank in 1935. Economic historians still wonder why, since its monetary system had withstood the depression better than those of other nations having central banks, including the U.S. system. Mr. Garten suggests that central banks such as the Fed prevent business cycles. But the United States suffered a serious downturn in 1921 and its most serious depression of all starting in 1929, notwithstanding the Fed's establishment in 1913. The years since World War II have not witnessed another Great Depression, but the business cycle has hardly disappeared, and secular *in*flation has become an additional problem.

The truth is that in combating financial crises, central banks have proven to be highly costly and unreliable substitutes for structural improvements in the banking industry, namely, branch banking, competitive note issuance, and foreign bank entry. Central banks have all too often undermined the solvency of private financial firms. The U.S. savings and loan

industry became insolvent in the early 1980s mainly because of Fed-sponsored inflation, which dissolved the value of long-term home mortgages negotiated a decade or more before. The S&L mess was worsened by the perverse effects of deposit insurance, administered in this case by the Federal Savings and Loan Insurance Corporation, which subsequently failed. So much for the stabilizing effects of "progressive" New Deal financial regulations.

According to a recent study by Kurt Schuler, central banks have done a poorer job historically at promoting low inflation, exchange-rate stability, open exchange markets, and economic growth than non-central banking arrangements, including free banking and currency boards. Indeed central banks offer only one clear advantage over these other arrangements: the ability to print money for their sponsoring governments. And that is one advantage the public can live without.

Seemingly unaware of the role national central banks have played in generating financial turmoil around the world, Mr. Garten can think of no better solution to the world's financial troubles than a *global* central bank. He does not appreciate the link between central-bank pegged exchange rates and speculative currency runs like those recently experienced in Southeast Asia (runs to which non-central-bank arrangements, such as currency boards, are invulnerable); he does not consider the possibility that Japan's present slump may be the payback for its aggressively expansionary monetary policy during the 1980s; and he doesn't contemplate the fact that Russian bank depositors might not have to watch their savings gradually erode were they free to do business with foreign banks. Worse still, Mr. Garten somehow imagines that the errors of national central bankers would somehow be avoided by an international bank, as if ignorance and short-sightedness were unable to transcend national boundaries.

Take Russia as a case in point. From June to October 1992, Russia's central bank tripled its lending to commercial banks. Most of this credit was in turn re-lent, *at a loss*, to the banks' own state-enterprise owners! The losses were then made up for by Russia's finance ministry. In the meantime, genuinely private Russian firms went begging for funds.

Eventually, the massive flows of central-bank credit began to reduce the value of the ruble, undermining Russian banks' ability to pay their foreign debts and rendering them that much more insolvent. And how has Russia's central bank proposed to resolve the crisis? By lending still more credit to commercial banks that should have been declared insolvent long ago!

Would a global central bank help? Not at all. On the contrary, such a bank would merely encourage Russian authorities to continue their perverse policies, by forcing citizens of other countries to bail out an essentially corrupt system.

Instead of performing their self-assigned task of stabilizing national financial markets, central banks have routinely attempted to prop up unsound banking systems with easy money. Jeffrey Garten believes that the cure for this failure is a bigger, better central bank, capable of acting as a world "lender of last resort," when in fact loans from such an institution would only make it easier for national governments to delay needed financial market reforms. Perhaps Mr. Garten believes that a global central bank would rise above domestic politics, resisting any pressure to bail out insolvent banks. But the record of existing central banks, and of the IMF and World Bank for that matter, provides no grounds for such optimism.

On the contrary, experience suggests that a global central bank would quickly be captured by international banking interests and that it would serve those interests (rather than the interest of the general public) by rushing to guarantee their loans even when doing so would be tantamount to rewarding irresponsible government policies and banking practices.

So Mr. Garten, kindly spare us a world central bank: your quaint belief that, when it comes to regulating financial markets, governments can never go too far, just ain't so.

—GEORGE SELGIN
Department of Economics
University of Georgia

THE FREEMAN
Ideas On Liberty

The Government Spiral

by Eric Nolte

The graveyard spiral is a maneuver known to students of airplane accidents as one of the most common reasons that inexperienced pilots unwittingly kill themselves.

In this utterly preventable maneuver, a pilot untrained to fly on instruments flies into clouds. Disoriented and suffering tunnel vision, he doesn't notice the airplane's bank. At this point, the airplane's inherent stability has not yet become overwhelmed by the ham-fisted exertions of the poor pilot. If he would just let go of the airplane, it would right itself, but he grimly hangs on, with the plastic of the control wheel oozing out from between his ever-whitening knuckles.

The airstream noise gets louder, causing him to pull back even harder on the control wheel because he thinks that simply raising the nose will pull him out of the dive. But this doesn't counter the fundamental problem, which is that the wings are banked. Pulling back on the wheel, heedless of the bank, tightens the turn. With the noise level of the dive up to the roar of a rock band in live performance, the airspeed and tachometer needles are pegged on the red lines, and the witless aviator hauls back on the controls with a mighty heave. The tail breaks off. He may wait as much as two minutes before impact with the earth puts an end to his terrified and uncomprehending ignorance.

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The way out of a graveyard spiral is to level the wings, reduce the power, and ease up on the nose. But you first have to know what has gone wrong.

Regulating Blind

Government regulation is like a graveyard spiral: you know something is dreadfully wrong, but unless you understand the signals, there is no way out. Regulation blinds an economy to signals comparable to an airplane's pitch and bank, signals that would let producers and consumers adjust their activities in response to their desires and available resources.

All too many people who otherwise understand the virtues of a free market become committed socialists when they reserve an airline seat. When they think of placing their precious hide in some fragile tube of aluminum hurtling along at nine miles a minute, six miles above terra firma, while dodging all the forbidding forces of Zeus and Mother Nature, their guts turn to battery acid. Suddenly they are eager for Big Daddy Government to protect them from all those capitalist pigs at the helms of airlines, who everybody knows are immoral, greedy profiteers who would sell their children to cannibals for the right price.

A recent *USA Today* debate on airline safety offered the political mainstream's usual false alternative between lots of government and *lots and lots* of government. The editors

held that too many violations go unreported, a situation they said would end with more Federal Aviation Administration inspectors wielding greater power to issue fines on the spot.

The editors lumped together every kind of violation. But not all violations are equal. Failing to dot an "i" in the aircraft logbook is a violation of federal aviation regulations; so is failing to install the bolts holding on the horizontal stabilizer. When these transgressions come to light, the public is scandalized to hear that there were *two violations*!

FAA administrator Jane Garvey, in her rebuttal to the editor's call for more regulation, correctly pointed to the dazzlingly good safety record of the airlines: 3.6 billion people on 55 million safe flights. Sleeping in your own bed is more dangerous! She credited government regulation.

That's a logical error, like concluding that x causes y because x precedes y. Goofy may suffer a streak of bad luck after breaking a mirror, but this conjunction of events is insufficient to show a causal connection. While the airlines' safety record is indeed impressive, that success is not half so impressive as it could be without government regulation. Allow me to explain this provocative assertion.

I have studied economics, history, philosophy, politics, and psychology for many years, and I have flown airplanes for 33 years. I know the aviation world firsthand. I fly DC-10s for a major passenger airline that uses these 300-seat jumbo jets to serve destinations all over the world. I have seen the inside workings of two regional and two major airlines. Significantly higher levels of safety will not be achieved by passing laws for our own good that threaten and intimidate peaceful people into behaving as the regulators decree.

Government Caprice

The federal aviation regulations comprise many volumes of boilerplate legalese that is variously interpreted by every regional office of the FAA. Despite the best will in the world, any pilot or mechanic can be found somehow in violation of something at any time. The interpretation of a regulation may have as much to do with an inspector's digestion as with the actual wording of any particular edict. This arbitrariness gives to regulators the power to examine each case "on its merits" and to enjoy the power to act with a "flexibility" that would delight a KGB agent. James Buchanan and F. A. Hayek have shown that such arbitrariness, which is the result of institutional incentives, frequently attracts those who lust after power.

When the regulators themselves cannot agree on what the rules mean (as is famously the case with such other documents as the Internal Revenue Code), then the rule of law has given way to rule by the arbitrary whims of those enforcing the police power. Those of us who are regulated then do business at the discretion of the government.

Most Americans would find it asinine to suggest that we live in a dictatorship, but what else can it mean when government forbids anyone to operate without its explicit blessings, or calls your ability to act peacefully on your own behalf a "privilege" granted by its largesse, and dictates—through the regulations of its dozens of agencies—virtually every detail of how a business is allowed to operate? The economic systems of Germany and Italy in the 1930s provided for private ownership of business, but the government dictated who could sell what to whom at what price, and the government decreed who, of which race, could be hired at what wages. If the soul of ownership is control, then we are experiencing a shift away from private ownership to state control of the means of production.

To insure that airlines fully complied with every regulation would require an inspector from each government agency with jurisdiction over the activity to hover diligently over each employee. But, as one wag put it, if people are too rotten to act responsibly, what makes anyone think the inspectors are any better than the inspected?

Lulling Consumers

Many customers mistakenly reason that if an activity is regulated, it must be safer than it would otherwise be. But government regulators don't make people safe. Aviation safety

results from the combination of people's own prudence as passengers and an economic system in which enduring success depends largely on how well airlines satisfy their customers' desire to travel affordably, conveniently, comfortably, and safely. Regulators can be duped by fraudulent paperwork and other antics. But customers, given a choice, can seldom be burned more than once before they turn elsewhere.

What best promotes these safe and pleasing outcomes? The free market. By "free market," I don't mean our mixed economy, the unholy marriage between big business and big government, in which special interests vie for success by lobbying for legislative advantages over their competitors instead of by satisfying their customers better than those competitors.

The elements of freedom in the mixed economy allow people to coordinate their activities and resources by mutual and voluntary action. When it intervenes, government forbids people to make voluntary choices according to their assessment of what will work best. Every action within the economic process is ultimately indivisible, as Ludwig von Mises pointed out so lucidly. Whether choosing a material, a supplier for an engine nacelle, a city to serve, or a price to charge, each action ultimately must be directed by the will of a single mind: that of a government bureaucrat or of a private individual. The idea of a "partnership" between business and government is as absurd as the notion of a partnership between a planter and the slaves who pick his cotton. In any disagreement, who gets the final word?

The Chimera of Risklessness

There is no such thing as absolute safety, contrary to the wounded, strident protests of such groups as the National Resources Defense Council, which finds even the tiniest risks anathema. The relevant questions are: how much safety, at what price, and who decides? So long as a legal system exists to protect individuals from violence and fraud, the safety of the flying public would best be served by the outright liquidation of the FAA.

"Oh, come on, now!" I hear lots of people protesting, with the exasperation of a practical, action-oriented American who hates pointy-headed theorizing. "That's voodoo economics! Ivory tower theory! Get real! What will protect people from fly-by-night predators calling themselves an airline?"

Disbanding the FAA would inform the public that its safety depends on its own judgment. In fact, this has always been the case, even when we think that regulators have done all our properly vigilant and wary thinking for us. Of course, it is absurd to expect ordinary people to become airline experts before buying a ticket. So how would they choose safe companies?

The power of reputation would once more matter hugely. A good reputation is not a perfect guarantor. But neither is the FAA. And I for one am happier with a sterling reputation maintained over a long time than with a government bureaucrat's stamp of approval. A good reputation is extremely hard to win—and quite easy to lose.

No airline with a desire to succeed in the long term could operate fast and loose with safety, because passengers would shun it. This is not just abstract theorizing. Observe how an outstandingly successful start-up like Air Florida found itself virtually without passengers from the day after its fatal crash of a 737 at Washington National airport until it financially bled to death shortly afterwards.

More technically accurate assessments of airline performance would be widely available through rating agencies similar to the Consumers Union, Moody's, Standard and Poor's, or Underwriters Laboratories. In the absence of the FAA, these companies would step forward to judge airlines, because the desire to stay safe would create a demand for this knowledge and the lure of profits would produce it.

Another powerful incentive for aviation safety in a free market is that no insurance company would dare cover an airline that operated without prudent procedures: the insurer would go bankrupt for covering a carrier that crashed airplanes willy-nilly.

Of course, a fraudulent start-up might somehow win capital enough to begin operations.

Con men have swindled people since the dawn of time. But solid research shows that while sleazy operators can fleece some folks for a little while, customers wise up. No company in a relatively free market has ever achieved any huge and enduring success without winning the continuing satisfaction of its customers.

In a free market, money changes hands because producers and consumers expect to be better off for the deals they make. This too is not just abstract theory. Without this expectation, they do not do business, absent a club over their heads. The purpose of government is solely to protect every individual's right to life, liberty, and property—a purpose it accomplishes by punishing fraudulent, predatory, and violent crooks.

Finally, here is the most important argument for disbanding the FAA and other regulatory agencies: the safety engendered by innovation. Regulation always benefits the status quo, the fat cats already in business. The status quo tends to fossilize a given level of technology with laws that make innovations difficult to implement.

Consider one among many persistent and annoying examples: airlines are chronically late out of some cities. Normal, occasional mechanical failures and company mistakes don't explain this problem. So why does it happen? The reason largely is that the FAA's air traffic control system can't handle the traffic.

Why is that system the world's largest consumer of vacuum tubes? It needs them in the antiquated radar systems. Why hasn't a more modern system been devised? Because air traffic control is a secure government monopoly, like the post office, and therefore has no incentive to accommodate itself to the preferences of its users.

Money is not a problem. We airline passengers have paid billions of dollars in ticket taxes for 40 years, ostensibly collected into the airport and airways trust fund to improve equipment and facilities. But the fund is a political football. Moreover, it is used to mask the full enormity of the federal government's plunder: in reports to the public, this money is subtracted from the federal debt!

By contrast to air traffic control's ancient technology, commercial airliners, created by companies that do stand a chance of going broke, haven't sported any vacuum tubes for nearly 40 years.

It was the Wright brothers, not Big Brother, who invented the airplane. Before long, Big Brother told Wilbur and Orville they needed a pilot's license. Of course, Big Brother's own efforts at learning to fly, contemporaneous with the Wright brothers, involved subsidizing Samuel Pierpont Langley, whose flying machine, launched repeatedly from a houseboat in the Potomac, did not fly so much as it tumbled into the river on each occasion. □

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THE FREEMAN
Ideas On Liberty

On Airports and Individual Rights

by Tibor R. Machan

For a couple of years, Orange County, California, has been buzzing with controversy over what to do when the El Toro Marine Air Base is closed. The question on everyone's mind is whether it will be transformed into an international airport by the local authorities. Airports of different sizes are being considered, but there are many citizens who would just as soon avoid the troubles they associate with a new airport.

In our time, such an issue is decided by a combination of federal, state, county, and local bureaucracies following various rules that have emerged over many years of similar haggling. Everyone considers the outcome a matter of public concern, and each citizen supposedly has an equal right to have his or her ideas implemented. Nevertheless, the authorities will make a decision driven by the special interests with sufficiently large constituencies and funds to make a serious difference.

In fact, there is no "right" disposition because the valid concerns of all the people expressing their demands are quite incompatible. The objectives of environmentalists, business people, and residents with various interests—the arts, commerce, education, science, travel, and more—are all over the map, and none can be given any rational public priority, despite what those who speak of the "public interest" would have us believe. The simple fact is that there is no public interest involved here. All interests are private and vested. The only bona fide public interest is one that actually benefits everyone equally. And there are very few such projects in any community—mostly they amount to keeping the peace and preserving the rule of law.

Resolving the Unresolvable

But could it be otherwise? Might there be some way of dealing with an issue of widespread yet still essentially conflicting concerns without several groups of people getting the short end of the stick?

Indeed, there is. Briefly, it involves the strict, unfailing protection of individual rights, specifically the right to private property.

Consider the proposal to have an airport in a community. How large should it be? Who will pay for it? And how should affected third parties be treated? In a system of private property rights, those who own the land in question have the authority to decide how it will be used. But that is by no means a simple matter.

For example, in a system of private property rights the use of a parcel of land as an airport may not place unwanted burdens on third parties—just as you may not dump trash on your neighbor's property. Thus, the operators of the airport may use it only in ways consistent with the equal property rights of their neighbors. Among other things, that means

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the operators will have to avoid impositions on their neighbors or offer them satisfactory compensation for the hardships.

One way to violate rights is to impose unreasonable noise on others. Serious noise during the night, for example, when folks are reasonably expected to be getting their rest, is a violation of individual rights. During the day the same degree of noise would not be a violation because nearly everyone is making noise as they go about their business.

Or take air pollution. At a certain level, "polluting" the atmosphere is normal—living itself produces waste that cannot be avoided. Yet to dump excessive, unreasonable levels of air pollution on third parties—levels not normal within a given realm—is to violate their rights. The details may be difficult to ascertain. But that's why we have courts and arbitration groups.

Rights Constrain Activity

Some people will say that stringent protection of rights would lead to small airports, at best, and many constraints on construction. Of course—but what's so wrong with that?

Perhaps the worst thing about modern industrial life has been the power of political authorities to grant special privileges to some enterprises to violate the rights of third parties whose permission would be too expensive to obtain. The need to obtain that permission would indeed seriously impede what most environmentalists see as rampant—indeed, reckless—industrialization. But it could also significantly impede environmental enthusiasts who gladly violate other people's rights in striving for their objectives (which at times involve returning to a pre-industrial age).

The system of private property rights—in which building, traveling, farming, woodcutting, and all other kinds of other human activity must be conducted within one's own realm except where cooperation from others has been gained voluntarily—is the greatest moderator of human aspirations, keeping them in balance with the diverse and reasonable aspirations of all others. In short, people may reach goals they aren't able to reach with their own resources only by convincing others, through arguments and fair exchanges, to cooperate.

Unfortunately, most special-interest groups —business, environmental, scientific, educational, artistic, and so on—construe their own objectives as superior to those of others. In the case of the El Toro facility, each side tends to believe that its cause is just and that the others are simply using financial and political muscle to thwart it.

In fact, however, many objectives are equally sound and should be carried out—within the limits of individual rights. Look at how this system of rights works in two areas of life: religion and publishing. Many different religions manage to co-exist in reasonable harmony, mainly because each group is able to operate unbothered within its own realm. Many diverse publications also manage to co-exist harmoniously. This, too, is largely because publishing organizations have the right to operate their own facilities and sell their own products unimpeded by the political and bureaucratic processes that govern broadcasting, public education, beaches, parks, and forests. In those areas, individual rights do not rule. Instead, there is a semi-democratic approach in which, at the end of the day, most people are left dissatisfied. Such is the "tragedy of the commons," especially in a country where most people implicitly (if inconsistently) believe the individual's pursuit of happiness is important.

There is, in short, no satisfactory answer to the El Toro controversy within our system of largely politicized social decision-making. But we are not necessarily stuck with this state of affairs. Eventually, we might transcend it. □



Privatize the Airports!

Waiting in long lines for everything from a boarding pass to a cheeseburger. Slow luggage delivery. Expensive parking. Jammed concourses. Surly workers. Small, dingy restrooms. Long walks from one flight to another that leave you worn out, with the only "consolation" being that the connecting flight is delayed anyway.

All that may sound like a scene from a Woody Allen movie set in some banana republic, but to midwestern travelers it rings with familiarity. It's just another day at Detroit Metro Airport, owned and operated by Wayne County, Michigan.

Thirty-six U.S. airports recently commissioned a survey of 90,000 passengers, who ranked Detroit dead last for overall quality. The poor rating comes despite hundreds of millions of dollars and many commendable efforts by county and airport officials to make Detroit Metro, in the words of director David Katz, "the most friendly place on the planet." Good intentions and lots of nice new carpeting notwithstanding, the aging airport is simply not keeping up with exploding traffic volume. The planned opening of a long overdue additional terminal in 2001 will help, but realizing Katz's ambition probably will require something much more dramatic and fundamental.

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Twenty years have passed since Congress deregulated the domestic airline industry. With airfares down and traffic volume up considerably, airports like Detroit's have experienced problems of congestion and a general decline in the quality of services. Though the general public is aware that *airlines* were deregulated (specifically, their fares and routes), what is much less known and appreciated is that almost all *airports* remain largely outside the marketplace, hostage to political decisions and budgetary concerns of the government entities that own and manage them. For consumers, the market has worked well in the skies. It's on the ground, where politicians and their employees rule the roost, that problems often seem frustratingly intractable.

These problems don't have to exist. A growing number of governments around the world are ending similar troubles, but they're doing so by making more than cosmetic changes. They are realizing that private for-profit firms have the incentive and the expertise to operate airports better than almost any public, politicized bureaucracy. These governments are privatizing the management and in some cases even the ownership of their airports. The results are impressive: privatized airports are far more innovative, efficient, and responsive to consumers than are public ones.

Twelve years after Great Britain sold seven of its largest airports in 1986—including Heathrow, Gatwick, and Glasgow—the program has proven successful by every measure. An astonishing 2.2 million citizens bought 1.4

billion shares in the newly privatized British Airports Authority (BAA). The flying public has been greeted with an aggressively entrepreneurial attitude aimed at pleasing customers. The airports themselves have undergone substantial physical improvements, and the British treasury has stopped being drained by subsidies.

The British model is spreading. Patrick Cowell, president and CEO of Airport Group International, reports that, "countries from Germany to Australia are now racing to privatize their airports." Operation and management of most of Canada's largest airports—including Vancouver—are now in private hands, as is air traffic control. This past November, I landed at Nadi International Airport in the Fiji Islands within days after it too went private, and I survived just fine.

In the United States there have been no outright sales of major commercial airports, but contracting with private companies for many elements of operation and management is taking off. Allegheny County in Pennsylvania contracted with BAA in 1992 to have it design, build, lease, and manage a retail complex for Pittsburgh International Airport. The resulting "AirMall" of commercial businesses—many entering the Pittsburgh market for the first time—has increased per-passenger sales at the airport from $2.40 in 1992 to $8.10 in 1997, generating at least 900 new jobs.

In 1995, the city of Indianapolis turned over the day-to-day management of Indianapolis International Airport entirely to BAA. The company agreed to a performance-based contract in which certain operations and maintenance-cost savings had to be met before it received compensation. That incentive spurred BAA to work hard to cut costs dramatically. At the same time, the addition of 22 new retail stores, 2,300 new parking spaces, and a shuttle bus service boosted non-airline revenue at the airport by 20 percent, with further increases expected. The next logical step—actually selling a major commercial airport to private owners—may occur within the next decade or so.

If Indianapolis and Pittsburgh—indeed, even London and Fiji—can privatize, why can't Detroit? One reason is the same political inertia that afflicts most government airports. As long as the airport is a patronage machine for the politically well connected, politicians naturally resist any move that diminishes their role.

Another reason that may be particularly acute in Detroit is organized labor. Excessive labor costs because of featherbedding and cumbersome work rules have characterized one Wayne County operation after another. For a privately run Detroit Metro Airport to happen, those practices must give way to more reasonable and hospitable labor-management relationships.

Yet another reason for the lack of privatization is the "Basic Agreement" that exists between Wayne County and the airlines, overwhelmingly dominated by Northwest Airlines. The agreement effectively gives Northwest a veto over the privatization option at Detroit Metro. The airline is worried about landing fees, among other concerns. (Interestingly, landing fees at Indianapolis have remained low and reasonable since BAA took over; the private company understands that gouging major customers is not in its interest.) Wayne County has done what no government should ever do: grant monopoly privileges to one firm when competition was not only possible but would surely have served the public far better.

There is nothing in the stars that ordains airports to be owned and managed by governments. Both economic theory and recent experience demonstrate that. The sooner airports are run by private enterprise, the better. □

THE FREEMAN
Ideas On Liberty

There's No Philadelphia in Europe

by Norman Barry

The member states of the European Union, in their struggles to find some form of international authority, are going through debates that have a strange resonance with America's arguments about constitutional forms in the late 1780s. However, there has been no Philadelphia—no equivalent European city at which the fundamental issues of freedom and constitutionalism have been thrashed out. Instead, there has been a steady accretion of power to central regulatory authorities in Brussels, either by international treaty or even more significantly, by innovative and creative decisions of the European Court of Justice, which is rapidly becoming what its U.S. equivalent took some time to achieve—the de facto creator of a constitutional order.

Even in its original structure the European Union (it's had various names in the past) was markedly biased toward the executive. The European Commission, executive arm of the EU, has always been more than a civil service. It actually initiates legislation, which is almost routinely passed by the Council of Ministers, the nominal legislature composed of representatives from the member states. The Commission keeps a close watch on them to prevent the emergence of any independent, competitive, and innovative actions. It normally wins cases against member states that it brings before the European Court. Indeed, Brussels, headquarters of the main governmental institutions, is rapidly becoming the capital of a new superstate.

In theory, the original Treaty of Rome (1957), which bound the creators of an economically integrated Europe, was not especially illiberal (in the classical sense). It embodied the "Four Freedoms"—of movement, of goods and services, of capital, and of labor—that constitute the sine qua non of a market society. International regulation was originally limited to the enforcement of the common rules of practice necessary for free economies. True, there were regulations that had immediate legislative impact on member states and directives that were adopted by local legislatures to fit particular circumstances. But in its early days, European-wide law did not automatically take precedence over the laws of member states; so there was some similarity with America's Articles of Confederation, which required the agreement of all states for laws to be nationally applicable. Unanimity was never achieved, and that is why the framers of the Constitution aimed to make federal law *directly* applicable to all Americans, as well as to permit direct taxation by the proposed federal government.

The End of Competitive Governments

In Europe, there was still the possibility of jurisdictional competition, which is the

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essence of federalism, up until 1964, when the *Costa v. ENEL* case was decided; the European Court held that European law was superior to any domestic law with which there might be a conflict. Nothing in the Treaty of Rome validates this legislative capture by the central body. It was simply another example of a centralized court asserting its power to create constitutional law. Ever since, the Court has expanded the power of the Council of Ministers and its legislation. As the American authors of the Anti-Federalist Papers said, a federal court is bound to augment central power at the expense of local autonomy: it reduces the effectiveness of "exit" (that is, voting with the feet), and eventually the domain of individual liberty is diminished. What is the value in moving to another state if all the laws are more or less the same?

Although the European authorities in Brussels have no direct taxation powers (they do have the power to set a minimum level of value-added tax) and the budget is financed by subventions from each member state, one doubts that this will survive very long. Encouragement toward a European-wide income tax will come about through the new European currency, which is under the control of the European Central Bank, an institution that will set an interest rate for all member states that join. (Britain negotiated an opt-out under John Major's Tory government, but this is not likely to survive the newly discovered Euro-enthusiasm of Tony Blair's Labour government.) With a monopoly currency, a central bank, and treaty obligations to maintain various fiscal targets, the tendency toward the promotion of European-wide economic policies will be irresistible. The power to tax, exercised in effect by a centralized state, will complete the European project.

It is a project that subjects European citizens to common economic standards, welfare arrangements, civil liberties, and ultimately most aspects of law. From its inception as the European Economic Community (a mere free-trading area with elementary uniform rules), each stage in its progress has been toward increasing centralization. The major developing institutional arrangements, from the Treaty of Rome itself through the Single European Act (1986), the Social Charter (1989), the Treaty of Maastricht (1993), and the Treaty of Amsterdam (1997), attest to this.

A Benign Beginning

Much of this evolution proceeded under the suitably benign banner of elaborating on the originally modest liberal project of fashioning the principles of a free market as envisaged in the Treaty of Rome. Indeed, some steps could easily find a rationale in public choice theory. For example, under the original arrangements, when unanimity prevailed in the Council of Ministers, progress toward a free common market was successively blocked by member states anxious to preserve anti-market privileges (such as restrictions on capital movement). In good Virginia-school style, qualified majority voting was introduced under the Single European Act, although unanimity remained in certain areas. However, this modest and necessary constitutional innovation soon made possible a mania for "harmonization": many competitive advantages were gradually eliminated so that every member state had to conform to uniform regulations on the environment, labor law, health and safety at work, and so on. A "social chapter" was introduced by which a common welfare policy was formulated.

Most of these standards were, in effect, set by the richer countries, especially Germany and France, which did not want competition from poorer countries anxious to attract capital by offering more favorable regulation. They were, in turn, "bribed" by significant financial redistribution. When countries attempted to avoid these standards, ways were found to thwart them. Britain tried to veto a directive limiting the number of hours in the work week (as proposed, unanimity was required), but it was carried as a health and safety measure, which can be passed under qualified majority rule.

Predictably, the European Court has been a complaisant actor in all this. It doesn't proceed like a common law court, working from case to case and deciding by purely legal reasoning, rather than on political grounds.

Instead, it tends to regard itself as being responsible for implementing the European "idea"; this of course lets almost anything in. Subordinate courts, for fear of being overruled, correctly anticipate what the European Court would do. Thus a British court struck down laws that exempted part-time workers from the anti-competitive requirements (including generous redundancy payments) enjoyed by full-time employees. It said that since most part-timers were women, the exemption was in breach of various equality provisions in European law. The court even had the audacity to add that this would have no effect on employment.

A great stride down the road to centralization was taken by the Maastricht Treaty (1993). This extended majority voting, introduced plans for a common currency (although not yet obligatory), and confirmed all the movements toward legal uniformity that had been previously established by the Court. The only interesting feature of the ratification process was the ruling of the German Constitutional Court in Karlsruhe. Although the legality of the treaty was upheld, (superficially) strict conditions were laid down for future European integration. Europe was declared to be a *confederation* of autonomous legal systems (to which European law was not superior), and no regulation or directive could abrogate any individual right protected by the German Basic Law.

This nicely contrasted with Britain's much-vaunted sovereignty system, in which its citizens had no recourse to constitutional law once its parliament had signed away legal authority by treaty. (There never was a British constitution.) It may have been a good thing for liberty that sovereignty was effectively renounced, but its replacement is hardly a bastion of freedom. The European Court may have been quite efficacious at striking down some national laws that were obstacles to economic liberty, but it has been singularly ineffective at protecting European market freedoms from regulations and directives from the Council of Ministers; the similarity here with the behavior of the U.S. Supreme Court since 1937 is striking. Whatever the German Constitutional Court may have said about Maastricht, there is no evidence that it will take a stand against European legislation; in fact, with scarcely a murmur it upheld Germany's abandonment of the *mark* on joining the European Monetary System.

What Is Federalism?

What the enthusiasts for Europe do not understand is that freedom is better protected by *competition*, both in economics and law, than by constitutional documents: "exit" always beats "voice" (democratic privileges).[1] This would be so even if the embryonic European constitutional documents were themselves particularly friendly toward liberty. It took the U.S. Congress and Supreme Court about 150 years to integrate the country under one more or less uniform economic, regulatory, civil liberties, and welfare system; Europe has done the same in less than 30. The elimination of constitutional competition in the United States was formally recognized in the notorious *Garcia v. San Antonio Transit Authority* case, where the Supreme Court, in defiance of the Tenth Amendment, said that federalism consisted merely in the fact that the states were represented in the Congress.

Europe has repeatedly given formal obeisance to the (originally Roman Catholic) principle of "subsidiarity," which in the Maastricht Treaty is held to mean that "in areas which do not fall within its exclusive competence, the Community shall take action . . . only if . . . the objective of the proposed action . . . can by reason of the scale of effects of the proposed action be better achieved by the Community." Subsidiarity is a kind of surrogate for genuine federalism. But even as a "parchment" protection for local autonomy, it is feeble. There is nothing like the precision of the original American Constitution, which at least does specify the areas of competence for the federal government and leaves the rest to the states. In Europe there is not even wording that can function as a principle for demarcating centralized authority from local. In any disputed area, the European Court will always side with Brussels.

One solution repeatedly recommended to stem the growing bureaucratization of Europe

is the closing of its "democratic deficit." It is true that European governmental institutions are not subject to much democratic accountability. The parliament has little or no formal legislative role (in fact, it is a rent-seeker's paradise, as is much of Europe), and the members of the Council of Ministers are only indirectly elected. But more "democracy"—that is, legislative authority for the directly elected parliament—is not the answer. People who make this case repeat the error of Madison, in Federalist 10, on the grand scale. He thought that the "extended republic" would remove the danger of faction because a federal system with divided legislative power would dissipate the malign effects of otherwise unrestrained majority rule. But he neglected the fact that modern-day factions, coalitions of interest groups, would form to plague the central legislature with sectional demands, and dispersed voters would have little rational incentive to control them. The same public choice considerations tell against a democratized Europe, for well-organized and committed minorities always have an interest in formulating (normally redistributive) policies that are inconsistent with the long-run aims and purposes of an apathetic and rationally ignorant populace. Only the objective enforcement of a universal rule of law, which protects property rights as well as civil liberties, can restrain potentially predatory government. Conventional majority-rule democracy is quite inadequate to the task.

One crucial feature of a genuine federal system is the right of exit from the constitutional arrangement: this is justified not merely on the ground of local autonomy but also as a prudential device to restrain the seemingly inevitable centralizing tendencies of all forms of government. For if enough provinces/states object to the actions of the general government, then that government will find it has very little left to govern over. There was always a great doubt about the constitutionality of secession in America, and a hypothetical federal government could go a great deal toward preserving that form by specifically acknowledging the right of exit.

It is continually debated now whether Britain (the least enthusiastic of member states) could *legally* leave the European Union. That question would appear to be answered by an obscure clause in the as-yet-unratified Treaty of Amsterdam, where it is declared that the Commission will bring actions against any member state thought to be in breach of its Treaty obligations; the case will be heard by the European Court. These are the two institutions least likely to be in favor of secession. There is, then, no right of exit; it is a permission that is never likely to be granted. Any such action by a member state will therefore be *political*, with all the adverse consequences that will follow from its exercise. Dover Castle may well be Britain's Fort Sumter.

It is not the case that British Euroskeptics are necessarily fanatics for parliamentary sovereignty, the very system that has done so much to undermine the market economy and the rule of law in their country.[2] What they fear most of all is the reproduction of that institutional phenomenon on a much more dangerous scale in Europe. There is no escape from its depredations except by the costly and time-consuming process of amendment by treaty. And the European rent-seekers will always be able to fend off any such move. The only virtue of retaining independent states (which could still bind themselves by minimalist general rules, mainly for promotion of free trade and protection of the right to free movement) lies in the possibility of preserving genuine institutional competition. This strategy has nothing to do with promoting grandiose schemes for a "more perfect union." □

1. See R. Vaubel, *The Centralisation of Western Europe* (London: Institute of Economic Affairs, 1995).

2. See my "Sovereignty, the Rule of Recognition and Constitutional Stability in Britain," in *Hume Papers on Public Policy*, vol. 2, no. 1, 1994, pp. 10–27.

THE FREEMAN
Ideas On Liberty

Come to America, John Paul

by David Boaz

You don't have to be Catholic to admire Pope John Paul II's role in undermining communism in Europe and his courageous visit to Cuba last year. Who else in the world could make Fidel Castro broadcast attacks on communism?

But some of the pope's most significant remarks in Cuba were almost lost in the media coverage, which focused on the delicate confrontation with Castro. Among John Paul's most provocative comments were those on education. Speaking at a mass in the city of Santa Clara, the pope called on parents to take back the responsibility of educating their children and chided the Cuban state for subverting the family's responsibility.

The pope's words found a ready audience among Cuban parents dissatisfied with the communist-run schools. But they are worth pondering in the United States as well, for they prompt some difficult thoughts about our own school system. Here's what the pope told millions of Cubans in his televised mass:

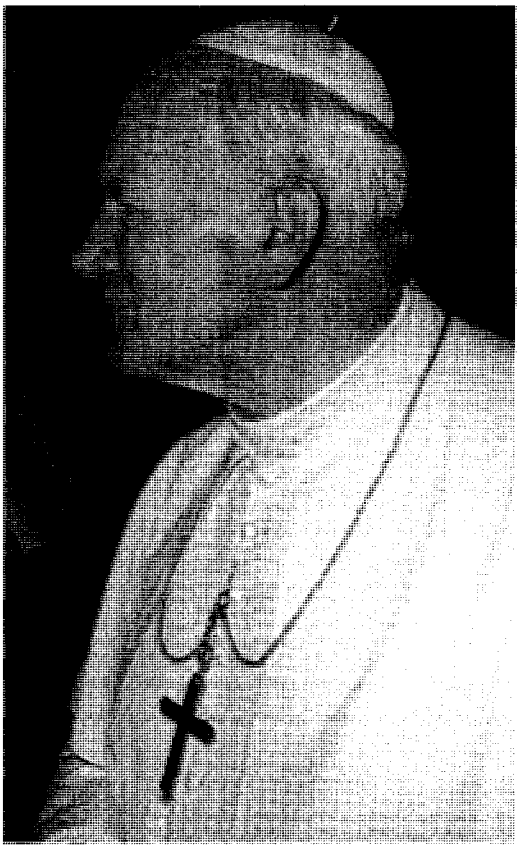
> Parents must be acknowledged as the first and foremost educators of their children. Their role as educators is so decisive that scarcely anything can compensate for their failure in it. . . . It is true that in the area of education, public authority has certain rights and duties, since it must serve the common good. Nevertheless, this does not give public authority the right to take the place of parents. Consequently parents, without expecting others to replace them in a matter that is their own responsibility, should be able to choose for their children the pedagogical method, the ethical and civic content, and the religious inspiration which will enable them to receive an integral education. They must not expect everything to be given to them; they should assume their mission as educators while seeking opportunities and creating adequate structures within civil society.

The pope's gentle but profound words were correctly understood as an indictment of Castro's schools, which teach children socialism, atheism, and anti-Americanism, no matter what their parents' values may be. Indeed, there's no question that in Cuba and other communist countries, the essential purpose of the schools is precisely to eradicate all traces of the parents' values, which are often religious or capitalist, and replace them with Marxist theory and submission to the communist state. All Americans, not just Cuban-Americans, must fervently hope that the pope's message will help to liberate Cuban children from the statist indoctrination of Castro's schools.

Does the American System Measure Up?

But how well does the American school system meet the pope's standard? Our own schools are mandatory and government run,

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Pope John Paul II

with little room for parental choice or control. Every line of the pope's message can be read as a criticism of our own educational monopoly—and perhaps also as a criticism of American parents who have let the state take over their responsibilities.

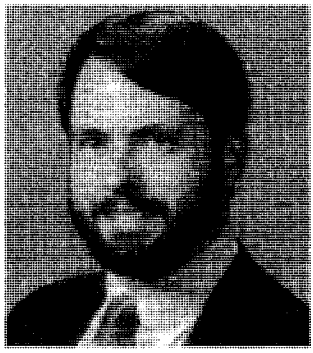
The pope says that "parents should be able to choose for their children the pedagogical method, the ethical and civic content, and the religious inspiration which will enable them to receive an integral education." Clearly, most parents can't do that today. Taxed to support the public schools, most parents feel unable to pay a second time for private schools that might better reflect their own values. Despite the Catholic Church's extensive network of schools, many Catholic parents feel too burdened by taxes and other living expenses to heed the pope's call. And of course American parents have virtually no control over the pedagogical method—that is, the style of teaching—used or the ethical values transmitted in their children's public schools. As for religious inspiration, that is entirely absent from American public schools. It's appropriate for government-run schools in a diverse society to avoid teaching religion, but that raises the question of whether the schools should be run by the government.

By the pope's standard, it would seem that American parents are being deprived of the freedom to exercise their responsibility to direct the education of their children. But American parents may find the pope's message a bit uncomfortable, in that it forces them to contemplate whether they are fulfilling their responsibilities as parents: "Their role as educators is so decisive that scarcely anything can compensate for their failure in it"; parents should not "expect others to replace them in a matter which is their own responsibility"; "they must not expect everything to be given to them."

The pope seems to be saying that parents must not relinquish their moral responsibility to direct the education of their children—and must not simply expect other people, or the government, to pay for something that is their responsibility.

That is not to say that parents must school their children at home. In fact, the pope points out that in "assuming their mission as educators" parents will "seek out opportunities and create adequate structures within civil society." In the pope's understanding, "civil society" means all the associations in society—churches, schools, clubs, and businesses—but not the government.

Parents, then, have a moral responsibility to direct the style and content of their children's education, government should not usurp their role, and parents should not expect education simply to be given to them. That's a message we should hear in the United States. The failure of our government-run schools is a direct result of government's taking over a critical family function and parents' abdication of their duty. Let's hope the pope's health will allow him to deliver this message in Washington, D.C., some day soon. □



Alliances: What's Friendship Got to Do With It?

America is the "indispensable nation," as Secretary of State Madeleine Albright likes to put it. But while the United States is supposedly indispensable, it can't seem to get along without allies—most of whom seem to think that the purpose of their "friendship" with Washington is to mulct American taxpayers.

The world is awash in U.S. allies. Most western and central European states are members of NATO; most eastern European nations yearn to join the organization. Allies fill East Asia—Japan and South Korea sport formal defense treaties, Australia enjoys regular military consultations, and the Philippines, Singapore, and Thailand benefit from less formal contacts. A score of Latin American nations are members of the decrepit Rio Pact.

Most of these arrangements were fashioned during the Cold War. Today, unfortunately, Washington's collection of allies is simply an economic and security black hole.

For instance, in Europe the United States pays to defend a collection of nations with more people and greater economic strength. To solve European problems of no concern to America, Washington is attempting to reconstruct Bosnia and micromanage the Kosovo civil war.

American policies make even less sense in East Asia, where U.S. forces remain on the front lines in Korea, a tripwire for involvement in any war, even though South Korea has 29 times the GDP and twice the population of the North. Washington is protecting Japan, the world's second-ranking economic power, from threats unknown. Almost every nation in the region expects the United States to solve any conflict arising from such parochial disputes as competing territorial claims over the Paracel and Spratly Islands.

Yet perhaps the most vivid example of the dead-weight loss created by unnecessary "allies" is Israel. There are few nations on which the United States has showered more money and support than Israel. In return Israeli politicians offer nothing but contempt, as evidenced by Prime Minister Benjamin Netanyahu's attempt to extort the release of Jonathan Pollard, convicted in 1985 of spying on America for Israel, as part of last year's Wye River peace negotiations.

At least during the Cold War there was a plausible security argument for a military relationship with Israel. But the United States never enjoyed any practical benefits. Although called an unsinkable American aircraft carrier, military aid always flowed from the United States to Israel, never the other way around.

Anyway, the Cold War is over. The United States can do just fine, thank you, without Israel's help. Indeed, Israel has made Americans less secure. Washington's support for Israel not only encouraged the Arab oil embargo a quarter century ago, but also turned U.S. citizens into targets of terrorists

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the world over. Were it not for America's perceived complicity in Israel's occupation of Palestinian land, Muslim fundamentalists might hate the United States no less, but they would be more likely to ignore than to kill Americans.

What is Israel's claim to the largesse lavished on it? Although a democracy among less free states, it has denied freedom to the Palestinians in its occupied territories for three decades. Anyway, there is no plausible security threat to Israel. It enjoys peace with Egypt and Jordan; however difficult their relations at times, war is extremely unlikely. Israel easily overmatches Syria, which also now finds itself threatened by Israel's unofficial ally, Turkey. And Israel's not-so-secret nuclear deterrent would make even the most extreme countries in the region—Iran and Iraq, for instance—think many times before striking.

Moreover, generous American subsidies have proven costly to Israel. It has one of the most socialized economies on earth, foolishness made possible by Washington's willingness to ship about $500 a person to Israel year in and year out.

This is the lesson of foreign aid the world over. Economic failure creates political pain, which forces economic reform. Foreign aid helps to mask economic failure and thus alleviate political pain—which, in turn, slows or stops economic reform.

Yet Israel retains the master key to the U.S. treasury and a claim to most anything else it wants. It is Washington's biggest foreign aid client, collecting $3 billion plus a year, not counting periodic special subsidies.

Muslim nations are equally undeserving of the aid they receive. The Camp David accords two decades ago promised billions for Egypt, informally pegged at two-thirds Israel's level. That money is almost entirely wasted, funding useless projects and propping up an inefficient, state-run economy. But the "aid," like Israel's subsidy, is beyond criticism.

The Wye accords will lighten the wallets of U.S. taxpayers even further. The Clinton administration has promised billions of dollars in weapons to Israel for use against who knows whom. Washington said it will dump additional billions into the hands of the corrupt and inefficient Palestinian Authority. In fact, the starting demands for economic assistance are $1.2 billion for Israel and $900 million for the Palestinians.

Even worse, the United States will be drawn more deeply into the region's fanatical currents. And the lead agency will be the CIA, reviled around the world for its intervention in the affairs of other nations, such as Iran (we must not forget the coup that helped return the Shah to power in 1953). The CIA will formally participate in a U.S.-Israeli-Palestinian committee "to assess current threats, deal with any impediments to effective security cooperation and coordination and address the steps being taken to combat terror and terrorist organizations."

Oh joy. Terrorism against the United States and its citizens will become even more likely.

Still, even this is not enough for Israeli officials. As the agreement was being wrapped up Prime Minister Netanyahu demanded the release of Jonathan Pollard.

Pollard, a former navy intelligence analyst, turned piles of documents over to America's alleged friend, Israel. Israeli officials, embarrassed at the spectacle of friends spying on friends, first claimed that it was an unapproved "rogue" operation. U.S. officials termed the resulting security breach "massive," and Pollard was sentenced to life imprisonment.

However, with time on his hands Pollard incessantly lobbied Israel to arrange his release. Israel finally admitted its responsibility and granted him citizenship. Then came Mr. Netanyahu's request.

Think of it. The U.S. subsidizes Israel and provides military aid for decades. America endures Arab hatred and terrorist attacks in return. Israel responds by spying on the United States, lying about it, and then threatening to block a peace agreement—for itself—unless Washington releases Israel's spy.

The end of the Cold War warrants a searching review of U.S. commitments around the world. □

Unhappy Returns

by Harry Dolan

On August 13, 1920, a confidence man named Charles Ponzi was arrested for running a pyramid scheme that had cheated investors out of millions of dollars. Ponzi had promised his investors a 50 percent return after 45 days, and he was able to deliver, at least in the beginning. As news of these fabulous returns spread, more and more investors were lured into the scheme. Of course, the money Ponzi collected was never invested in any wealth-creating enterprise: the "profits" of the earlier investors were paid with money collected from later investors. Ponzi kept his scheme going for less than a year. He was tried and convicted on federal and state charges and served a pair of lengthy prison terms. He was released in February 1934.

Later in 1934, by a kind of charming historical coincidence, President Franklin Delano Roosevelt appointed a Committee on Economic Security to study ways of dealing with financial insecurity, particularly among the unemployed and the elderly. The Committee's recommendations were embodied in the Social Security Act, which Roosevelt signed into law in August 1935. Under the resulting Social Security system, the payroll taxes paid by workers and their employers were not invested in any wealth-creating enterprise; rather, the contributions were used to pay the benefits of retirees.

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The members of the Committee were hardly con artists; they were sober and thoughtful people grappling with a serious problem. In the depths of the Great Depression, the plight of elderly Americans without reliable sources of income or family support was dire. But the remedy the Committee proposed was not some modest and temporary measure designed to relieve suffering: the system they helped put into place has become a (seemingly) permanent arrangement by which wealth is transferred from workers to retirees.

When Social Security was established, it may have seemed plausible that such a system could be made to work. In 1940, when the first monthly benefit payments were sent out, there were only 222,000 beneficiaries. The age at which one could retire and begin to collect benefits was 65, four years beyond the average life expectancy. The system was financed by a relatively small (2 percent) payroll tax, paid half by the employee and half by the employer, and the amount of income subject to the tax was capped at $3,000. Today there are over 43 million beneficiaries. The retirement age is set to rise to 67 in the coming decades—but even so, people are living far longer (around 76 years on average) and thus spending far more time in retirement. The payroll tax, after a series of increases over the years, rests at 12.4 percent, and the amount of income subject to the tax has climbed to more than $60,000—and still, no one expects the system to remain solvent long enough to shepherd today's younger genera-

tion of workers through their retirement. The Social Security Administration's own best estimates indicate that the system will fall far short of being able to pay its present level of retirement benefits beyond the year 2032.

The Culprit: Demographics

Unlike Charles Ponzi, the Social Security system never promised to make anyone rich—and it hasn't. At present, the average Social Security benefit replaces roughly 43 percent of the beneficiary's pre-retirement income (a replacement level of 60 to 85 percent is needed to maintain one's pre-retirement standard of living). The key to understanding this humble benefit level—and the system's long-term insolvency—lies in the demographic changes that have taken place in the United States since the system's inception.

These changes are actually a broader phenomenon, common to nearly all developed countries, and thus the Social Security crisis in the United States is mirrored by similar troubles in the old-age social-insurance programs of western European nations, Japan, and numerous other countries. The fundamental "problem" is that people are living longer and, at the same time, deciding to have fewer children. This leads to a general aging of the population, as more and more people live to collect retirement benefits—and go on collecting them for longer than ever before—while at the same time, proportionally fewer young people are in the work force paying into the system. The result is a declining "support ratio"—the ratio of current workers to current beneficiaries. In the United States, this ratio dropped from a high of more than 40-to-1 in the late 1930s, to 16-to-1 in 1950, to 3.4-to-1 today; it is expected to fall to 2-to-1 by 2030.

The declining support ratio is problematic for government pension programs because, as noted, these are essentially systems for transferring wealth from workers to retirees. In the language of policy analysts, they are predominantly "pay as you go" plans. Over time, as there are fewer and fewer workers to support each retiree, something has to give: payroll taxes must be increased, benefits must be cut, or the age of retirement must be pushed back (which is really just another way of cutting benefits). In the United States, Social Security benefits were essentially set at a fixed level in 1972, with mandated cost-of-iving adjustments (COLAs) put into place to ensure that benefits keep pace with inflation. The primary method of dealing with the declining support ratio has been payroll-tax increases, more than a sixfold rise since the beginning.

The burden imposed on workers by the current 12.4 percent payroll tax should not be underestimated: many workers pay more in payroll taxes (which are levied from the first dollar of wages, without exemptions) than they do in federal income taxes. And while payroll taxes are nominally paid half by the worker and half by the employer, in reality the worker bears the full impact of these taxes. The share paid by the employer is part of the worker's overall compensation package, and it necessarily reduces the amount of money available for wages and other benefits.

The most recent payroll-tax increase was passed as part of the 1983 Social Security amendments, which were intended to address the looming problem of how to finance the retirement of the "baby boom" generation. At their present level, these taxes generate a yearly surplus, which is invested in U.S. Treasury bonds (held in the Social Security Trust Fund). Thus, the current system is not entirely pay-as-you-go, yet it is still predominantly so, since the lion's share of payroll taxes (80 percent in 1998) is paid out directly to current retirees. Nevertheless, this "partial reserve" method of financing is expected to postpone the system's demise. According to the Social Security Administration's projections, yearly outlays (benefits) will begin to exceed income (payroll taxes) in 2013. At that time, in order to continue to meet the system's obligations, it will be necessary to begin redeeming the treasury bonds in the trust fund. This process is expected to extend the system's life until 2032, at which time the fund will be exhausted and income from payroll taxes will meet only 70 to 75 percent of obligations to retirees.

It is worth noting, however, that most critics of Social Security view the trust fund as a

dubious accounting device. As they point out, when surplus funds from payroll taxes are invested in treasury bonds, the federal government uses the money to finance its day-to-day operations. When the time comes to redeem the bonds, the government must come up with the money either through other borrowing, tax increases, or spending cuts. Depending on how palatable these various options are, the need to start cashing in the treasury bonds in the trust fund may precipitate a crisis long before 2032.

Poor Investment

The payments that individual workers and their employers make into the Social Security system are not, in a strict sense, investments. Unlike funds invested in equities, corporate bonds, or even savings accounts, payroll taxes are not put to productive use and do not earn a market return for the people who pay them. Nevertheless, those who retire after paying into the Social Security system do receive benefits, and these can be thought of as the "return" on their payroll-tax "investments." If we think of Social Security this way, we see that it has, over the years, become an increasingly bad investment—especially if we consider the rates of return that would have been available through other forms of investment.

During the early phase of any old-age social-insurance system, the typically high support ratio (the high number of workers per retiree) allows an excellent rate of return for retirees—as might be expected, since some people are able to collect full benefits from the system after contributing to it for only a few years.[1] As it turns out, however, the very best rates of return go to those who are between 30 and 50 years old when the program begins. This is because social-insurance programs tend to begin modestly (since a radical new program would be politically unpalatable), and benefits are gradually increased over time. Eventually, as the support ratio worsens, payroll taxes must be increased if benefits are to be maintained at the same level. Workers who come into the system late, after payroll taxes have been increased, will pay much more over the course of their working lives. Their benefits—even if adjusted each year to keep pace with inflation—will represent a terrible return.

Social Security in the United States has followed this pattern. For example, workers who retired in 1975 received, in just two years, benefits equal to their entire lifetime contributions. In contrast, a worker who retires in 2035 will take anywhere from seven to 17 years (depending on his income level) to get back the money he put into the system. That's assuming he lives long enough—and that the system is still around in 2035.

The gravity of the situation for young workers becomes clear when we look at the annual real (inflation-adjusted) rate of return on their contributions to Social Security. This rate is estimated to be 1 to 2 percent for most workers (although it may be as much as 3 percent for the very lowest earners).[2] And the situation may even be worse: economist Martin Feldstein estimates that those who are presently in their 40s or younger will earn a negative return: that is, they will actually receive less in benefits than they and their employers have paid into the system.[3] Compare this with the real rate of return on stocks, which has averaged 7 percent from 1926 to the present, or on a mixed portfolio of stocks and bonds, which comes in at around 5 or 6 percent.[4] The magnitude of the difference means that if workers were free to invest their money, rather than being compelled to contribute to a system that merely transfers their wealth to others, they could earn returns many times larger than those promised by Social Security.

In fact, William Shipman estimates that if workers born in 1970 were able to invest an amount equal to their Social Security contributions in stocks, they would (assuming they earned historically average returns) receive almost six times the benefits they would get under Social Security. Low-income workers would do less well, but would still receive almost three times what Social Security offers.[5]

Harnessing the Market

It is the prospect of these kinds of returns that has led some critics of Social Security to

call for privatization: they argue that it should be replaced by a system of individualized private retirement accounts, financed (as the current system is) through compulsory contributions. The difference, of course, would be that contributions would actually be invested (in some combination of stocks, bonds, and mutual funds), rather than being paid out as benefits to current retirees. The amount contributed, plus accumulated earnings, would be used to fund the individual's retirement. The model for this type of privatization is the system instituted in Chile in 1981.

Critics of this type of proposal point out that investing in stocks can involve substantial risks—to see this, we need look no farther than the 19 percent drop in the market between July 17 and August 31 of last year. That kind of volatility, critics say, is hardly a recipe for retirement security. The trustees of the Social Security Trust Fund appeal to this sort of reasoning in their 1998 annual report: "Social Security," they write, "is a compromise that assures all workers a modest retirement base on which they can, if possible, add a private pension and personal savings. The tradeoff for this safety is a lower retirement benefit than at least some knowledgeable individual investors might build over their lifetimes."

This is at least half true. The "retirement base" provided by Social Security is indeed very "modest," as we've seen—and is sure to get even modester after 2032 if nothing is done. But would only "knowledgeable investors" reap better returns by investing in private markets than they would through Social Security? In assessing the risks of investing in stocks, we need to look at the long term—and in the long term, things look good even for novice investors, assuming they recognize the limits of their knowledge and invest in broadly diversified mutual funds or stock index funds that track the performance of the market as a whole. Even during the worst 20-year period of stock market returns, which ran from 1929 to 1948, the market as a whole yielded a real annual rate of return of more than 3 percent—which suggests that even under the gloomiest of conditions, workers wouldn't do worse on their own than they would under Social Security. Indeed, if Feldstein is right and workers in their 40s and younger can expect a negative return from the current system, then any investment that merely keeps pace with inflation would offer a better deal than Social Security. If the dollar could be relied on to hold its value, you could beat Social Security's return by stuffing your payroll-tax money into mason jars and burying them in the back yard.

Reform Proposals on the Table

What can be done to address the serious problems facing the Social Security system? Congress is expected to take some action on the matter this year. The two main alternatives that seem to be emerging both involve using the potential gains from investing in stocks to shore up the system without radically altering its basic structure. The first alternative would simply invest some part of the present annual Social Security surplus in private financial markets, in the hope that higher returns would help to cover the shortfall that the system is expected to experience as the baby boomers retire. The best that can be hoped for from this option is to preserve the current system as it stands—to perpetuate the current meager level of benefits, which could not otherwise be maintained beyond 2032.

The second, more ambitious alternative is backed by Senators Daniel Patrick Moynihan and Bob Kerrey. It would attempt to salvage the current system by supplementing it with private investment accounts—into which an individual could divert 2 percentage points of the 12.4 percent payroll tax. Individual workers could choose how to invest the money in their accounts—at least within government-approved limits. The returns from these accounts would be added to the individual's standard Social Security benefits. Since diverting 2 percentage points of the payroll tax would actually worsen Social Security's long-term financial imbalance, the difference would have to be made up somewhere. Accordingly, the age of retirement would gradually be raised to 70 between now and 2029, and any further shortfall would be paid for out of general tax revenues (the plan

assumes that the overall federal budget will be running at a surplus).

A Better Alternative

Neither of these proposals challenges the fundamental assumption underlying Social Security (and old-age social insurance in general): the idea that society is responsible for ensuring some level of retirement security for all its members. Even a radical Chilean-style privatization plan (one that diverted all of an individual's contributions into a private retirement account) would not challenge this assumption, so long as the contributions remained compulsory.[6]

But the path to security does not lie in surrendering responsibility to society. Indeed, to live a human life is to embrace the responsibility of living long range: it is to realize that there may come a time when one will not want—or simply will not be able—to continue working. Planning for such a contingency is a profoundly moral issue. It is a weighty undertaking; there are any number of things that might go wrong. The assumption behind Social Security is that it is too heavy a burden for any one person to bear, so the collective will relieve the individual of the need to think and plan for the long run.

The irony is that the creators of Social Security failed to think and plan long range. The system they designed has—in less than the span of a human lifetime—reached a crisis. The burden of its payroll tax robs many people, particularly the poor, of the opportunity to make investments that might actually provide them with a comfortable retirement. It represents a deal that no one would accept willingly and that no one should be forced to accept.

The inevitable response to the suggestion that Social Security should be abandoned is that its elimination would betray current and future retirees who have assumed they would receive its benefits. Indeed, elimination of Social Security would require a costly transition. This fact is an indictment of the system itself, and can hardly be used as an objection against the system's critics.

What should ultimately replace Social Security? The Chilean-style privatization alternative mentioned above—essentially a compulsory savings plan—would undoubtedly provide a superior return for workers if it were properly implemented. Yet it fails to challenge the idea of collective responsibility that lies at the heart of Social Security, thus opening the door to large-scale government interference in private financial markets. The temptation to regulate investment for "the good of society" when the future of the nation's retirees is at stake would be strong. What's more, a compulsory private system would share Social Security's assumption that individuals are not to be trusted to plan their own lives. The regimented existence that any compulsory system must impose is, at root, incompatible with human freedom and human responsibility.

The real alternative to Social Security is privatization in a literal sense—the realization that planning for retirement is a private matter, that it should be left to individuals and their families, who would be free to seek the soundest advice they could find and make the best arrangements that were within their means. Such a system—which is really not a "system" at all—would be far more secure than Social Security, since it would not leave people at the mercy of demographics and support ratios—or of politicians. □

1. For an excellent discussion of old-age insurance, from which the account in this paragraph is drawn, see Daniel Shapiro, "Can Old-Age Social Insurance Be Justified?" in *The Welfare State*, ed. Ellen Frankel Paul, Fred D. Miller, Jr., and Jeffrey Paul (New York: Cambridge University Press, 1997).

2. Peter J. Ferrara, *Social Security Rates of Return for Today's Young Workers* (Washington, D.C.: National Chamber Foundation, 1986); Michael W. Lynch, "Retirement Plans," *Reason*, August 1998, p. 56.

3. Martin Feldstein, "How to Save Social Security," *New York Times*, July 27, 1998, p. A17.

4. Testimony by Carolyn L. Weaver before the Senate Committee on Finance, September 9, 1998.

5. William Shipman, *Retiring with Dignity: Social Security versus Private Markets* (Washington, D.C.: Cato Institute, 1995).

6. For details on how a compulsory private system might work, see Peter J. Ferrara, "Privatization of Social Security: The Transition Issue," in *The Welfare State*.

THE FREEMAN
Ideas On Liberty

Distrust and Verify

by Dwight R. Lee and Jeff R. Clark

Perhaps the most positive legacy of the Clinton administration will be that it further eroded the public's trust in the federal government. Trust has declined significantly since the Great Society programs of the Johnson administration. According to University of Michigan surveys, the number of people who responded that the federal government does what is right "always" or "most of the time" has dropped from 75 percent in 1964 to less than 30 percent in the mid-1990s.

Our view is that this decline in trust is a good thing because it mirrors rather accurately the performance of a government that has become less trustworthy. However, before making our case for less trust in government, we acknowledge that most people see the decline in this trust as a serious problem.

The Cart Before the Horse

People have worried about lack of public confidence in government for a long time. For example, Benjamin Franklin fretted that "Much of the Strength and Efficiency of any Government, in procuring & securing Happiness to the People, depends on . . . the general Opinion of the Goodness of that Government."

This was no doubt a legitimate concern in Franklin's day, when the federal government was undergoing a controversial birth and controlled little of the people's wealth. But today, with the federal government commanding over 20 percent of our income directly through spending, and significantly more through regulation, some are still concerned that confidence in government might be too low to allow it to seize more of our resources. For example, Joseph Nye, dean of Harvard's Kennedy School of Government, worries that "if people believe that government is incompetent and cannot be trusted, they are less likely to provide [critical] resources. Without [these] resources, government can't perform well." Studies investigating the decline in trust, and fueling concern about the consequences, have been published recently by the Kennedy School, University of Virginia, and Pew Research Center for the People and the Press.

These studies sometimes admit that government's performance leaves something to be desired, but suggest that the best way to improve its performance is by restoring trust in it. This puts the cart before the horse.

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Where is the advantage in placing more trust in an organization whose performance does not justify trust? How many people needing heart bypass surgery would trust a surgeon who kills most of his patients on grounds that he will become a better surgeon only if more people trust him?

The only sensible way to restore trust in government is by making it more trustworthy. And a trustworthy government is more likely to be undermined by too much trust than by too little. Indeed, a major reason government performs so poorly is that persistent political influences encourage citizens to put far too much trust in it.

The Arithmetic of Voting

Public trust is easily transformed into political power that will be used to promote private advantage at public expense. The reason is rooted in the simple arithmetic of voting. Voting is an important civic responsibility, and nothing here is meant to suggest otherwise. But in state and national elections, the probability of your vote deciding the outcome is far less than that of being injured driving to the polls. This means that favoring one candidate or proposal costs you almost nothing in terms of sacrificing the alternative. Only in the rare case of a tie is your vote decisive; only then does your vote for one alternative cause you to sacrifice the other.

This arithmetic is important because it explains why charisma and emotion can trump substance in politics. Registering support at the polls for a superficially attractive candidate or a superficially compassionate proposal allows a voter to identify with the glamorous or feel virtuous with little concern about cost or effectiveness. For example, if voting for a proposal to combat "global warming" (or for a candidate who supports the proposal) makes you feel good, you might be tempted to shelve any doubts and vote regardless of the cost to you if it passes, since your vote is not decisive. The more people trust government, the more virtuous they feel when voting for a wide range of government initiatives that end up costing far more and delivering far less than promised.

Exploiting the Public's Trust in Government

The nature of government programs enables well-placed interest groups to capture private benefits at public expense. The Environmental Protection Agency (EPA) has increased the size of its budget by championing command-and-control approaches to reducing pollution. Market-based measures are more effective and cheaper, but require fewer bureaucrats and have been resisted by the EPA. Industry groups (such as the eastern coal industry) have also supported command-and-control approaches to protect themselves against competition (from low-sulfur western coal), at the expense of consumers (higher electricity prices) and environmental quality (more sulfuric oxides in the atmosphere). The list of government activities supported by well-intended citizens, but perverted by organized interests, is painfully long.

Every interest group wants to convince the public that government can be trusted to promote the general well-being by increasing some spending or regulating. The result is a steady stream of rhetoric aimed at making people feel good about trusting government to solve almost every imaginable problem.

Unfortunately, a widespread belief that discretionary government power can and should solve every social problem is incompatible with government's performing well. Such trust leads to politically compelling demands for government to do lots of things it has no business doing, with the result that it does poorly the few things it should be doing.

The best way to make government more trustworthy is for voters to resist the temptation to achieve a cheap sense of virtue by voting for every "virtuous" proposal that comes along. The real virtue is in voting against most government programs (and the politicians who support them), no matter how virtuous those programs are supposed to be.

We need plenty of public skepticism toward government to counter the voters' tendency to support government activities that purport to "do good" with power that will invariably be captured and corrupted by special interests. A trustworthy government requires a healthy measure of public distrust. □

THE FREEMAN
Ideas On Liberty

Sen or Sense

by Barun S. Mitra

In the battle over economics, the victory of the market seemed decisive. It had not been easy. Since the days of Adam Smith, the world economy had to cross the turbulent waters of colonialism, mercantilism, socialism, fascism, and communism before liberalization, globalization, and privatization became accepted as part of our general vocabulary. But even before the process of consolidation is over, it now seems that free market ideas are faced with insidious threats as never before.

Indeed, the popular appeal of socialist ideas was not primarily based on economic principles but on ethical and political ones—an egalitarian world view. (Discussions rarely focused on the morality of the methods that would be necessary to create such a world order.) On the other hand, many advocates of the free market rarely went beyond economics and utility, and generally ignored the moral basis of the marketplace.

This is best reflected in the criticism of the market that has inevitably followed as the so-called "transition" economies in eastern Europe, Russia, and Latin America have run into rough weather. This criticism has gained considerable credibility after the turmoil in the currency markets in Asia over the past year. Not surprisingly, "liberalism with a human face" has become the new mantra.

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No one today epitomizes this sentiment more than Amartya Sen, the Indian-born 1998 Nobel laureate in economics. In a congratulatory message the president of India, K.R. Narayanan, said, "You have brought to bear upon the science of economics a compassion for the ordinary human being and a vision of an egalitarian world society."

Empowering the Poor

Sen's recipe for inducing long-term sustained growth involves empowering of the poor through education, health, entitlements, and removal of gender disparity. His method for delivering these services is democracy. And he mainly rests his case on the evidence that independent democratic nations have been more successful in eliminating famines than others.

There is much more than a grain of truth in Sen's arguments. However, grains are necessary but not sufficient for a balanced diet. Democracy may be a necessary condition for alleviating poverty, but it is not a sufficient condition. Otherwise, India, the largest democracy, would not have remained in the club of poorest nations of the world.

Let us take a closer look at a few of Sen's propositions in broad context.

Democracies, with periodic elections and a free press, keep elected representatives on their toes and the government more responsive to the population. In times of large-scale tragedies, such as famines or floods, when

opposition parties and the media are on the lookout for opportunities to discredit the authorities, representatives work overtime to get as much relief as possible to their constituents.

Indeed, so successful has this process been that, today, whether in the United States or India, politicians continually vie with each other to declare some of their constituents victims of one disaster or another—famine, flood, fire, cyclone, earthquake, crop failure, indebtedness, bankruptcy, job loss, child neglect, old age, to name just a few. Pork-barrel politics is the natural outcome of such an approach. After all, if the benefits can be appropriated to a few and the cost distributed among the whole population, it would be irrational not to try to corner as large a share of the "public pie" as possible.

Apart from the social and economic damage it may cause, this approach legitimizes state intervention through control and expropriation, even if only in the "social sectors." Once that approach to governance is accepted, it becomes almost impossible to draw a line, since all such intervention is always justified by some alleged social good.

Moreover, this governance becomes extremely short-sighted, moving from one opinion poll to another, from one election to the next. Such a government is hardly ever in a position to concentrate on programs that require a much longer time frame, for example, education or health, two of Sen's principal concerns. On one hand, he laments the failure of the leftist forces in democratic India to capitalize on their natural constituency among the poor by stressing these two most basic of "entitlements." On the other hand, he points to the success of the non-democratic, socialist economies in those areas, implying an astonishing lack of regard for the methods that were adopted by these countries to achieve that "success."

There is no doubt that education and health care are the two basic tools with which an individual can improve himself. So Sen's concern for those who apparently cannot secure these, and his fear that they may not benefit from a liberalized and globalized economy, need to be addressed.

The Power of Vested Interests

As Sen consistently points out, the performance of the Indian state in primary education and health has been dismal. Indeed, the power of vested interests and pork-barrel politics in the field of education is distinctly visible. For instance, in a country where almost half the population is considered illiterate, higher education is most heavily subsidized! Or at a time when provincial governments can only try to ensure at least a primary school within a reasonable distance of every village, students in Delhi travel almost free to their colleges and universities. Icing on top of their cheap education cake! Another problem is that the content of education has been completely politicized.

Furthermore, there is no real evidence that opposition to liberalization comes from the millions of illiterate, low-skilled workers, an overwhelming majority of whom are engaged in the informal and unorganized sectors of the economy. They provide a range of goods and services—from collecting garbage to manufacturing vehicles—which either the state has failed to deliver despite promises or which the formal sector has been unable to provide. (There is no welfare to speak of.) Clearly, then, the basic problem is not lack of education, but almost total lack of employment opportunity in the formal sector.

According to official estimates, barely 30 million of India's work force of 400 million are in the organized sector. Not surprisingly, it is this small but entrenched minority, who fear the loss of their unearned privileges, that are at the forefront of the anti-reform group. Their share of the national pie is best indicated by the fact that since the 1970s, while the consumer price index increased by about 750 percent, per capita emoluments rose by a whopping 1,600 percent—a remarkable demonstration of the power of vested interests. The only other explanation is an amazing increase in their productivity. No wonder that the quartet of politicians, bureaucrats, organized labor, and businessmen who have benefited from state patronage and thrived in a protected environment are so keen to defend the status quo.

By adopting the "socialist pattern of development" since the 1950s, the Indian state has been very successful in choking the economy and thereby wasting the most precious of all resources, the spirit and enterprise of her people. As P.T. Bauer, the other development economist deserving of the Nobel Prize, has said, it is policy not poverty that keeps people poor.

The result of Indian socialism has been rampant underemployment, and consequently there seems to be little rational basis for the illiterate to demand better education. Is it any surprise that despite an enrollment of over 90 percent at the primary-school level, the dropout rate after five years ranges between 35 and 40 percent.

Land Reform

Another issue Sen has stressed is land reform. But even the much talked-of land reforms in states like West Bengal have not been able to stimulate growth. Forcible land distribution has led to fragmentation of holding, and productivity has not improved much as a result. This has led to the rise of political brokers in the countryside and forced people to stay on the land. Lower labor mobility has permitted the state government to ignore the virtual collapse of the industrial sector. Bureaucrats are more concerned about preserving the privileges of the existing work force than about increasing employment opportunities. Clearly, land reform in West Bengal has, perhaps unintentionally, helped slow the pace of urbanization, industrialization, and, consequently economic growth. Seen in this light, it should not surprise anyone that West Bengal, which peaked in those respects in 1947, has been sliding over the past decades.

Land reform is necessary. But this cannot be isolated from general economic policy. Today, the state is the largest landlord and is increasingly involved in disputes with indigenous people, whose title to their traditional land is not recognized. Rural communities are being torn apart by contentious litigation and frequent violence. Maintenance of land records by state governments is pathetic and open to rampant manipulation and corruption. Also, land reform cannot be a one-way street to land distribution. There is an urgent need to recognize that productivity, efficiency, and economies of scale are as relevant in agriculture as they are in other sectors of the economy. By obstructing consolidation of landholding in the name of land distribution, India has been spectacularly successful in making agriculture unviable, sealing the fate of the 70 percent of the population that lives in perpetual poverty in our countryside.

To successfully move away from this self-destructive course, a new vision is required. Sen's concern for the poor, the hungry, and the deprived runs very deep. But there is a need to go beyond good intentions, which, though necessary, cannot be sufficient for the alleviation of India's ills. Sen deserves credit for highlighting the need to re-establish the relationship between ethics and economics. However, the ethical premise may have to be quite different from the one Sen proposes.

The Morality of Free Exchange

It must be recognized that voluntary exchange in the marketplace is infinitely more moral than expropriation under the sponsorship of the state. It has to be acknowledged that the best way to empower the poor is to allow the market to operate unhindered so that even the poorest have the widest range of options.

The world has taken over two hundred years just to begin to appreciate the power of Adam Smith's "invisible hand" in economics. Let's hope we don't take another two hundred years to appreciate the morality of the marketplace. It will be a tragedy if after winning the battle over economics, the war is lost on ethics. □

THE FREEMAN
Ideas On Liberty

Abolish Legal Tender

by D. Alexander Moseley

An advertisement in an English newspaper offers a one-million-dollar bill for sale—at the remarkably reduced price of £29.95 (about $50.00). However, this great deal comes with the words "Not Legal Tender." Thereby the advertisement unwittingly presents the essential problem of national currencies in a nutshell. Two magic words are all it would take for the note to become spending money. Surely, monetary policy cannot be that simple? In an age of government-issued currencies, unfortunately it is.

Government control of national currencies has not been stable or beneficial to say the least. In the last year, currency crises hit the news frequently. The resulting lack of confidence in a nation's currency means that international investments will seek more profitable ventures where the fear of devaluation is not so acute. Devaluation follows from governments' inflating their currencies through central banks and fractional reserve banking; as money is "created," exchange rates are affected and investors have to reconsider their projects.

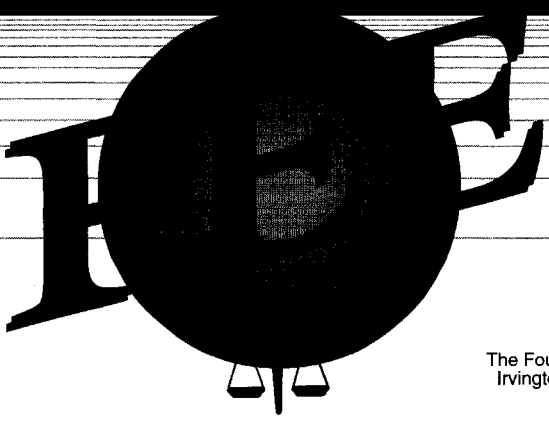
Traders have long learned to avoid a great part of exchange rate risk by employing currency futures and options. Even so, an unanticipated currency movement can have a deleterious effect on a company's profit forecasts and its investments and employment. The ensuing effects on national economies can be disastrous; yet the cause is not difficult to define. It lies with the uncritical acceptance of legal tender rules. By maintaining those rules, national governments permit their central banks to issue base money—effectively paper, although soon it could be electronic cash—at their discretion. Any central bank has the legal power to print a run of million-dollar bills, define them as legal tender, and create new money out of thin air.

Rippling Effects

The repercussions of legal tender laws are quite visible: by printing paper the central bank inflates the currency. Some of that currency will seep into loan markets, affecting interest rates; some will affect particular price ratios in markets, causing economic dislocations; some will enter the foreign currency markets, reducing the price of the national currency in terms of other currencies. Overall, local prices will rise and the exchange rate will fall. The effects are complicated by the actual paths that the new money takes, but the overall qualitative result can be ascertained—resource allocation is distorted and irrevocable damage done. It does not matter if the central bank's inflation was anticipated beforehand—something that modern macro theory attempts to argue—for no one is in a position to pursue the transactions of every single new note printed. Therefore, no one is in a position to establish the overall quantitative effects until afterwards, at which point the damage has been done.

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N O T E S F R O M



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February 1999

Countless Wonders

On a recent drive through an affluent San Francisco neighborhood boasting truly spectacular homes, I did what almost every ordinary person does in such circumstances: I wondered to myself, "What can *I* do to earn enough money to be able to afford such a home?" My thinking continued: "To earn such wealth requires that I produce a product that lots of people value more than it would cost me to produce. Okay! Good! I've identified the general formula. Now all I need to do is to think of a product for which people will pay a price higher than my cost of production."

"What can I produce? . . . What can I produce? . . . What creative idea can *I* come up with that will earn me a bundle? . . . What can *I* produce? . . . Think, Don: think, think, THINK!"

Melancholy engulfed me as I drew a blank—the same embarrassing blank that I drew on each of the thousand-and-one previous occasions when I tried to think of a new product or service that consumers would value.

Fact is, I possess absolutely no such entrepreneurial creativity. None. Zippola.

And yet, despite my mind's barrenness on this front, how fortunate I am! How amazingly, breathtakingly fortunate—and wealthy—I am!

My good fortune is that I live in a society in which I benefit immensely and directly from other people's creative ideas—no one of which *I* would have dreamed up in several lifetimes. The distinguishing feature of a depoliticized free-market economy is that it not only inspires creative people to create, but it also inspires these creative people to create things and processes that benefit even me and others who are hopelessly non-creative.

Here's what I mean. I'm writing these words somewhere over the State of Utah as I hurtle toward New York City at a speed of 600 miles per hour. Less than a foot from my arm the air temperature is 50° Fahrenheit below zero. And yet I'm cozy, comfortable, and safe as I sip complimentary gourmet coffee. Two hours ago I was in California; three hours from now I'll be in New York. My thoughts are being recorded (with help from my fingers) on a laptop computer that has more computer power than was on Apollo 11. I can check my e-mail messages by plugging my laptop into the telephone nestled in the seat in front of me.

Each of these wonders—and they *are* wonders!—is made possible by countless creative ideas of people whom I don't know and who don't know me. I am responsible for none of the ideas that

enable me to write on a computer as I fly safely across the continent. But here I am, the happy beneficiary of these astonishing creations.

What's more, I'm an ordinary American. I'm not rich by modern American standards. But so what? In truth, I'm astoundingly wealthy. I (like nearly all other Americans) can acquire these luxuries in exchange for just a tiny fraction of my work time.

Let's tally up the cost to me, today, of the luxuries that I identify above. The round-trip coach airfare is $338. My new laptop, complete with modem and all of the requisite software for word processing and for e-mailing, costs a total of $2,000. Because I'll probably keep this laptop for at least two years, the *daily* cost to me of this laptop is no more than $2.74 (which is $2,000 divided by the 730 days that there are in two full years). To check my e-mail will cost me about $35 in telephone charges—a figure calculated on the assumption that I'll be on the air-phone for ten minutes (which is far more connect time than I'll probably need).

So what do we have? All told, it costs me a paltry $375.74 to fly from New York to California and back *and* to write this column en route *and* to check my e-mail. $375.74—that's all! A mere $375.74 is all that I paid to do what twenty years ago no one at all could do, and what only four or five years ago only the wealthiest of the wealthy could do.

Yet today laptop computing on a jetliner is so common in Western society that we take it for granted. My fellow passengers are no more astonished to see me typing on my laptop than they would be to spot a pigeon in Central Park.

The 1997 annual report of the Federal Reserve Bank of Dallas is entitled *Time Well Spent: The Declining Real Cost of Living in America*. I encourage you to read this remarkable document. (Note: The Dallas Fed is something of a renegade among government agencies. Its leadership and staff of economists rank among the most free-market-oriented group of scholars in America today.) The report's authors—W. Michael Cox and Richard Alm—document how the real cost of living in America has fallen dramatically over the past century, and how it continues to fall. Cox and Alm measure cost of living by using work time—the amount of time the typical American worker must labor to purchase various goods and services.

Almost any good or service you can name costs less work time today than it cost just a few years ago. For example, in 1984 the typical American worker had to work 435 hours to purchase a personal computer. Today, a vastly more powerful computer is available for only 76 hours of work by the typical American worker. A cell phone in 1984 cost 456 hours of the typical American's work time. A much better cell phone today costs a mere nine hours.

Of course, many goods and services that we today take for granted could ten years ago be purchased at no price whatsoever—such as checking e-mail from a commercial jetliner.

The marvels to which we each have daily access are the product of millions of creative minds figuring out how better to please consumers—by producing new or improved products and by reducing the costs of producing existing products. Many of these creative people earn (and deserve) millions of dollars; some earn (and deserve) billions of dollars; most earn handsome but not princely sums. Everyone, however, in industrial society profits greatly from every market entrepreneur's creativity.

I need not lament that I, personally, have no creative, productive ideas. I have the great good fortune to live in a society that encourages truly creative people to share the fruits of their creativity with me. My blessings are literally too great to count.



Donald J. Boudreaux
President

FEE Heritage Book Sale

Throughout its history, a number of notable authors have been associated with the Foundation. This month we highlight that legacy by featuring the works of former FEE staff members and Trustees. In each of these books you'll find a discussion of some important aspect of the freedom philosophy. Moreover, each work reflects the studied inquiry of a lifelong defender of liberty.

American Federalism, George C. Roche III. George Roche is now President of Hillsdale College, but prior to going to Hillsdale in 1971, he was Director of Seminars at FEE. A talented historian and biographer of Bastiat, Dr. Roche is also a uniquely capable advocate of individual liberty and free markets. *American Federalism* is one of our older publications, but its message remains imperative. In it, Dr. Roche discusses the intellectual origins of our federal system, how federalism developed in the 19th century and then, sadly, eroded in the 20th. In his concluding remarks, he calls for a return to a decentralized political system and a reinvigorated moral ethic of individual responsibility. This concise pamphlet explains why limited government is the best government—an excellent choice for handing out!

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Can Capitalism Survive? Benjamin Rogge. Dr. Rogge was professor of political economy and dean at Wabash College and a FEE Trustee for many years. He is remembered fondly as a much valued regular lecturer at FEE's Seminars. This truly insightful, clear, and eloquent book is, like *American Federalism*, one of our older titles but, is it ever good! Starting from Joseph Schumpeter's famous hypothesis that capitalism cannot survive because its success inevitably undermines the social institutions that protect it, Dr. Rogge examines the case for economic freedom, the libertarian philosophy, and the nature of economics. He looks at several topics in some detail: money, labor, education, and cities. He concludes with a challenging discussion of FEE's role as a disseminator of these ideas and as a force for change in the United States.

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Faith of Our Fathers, Mary Sennholz, ed. Back in the late 1940s and early 1950s Mary Sennholz (then Homan) worked for FEE's founder, Leonard Read. She returned to the Foundation in 1992 with her husband, Dr. Hans Sennholz. From 1992 until 1997 Mrs. Sennholz helped the Foundation with its book publication program. *Faith of Our Fathers*, published in 1997, contains essays by Clarence Carson, Ridgway Foley, George Roche, F.A. Harper, Ben Rogge, and Ed Opitz, among others. The authors discuss the importance of the natural-rights philosophy for the Founding Fathers while also examining the negative influence of the 19th-century doctrine of positivism. This compilation is a useful resource for all students of history, philosophy, and freedom.

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Reflection and Remembrance, Hans Sennholz. Dr. Sennholz was a long-time Trustee of the Foundation as well as a regular seminar lecturer. From 1992 until 1997 he served as President of the Foundation. Dr. Sennholz is known for his knowledgeable and enthusiastic support of the Austrian School of Economics. This book collects his "Notes From FEE" columns. Grouped into six categories, these essays address first principles, education, the poverty of politics, ideas and policies, a look abroad, and the future. This anthology presents a broad overview of Dr. Sennholz's unique perspective.

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THE FREEMAN
Ideas On Liberty

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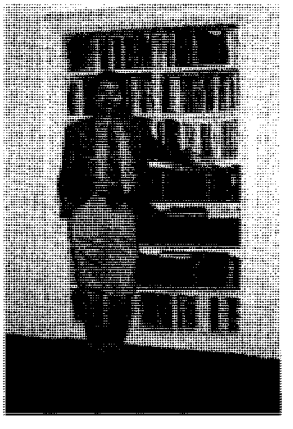
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Don Boudreaux

Donald J. Boudreaux
President

Contributions can be made by telephoning (800) 452-3518 and using your Visa, MasterCard, American Express, or Discover Card, or by using the reply envelope included in this issue. For those who have recently contributed, a heartfelt thanks from the entire FEE staff and Board of Trustees.

The inflationary policy can only be effective *if governments decree that the notes be deemed legal tender.* Legal tender imposes on traders the requirement to accept the note at its face value. Therein lies the rub. If the government had to pay off a million-dollar debt but could not stomach a rise in taxation, its central bank could print the necessary legal tender bill, and the newly printed note could discharge the government's debt. Such an action costs the government nothing but the paper and ink the note is printed on, and traders cannot discount the bill except through increasing their prices.

Legal tender thus provides national governments with a covert method of raising funds without raising taxes. But once the money seeps into the foreign currency markets to pay for increased imports or to pay off debts, the currency must depreciate, for in the international arena traders mark down the value of the currency against others.

It would be otherwise for national traders if legal tender laws were abolished. Under a free tender scenario, traders would use those currencies in national and international trade that prove to be useful to them—that is, those that keep their value. Which currency traders would choose is not something that can be determined by legislation or a priori; the choice is fully in the hands of the millions of traders in millions of markets.

If legal tender laws were abolished, traders would discount government notes in local as well as international markets, which would remove from government the possibility of earning revenue from inflation (that is, paying off debts with legal-tender devalued currency). The resulting effect is the reverse of Gresham's Law, in which bad money drives out the good. Gresham's Law prevails when legal tender rules apply; however, if traders were free to choose between currencies, the good money would drive out the bad, a point noted by F.A. Hayek. Ample evidence of the Hayek-Gresham Law can be found in economic history from early American currency history to pre-Revolutionary Russia and to the more recent hyperinflations in which street traders clamor for alternative currencies such as the dollar and deutschmark.

Money Can't Be Invented

Legal tender laws effectively have nationalized currencies, making them the prerogative of the state. Economics teaches that money cannot be invented or created by decree, that it is very much the result of traders' decisions across many markets and over much time. It is time to return currency to the market.

With free choice in currency, traders would converge on the money that best suited their needs. In the last two decades economists have conjectured what forms such money could take, from electronic cash to redeemable currencies, some redeemable against a basket of goods or even a basket of futures, or against gold and silver. What is certain is that the choice is and should be the market's. No one can predict the media that present businesses would find most useful—most probably they will converge onto one medium or onto a few universally accepted media, but the definite result would be an end to the credit creation and inflationism of central banks and national governments. Central banks would most certainly lose their powers, but currencies would lose their chains. □

THE FREEMAN
Ideas On Liberty

Small Is Awesome

by Max More

Giant corporations controlling national governments. Corporate behemoths regimenting their workers, controlling their customers, and obliterating their smaller competitors. The rich get richer and the large get larger until a small handful of megacorporations rule the planet.

We have heard this warning about King Kong capitalism from Marxists and other statists for decades. The future is always about to bring about the death of small companies and individual initiatives. Since the 1980s a new, popular form of science fiction known as "cyberpunk" has reinforced this view in the popular imagination. Books such as William Gibson's *Neuromancer* suggest that our economic system will become utterly dominated by a few faceless bureaucratic megacorporations. One of the great appeals of a free-market economy is precisely that it promises to distribute power widely. But the image of the future being pushed at us will undermine that appeal if it goes unchallenged. Ironically, the result will be a call for more intervention by the state—the most monolithic, bureaucratic institution imaginable.

Those who understand how free markets really work have long responded to these dire predictions with economic theory and history. We know that harmful monopolies have little chance of forming and surviving without government intervention, whether in the form of direct government ownership, subsidies, legal privileges, trade protection, and so on. Contemporary enemies of the market may suggest that advanced technology has changed the rules, making megacorporations and monopoly inevitable.

On the contrary, an analysis of what makes firms a certain size, combined with an understanding of technological change, reveals a far different and more exciting picture.

Over 500 million years ago, sparked by the introduction of sexual reproduction, the Cambrian Explosion brought a massive proliferation of new life forms. Multicelled organisms appeared (jellyfish, sponges, and worms) along with the first shelled creatures. As we enter the 21st century, technological changes will have a similar effect on another kind of ecosystem: the economy. Contrary to the expectation of highly concentrated corporations, we will see the proliferation of new organizational forms. The keys to success will not be overwhelming size but flexibility, agility, rapidity of response, and the ability to reform, spin off, dissolve, and recombine into new business structures. These changes are already underway.

To understand what kind of corporate environment will emerge in the markets of the next century, we need to answer two questions:

- What economic forces determine the size of firms?
- How will information technology affect those forces?

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The answer to the first question lies in economist Ronald Coase's theory of transaction costs. The answer to the second lies in the Internet and a powerful new form of business software called enterprise resource planning software.

The Size of the Firm

Why do firms exist in the first place? And why do they grow to a particular size? Ronald Coase won a Nobel prize for being the first to seriously tackle these questions. His answer involves the concept of "transaction costs." We might wonder why, for any production job, individuals do not simply make contracts with each other on the market instead of forming a firm. Why not carry out production in a completely decentralized manner rather than centralizing activity within a firm?

The problem is that negotiating and settling contracts for every exchange transaction consumes time and energy. Every time something new is to be done, contracts have to be renegotiated. These transaction costs often make it difficult and expensive to be productive. If you simply want someone to paint your garage, an individual agreement with the painter makes sense. It would be pointless to form a corporation with the painter. But if you wanted to work with the painter and 20 of his buddies to paint a variety of buildings over a long period of time, forming a corporation and hiring them as employees might make sense.

Carl Dahlman has identified several kinds of transaction costs. Search and information costs involve the difficulty in finding the right people with whom to make a contract for each task. Bargaining and decision costs involve the time and energy used to reach agreement on the terms for each task. Policing and enforcement costs involve the expense in ensuring compliance with each individual contract. When individuals form a firm, a single employment contract replaces this complex series of contracts. The contract states that the person agrees to do what the employer or entrepreneur says within certain limits in exchange for specified compensation. Direction by the entrepreneur replaces numerous contracts made in the market.

Firms will continue to grow so long as the cost of adding activities by organizing labor and resources within the firm is less than the cost of contracting for those factors on the market. The firm will stop growing at the point where the costs of organizing a transaction internally equals the cost of carrying it out through market transactions.

Firms will tend to grow under several conditions. If workers are closer together, it becomes easier to organize them. The movement of people to cities in the Industrial Revolution helped companies to get bigger. Government policy can also alter transaction costs to favor growing firms. For example, sales tax is imposed on market transactions but not on activities within the firm. The higher the sales tax the more the cost advantage to corporate organization of economic activity.

Technology and Transaction Costs

Technological change can strongly alter transaction costs and so affect the size of firms. Coase himself noted that an invention like the telephone may tend to increase the size of the firm. It does this by making it easier to organize widely dispersed individuals. Yet as Coase also noted, every invention will change not only the costs of internal organization but also the costs of using the price mechanism. Whether firms get larger or smaller depends on which effect is greater. In today's world of a rapidly evolving Internet and increasingly powerful business software, technology is already changing the optimal size of the firm and the look of the business ecosystem.

We don't need to look to the future to see the effect of technology on the size of firms. Twenty-five years ago Fortune 500 companies employed 20 percent of workers. Now it's only 10 percent. Many observers have noted that the widespread use of e-mail has flattened corporate hierarchies. These companies may be larger than ever in terms of money flows, but the number of layers of communication between top executives and lower-level operatives has shrunk. Some fast-paced technology companies actively encourage their

employees to communicate directly with high-level planners. The popularity of software such as Lotus Notes and "groupware" is enabling groups of employees to communicate with less managerial mediation.

Two areas of technology will have the most profound impact on business organization, flattening hierarchies, enabling innovative business structures, and fostering temporary, flexible work teams in place of fixed giant corporations. These areas—computer networks and enterprise systems—work together to alter the incentives of business.

Computer networks include the rapidly growing Internet. The utility of the Internet grows as the number of computers and users on it grows and as bandwidth expands. Fax machines were not terribly useful when only a handful of people had them. Once they became almost ubiquitous, their utility improved drastically. Similarly, when only a few physicists in Switzerland used the World Wide Web, its utility was severely limited. As millions of individuals and tens of thousands of businesses go online, more and more of us find the Internet indispensable. As bandwidth improves, its utility will grow further as we move to real-time video and interactive virtual environments.

Along with the Internet, businesses are developing "intranets" and "extranets." Intranets are computer networks accessible only within the corporation. They allow the easy and efficient sharing of corporate information, tracking of activities, and communication of ideas. Extranets extend a company's networks over the Internet to its suppliers, customers, and partners. Intranets reduce transaction costs within the firm, while extranets and the Internet itself also reduce costs in the market.

Dramatic Productivity Gains

Enterprise systems add to the business transformations being wrought by computer networks. Enterprise systems take the form of enterprise resource planning (ERP) software (and related packages such as supply-chain management and sales-force automation software). When a company installs ERP software it is not simply running another piece of business software. It is installing a business model—a way of doing business embodied in the structure of the program. Enterprise systems organize and integrate a company's reporting, sales and delivery, financials, manufacturing, service, inventory and supply, and human resources. More and more businesses are installing these programs in pursuit of enormous productivity gains. A company might reduce the time it takes to re-price all its products from five days to five minutes, reduce credit checks from 20 minutes to three seconds, and ship products within 24 hours instead of two weeks.

The development and convergence of computer networks and enterprise systems are changing the shape of corporations by reducing transaction costs. Even when companies appear very large, as measured in terms of their revenues, they employ relatively few people. They are becoming increasingly "hollow." Dell Computer, for example, differs greatly from traditional manufacturers. It not only does not make computer parts, it does not even buy the low-level components. Instead it buys subsystems and assembles them into a range of computers. Since Dell does no manufacturing, it can fulfill orders rapidly. Thanks to its enterprise system, it carries an incredibly low eight days of inventory (compared to two months for competitors).

Some companies are so decentralized that they never even handle their products at any point. One fashion accessories company with $80 million in revenues has only three employees. It contracts with other companies and individuals to make its products, design its packaging, and distribute and sell its products. The automobile industry is experiencing similar changes. A modern factory will simply fit together pre-assembled parts.

Companies are not only hollowing out; they are becoming more fluid in organizational structure. I have already noted that e-mail and intranets allow employees to communicate directly and easily. Intranets also give everyone ready access to corporate information without having to go through management. As the flow of information has improved, it

has become easier to loosen the corporate structure while continuing to track activity. Largely autonomous temporary work teams have been one result. Traditional companies maintain a strict organizational hierarchy. Each employee has a superior, and that superior has a higher level superior. Increasingly, employees are forming independent work teams with no fixed boss. Business units within corporations even deal with one another as if they were independent companies, having to make competitive offers for their services. This is sometimes called "intrapreneurship."

Hollow corporations, outsourcing, independent business units, and intrapreneurs join other trends to transform the corporate landscape. Temporary workers and free-lancers add to organizational flexibility. The temporary agency, Manpower Services, now employs more people than any other private company. As Internet access improves and bandwidth expands, telecommuting becomes an option for more and more people. As these new options proliferate, bigness often becomes less appealing. More companies spin off operations into new corporations, adding to their flexibility and focus.

Computer networks continue to spread and to expand in capacity. We find sound and video appearing all over the Web. Full motion teleconferencing is becoming feasible. Before long we will see virtual reality technology reach a point where virtual meetings can take place, making physical proximity unnecessary. Individuals will search for one another over the Net, set up businesses using off-the-shelf enterprise systems, then dissolve their team when the job is done, perhaps never having physically met at any time.

Large, stable, enduring corporations will not disappear. But they will cease to dominate the corporate ecosystem. The new face of business will look far more diverse. We will see constellations of activity, including large corporations, corporations with vast revenues but few employees or production facilities, temporary firms formed for a single project (which might be hugely complex), and semi-independent work teams. The existing large companies may perform the valuable role of creating the cultures and standards that allow these corporate mutations to emerge and flourish.

Government: Stay Out of the Way

Governments may slow down this process, but cannot stop the forces of technological change. The best way to help is to stay out of the way as new business structures form. They can also help by cutting sales taxes. Sales tax is paid on exchanges between companies but not within a company. This makes it more economic to organize activity internally rather than contracting for it on the market, making companies bigger.

We will not become citizens of Microsoft or General Electric. While large corporations will probably continue to exist in the future, they will not dominate the economy. On the contrary, the continuing reduction in transaction costs, the expansion in computer network bandwidth, and the ability to quickly create a business using off-the-shelf processes will accelerate today's trends toward a more diverse and flexible business environment. Free markets will bring not King Kong capitalism but a network of dynamically changing organizations. Permanent corporations will be only one of many species in the business ecology of the 21st century.

The market is vastly smarter than any individual, so we cannot predict exact or complete details of the emerging economy. Yet the trend clearly favors flexibility over rigidity, responsiveness over resistance, and speed over size. □

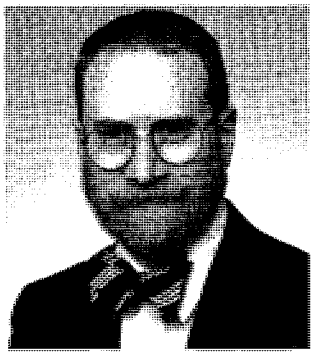
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Economics



Captain Consumer

"The direction of all economic affairs is in the market society a task of entrepreneurs. Theirs is the control of production. They are at the helm and steer the ship. A superficial observer would believe that they are supreme. But they are not. They are bound to obey unconditionally the captain's orders. The captain is the consumer."

—LUDWIG VON MISES, *Human Action*

Every day the business pages of the newspaper affirm Mises's claim about consumer supremacy. Within a three-week span last fall, the *Washington Post* reported:

> Toys R Us to Close 90 Stores
> Retailer Announces Restructuring, Charge Against Earnings
>
> Boston Chicken Files for Protection, Lays Off 500, Shuts 178 Restaurants

For years, Toys R Us has been the largest toy retailer in the United States, with 25 percent of the market. Yet in September it announced it would close 90 of its 900 stores in the United States and elsewhere around the world and redesign the rest. Boston Chicken (which calls its restaurants Boston Market) said in October it would close 178 of its 1,143 outlets, lay off 500 employees, and reorganize under the bankruptcy laws. It was once a hot stock, as patrons found the rotisserie chickens and other dishes attractive dining alternatives. But from a high of almost $40 in late 1996, the company's stock closed at 50 cents a share when the bankruptcy was announced.

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What happened to these once-booming companies? Captain Consumer found something he liked better.

Parents came to feel the Toys R Us stores were poorly organized and unfriendly; kids' taste in toys shifted to high-technology, and the chain was slow to notice. Hungry folks decided that, rather than stop at Boston Market for dinner, it was more convenient to buy rotisserie chickens and other ready-to-eat meals at the supermarket.

People changed their minds. Without notice and without asking anyone's permission, they abandoned Toys R Us and Boston Market and took their money elsewhere. (Try that with the public school or post office.)

Mises had it right: consumers "are merciless bosses, full of whims and fancies, changeable and unpredictable. . . . If something is offered to them that they like better or that is cheaper, they desert their old purveyors. In their capacity as buyers and consumers they are hard-hearted and callous, without consideration for other people."

Critics of the free market focus their animosity almost exclusively on the businessman. He is the boss. He decides what to produce and what to charge for his goods. He

decides who is hired and at what wage. As Mises notes, it does look that way. Appearances, however, are deceiving.

Entrepreneurs at one level drive the market process. But in an important sense, they don't act independently. They try to anticipate what Captain Consumer will want. He doesn't always know what he will want tomorrow because he doesn't know all that there *is* to want. No one wanted a personal computer before the idea was thought up. But a few entrepreneurs bet that people *would* want PCs when they learned of their existence. In that case, the businessmen were right. With the Edsel and countless other things, businessmen were wrong. Those who anticipate correctly make money; those who don't, lose it. Bankruptcy is the consumers' way of telling a businessman they would prefer that his capital were in more capable hands.

"Their buying and their abstention from buying decides who should own and run the plants and the farms," Mises wrote. "They make poor people rich and rich people poor. They determine what should be produced, in what quality, and in what quantities."

In terms of law, particular individuals own the means of production. But in economic terms, they hold their property only at the pleasure of consumers. "Thus the owners of the material factors of production and the entrepreneurs are virtually mandataries or trustees of the consumers, revocably appointed by an election daily repeated," Mises said.

The point applies as well to the businessman's employees. He may write the paychecks, but "The consumers, not the entrepreneurs, pay ultimately the wages earned by every worker, the glamorous movie star as well as the charwoman," Mises wrote.

That's the answer to the market's critics, who can't understand why Jim Carrey or Mark McGwire command such high salaries, while people in "more important" occupations are paid much less. When fans stop going to Carrey's movies or McGwire's ball games, those salaries will fall. The same is true for the "obscenely" large paychecks that corporate executives collect. If consumers reject a corporation's products, its executives will see their incomes shrink.

Unless the government intervenes. The market's critics will point to notorious cases of highly paid executives who run inefficient companies. Blame the mixed economy. That term is a euphemism for a market-based society in which government routinely countermands Captain Consumer. When the government bailed out Chrysler, permitting Lee Iacocca and his managers to remain in charge, politicians forced people to do as taxpayers what they had refused to do as consumers. (The bailout consisted of taxpayer-backed loan guarantees. Diversion of capital to Chrysler of course left less for projects consumers would have embraced.)

Government has more subtle ways to keep consumers from carrying out their will. In a free market, if they are unhappy with a corporation's products, investors will anticipate low or no profits in the future. That will translate into a lower stock price. Noticing the squandered potential, an entrepreneur specializing in takeovers might buy the stock (undervalued in terms of the profit potential), put in better managers, and reap the benefits of a later rise in the stock price. This process is what economist Henry Manne calls the market for corporate management. It protects consumers and stockholders. Of course, it also threatens the jobs of bad managers, which is why the takeovers are called "hostile."

How might the government, backed by incumbent managers, interfere with the market for corporate management? It can enact measures to impede takeovers. The federal Williams Act, for example, makes it illegal for entrepreneurs quietly or anonymously to buy up controlling shares of a company's stock. Under cover of "full disclosure" and "investor confidence," the Act requires that entrepreneurs show their hands early. That of course gives targeted managers time to defend their jobs. Disclosure also tends to push stock prices higher, spoiling many takeover plans.

Ironically, the same market critics who believe that businessmen rule consumers also favor anti-takeover laws, which shelter businessmen from the same consumers.

Maybe it's not so ironic. Maybe the market's critics think someone else should be captain. □

THE FREEMAN
Ideas On Liberty

A Program the Borg Would Love

by Karen Selick

ONTARIO, CANADA—Suppose you're out for a stroll one evening. A scruffy-looking stranger approaches you and says, "Hand over all your valuables, and make it snappy." "Is this a stickup?" you gasp, stupidly.

"Why, no," says the stranger, "it's merely the result of a cost-benefit analysis I just performed. I saw you come out of that nice-looking house over there, with the late-model car in the driveway. You're pretty well dressed, and that's a nice Rolex you're wearing. By comparison, the rent's overdue on my grungy apartment, my 12-year-old car needs its engine overhauled, my bank account's overdrawn, and just look at these worn-out clothes I'm wearing. I estimate that the benefit to me of having your valuables outweighs the cost to you of losing them by at least two to one. So hand them over."

If the robber's logic wins any points with you, then I've got a new government program to sell you. It's called national child care. Of course, it's not really new, but with all the recent talk about the "fiscal dividend," we can expect to see renewed hoopla over it in coming months.

An opening salvo was fired in March 1998 with the publication of a study titled "The Benefits and Costs of Good Child Care" by the University of Toronto's Centre for Urban and Community Studies. This study made national headlines in Canada because of its dazzling cost-benefit analysis. An expenditure of $5.3 billion on child care, it said, would generate benefits to children and parents of $10.6 billion—exactly double. Such a program should therefore be looked upon not as an expense, but rather as an "investment."

Misuse of Cost-Benefit Analysis

Unfortunately, the authors of the study make the same fundamental error as my fictitious robber. A cost-benefit analysis makes sense only when the costs are incurred and the benefits are received by the same person. If costs are inflicted on one person while benefits are reaped by someone else, it is simply impossible to say whether the world has been made a better place. For the person receiving the benefits, things have improved. For the person bearing the costs, things have deteriorated. But there is no way to measure the absolute quantity of either person's happiness. Individuals can rank their preferences (having more money usually ranks higher than having less), but they can't quantify them. There are no units of satisfaction or contentment. Using dollars as proxy measuring sticks doesn't help, because each additional dollar a person acquires adds less to his well-being than the previous dollars. You can't measure something when the measuring stick itself continually alters in size.

If you can't measure one person's quantity of happiness, it's even more obvious that

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you can't compare quantities of happiness between different people.

Economists have recognized these concepts for years, yet some people insist on fudging the issue by speaking of costs and benefits to "society," as if we were the Borg of *Star Trek* fame, all controlled by a single communal brain, all willingly subordinating our individual personalities and goals to the will of the collective. We aren't—at least, not yet. (One can't help wondering, however, whether the push toward government control of the country's children at ever younger ages reflects proponents' desire to achieve a state of Borg-like submissiveness.)

The fact is, some people would be net beneficiaries of national child care—primarily families with young children in which both parents wish to work outside the home. Other people would be net payers—namely, childless taxpayers, families with older children, and families that prefer to have one parent provide care to preschoolers at home. There is no fair, just, or moral case to be made for harming the second group in order to indulge the first.

The Unseen Neglected

The study contains a second fundamental flaw. In computing the cost side of the balance sheet, the authors fail to include any estimate of the advantages that would accrue if the same $5.3 billion were spent on something other than child care. Somewhere out there, toiling away in some laboratory, there is undoubtedly someone who could make a plausible case for "investing" $5.3 billion on his own pet project—perhaps a cold fusion machine. If he were successful in inventing such a device, the benefits to mankind would be incalculable—far more than the paltry $10.6 billion that child care would supposedly produce.

There are always competing uses for any resource. In deciding how to invest resources, you don't look just at the potential returns from a single alternative. You compare the expected returns from many different alternatives.

We don't know what alternative uses taxpayers would find for their money if we simply gave it back and let them invest it themselves, instead of spending it collectively. We can't calculate the benefits their myriad individual projects would generate. We do know, however, that taxpayers would probably prefer this to all other alternatives. Otherwise, we wouldn't have to force them to pay their taxes on pain of imprisonment.

There are many other good reasons for opposing national child care. Suffice it to say that if it's going to be as effectual as the public school system, let's nip it in the bud. □

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THE FREEMAN
Ideas On Liberty

Wisconsin's Choice

by Jon Sanders

The plaque is proudly posted at the front entrance to Bascom Hall on the campus of the University of Wisconsin at Madison. It memorializes the eloquent defense of academic freedom made by the university's Board of Regents in 1894 in exonerating Richard T. Ely, an economics professor accused of teaching socialism and other "dangerous" ideas.

"Whatever may be the limitations which trammel inquiry elsewhere," the plaque proclaims, "we believe the great University of Wisconsin should encourage that continual and fearless sifting and winnowing by which alone the truth can be found."

Donna Shalala walked by that plaque countless times when she served as the university's chancellor from 1988 to 1993, the year she became Bill Clinton's secretary of Health and Human Services. But she paid no attention to it. Her ideal campus of sensitive minds had no place for the plaque's dangerous idea.

Under Shalala's administration, and counter to the school's heritage, Wisconsin suffered severe limitations on inquiry in the form of speech codes for faculty members and students. The student speech code that went into effect in 1989 was one of the first standards on "hate speech" in the nation. It prohibited students from uttering slurs or epithets based on a person's race, gender, sexual orientation, religion, disability, or ethnicity. In 1991 a federal judge struck it down as unconstitutional. The faculty speech code, however, has faced no such court challenge.

The speech codes were part of several politically correct campus initiatives designed to make minority students feel more welcome on campus. Other initiatives included requiring students to take ethnic-studies courses, designing orientation programs to increase awareness of racial and ethnic diversity, setting enrollment goals for black, Hispanic, and American Indian students, and urging that the ROTC program be banned from campus until the military stopped discriminating against homosexuals.

Speech Further Restricted

Wisconsin's faculty speech code was originally established in 1981, but Shalala considered it insufficient to protect minorities from being offended in the classrooms. She asked the faculty senate to pass a revised code that further restricted faculty speech, which it did in 1989.

The enhanced code has trammeled speech in Wisconsin's classrooms for nearly a decade. It forbids faculty members from slurring students according to their gender, race, ethnicity, and so on, but it also punishes the use of teaching techniques that make "the instructional setting hostile or intimidating, or demeaning" to students according to their "group." If a professor invokes a theory in

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class that offends a particular group, he violates the code, probably without even realizing it. Under the code, however, the offense is in being offensive—whether intended or not.

Wisconsin's revised faculty speech code quickly became a wellspring of consternation for the teachers. Although no faculty members were ever formally investigated and disciplined for violating the code, several underwent grueling informal investigations for alleged violations about which they were told very little. The Kafkaesque investigations made it patently clear on campus that Wisconsin tolerated no breach, however slight, of the PC ethic.

In 1990, Richard Long, an art professor, was investigated by the Affirmative Action Office after two graduate students accused him of being anti-Semitic, racist, sexist, and homophobic. Although formal charges were never brought and he was never officially informed of his situation, Long underwent a six-month investigation before the matter was dropped for lack of evidence. "I never received anything resembling due process," he wrote in 1995 in a letter to the *Wisconsin State Journal*.

In 1992 Lester Hunt, a philosophy professor, was investigated after a student accused him of making racist jokes and comments. Like Long, Hunt was neither told of the charges against him nor given an opportunity to confront his accuser. "I would not want my worst enemy to go through what I went through," he told *The Daily Cardinal*, Wisconsin's online student newspaper.

In 1995, Robert Eric Frykenberg, a history professor, was accused of making disparaging comments to female graduate students. During the nine-month investigation, Frykenberg was never told which university rule he had allegedly violated. Finally, after he retained a lawyer and threatened to sue the university, the investigation was dropped and the university agreed to pay his legal bill. Frykenberg retired not long afterward.

Other teachers, understandably unwilling to risk the problems faced by their colleagues, voluntarily excised from their lectures anything that could be construed as offensive. The fierceness in investigating supposed violators frightened them, which was exactly the intent behind the code, said Stanley G. Payne, a professor of history at Wisconsin. "This helps to guarantee that no one will very seriously question any P.C. proposition," he told *The Chronicle of Higher Education*. "[The code] doesn't need to be invoked to police discussion in the classroom."

By this declension, "fearless sifting and winnowing" on the Madison campus became fearful shifting and whimpering. The code turned the faculty lounge into a Damocletian feast.

The Last Straw

The Frykenberg case, however, proved to be the final straw for some Wisconsin professors. In 1996 Payne formed the Faculty Committee on Academic Freedom and Rights (FCAFR). Well-known academics were brought to campus to denounce the code. In 1996, for example, Harvard University Law Professor Alan Dershowitz, known to many Americans for serving on the team of attorneys who defended O.J. Simpson, called the faculty speech code "abominable" and urged the capacity crowd in attendance to defeat it, saying the university would make national headlines by repealing it without being forced to do so by the courts. In 1997 Professor Glen C. Loury of Boston University argued that any legislation restricting speech is wrong. "Our job as faculty members is to be provocative and challenging," Loury told the Wisconsin crowd. "You're not there to make students comfortable, you're there to break through conventional ways of thinking."

Meanwhile, Hunt and FCAFR member Donald A. Downs, a professor of political science, shamed the University Committee into taking another look at the code, charging that it infringed free speech and academic freedom. The charge struck at the heart of the matter, pitting Shalala's legacy against the university's. In May 1997 the University Committee formed a panel of ten faculty members, four academic staff members, and three students to investigate the code.

The panel, the Ad Hoc Committee on Prohibited Harassment Legislation, was as congenial as a coalition of Middle East coun-

tries. Among the members who favored the Shalala code were Ted Finman, an emeritus professor of law who wrote the original speech code; Evelyn Howell, a professor of landscape architecture who had served as chairman of the University Committee when it selected the panel members; Phillip R. Certain, dean of the College of Letters and Science; and Stanlie M. James, an associate professor of Afro-American and women's studies. Among those seeking to overturn the code were Downs, journalism professor Robert E. Drechsel (the panel chairman), and the three student members.

Early last October, the so-called liberals on the panel succeeded in getting enough of their conservative counterparts to agree to send a compromise revision of the code, which would scale back the Shalala revisions, to the faculty senate. The new revision would penalize professors who use "an epithet or a comment concerning a specific student that clearly derogates and debases the student on the basis of the student's gender, race, religion, ethnicity, sexual orientation, or disability" or who utter such comments without "a reasonable pedagogical justification for using the teaching technique in question."

The revision would add a preamble discussing the university's legacy of academic freedom and include examples of teaching techniques that would and would not be protected. Protected speech would include an instructor's assigning a "pertinent novel that expresses racist ideas or contains a racial epithet" or asserting that "the intellectual capacity of men for scientific analysis is superior to that of women." Prohibited speech would include an instructor's referring to Africans transported to the United States in slave trades as "niggers" or responding to a female student's rebuttal of his assertion of women's inferior scientific intelligence with "See! Your stupid female comments just prove my point." The faculty senate recommended adoption of the revision late last year.

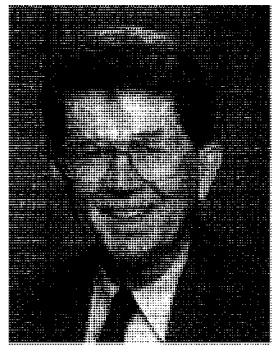
The faculty senate also received a report from a stubborn minority comprising Downs, Drechsel, all three student members, and two others on the committee. That report would narrow the speech code further than the majority recommendation, penalizing professors only for using slurs expressly for the purpose of harming a student.

A split in such a committee is unusual, and it has set the stage for a potentially raucous faculty senate meeting. It is fitting that the fight end there. The issue is essentially whose idea of academic freedom will rule, Shalala's or the 1894 regents'. *Essentially*, but not exactly. The compromise revision, which likely will be adopted, represents only a step back from the PC precipice to which Shalala brought the university. The minority report recommends a narrower speech code, but as the student editorial staff of *The Daily Cardinal* opined, "The committee must understand that any new speech code—no matter how well written—is still a speech code." Neither allows inquiry as open as it was before 1981.

As that statement shows, it is the students, the supposed beneficiaries of the code, who are most vociferous in trying to end it. More so than the faculty and administration, they seem to understand the importance of free, even offensive speech. In fact, they appear to be less insulted by ill-advised faculty speech than by the idea that such speech would harm them. "Are they saying I can't stand up for myself?" asked one student on the panel, Amy Kasper, in *The Chronicle of Higher Education*. "Am I being wrapped in a security blanket here, and I'll go out in the real world and find there isn't one?"

The student panel members should be of particular interest to those of the PC mindset. They are a white woman, an Asian woman, and a gay man. All consider the code—and the attitude behind it—"demeaning." For unlike the Wisconsin teacher who argued that the code is needed so students "don't get insulted or assaulted by a professor," Wisconsin students of all stripes know that words, even those uttered by professors, are neither sticks nor stones. □

Economics



The Market for Honesty

The recurring theme of all my columns has been that economics is a study of how people cooperate with each other and that market economies succeed because of the incredible amount of cooperation they promote. Market cooperation, like all cooperation, depends on a high level of honesty. People who cannot trust each other cannot cooperate with each other, certainly not for long. And with the market, it's not just a matter of trusting a few people whom we know and care about. Market cooperation depends on our being able to trust large numbers of people, most of whom we will never know.

Consider the behavior of business people. If the proverbial man from Mars observed our business activity, he would surely conclude that business people are extraordinarily honest. For example, they sell precious gems that really are precious to customers who cannot tell the difference between diamonds and cut glass. They promise not to raise the price of a product once customers commit themselves and make switching to another product costly—and they keep the promise. They make good-faith promises that the business they own, but are about to sell, will continue to give their customers good service. The examples could be continued indefinitely since honesty and trust are essential for all but the simplest business transactions.

I am not naïve enough to argue that business people are never dishonest. Just like people in all walks of life, some will cheat, lie, and steal to snatch short-run advantage. But they are not nearly the scoundrels as presented in the media and popular entertainment. According to one study, almost 90 percent of all business characters on television are portrayed as corrupt.[1] In fact, business people can be depended on to act more honestly than most. This is not because business people are inherently more virtuous than others (though there is no reason to believe they are less virtuous), but because the free market penalizes those who do not provide consumers with things they value—and consumers value honesty.

The reason the market penalizes dishonesty is obvious at one level. Those who fail to provide the quality they promise, and charge for, may profit in the short run, but not in the long run. But even in the short run there are gains from honest dealing, and those who can credibly promise to deal honestly can capture some of those gains. So business people are strongly motivated to put themselves in situations in which dishonest behavior is quickly penalized. By doing so they are better able to entice customers with assurance of everyday honest dealing.

Committing to Continuity

Consider the fear of dishonesty that can arise when it is believed that a business is about to shut down, say, because the proprietor is getting old. Even if such a proprietor has no intention of cheating customers, they

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will have reason to worry without some credible assurance of the proprietor's long-run interest in the business. An owner can often provide this assurance by bringing his offspring into the business ("Samson and Sons" or "Delilah and Daughters"). Not surprisingly, research shows that children of single proprietors are three times more likely to follow in their parents' lines of work than the children of others. Even large corporations, with lives that extend far beyond those of any of their managers, often depend on single proprietorships to represent and sell their products. This explains why Caterpillar, for example, has a school on running Caterpillar dealerships for the sons and daughters of the owners of those dealerships.

To consider another example of the importance of business continuity in promoting honesty, ask yourself where you would rather shop for an expensive piece of jewelry, a jewelry store with a well-advertised brand name and ornate fixtures, or a sidewalk vendor operating out of a Volkswagen van parked at the curb? What could the store do with its brand name and fixtures if it went out of business? Not much, and this tells customers that the store has a lot to lose by misrepresenting its merchandise to capture short-run profits. It has made a commitment to staying in business by being honest.

Embracing Competition

Intel, having received a patent on its 286 microprocessor in the early 1980s, immediately gave up its monopoly by licensing a competitive firm to also sell the microprocessor. Why would any company give up a legal monopoly? Because of the importance of honesty. Intel was willing to sell its new microprocessor to computer manufacturers at a reasonable price, and promised to do so. But the manufacturers were afraid that once they committed to using the new microprocessor (making expensive changes in their production process that would be difficult to reverse), Intel could exploit its long-term patent monopoly by raising the price. Intel could make a credible promise that it would maintain competitive prices by giving up its monopoly. Committing itself to honest dealing was more important to Intel, and more profitable in the long run, than exploiting a monopoly position in the short run.[2]

Selling and Repairing

It is difficult for consumers to determine the quality of automobile repair. They can generally tell if the work eliminated the problem: the car starts, the rattle is gone, the oil light is off, and so on. But few people know if the repair shop charged them for only the repairs necessary, or if it charged them for lots of parts and hours of labor when all the mechanic did was tighten a screw. One way repair shops can reduce the payoff from dishonest repair charges is through joint ownership with the dealership selling the cars being repaired. In this way the dealer makes future car sales largely dependent on honest repair work. Dealerships depend on repeat sales from satisfied customers, and an important factor in how satisfied people are with their car is the cost of upkeep and repairs. The gains a dealership could realize from overcharging for repair work would be quickly offset by reductions in car sales.

Automobiles are not the only product for which it is common to find repairs and sales tied together in ways that provide incentives for honest dealing. Many products come with guarantees and warranties entitling the buyer to repairs and replacement of defective parts for a specified period. These guarantees provide confidence in the seller's honesty when advertising the quality of his product.

Some will always go for the short-run gain through deceit and dishonesty. But the greater the freedom of others to compete with credible commitments to honesty, the less dishonesty pays even in the short run. The cooperation that characterizes the free market would never be possible without the high level of honesty and trust motivated by market competition. □

1. See Robert Lichter, Linda Lichter, and Stanley Rothman, *Watching America* (New York: Prentice Hall, 1990), p. 146.

2. Adam M. Brandenburger and Barry J. Nalebuff, *Co-opetition* (New York: Currency/Doubleday, 1996), pp. 105–106.

THE FREEMAN
Ideas On Liberty

The Life of a Grand Old Liberal

by Wendy McElroy

Moses Harman (1830–1910) is the sort of social visionary whom historians often overlook, even though his influence during his own lifetime was immense. Harman lived most of his life in the American midwest, sharing many of the values that are associated with the region: he was a soft-spoken, hard-working, and devoted family man with an unswerving sense of right and wrong.

He was also one of the most stubborn and persistent nineteenth-century Americans involved in the fight to preserve individual rights. Most of his writing remains buried in the pages of the now obscure periodical he edited for 24 years. His main impact derives from his decades-long fight for freedom of speech, which resulted in numerous imprisonments and culminated in his breaking rocks at Joliet (Illinois) prison at the age of 75.

George Bernard Shaw referred to Harman's last imprisonment in a letter to the *New York Times* (September 26, 1905), in which he explained why he would not visit the United States: "The reason I do not go to America is that I am afraid of being . . . imprisoned like Mr. Moses Harman. . . . If the brigands can, without any remonstrance from public opinion, seize a man of Mr. Harman's advanced age, and imprison him for a year under conditions which amount to an indirect attempt to kill him, simply because he shares the opinion expressed in my *Man and Superman* that 'marriage is the most licentious of human institutions,' what chance should I have of escaping?"

Harman and Shaw shared the same opinion of nineteenth-century traditional marriage: it was defined by laws and customs that enslaved women, who were stripped thereby of the right to their own wages, custody of their children, and the ability to defend themselves against physical or sexual attack by their husbands. As a personal matter, Harman believed in monogamy and conducted his life without scandal. But as a point of social theory and practice he insisted that "true marriage" must be an equal union between consenting adults in which the state had no rightful place. It was his insistence on speaking out for true marriage and the rights of women that led to Harman's many years of legal persecution under the Comstock Act, which forbade the circulation through the mail of information on "obscene" matters such as birth control or marriage reform.

With the streak of stubbornness that often arises in the American personality, Harman persisted in speaking out because, as he phrased it, "I believe in Freedom—equal freedom. I want no freedom for myself that all others may not equally enjoy. . . . The Spencerian formula: 'each has the right to do as he pleases, so long as he does not invade the equal right of others,' tells what freedom means. It is equivalent to saying that liberty, wedded to responsibility for one's acts, is the

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true and only basis of good character, or of morality." He wished to offer women equal freedom with men to control their bodies and their property, especially within the context of a true marriage. It was part of his lifelong battle to secure what he called the right of private judgment in moral matters.

Little Formal Schooling

Born in western Virginia to a poor family, Moses Harman grew up in southern Missouri. Although he had only a few months of formal schooling, the young Moses became an avid reader, especially after an accident left him crippled. At 16 he began teaching school and then went on to attend Arcadia College, in Missouri; the education came at great financial sacrifice to his family. Harman soon became galvanized by the ideal of abolitionism—the pre-Civil War movement that demanded an immediate cessation to slavery on the grounds that every human being had a right to his own body. When the Civil War erupted, Harman was unable to enlist in the Union army owing to his lameness. But he remained such an outspoken abolitionist that the pro-slavery county of Crawford, Missouri, once voted to run him out because of his unpopular sentiments.

When Harman married Susan Scheuck, the daughter of a Union sympathizer who had been executed by a roving band of Confederates, their marriage was a harbinger of his later commitments. Although the ceremony was conducted according to law, the young couple also entered into a personal contract that based their voluntary union on love, not duty. Their two children, George and Lillian, were both born in Missouri. A third child died with Susan during birth in 1877. One can only speculate on how deeply watching the death of his much-loved wife in childbirth influenced Harman's later insistence on the availability of birth control information to women.

In 1879, Harman took his young children to live in Valley Falls, Kansas, where his cousin Noah was a well-to-do farmer. Moses took a job teaching at the district school, and soon became known for speaking his mind in a dignified but blunt manner. One exchange in particular would determine much of his future course.

Harman became involved in the Valley Falls Liberal League, a local branch of the National Liberal League, which sought to separate church and state. This was an issue around which many figures in the American individualist tradition gathered after the Civil War. In the words of Harman, the local "club was the successor of an older club . . . which meetings were conducted on the plan of equal rights for all, regardless of race, color, party or creed." The League soon became involved in an exchange conducted with clergymen in the local Republican paper on "issues dividing the current and popular theologies from the deductions of modern science." Although respectful of Christianity, Harman argued the scientific point of view under the pseudonym "Rustic."

When the newspaper proved unwilling to continue the voluminous debate, the Liberal League issued its own periodical, the *Valley Falls Liberal* in August 1880, with Harman serving as one of the unofficial editors. It became the foremost voice in Kansas of liberalism in the nineteenth-century sense of individualism in active opposition to state interference. In 1881, it was rechristened the *Kansas Liberal,* and Harman shared editorship with Annie L. Diggs, a well-known populist. After a dispute about prohibition, which the teetotaling Harman opposed in the belief that temperance must be voluntary, he assumed sole control.

The *Kansas Liberal* would eventually be renamed *Lucifer, the Light Bearer* (1883–1907) for which Harman would soon become notorious nationwide. The name was unfortunate because it raised the worst suspicions within and created an emotional backlash among many religious-minded people. Indeed, since periodicals as controversial as *Lucifer* were able to publish without facing the legal problems that constantly confronted Harman, it is probable that at least some of his subsequent persecution was sparked by the provocative title. Harman had chosen it innocently. He wrote, "Lucifer, the ancient name of the Morning Star, now called Venus, seems to us unsurpassed as a cognomen for a journal

whose mission is to bring light to the dwellers in darkness." When more cautious minds advised against the name, Harman characteristically dug in his heels and continued to maintain that "words are not deeds" and that neither the state nor society could rightfully restrict the words he chose.

The Censor's Watchful Eye

If the kindly and cultured Harman had been the only one to choose the words printed in *Lucifer*, his policy might have proven harmless. For better or worse, however, Harman permitted his contributors to write what they pleased. He believed that absolute freedom of speech cleansed society by allowing individuals to feel honestly drawn or repelled by certain ideas, and to understand their reactions rather than suppress them. *Lucifer* was not salacious, but merely blunt in its social and political discussions. For censors of the day, this was enough.

In June 1886, *Lucifer* published a letter from W.G. Markland, which described an especially brutal instance of forced sex within marriage and called it rape. Indeed, it may have been the first discussion in print of this subject on the American scene. The letter was graphic, but used no words that were not to be found in a dictionary or a medical textbook.

In sending the issue of *Lucifer* containing the letter through the mails, Harman ran afoul of the Comstock Act, which provided a penalty of up to ten years' imprisonment for anyone who intentionally mailed or received obscene material. Ominously, the word "obscene" had not been defined by the Act. But Anthony Comstock, its author in 1873 and organizer of the New York Society for the Suppression of Vice, defined "obscenity" to include the discussion of and protest against rape within marriage. Under the Act, the Post Office assumed the power to destroy mail arbitrarily without either reimbursing the sender or providing due process.

There is a sense in which *Lucifer* was an unlikely target for Comstock: it seemed to be an idyllic family business, a labor of love. Harman described the set-up: "I did the office work, assisted by my son George, aged fifteen, and daughter Lillian, aged thirteen who had already learned to set type. We lived on a little fruit farm one mile from the printery at which the typesetting and press work were done. Editorial work was mainly done at home, in the early morning hours and late at night, while much of the day was spent by all three at work on the farm, raising fruits and vegetables, from the sale of which we supplied our own daily wants, besides helping to defray the expenses of publication; the folding and wrapping of the paper being done at night by the entire family, including wife Isabella, whom I had married since our removal to Kansas."

This contented picture was shattered in February 1887, when a warrant was served for the arrest of the editors and publishers of *Lucifer*: Moses Harman, Edwin C. Walker, and George Harman. Harman and his son were taken to Topeka where, on executing bonds of $500 each to appear at the April term of court, they were allowed to go home. (Walker, and his 16-year-old wife, Lillian Harman, were already in jail for their non-state marriage, which Moses called an "autonomistic marriage.")

The Legal Persecution of Moses Harman

After attending the April term court, Moses and George Harman were ordered to execute another bond and to reappear the following July. At the July term, they were told the weather was too hot to present the charges against them to the grand jury. They executed another bond to appear at the October term and went home. Over the next eight years, Harman was forced to waste large portions of time traveling back and forth to Topeka at the legal whim of the court and to spend scarce money in executing dozens of bonds, even though one bond alone would have answered the requirements of law.

Finally, in October, the accused learned the nature of the charges brought against them. The grand jury indicted *Lucifer* on 270 counts of obscenity, which were eventually quashed because neither the judge nor the district

attorney could discern a legally intelligible charge in any one of the counts. Not to be thwarted, the district attorney procured a new set of indictments, totaling 216 counts in all. The indictment was based on four newspaper articles, though charges were withdrawn on two of them. The articles included the Markland letter and a letter to the editor written by Celia B. Whitehead, a well-respected mainstream reformer. Ironically, Whitehead's letter argued *against* the birth control that Comstock considered obscene.

As a consequence of their withdrawing from the management of *Lucifer*, charges were dropped against George Harman and Walker in 1888. Moses Harman stood alone as the sole defendant. He was a defiant one. In the June 22, 1888, issue of *Lucifer*, he reprinted the Markland letter—along side the 38th chapter of Genesis, to demonstrate that the language of the letter was no more offensive than that of the Bible.

Meanwhile, Harman's ordeal stirred up a storm of protest. As a result of the controversy, the district attorney continued the case until 1890, when he would no longer be in office.

In February 1890, Harman was arrested on fresh charges arising from a letter written by a New York physician, known as the O'Neill letter. Graphic in its language and speaking from 19 years' experience in the medical practice, Richard V. O'Neill testified that he had seen many cases of the derangement or early death of women caused by "rape within marriage," similar to what had been described in the Markland letter. For publishing the O'Neill letter, Harman was escorted to Topeka once more, then released on bail of $1,000.

In May 1890, Harman was finally tried and sentenced to five years' imprisonment and a $300 fine for mailing the Markland Letter. The following August he was released by virtue of a writ of error, but a new bond was required. In January 1891, Harman was sentenced to one year's imprisonment for the O'Neill letter. Another writ of error and another bond ensued in March. The legal harassment continued for years, until in June 1895 a new sentence was passed under which Harman was lodged in the Kansas state prison at Lansing. On release in 1896, the exhausted editor moved his family and *Lucifer* to Chicago.

Of this period, he later wrote, "[F]or more than nine years, I was never for one moment free from the 'shadow of the jail'—that is, I was either securely locked within prison walls or was under bonds outside of those walls, with the threat of imprisonment, like the sword of Damocles, constantly hanging over my head." He continued by proudly declaring, "Meantime Lucifer, the real object of the prosecutors, did not die; Lucifer did not suspend; Lucifer did not retract; Lucifer, 'Son of the Morning,' did not cease to shine on friend and foe alike."

The Final Imprisonment

From battling the Comstock laws, Moses Harman had acquired the aura of a folk hero, which extended into mainstream periodicals. But the move to Chicago did not prevent the same sort of legal problems that had arisen in Topeka. Postal harassment preceded Harman's final arrest, with *Lucifer* being denied the use of second-class mail rates until the matter was appealed to Washington. Then the Chicago post office began to confiscate and destroy certain issues it declared to be obscene. One issue was destroyed because it contained an article by the venerated feminist Alice Stone Blackwell that had been reprinted from the *Woman's Journal*. Another article declared obscene by the postal authorities was an excerpt from a United States Bureau of Animal Industry report that had been issued by authority of Congress.

Finally, Harman was indicted and tried in May 1905 for mailing two articles: "The Fatherhood Question" (written by an author identified only as T.V.A.), arguing in an inoffensive manner that every prospective mother had the right "to select the best possible conditions for" procreation, and "More Thoughts on Sexology" by Sara Crist Campbell, who was nearly 70 years old, arguing that sexual ignorance inflicted needless pain on women. The court refused to allow testimony about Harman's medical condition, and the judge's instructions to the jury left little doubt as to his opinion that the articles were legally

obscene. Thus, at the age of 75, Moses Harman was sentenced to one year at hard labor.

From Cook County jail in Chicago, Harman wrote a "hail and farewell" letter to his friends, restating the object of *Lucifer*'s publication: "to help woman to break the chains that for ages have bound her to the rack of man-made law, spiritual, economic, industrial, social and especially sexual, believing that until woman is roused to a sense of her own responsibility on all lines of human endeavor, and especially on lines of her special field, that of reproduction of the race, there will be little if any real advancement toward a higher and truer civilization."

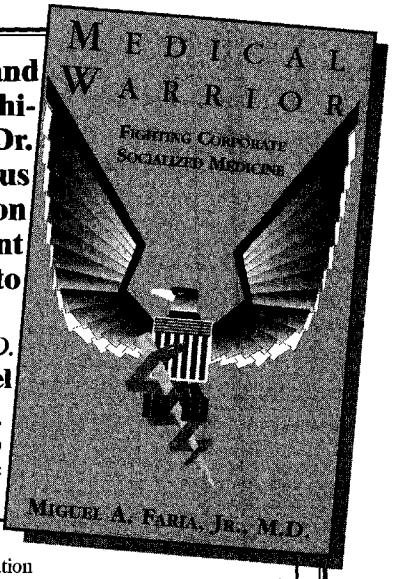
At Joliet, where he broke rocks during the bitter winter months, Harman's health deteriorated disastrously. A transfer to Leavenworth—secured by the determined intervention of family and friends—probably saved his life. There, he spent a large portion of his remaining sentence in the hospital.

On release in 1907, the 76-year-old Harman changed *Lucifer*'s name to the *American Journal of Eugenics*. The format became more scholarly, and the focus shifted more firmly to improving reproduction and the human race, a subject that captivated many early twentieth-century reformers. The eugenic theories of Harman and similar individualist radicals were based largely on the work of such popular scientists as Francis Galton (coiner of the word "eugenics"), who believed the human race could be improved through heredity. For Harman, the main barrier to proper reproduction was the state. He believed its oppressive marriage, divorce, and anti-birth control laws almost ensured that poverty-stricken women would give birth to ill-nourished, sickly children. In calling for removal of the state from reproduction, rather than stricter regulation, the American individualists were a unique voice for individual freedom within a movement that tended toward state control.

On January 30, 1910, Moses Harman died in Los Angeles, where he had moved in 1908. *The American Journal of Eugenics* died with him. Although two memorial services were held for the venerated editor—one in Los Angeles, the other in New York City—the most fitting memorial may well have been a letter written to *Lucifer* by Lizzie Holmes almost 20 years earlier. She called Harman's periodical "the mouthpiece, almost the only mouthpiece in the world, of every poor, suffering, defrauded, subjugated woman." □

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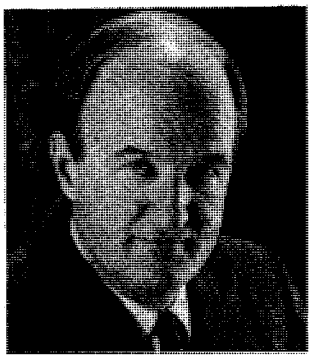
Miguel A. Faria, Jr., M.D. argues that managed care and HMOs are not "free market" alternatives, but rather an unholy partnership of government and corporate interests seeking monopolistic government protection to eliminate competition...



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THE FREEMAN
Ideas On Liberty
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A One-Armed Economist, Please

"[W]hile purity is an uncomplicated virtue for olive oil, sea air, and heroines of folk tales, it is not so for systems of collective choice."
—AMARTYA SEN[1]

President Harry Truman hated what he termed two-armed economists, those who would advise him first "on the one hand" and then "on the other hand." Give me a one-armed economist, he demanded, an adviser who wouldn't waffle.

I was reminded of this story when I read some of the writings of the Indian economist Amartya Sen, the latest winner of the Nobel Prize in economics. He won the prestigious award (worth nearly $1 million) for his work on poverty, famine, inequality, growth theory, human rights, and ethics, all those wide-ranging debate topics common to development economics.

Writing on these topics is commendable; I just wish I knew what he was saying. Sen is one of those economists that Truman complained about. He represents everything that is wrong-headed about modern economics, which Peter Drucker has rightly described as "clever, brilliant, and bankrupt economics."[2]

Too Much Sen

Sen has all the establishment credentials. He's taught at Harvard and Cambridge and was president of the American Economic Association in 1994. His mentors are Joan Robinson, Kenneth Arrow, and philosopher John Rawls. A prolific scholar, Sen has written and read everything imaginable on his favorite subjects. He cites dozens and dozens of authors. He engages in heavy mathematical modeling and game theory. He weighs the pros and cons of every nuance of high theory. And yet, when it comes to his own view, he never seems to come to a simple conclusion. For Sen, everything is complex and indeterminate.

For example, in 1985 he gave a series of lectures at Cambridge University, subsequently published as *The Standard of Living* (Cambridge University Press, 1987). Is it possible to measure and compare living standards between individuals or nations? Sen is never sure. In his works on inequality, he rejects utility-based comparisons of income and even distinguishes between "well-being" and "standard of living." When you're through reading Sen, you feel like joining the pure subjectivists-relativists. In an often-cited article, "Rational Fools," Sen offers a critique of utilitarianism and self-interest, saying at one point, "this approach presumes both too little and too much."[3] Only in Sen's world would that be possible.

The only case I know where Sen establishes a clear position is on famines, an area he

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knows firsthand. Liberal democracies, he says, avoid famines. "In the terrible history of famines round the world, no substantial famine has ever occurred in a democracy."[4]

In trying to be ultra-scholarly, Sen obfuscates more than he elucidates. As Sylvia Nasar wrote in the *New York Times* (October 15, 1998), Sen is "highly influential, but wide-ranging, diffuse, lacking a single killer theorem." The Chinese philosopher Lin Yutang put it best, "If one is too well-read, then one does not know right is right and wrong is wrong."[5]

"One-Armed" Bauer

Give me a one-armed economist! In development theory, that candidate would be Lord Bauer. Whether you agree with him or not, you have no doubt where he stands. He is an ardent polemicist in defense of democratic capitalism (including private property, free trade, and limited government) in developing countries.

P. T. Bauer is a long-time dissenter in development economics who has finally been vindicated. In that sense, he follows in the footsteps of other free-market economists—including Milton Friedman, who was ultimately proven right about the efficacy of monetary policy, and Ludwig von Mises and F. A. Hayek, who accurately predicted that socialist central planning could never work.

In the postwar period, Bauer waged a lonely battle against foreign aid, comprehensive central planning, nationalization, and other anti-market schemes. He denied the then-current orthodoxy, such as the vicious cycle of poverty and W. W. Rostow's stages of economic growth. Today even Rostow admits, "there are, evidently, serious and correct insights in the Bauer position; for example, the shrewd and quick responsiveness of farmers to incentives and disincentives, the superiority of competitive private over public trading systems."[6]

Like Sen, Bauer has extensive experience in the developing world, having spent years in Asia and Africa as a writer and consultant. He warned the Indian government repeatedly that its five-year plans would never achieve their lofty goals. (The only Indian economist he respected was B.R. Shenoy, a lone dissenter.)

The IMF could learn a lot from reading Bauer's classic textbook, *The Economics of Under-Developed Countries*, co-authored by B.S. Yamey (Cambridge University Press, 1957). And one of the best short essays ever written is "The Lesson of Hong Kong."[7] Other essays can be found in *Dissent on Development* (Harvard University Press, 1976) and *The Development Frontier* (Harvester, 1991). The Cato Institute recently published a book, *The Revolution in Development Economics*, edited by James A. Dorn, Steve H. Hanke, and Alan S. Walters, that was dedicated to Lord Bauer and includes many of his articles. Nothing could be better, short of a Nobel Prize. □

1. Amartya K. Sen, *Collective Choice and Social Welfare* (San Francisco: Holden-Day, 1970), p. 200.
2. Peter F. Drucker, *The Unseen Revolution* (New York: Harper & Row, 1976), pp. 114–15.
3. Amartya K. Sen, "Rational Fools: A Critique of the Behavioral Foundations of Economic Theory," cited in H. Harris, ed., *Scientific Models and Men* (New York: Oxford University Press, 1978), pp. 317–44.
4. Amartya Sen, *Prospect*, October 1995, cited in Chris Patten, *East and West* (New York: Macmillan, 1998), p. 198.
5. Lin Yutang, *The Importance of Living* (New York: John Day Company, 1937), p. viii. Yutang's profound book has recently been reprinted by William Morrow. I highly recommend it.
6. W.W. Rostow, *Theorists of Economic Growth from David Hume to the Present* (New York: Oxford University Press, 1990), p. 386.
7. P. T. Bauer, "The Lesson of Hong Kong," *Equality, the Third World and Economic Delusion* (Cambridge, Mass.: Harvard University Press, 1981).

BOOKS

New Schools for a New Century: The Redesign of Urban Education

edited by Diane Ravitch and Joseph Viteritti

Yale University Press • 1997 • 320 pages • $30.00

Reviewed by George C. Leef

Socialism cannot work, Ludwig von Mises argued from the 1920s until his death, because of a central flaw—the lack of market prices. Socialists argued back that they could simulate market prices, but Mises countered that *pretending* to have a market could never come close to the real thing. Following the collapse of communism in Europe, even some hard-core statists admitted that he had been right.

What does that have to do with a book on education in the United States? The two cases are remarkably similar. Socialism necessarily produces poor results because it does away with the market. No amount of tinkering can change that. Likewise, "public education" (another of those mushy phrases that get in the way of clear thinking) necessarily produces poor results because it does away with the market.

In place of property rights, competition, entrepreneurship, and the search for profit, the socialization of education gives us coercion, bureaucracy, taxation, and the search for political power. The incentives for quality and efficiency that drive market participants are diminished and perverted when schools and educators do not derive their revenues from willing customers, but instead derive them through the tax system. That's the ineradicable, disastrous flaw in "public education." Market-imitating reforms in education are a shabby substitute for the market itself.

This book, edited by Diane Ravitch, a Brookings Institution scholar, and Joseph Viteritti, a New York University professor of public administration, is typical of the books by educational theorists who, like the socialist intellectuals, know that the system isn't working, but want to modify and improve it without giving up on the system itself. While there are many insightful points in the ten essays included, not one grapples with the fundamental problem: turning education from a private investment into a government entitlement ensures politicization and decay. Popular ideas such as charter schools, contracting, vouchers, and choice abound, but conspicuously missing is any radical, Mises-like author arguing against continued reliance on government education.

What I regard as the best essay in the book, Chester Finn's "The Politics of Change," comes rather close to arguing that trying to reform public education is a lost cause. He recounts numerous episodes in which defenders of the system defeated changes that even remotely threatened their beloved *status quo.* Consider, for example, the reaction of the New Jersey education establishment when PepsiCo announced its participation in a program to provide scholarships to poor youngsters so they could get out of the Jersey City public schools. Suddenly, the company was faced with a union-instigated boycott of its products, and there was a mysterious wave of vandalism aimed at its vending machines. Pepsi backed down. The education establishment presents a smiling face to the public, but turns into a pack of snarling Dobermans when anyone comes near its turf.

Far worse is the incessant thought-control campaign waged by the educational establishment. Finn writes that it "cleverly manipulates Americans' strong affection for the concept of public education while imposing a double standard on proposals to reform its reality." The propaganda organs never stop informing voters that "their" schools are *award-winning, progressive,* and *improving.* Furthermore, they automatically label any proposed change that doesn't involve more money and authority for the schools *anti-education.* This works marvelously; opinion polls show that the great majority of parents are satisfied with the public schools their children attend and leery of "dangerous" changes.

When all else fails, the public education crowd resorts to political intimidation. Finn

recounts how one of those market-imitating reforms was beaten in Arizona when the education lobby persuaded several Republicans in swing districts that it would be wise for them to vote against the bill.

From this essay, one might conclude that the prospects for significant change in—much less the defeat of—public education through the political system, are nil. Finn is not quite so pessimistic, noting some "cracks in the glacier." He acknowledges, however, that a glacier can continue on, grinding down all in its path, even with some cracks in it. Perhaps people who care about education should just give up on the political process and concentrate instead on creating a modern version of the Underground Railroad to help children escape from the public education trap.

If you want to know more about the problems and prospects of the Milwaukee school-choice plan, what has become of the Edison Project, or the battles over public school contracting, this book will serve you well. If you want to raise your blood pressure over the venality of the teachers unions and their political supplicants, this book will get you hot under the collar. But if you want a book on education that challenges the prevailing wisdom that public education is both necessary and reformable, look elsewhere. □

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Those Dirty Rotten Taxes: Tax Revolts that Built America

by Charles Adams

The Free Press • 1998 • 242 pages • $25.00

Reviewed by James A. Woehlke and Nikolaus P. Woehlke

IRS reform has been a hot topic in Washington recently. Last spring, more than 80 legislators attempted to repeal the Internal Revenue Code—unsuccessfully. Fundamental tax reform, the attempt to replace the graduated income tax with a flat tax or national sales tax, was a guiding theme for the newly elected reformist Republican Congress in 1995. Although the ponderous tax code is still very much alive, its future is in doubt.

In this legislative milieu, Charles Adams has unleashed his new book, *Those Dirty Rotten Taxes*, in which he shares his view of American history as a hotbed of tax revolt. The book tells of the injustice and oppression wreaked by tax collectors, and shows how tax avoidance and revolts have influenced our current tax system.

The book abounds in historical detail. For instance, the whiskey rebellion of 1794: farmers were unfairly taxed for producing whiskey, which for some was the only viable means of transporting their corn. The farmers quickly rebelled and refused to pay the tax. The new federal government, which had only recently been founded on, among other things, the principle of fair taxation, responded harshly by sending an entire army, led by President George Washington in general's garb, to force the farmers into compliance.

Adams emphasizes the role taxes played in causing the Civil War. The Republican Party's key plank in the 1860 election was the imposition of a severe tariff, a disguised subsidy to northern industry that would have hurt the agrarian southern economy. Adams argues that the concessions Lincoln offered the South on the issue of slavery—including a constitutional amendment that would have preserved the "peculiar institution"—prove that economic exploitation of the South was a more significant cause of the war than was slavery. His view of the War Between the States makes this a particularly thought-provoking counterweight to the typical U.S. history text, which presents slavery as the prime cause of the war.

American history includes another tax on whiskey that led to yet another whiskey insurrection, this one a small-scale war between the moonshiners and the revenuers that began shortly after the Civil War. (At this point, the reader has to wonder if Americans were characterized more for their hatred of taxes or their love of good whiskey!) This whiskey rebellion can be regarded as successful, since the government chose to repeal a tax that the people simply wouldn't pay.

Adams then comes to the ugliest monster of them all, the income tax. He blames it for intruding into the private lives of citizens and chasing some of our most prosperous businessmen out of the country. For Adams, the IRS is an abomination. He reveals, for instance, that it paid agents according to how many foreclosures they caused. How quick the IRS has been to take cars, homes, or money, yet unbearably slow to fix its mistakes or the damage it caused to innocent people's lives! Adams also discusses the high death tax and how it causes the elimination of over 90 percent of family businesses after the founders die.

Those Dirty Rotten Taxes makes a strong case for abandoning intrusive direct taxation to the greatest extent possible. Adams, like the Founders before him, prefers indirect taxation, such as a sales tax, and so is no fan of any of the various flat tax proposals.

Those Dirty Rotten Taxes is not a rigorously documented book, unlike Adams's previous work, *For Good and Evil: The Impact of Taxes on the Course of Civilization*. It is lighter, and at times prone to hyperbole. But its straightforward view of the ingrained American antipathy to taxation is exhilarating. There are lots of illustrations and political cartoons, and the writing is engaging and easily understood. We highly recommend this book to anyone interested in taxes, history, or government. □

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Enterprising Southerners: Black Economic Success in North Carolina, 1865–1915

by Robert C. Kenzer

University Press of Virginia • 1997 • xvi + 178 pages • $30.00

Reviewed by Richard M. Gamble

In this meticulous and tightly argued volume, historian Robert Kenzer corrects what he describes as the prevailing "monolithic" view of the economic condition of North Carolina blacks in the 50 years between the end of the Civil War and the First World War. By no means dismissing or even minimizing the impact of racism and the legacy of slavery in shaping the black experience in those years, Kenzer presents compelling evidence of "slow but steady progress" in land-ownership and business enterprises. Drawing imaginatively on extensive primary statistical evidence, yet going far beyond mere quantitative history, Kenzer analyzes the range of economic, cultural, and political factors that encouraged economic success among an exceptional group of blacks in the postbellum South, a success that they took pains to pass on to their children through higher education for careers in teaching, the ministry, medicine, and business.

Kenzer found that blacks' success in acquiring land, launching viable businesses, and achieving political and social leadership in their communities was related to several clearly identifiable factors, some economic, some cultural. Land-ownership, for example, was highest both in amount of and value of acreage among blacks who had been free before the war, were mulattos, held non-agricultural occupations, and lived in the more fluid real estate market of the cities. Similar patterns held true for success in business and politics. To be sure, success was not limited to blacks who fit this statistical profile, but urban blacks who had been free before the war experienced the highest degree of success as landowners, businessmen, and political leaders.

From the perspective of free-market economics, two important contributions stand out in Kenzer's work. While not the main point of his study, his observations about blacks' relationship to the market economy and their network of self-help organizations bear noting. Black leaders in North Carolina defended an open market in real estate free from government intervention and special-interest legislation. Faced with proposed legislation in 1915 designed to prevent blacks from buying land in majority-white districts, for example, black leaders argued for a free market for both blacks and whites in which to buy and sell property under the most favorable terms.

Blacks simply wanted the freedom to acquire land and homes in an open market. Under pressure from like-minded white landowners, who did not want their freedom restricted either, the state senate rejected the bill. In business enterprises as well, black entrepreneurs proved their business savvy by their ability to adapt to changing market conditions, even in enterprises and localities formerly dominated by white Southerners. They understood that an open market was their friend, politics their enemy.

More striking is Kenzer's discussion of black leaders' efforts to strengthen their communities' economic and social well-being with a network of effective voluntary organizations. Local chapters of the Masons, for example, provided financial assistance and emotional support in times of sickness, unemployment, and bereavement. Drawing members largely from the black economic and political elite, these voluntary societies encouraged success by providing a framework of moral and ethical accountability and helpful practical experience in managing lodge assets.

To advance their business opportunities further, enterprising blacks also founded banks, building and loan associations, and insurance companies, and joined state and national black industrial organizations. The extent of black economic success that Kenzer recounts is both remarkable and at odds with the prevailing notion that post-Civil War blacks all lived in grinding poverty.

Beyond individual and collective economic success as landowners and businessmen, postbellum black elites in North Carolina also achieved a degree of political success. Beginning as loyal party members, generally in the Republican ranks but later in the Populist movement as well, blacks often held patronage jobs (such as tax collectors) before seeking elective office. They found political success as local, state, and national officeholders and, not immune to the temptations of rent-seeking behavior, used their positions to enhance their business opportunities, dispense patronage jobs, and shape tax policy.

Kenzer's history is intended for the specialist in American economic history, and the general reader may be put off by its comprehensive detail. Nevertheless, his gift for organization, his sense of narrative flow, and his effective use of telling anecdotes combine to make this an accessible study of the period even for the non-specialist. Overall, Kenzer has provided historians and economists with a convincing account of the diverse world of postbellum black success, a commendable book that is lucid, grounded in extensive archival research, conversant with the secondary literature, and a pleasure to read and learn from. □

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The Costs of War: America's Pyrrhic Victories

edited by John V. Denson

Transaction Publishers • 1997 • 450 pages • $44.95 cloth; $29.95 paperback

Reviewed by Doug Bandow

Advocates of limited government have long known that war and preparation for war are enemies of liberty. War obviously destroys lives and consumes wealth—new technologies have made genocide a simple matter of pushing a button. But war has another, long-lasting consequence: it centralizes power. "War is the health of the state," observed Randolph Bourne.

Many conservatives were willing to pay this high price during the Cold War because of the threat of hegemonic communism. But now America reigns supreme internationally. Those who believe in individual liberty must work to limit government power internationally as well as domestically.

John V. Denson's *The Costs of War: America's Pyrrhic Victories* provides a desperately needed call to arms. As he explains: "[B]ecause liberty is so fragile, its true defender recognizes that war is its greatest enemy, and therefore the true patriot is often the courageous individual who opposes a particular war because he recognizes that it is unjust—that it would be fought for the wrong

purposes or that the risk for the loss of liberty is greater than any benefit to be gained by the war."

The Costs of War emphasizes the fragility of liberty and chronicles the devastating impact of past conflicts. This comprehensive volume covers everything from the War of Northern Aggression (sometimes called the Civil War) to the role of conscription and the record of Winston Churchill.

Denson leads off with a sweeping essay on U.S. history. The nation's founders feared the costs of war, which is why they worked to prevent intervention in foreign conflicts. Their fears were well founded: the Civil War and Spanish-American War both spurred the growth of federal power. World War I, however, was a truly epochal event. Not only did the national government institute mass conscription and seize control of the economy, but, as Denson relates, "President Wilson followed Lincoln's example and ruthlessly crushed the civil liberties of those Americans who opposed his war." Although government power receded some after the conflict, World War II and the Cold War fueled state growth anew.

The lack of serious opposition to warlike policies today conflicts with America's long anti-interventionist tradition, of which Justin Raimondo, of the Center for Libertarian Studies, writes: "It wasn't just the founders who opposed fighting other people's wars. There was strong opposition to the Spanish-American War and World War I—which is why Wilson resorted to jackboot tactics against his critics."

What makes *The Costs of War* particularly valuable is its willingness to slaughter sacred cows. Such as Abraham Lincoln and his war for the Union—which ended up killing more than 600,000 people, distorting the constitutional order, and violating civil and political liberties. History professor Richard Gamble explores Lincoln's ugly legacy of the "destruction of the old Republic, a more modest federation with a regard for localism and states' rights, a sense of limits, and a relative freedom from foreign entanglement."

Equally subversive, but also persuasive, is the analysis of Winston Churchill's record by historian Ralph Raico. There is perhaps no more venerated figure from World War II, but Raico's view is rather less positive. He contends that "Churchill was from first to last a Man of the State, of the welfare state and of the warfare state." Indeed, argues Raico, war "was his lifelong passion." This is the record that virtually no one knows.

Some of the impacts of war are unintended and even unimagined. Allan Carlson of the Rockford Institute explains how war swells the state; in turn, "as the state grows, the family declines." He warns that the military today is "being used to re-engineer our society to serve the total state." He therefore calls on conservatives to "cast off lingering delusions about the 'conservative traditions' of the military."

Real patriotism means risking the lives and wealth of Americans when their future as a free people is at stake. *The Costs of War* illustrates why there may be no more important duty today for advocates of limited government than to steadfastly oppose war. □

Doug Bandow is a senior fellow at the Cato Institute and author of Tripwire: Korea and U.S. Foreign Policy in a Changed World. *He formerly served as a special assistant to President Reagan.*

Enviro-Capitalists: Doing Good While Doing Well

by Terry A. Anderson and Donald R. Leal

Rowman & Littlefield Publishers, Inc. • 1997 • 189 pages • $52.50 cloth; $16.95 paperback

Reviewed by Bruce Yandle

Writing about Austrian economics and the market process, Israel Kirzner explains how entrepreneurs play a crucial role in discovering products, markets, and processes for improving human welfare (*Journal of Economic Literature*, March 1997). The interesting aspect of all this is *surprise*. In Kirzner's view, entrepreneurs identify profit opportunities that, once revealed, seem rather simple and obvious. An accompanying expression of surprise usually charac-

terizes the outcome. The question "Why didn't I think of that?" is more common than the statement "Boy, that surely is complicated; I can't imagine how they came up with it."

Paper clips with wrinkles, self-serve supermarkets, moving assembly lines applied to auto production, Post-It notes—all relatively simple things that reflect a combination of imagination and market savvy. This is the stuff that built America's market economy. Is it possible for this same creative energy to provide improved environmental quality?

Readers of *Enviro-Capitalists: Doing Good While Doing Well,* by economists Terry Anderson and Donald Leal, will be convinced that the same unquenchable entrepreneurial spirit that delivers an abundance of food, clothing, communications, health, and other critical features of life can be relied on to deliver environmental quality—if only entrepreneurs could be encouraged rather than delayed and discouraged by government action.

The authors do not dwell on theories and assertions about free-market environmentalism. Instead, they recount fact-filled stories about past and present activities of enviro-capitalists. Those who erroneously cling to the idea that capitalism is inherently destructive to the environment will find their prejudices strongly challenged. This collection of stories about real people and their profit-making ventures in environmental production reminds us again that capitalism works.

We learn, for instance, about Joseph Crisafulli, a successful entrepreneur in Glendive, Montana, who established a paddlefish roe enterprise. He discovered that paddlefish roe would pass the market's test for caviar. Sensing a profit opportunity, Crisafulli and other town business people began a paddlefish cleaning service for fishermen who prize the fish but dislike cleaning them; they obtained pounds of valuable roe in the bargain.

However, Crisafulli and his associates had to work through a deep political bureaucracy. They needed permission from both state and federal regulators before beginning their enterprise. Moreover, the regulators insisted that net proceeds go to "community improvements" including the preservation of the habitat of the fish. They consented to these dictates, which happened to largely coincide with their plans, but it is easy to imagine that bureaucratic red tape and micro-management could easily stifle other environmental projects.

Another case the authors discuss is International Paper's realization that large amounts of its forestland produced more wealth when managed and maintained as wildlife habitat and recreational space than when used as a source for cut timber. This led the firm to allocate more than a million acres of land to those purposes. Why did International Paper do it? The same reason that causes the firm to search for lower-cost paper and timber products—profit. Market forces are delivering environmental quality.

What about Yellowstone, that paragon of America's park system? Was it the unblemished foresight of government that preserved this collection of natural wonders? Hardly. Instead, we learn that "robber baron" railroad capitalists recognized the market value of the territory that became Yellowstone Park. Seeing a promising attraction for eco-tourism and rail traffic, railroad capitalists sought to purchase the land from the federal government, but were prevented from doing so by an egalitarian federal law limiting land ownership to only 160 acres. Frustrated in their attempt to purchase the asset they wanted, the railroaders then lobbied for Congress to establish Yellowstone National Park and once it had done so, they promptly built the rail lines and hotels.

Anderson and Leal also explain how entrepreneurs are finding market niches for protecting endangered species, such as the peregrine falcon. The common assumption that government action is the only means to protect species cannot survive a reading of this book.

Enviro-Capitalists should be read both by environmentalists and friends of liberty. True environmentalists, those who seek to protect the precious biological envelopes that support life and are not simply dedicated to the replacement of individual freedom with command-and-control regulation, will be encouraged to know that markets are on their

side. Friends of liberty, who sometimes find themselves hard-pressed to defend markets in the face of attacks from environmentalists, will welcome the reinforcements provided by this excellent, if too-short book. □

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Higher Superstition: The Academic Left and Its Quarrels with Science

by Paul R. Gross and Norman Levitt

Johns Hopkins University Press • 1997 • 314 pages • $35.95 cloth; $16.95 paperback

Reviewed by Thomas F. Bertonneau and Richard L. Cutler

Science, along with the technology that develops out of it, is a unique and vital source of the high civilization in which we dwell. Science is enthroned as the reigning model of Enlightenment thought; the methods of science represent an epistemology involving objectivity, real-world absolutes, and the pursuit of truth through hypothesis, observation, validation, replication, and prediction. Science presents an ordered, reasoned, rigorous world marked by precision, unambiguous definition, and the established rules of logical argument.

If science is the monarch of our worldview, however, it is increasingly the target of would-be revolutionaries and regicides—members of what Paul Gross (professor emeritus of life sciences at the University of Virginia) and Norman Levitt (professor of mathematics at Rutgers University) identify as the "academic left," who insist that there are no absolutes, that objectivity is a fiction used by vicious oppressors, and that the world is essentially chaotic.

Higher Superstition is a defense of science against attempts by badly informed nonscientists to dethrone and discredit the Western tradition of scientific investigation. They were not satisfied with their deconstructive wastelaying among the treasures of Western art and literature. They make the same claims, say, for Newton and Darwin as they do for Shakespeare and Melville: all authority and claims to truth are but shams whose only purpose is to protect the unjust distribution of power that earmarks our "oppressive" society. Feminists, for example, indict Newton for attempting to master the universe by constraining it under "patriarchal" laws and Darwin for his "male" notion of the survival of the fittest.

Gross and Levitt note that claims of this type are not entirely new—prototypes may be seen in Rousseau and Blake—but they argue that in America's colleges and universities the anti-science ideology has grown dangerously influential. Academic careers are now built on jeremiads against "sexist" canons of proof-through-replication and the alleged exclusion of women (that is, feminists) from scientific debate. Ideas that used to be regarded as the rantings of reactionaries now find fulsome praise in the tracts of academicians who claim to be in the vanguard of radical liberation.

When one remembers the distortions that Soviet biology suffered under Lysenko's Stalinist genetics, it becomes clear that the real conflict is not between reactionism and science but between power-mongering and science. It is no coincidence that the left-wing professors who think that they can play the same games with the third law of motion that they do with Virgil and Shakespeare generally follow Michel Foucault, a pseudo-Nietzschean who claims that there is no knowledge, only power, and that those who have power are, a priori, evil. That this position entails a claim of knowledge and that its exponents themselves wantonly seek the very power that they denounce never enter the argument.

Nuttiness among intellectuals flourishes perennially. So tight is the grip of the left on institutions of higher education, however, that Gross and Levitt fear an impending struggle in which affirmative action will force science departments to change their practices under naked political pressure. The authors also see another problem. Real science is so badly taught to undergraduates that many get only "science studies" courses concocted by the postmodern anti-scientists. Gross and Levitt decry the trendiness of schools of education that have embraced anti-science and that send

into K-12 schools newly certified teachers whose knowledge of physics, chemistry, and biology is nugatory.

In their penultimate chapter, the authors speculate on the psychological origins of anti-science. They trace the pretensions of the feminists, earth-worshipers, and "deep ecologists" to resentment. Precisely because science succeeds, and because it so impressively informs the daily reality of modern life, the intelligentsia feel diminished; they exercise no similar influence. A feeling of inferiority breeds petulance, manifested in puffed-up vocabularies, moral posturing, and a need to disparage. Those who hate the West because they despise their own paltriness naturally attack science and scientists as ready scapegoats.

Representatives of the sciences, Gross and Levitt say, have too long stood on the sidelines, amused perhaps by the display of folly. The time for that is over; the folly portends real danger. Science must begin to answer the absurd but pernicious claims of anti-science, if only to remind the public that the strutting peacocks of postmodernism are not free from chastisement, and that their fantail of claims collapses—epistemologically speaking—at the pressure of a glance. □

Thomas Bertonneau is the author of Declining Standards at Michigan Public Universities *and teaches literature at Central Michigan University. Richard Cutler is president of the Michigan Association of Scholars and a former vice president of the University of Michigan.*

Between Power and Liberty: Economics and the Law

edited by Richard M. Ebeling

Hillsdale College Press • 1998 • 169 pages • $9.95 paperback

Reviewed by Philip R. Murray

Between Power and Liberty: Economics and the Law, is the publication of the 1997 Ludwig von Mises lectures at Hillsdale College. The book's title comes from James Madison's description of the Constitution and the Bill of Rights: "every word . . . describes a question between power and liberty."

The essays in this book brilliantly make the case for liberty over power. Three key points emerge: First, that private property is the key to individual liberty. Second, that the Constitution was intended to protect private property against government intrusions. And third, that we have reasons to be optimistic, despite the panoply of governmental restrictions on our private property and individual liberty.

Richard Ebeling, chairman of Hillsdale's economics department, contrasts "The Free Market and the Interventionist State." The role of government in a free society, he argues, is to protect private property, maintain order, and thus maximize the incentive to create wealth. Interventionism violates property rights so that government officials can redistribute wealth according to their own plans. Ebeling laments the conception of "public policy" as synonymous with government intervention. Discussions of public policy almost always center on "What can the government do?" instead of "What can we do as individuals?" or even "What did the government do to get us in this mess in the first place?" Ebeling explains how to defend the free market against attacks based on spurious economic theory, "social justice," and "the public interest." Those who wish to improve their ability to defend the market will learn much from his essay.

Several of these lectures make an excellent introduction to constitutional economics. Hillsdale President George Roche notes that the Declaration of Independence proclaims the "unalienable Rights" of individuals, as opposed to the idea that rights are grants from the state. He outlines the economic philosophy of the Constitution: that government taxation, borrowing, and spending should be kept to a minimum and that government should permit free trade to grow.

Cato Institute fiscal analyst Stephen Moore calls the Constitution "A Rulebook for Government." He says that "No matter how long one searches, it is impossible to find in the Constitution any language that authorizes at least 90 percent of the civilian programs that Congress crams into the federal budget." Moore relates that early in our nation's histo-

ry members of Congress and presidents used to reject even charitable acts of government spending as unconstitutional. What led to the current high levels of government spending? The Sixteenth Amendment (which permitted a federal income tax), a glaring misinterpretation of the "general welfare" clause of the Constitution, and the New Deal.

No discussion of economics and the law would be complete without recognition of the great French economist Frederic Bastiat. Harry Browne explains Bastiat's definitions of "the law" and "the law perverted." The law protects life, liberty, and property. The law perverted transfers property. For example, Social Security taxes the income of workers and transfers it to retirees. The law perverted plunders people rather than protecting them. What are the results of using the political process instead of the market process to achieve what we want? Roche puts it well: "The average person no longer looks to his own talents to get ahead; he looks to the state."

Despite the reduction in our property rights and the corresponding loss of liberty, we have reasons to be optimistic about the future. In his essay, "The Grassroots Legal Reform Movement," Clint Bolick of the Institute for Justice recounts his organization's successes in eliminating restrictions on economic liberty through constitutional litigation. Likewise, Bernard Siegan sees promise in a revival of the "takings" clause of the Fifth Amendment, which bars government from taking property without paying for it.

Perhaps the most valuable contribution these lectures make is their emphasis on self-government. It is primarily the duty of each citizen to restore liberty through the practice of self-government. This means refusing to take assistance from government and using our own talents in conjunction with the voluntary cooperation of others to live the free, responsible life. □

Philip Murray is an associate professor of economics at Webber College in Babson Park, Florida.

The Foundations of Morality

by Henry Hazlitt

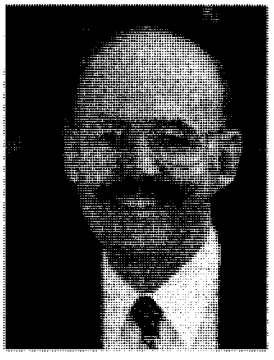


In this impressive work Hazlitt explores the proper foundation of morality. It would give the game away to reveal his conclusion, but suffice it to say that Hazlitt conducts a detailed and scholarly inquiry into the many possibilities.

Leland B. Yeager, noted economist, has written a new foreword to the book, in which he says that *The Foundations of Morality* "provides (in my view) the soundest philosophical basis for the humane society that is the ideal of classical liberals."

This challenging work on ethics fits in the great tradition of Adam Smith's *Theory of Moral Sentiments* and David Hume's *Treatise of Human Nature.* It is a well-reasoned, tightly argued book that amply rewards its readers.

398 pages Regular Price: ~~$18.95~~ Sale Price: **$14.95**



The ILO's Strange Use of Words

Last June the International Labor Organization (ILO) put forth its "Declaration on Fundamental Principles and Rights at Work." U.S. Labor Secretary Alexis Herman asserted that the declaration is "a big step forward for the ILO and its members as we enter the 21st century." John Sweeney, president of the AFL-CIO, called it "an historic breakthrough that dramatically underscores the importance of basic rights for workers in the global economy."

The core of the declaration requires the governments of all ILO member countries "to promote and to realize, in good faith" four basic principles: "(a) freedom of association and the effective recognition of the right to collective bargaining; (b) the elimination of all forms of forced or compulsory labour; (c) the effective abolition of child labour; and (d) the elimination of discrimination in respect of employment and occupation." Forty-three developing countries refused to support the declaration because they saw it as an attempt by industrialized countries to eliminate their competitive advantage in labor costs and as a pretext for the imposition of protectionist trade restrictions. They were right. That, I submit, is what makes Herman and Sweeney tingle all over.

While all classical liberals can enthusiastically agree to item (b) in the declaration, item (c) is problematic. Today's industrialized countries abolished child labor by statute only after labor productivity had risen to the point that markets had abolished it by choice. Item (d) is also problematic because of the wide variety of meanings attached to the word "discrimination." In the United States, for example, most so-called civil rights leaders say that it is discriminatory not to discriminate. Moreover, elimination of discrimination in employment by law often means legal mandates to pay equal wages for labor services of unequal value.

However, most problematic of all is item (a). What does it mean? If "freedom of association" means that government is forbidden to interfere with individuals who wish to affiliate with each other for legal purposes, or to interfere with other individuals who choose not to enter into such affiliations, then I concur. If "collective bargaining" means voluntary bargaining involving individuals who have each chosen to be represented by the same agent, then I concur.

A brief glimpse at ILO documents through the years, however, shows that this is not what the organization means.

Its definitions of these terms are made clear in the 1994 report of its Committee of Experts, "Freedom of Association and Collective Bargaining," and in how its Committee on Freedom of Association applied these principles in its 1994 evaluation of New Zealand's Employment Contracts Act (ECA).

The Committee of Experts wrote that "trade union rights violations may . . . result by reason of legislation . . . which favour[s]

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individual rights to the detriment of collective rights." This distinction between individual rights and collective rights is curious. Human rights reside in individuals. They are prior to government, and it is government's duty to protect them for all individuals. Individuals can voluntarily associate with each other in the pursuit of legal ends, but the association is nothing more than the sum of its constituents. It can have no rights other than the rights that its individuals bring into it, and those individuals have exactly those rights that all individuals have, no more and no less.

The ILO endorses rights to trade-union association that are distinct from, and in conflict with, individual rights to free association. It asserts that those who wish to join trade unions must be free to do so, but it does not say that those who choose not to join, be represented by, or to pay union dues should be free to abstain. In 1947 the ILO rejected an amendment to its Convention No. 87, "Freedom of Association," that would have "grant[ed] workers the right not to join an organization." But correctly understood, freedom of association means just that. Likewise, the Experts endorse the principle of exclusive representation, under which unions are granted the legal privilege of representing workers other than their voluntary members. They also espouse union security, which means workers can be forced to join unions or at least to pay union dues.

Article 4 of the ILO's Convention No. 98, "Right to Organize and Collective Bargaining," states, "Measures . . . shall be taken . . . to encourage and promote the full development and utilization of machinery for voluntary negotiation between employers or employers' organizations and workers' organizations." This sounds good but it's not what it seems. First, note that individual employers can bargain with workers' organizations, but there is no provision for individual workers to bargain with employers. The word "voluntary" doesn't apply to workers who choose to bargain for themselves. Furthermore, the Experts approve mandatory good-faith bargaining between trade unions and employers. Under this principle employers are forced to bargain with unions and to make concessions to unions. The word "voluntary" in Article 4 is meaningless.

New Zealand's ECA became law in 1991. It eliminated almost all forms of compulsory unionism. Individual workers are free to decide whether to represent themselves or to authorize an agent to represent them. Agents can be unions, individuals, or non-union organizations. While employers must recognize agents chosen by individual workers, they do not have to bargain with them. Unions may represent only workers who choose to join. There can be no forced membership or forced dues. Employers and workers are free to choose whether to enter individual or collective contracts. In 1993 the New Zealand Council of Trade Unions complained to the ILO that the ECA violated Conventions 87 and 98 on freedom of association and the right to collective bargaining. The 1994 "Report of the Committee on Freedom of Association" that evaluated the complaint speaks for itself: It could not accept the ECA's "underlying philosophy, which puts on the same footing (a) individual and collective employment contracts, and (b) individual and collective representation."

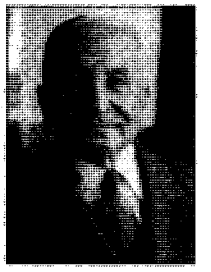
Imagine that! The ECA "allows" workers freely to choose to negotiate employment contracts individually or collectively. But the ILO doesn't approve. It prefers "promoting and encouraging" (read "coercing") mandatory good faith collective bargaining through trade unions vested with collective rights that trample individual rights.

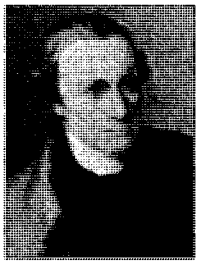
This is Secretary Herman's "big step forward into the 21st century" and John Sweeney's view of "basic rights for workers in the global economy." In reality the ILO's views are based on the nineteenth-century idea of class struggle and the twentieth-century illusion that the working class needs compulsory trade unionism to defend itself against predatory employers. In my view the ECA is the real giant step forward into the 21st century precisely because it is based on *genuine* rights. □

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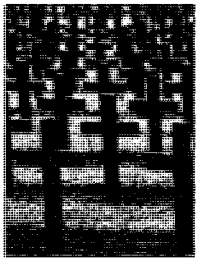
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Cover image of World War I soldiers courtesy of Lebanon County (Pa.) Historical Society.

PERSPECTIVE

Life Imitates Gilbert

In jolly old England Queen Elizabeth II has stripped the hereditary peers of their parliamentary power in the House of Lords. The act constitutes the leveling of the dukes, earls, marquesses, viscounts, and barons, some of whose titles go back to William the Conqueror, Duke of Normandy, who subdued England in 1066 and became William I.

For devotees of another William—William Schwenck Gilbert (1836–1911)—this all has a familiar ring. Gilbert, of course, was the liberal spirit and comic librettist who with Arthur Seymour Sullivan composed the greatest collaborative effort by Englishmen ever—Monty Python, Lennon and McCartney, and Churchill and Bomber Harris included. Mencken called Gilbert "even above Mark Twain, the merrymaker of his generation."

Gilbert's arsenal of jibe and joke and quip and crank was reserved almost exclusively for men of rank. As his alter ego, Jack Point, put it in *The Yeomen of the Guard*:

> At peer or prince—at prince or peer,
> I aim my shaft and know no fear!

Gilbert played with the idea of radical change in the House of Lords in his and Sullivan's opera *Iolanthe*. In synopsis, a band of fairies casts a spell on the Lords for coming between a young shepherd and his betrothed, Phyllis. Magically, Strephon is seated in Parliament and "carries every bill he chooses." But the fairies go further. Speaks the Fairy Queen:

> Peers shall teem in Christendom,
> And a Duke's exalted station
> Be attainable by Com-
> Petitive Examination!

Gilbert had no more mercy for the Peers than the Fairy Queen did. His Lord Mountararat explains that an undistinguished group of noblemen had never barred England from greatness in the past.

> When Wellington thrashed Bonaparte,
> As every child can tell,

The House of Peers, throughout the war,
Did nothing in particular,
And did it very well:
Yet Britain set the world ablaze
In good King George's glorious days!

Even a lowly sentry knew the score. Private Willis points out that members of Parliament, "if they've a brain and cerebellum, too," leave their brains outside Westminster Hall "and vote just as their leaders tell 'em to." Not that that's a bad thing:

But then the prospect of a lot
Of dull M.P.'s in close proximity,
All thinking for themselves, is what
No man can face with equanimity.

All ends well, of course. Each Lord marries a fairy—happily exchanging House of Peers for House of Peris.

No moral here, just an observation: Gilbert saw hereditary rank, and government in general, as something to be knocked down a notch. It's good to see the world catching up with him.

* * *

It cannot be said too many times: Property is the key to liberty, justice, and prosperity. Which is why Tom Bethell's new book, *The Noblest Triumph*, is such a welcome addition to the literature of freedom. In the excerpt reprinted herein Bethell examines the crucial connection between property and justice.

Speaking of justice, more than a few people think the gap between what corporate CEOs and workers are paid is a scandal. The gap is real; the injustice is illusory, as Charles Baird demonstrates.

Since the atrocious murder of a young homosexual man in Wyoming last year, the push for a national "hate crimes" law has been renewed with vigor. Not so fast, writes Melissa Suarez, who finds good reasons to be wary about well-meaning legislation aimed at states of mind.

In 1943 the great classical liberal Ludwig von Mises wrote a book about Mexico's economic problems. The manuscript lay forgotten in his papers until our own Bettina Bien Greaves found it in 1997. It was translated into Spanish and published in Mexico. Eduardo Turrent discusses the significance of Mises's work.

The cost of government regulation is not merely the money spent but the untold things we must do without because innovation is stifled. Eric Nolte provides a glimpse of what we would be enjoying were the federal government not regulating aviation.

The Western idea of limiting government power—and clearing a large space for individual creativity—is the product of a long, complex, and unplanned historical process. Tom Palmer takes us on the consequential journey from servitude to freedom and back.

Everyone knows that Americans save too little. Too few know why. John Hood puts the idea of saving into historical perspective and comes to some provocative conclusions.

Remember the last time the government declared some problem solved and disbanded the agency charged with solving it? Neither do we. Harold Jones, Jr., says it's not our memory that is failing.

To win someone over to the freedom philosophy, it helps to connect with the intuitions he already possesses. James Otteson sets out a game plan for persuading philosophers that liberty is indivisible. It's not just for philosophers.

In columns this month, Lawrence Reed inveighs against "living wage" legislation, Dwight Lee expounds on opportunity costs, Doug Bandow revisits the stupidest war of the twentieth century, Mark Skousen ponders the millennium bug, and Russell Roberts, our newest contributor to "The Pursuit of Happiness," looks for the unseen. Lawrence White mulls over Jagdish Bhagwati's nod to capital controls, and counters, "It Just Ain't So."

Books that come under review this month deal with the war on tobacco, the ten "worst" presidents, the post-communist world, judicial corruption, and Paul Johnson's history of America.

—SHELDON RICHMAN

THE FREEMAN
Ideas On Liberty

Asia Needs Capital Controls?

It Just Ain't So!

Citing the East Asian financial crisis, the well-known trade economist Jagdish Bhagwati has recently given support to retaining capital controls in developing countries. In essays in *Foreign Affairs* and more recently, the *Wall Street Journal* ("Yes to Free Trade, Maybe to Capital Controls"), Bhagwati cautions that the "overwhelmingly powerful" case for free trade does not imply an equally strong case for free capital flows because there is "a unique downside to a policy of free capital flows." The downside is that "capital flows are subject to what the economic historian Charles Kindleberger of MIT has called panics, manias, and crashes."

Bhagwati contends, against the well-known argument that speculators who bet against fundamentally strong economies will be disciplined by losses in the marketplace, that "the unfortunate fact is that speculation can be self-justifying." That is, by abandoning an economy, investors can themselves weaken it. He asks rhetorically: "Is this not what most likely happened when, out of panic, investors fled from what they perceived as weakened Asian economies, weakening them when they were originally strong?"

No, this is not what most likely happened. Blaming investors for the fall of the Thai bhat or the Indonesian rupiah is like blaming umbrella-carriers for the fall of rain. Capital flows can of course be volatile, but attributing a shift in the behavior of independent and calculating investors to a self-validating "panic" or "mania" is at best an explanation of last resort. A large speculative attack on a central bank to get foreign currency before the fixed exchange rate collapses—like an old-fashioned run on a deposit bank to get cash before it is gone—*could in principle* be self-validating, because a central bank with fractional reserves will eventually run out of foreign currency reserves and be forced to devalue.

But *in practice* the speculative attacks we witness are not of this self-validating sort. Just as the historical evidence indicates that nineteenth-century runs on deposit banks were generally triggered by bad news indicating the likely insolvency of those specific banks, speculative attacks on fixed exchange rates are generally triggered by bad news about economic fundamentals. The idea that unrestricted financial markets are prone to manias or bubbles is founded on historical myth, as my colleague George Selgin has shown by re-examining the historical episodes cited by Kindleberger and others as supposed examples of bank-lending manias (*Journal of Financial Services Research*, August 1992).

At its root, the fall of their currencies' exchange values, and the subsequent reversal of capital flows to Thailand, Indonesia, the Philippines, and Malaysia, were votes of no confidence in the exchange-rate and monetary policies of their governments. It is of course a challenge to explain the exact timing and size of the dramatic shifts observed. But if some sort of pure self-validating mania or panic had been afoot in the region, it would be hard to explain why Hong Kong, Singapore, and Taiwan were spared devaluations.

The countries that crashed were basically those where expansionary monetary policy was on a collision course with the supposed commitment to a fixed exchange rate against the U.S. dollar. As basic exchange-rate theory tells us, a fixed exchange rate between the local currency and the dollar cannot be maintained unless the creation of local money is limited to the amounts consistent with holding the local inflation rate down to the U.S. dollar inflation rate.

To generalize rather sweepingly, large amounts of capital had flowed in during the 1990s because, if the exchange rates really did remain fixed, high real returns were available from nominal interest rates well above U.S. dollar rates. Local commercial banks became loaded with poor-quality loans, in some degree because of government intervention or corruption in allocating loans, and in some degree because of excessively risky lending encouraged by implicit government guarantees to the banks. The nonperforming loans of Indonesia's banks, for example, reached more than a quarter of total loans before 1996. International investors finally lost faith because it became clear that the central banks, when forced to choose, would print money to keep the banks afloat rather than exercise the monetary restraint necessary to maintain the fixed exchange rate.

The succession of crises in several southeast Asian countries, beginning with Thailand, has led many commentators to speak of a "contagion" by which crisis spreads from one country to another. The solution supposedly lies in global crisis management by the IMF. But as Anna J. Schwartz has noted in the *Cato Journal* (Winter 1998), "it was not contagion from Thailand, however, that made the countries vulnerable to a financial crisis. They were vulnerable because of their home-grown economic problems. Capital flight from countries with similar unsustainable policies is not evidence of contagion."

Capital flight imposes a very useful, if sometimes harsh, discipline. As former Citicorp CEO Walter Wriston notes (in an interview with *Wired*), the flow of short-term capital "functions as a plebiscite" on a government's economic policy. When a change in policy is observed, "by the end of the day, the market will have conducted a referendum reflecting the collective wisdom of people all around the world on what they think of [the new] economic policies. If your economic policies are lousy, the market will punish you instantly." Wriston adds: "I'm in favor of this kind of economic democracy. There's nothing you can do to change it, except do right."

Governments, of course, deeply resent the discipline that the market imposes. In an interview with *Business Week* earlier this year, Malaysian Prime Minister Mahathir Mohamad blamed the fall of the ringgit on the "herd" mentality of currency traders, likening them to "buffaloes." Even more notoriously, he intimates that "since most of the currency traders are Jewish, and it affects Muslim countries in East Asia, people will think this is a Jewish conspiracy." The Prime Minister imagines that the traders, acting with one mind, can "devalue our currency at will," and that doing so is a riskless get-rich-quick scheme: "When you devalue currency and you short-sell, you make a lot of money. You just push figures on a computer screen, and you make a billion dollars." One marvels that a conspiracy of traders would have waited until 1997 to grab this windfall.

In September, Mahathir announced new restrictions on the convertibility of the ringgit. Among other measures, Malaysian citizens may not take more than small amounts of cash out of the country when they travel abroad. Restrictions of that sort are a nuisance. Still more damaging to prosperity are the restrictions many developing nations impose on large financial outflows. Such capital controls are a cruelly effective investment repellent. No investor wants to bring wealth into an economy where it might become trapped.

It is sad enough when a politician engages in scapegoating and uses it as an excuse to restrict his citizens' freedom to trade in financial contracts. The shame is compounded when a well-meaning economist countenances the herd-mentality view of foreign exchange markets and derives from it a counsel of hesitation in lifting capital controls.

—LAWRENCE H. WHITE
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THE FREEMAN
Ideas On Liberty

To Each His Due

by Tom Bethell

We lead lives that are so immersed in private property that we easily take its benefits for granted. Some everyday situations give us the opportunity to examine aspects of life without it, however. They permit us to see the great transformation that takes place when a communal arrangement is privatized: efficiency is enhanced, and, far more important, justice itself is routinized. The argument can be illustrated by an apartment building in Washington, D.C., in which the author lived. In one significant respect, the living arrangement resembles Plymouth colony. It is a condominium building of approximately 300 privately owned apartments, bought and sold on the free market. Its total population is perhaps twice as large as that of Plymouth in the 1620s. Owners are assessed a condo fee, arrived at by adding up all expenses jointly incurred, and dividing them by a formula that takes into account the size of the apartments. But for the sake of simplicity, it is here assumed that all units are the same size and that all owners are charged the same condo fee.

The key point is that there are no individual utility meters. The entire building is "master metered" as an undivided whole. The utilities—gas, water, fuel oil, and electricity—make up about one-third of the building's million-dollar annual budget. In the consumption of energy, then, great opportunities for free riding occur.

How are property rights to utilities allocated in the building? All apartment owners (or their tenants, for many units are rented) may use as much water, electricity, and heating oil as they like, without limit. Each owner is then assessed approximately one three-hundredth of the building's total utility bill. In short, it would be a miraculous coincidence if consumption and billing were proportional. In the absence of separate meters, it is very difficult or impossible to achieve such proportionality. This leads directly to the following scenarios. Both are hypothetical, but plausible.

Meticulous Mary

Consider first Mary, a resident who conscientiously turns off her lights and turns down her thermostat. By the end of the year, she will have reduced the building's overall energy consumption by a small amount, and will personally "recapture" only one three-hundredth of her own saving. She will export to everyone else in the building the benefit of her frugality, but will herself experience the full cost of that frugality (in terms of dimmer lights, hotter summers, and chillier winters). And she will receive a bill only fractionally lower than it would have been if she had been an "energy hog." Let us assume that by her frugality, she saves $150 in utility consumption in the course of a year. That saving is then

Tom Bethell is the author of The Noblest Triumph: Property and Prosperity Through the Ages *(St. Martin's Press, 1998), from which this is excerpted with permission of the author.* *Copyright © Tom Bethell.*

spread over the entire building. As a result, her condo fee—and that of everyone else—will be reduced by 50 cents per annum.

Now we come to Tom, her neighbor (whose resemblance to the author is entirely coincidental). At the supermarket, he buys high-wattage light bulbs, and when he goes out in the evening he carelessly leaves lights on; he turns up the heat in the winter and lets the air conditioner run in the summer. But he will bear only one three-hundredth of the cost. Master-metering and equal division of the bill permits him to saddle everyone else with the consequence of his extravagance, and yet to enjoy the benefits himself. He lives comfortably and makes others pay for it.

Consider what happens when he goes away for a week in August. He briefly considers, in a moment of public-spiritedness, turning his air conditioner off. Then he thinks again: He will have to return to a hot apartment, which will take hours to cool down. So he leaves the unit running. Let us say that the additional cost of this extravagance is $15. Consciously or subconsciously, he may have performed the following calculation: *He* will pay only one three-hundredth of this increment, which is to say five cents. But so will everyone else. His cost of enjoying a cool apartment during the few hours that it would otherwise be hot is a nickel; but everyone else in the building will be unjustly burdened with an additional nickel as well.

Such an arrangement obviously encourages wasteful consumption. Historically, the building's utilities bills have slowly risen, as a percentage of overall expenditures, despite the gradual replacement of inefficient electrical equipment by more modern hardware. When you drive past the building at night, it is a Christmas tree of blazing lights. A spokesman for the Potomac Electric Power Company reports that when individual meters are installed in such buildings, energy consumption usually drops by about 25 percent.

Separate Meters

The corrective mechanism is readily at hand—separate meters for each apartment. The condo equivalent of separate checks, meters would effectively privatize utilities within the building. Thanks to the walls separating one unit from another, energy *consumption* within the building is already privatized. The role of meters is to permit billing in proportion to consumption. The utilities in the building would then be converted from communal to private property.

But the internal politics of the building make such a remodeling change difficult to carry out. The rewiring is expensive. Admittedly, the energy saving is large enough to permit the cost to be recaptured, perhaps within ten years; but the condo board is reluctant to consider such an expenditure, mainly because the owners of the units (which is to say, the people who elect the board) generally do not consider their investment in the building to be a long-term one. The building's future may not be in their future. Most are planning to sell and move out within a few years, and do not want to finance improvements that may benefit the next generation of occupants more than it will benefit them.

Admittedly, separate meters would increase the value of the building, and the sale price of apartment units would rise commensurately. A persuasive board could possibly prevail on the membership to approve such an expense. In reality, however, the problem of free riding in utilities is virtually invisible. When the great scope for free riding was brought up at a board meeting, one member responded that *less* energy would surely be used in a situation where everybody "took in" everybody else's consumption. He was persuaded otherwise, but this showed that the free-rider problem is not intuitively clear, even to those elected to an office in which they are expected to hold down costs. The inconspicuous nature of the problem, and the visible upfront cost of correcting it, ensures that the issue is perennially postponed. (The problem may eventually be solved by the development of less-expensive metering technology.)

Let us take the logic of communal utilities one stage further. Suppose that board members do conclude that the single-meter system is intolerable. But they resist installing separate meters, let us assume, not just because of the expense, but also because the board mem-

bers share a philosophical aversion to privatization. They recognize that free riding in utilities results in winners and losers—good people subsidizing bad people—and they decide that this must be corrected. So they declare a goal of "eliminating energy selfishness," and "achieving energy justice" within the building, but without privatizing. How can they do this?

First, they try exhortation. Slogans are posted in elevators and along corridors, circulars are slid under doors, THINK OF OTHERS! TURN OFF LIGHTS WHEN NOT IN USE! A big sign is placed along the roof (as in Soviet Moscow): "Another Building Dedicated to Energy Fairness and Justice!" But within a few months, it is clear that this is not having the desired effect. Tom ignores the signs, Mary is more frugal than ever.

Now the condo board adopts a sterner measure. "Energy monitors" are hired, and they spend their evenings patrolling the corridors and knocking on doors. "Is anyone at home? The weather just turned cooler. Did you turn down your air conditioning?" But after a few months the occupants learn to ignore the knock. Mary has already been doing the right thing. Tom remains unregenerate. Energy consumption remains at its old level.

Then a more drastic step is taken. The energy monitors are provided with apartment keys. It is explained to all occupants that the invasion of privacy will be minimal, because the monitors may enter only after knocking and receiving no reply. That way, they will only enter apartments when people are not at home, "and when people are away, they shouldn't have their lights and air conditioners on anyway." After a while, however, it is discovered that some apartment owners, who are in fact absent, learn to reply to the knock with prerecorded "decoy" messages. Others bribe monitors to stay away.

Meanwhile, the board has saddled the building with a considerable new expense: wages for the energy monitors. And so it goes. Nothing seems to work. Eventually the monitors are given full police powers and may enter any apartment at any time. How does the board justify this final, draconian step? They cite a twentieth-century authority on the subject. It was Lenin who said, in 1918: "We recognize nothing private."

The scenario is fanciful, of course, because the membership would have elected a new board long before the conflict escalated to such a level; or the members would have sold their apartments and left the building. Nonetheless, it is useful in suggesting that if private property is banished, and exhortation (or "education") is put in its place, both economic efficiency and justice will prove elusive. If coercive measures are introduced, privacy must be swept aside.

The Morality of Private Property

According to Gresham's Law, bad money drives out good. According to the logic of the commons, bad people drive out good. Consider an example that may appear unrelated to energy consumption: the federal budget. The budget can be thought of as a common pool of money replenished every year with approximately 1.7 trillion dollars from taxpayers. Gathered around the pool are 435 congressmen and 100 senators. What gives them power and influence is that they have exclusive "siphoning rights." They are subject to the constraint that siphoning operations can proceed only if a majority participates simultaneously. When this constraint is satisfied, money can be siphoned out and channeled back to constituents within the congressional districts. The necessary majorities may be achieved by "logrolling": one congressman votes for a project in a colleague's district, in return for a reciprocal favor for his own, and so on.

Federal spending keeps on rising for the same reason that utility consumption keeps on increasing in master-metered buildings. Congress itself is "master metered," because the taxpayers, like the residents of our apartment building, are all "billed" at the same rate, whether or not federal projects are financed in their districts. The point is that the federal tax code is the same in all states. This encourages all legislators to behave like energy hogs—to siphon from the common pool as fast as they can (that is, to vote for most spending bills).

Suppose that a candidate campaigns on the promise that, unlike his opponents, he will be cautious with the taxpayers' money. He will dare to vote "no" on spending bills when he gets to Washington. The problem is that his restraint, meritorious though it may be, will not encourage a like restraint in others. On the contrary, it will leave more money for them to siphon back to *their* districts. It is unlikely, then, that such a candidate will be elected. But let us assume that he is.

Having arrived in Washington, he figures out something that he hadn't quite visualized on the campaign trail: If he votes "no" on spending bills, he will frequently deprive his constituents of an opportunity to get back from Washington what they put into the common pot (in taxes). So, instead of voting to hold down spending, he joins in the general logrolling, teaming up with other big spenders to form majorities (some of the money being earmarked for his district). Some voters back home, recalling his campaign promise, may think that he "sold out." In reality, it was the institutional arrangement of Congress that encouraged his change of heart, not weakness.

The analysis of the budget as a "commons" helps to explain why voters tend to elect both big-spending legislators and fiscally conservative presidents. Armed with the veto power, and with influence over tax proposals, the president (unlike the separate legislators) is in a position to hold down the size of the overall "pool." It also helps to explain why voters will tend to support limits on congressional terms. They give voters an opportunity, not available in regular congressional elections, to effectively vote against all the other legislators—the ones who are siphoning dollars away to remote and unknown places.

The budgetary equivalent of individual meters would be to change the tax code so that the income-tax rate would be adjusted up or down in each congressional district, depending on how much the Congressman from each district voted to spend in the previous year. Big spenders would then impose high tax burdens on their own constituents. It is a safe prediction that this reform would bring about a rapid decline in federal spending, and all talk of the budget deficit would be a thing of the past. Needless to say, no such reform of the tax system is contemplated. . . .

To return to the condo case, readers will no doubt agree that the installation of individual meters in an apartment building will reduce energy consumption: that is, that it will be economically efficient. But the more important point is that such a change will also introduce the missing ingredient of justice. When Tom leaves his air conditioner running in the summer, knowing full well that it will cost "the building" dollars but him only pennies, the waste may be bad but the injustice is worse. Systematic injustice within a society will introduce a far greater sense of discord than systematic waste.

In his *Summa Theologica*, Saint Thomas Aquinas argued that "the act of justice is to render what is due. . . ." On another page, Aquinas said that "justice, property so-called, is one special virtue, whose object is the perfect due, which can be paid according to an exact equivalence. But the name of justice is extended to all cases in which something due is rendered." By seeing to it that something due is rendered (high utility bills to the squanderers of electricity, low bills to careful users), private property helps to establish justice in the economic realm.

In the condo, then, the effect of privatizing the utilities corresponds exactly to the traditional definition of justice. The great blessing of private property, then, is that people can benefit from their own industry and insulate themselves from the negative effects of others' actions. It is like a set of invisible mirrors that surround individuals, households, or firms, reflecting back on them the consequences of their acts. The industrious will reap the benefits of their industry, the frugal the consequences of their frugality; the improvident and the profligate likewise. They receive their due, which is to say they experience justice as a matter of routine. *Private property institutionalizes justice.* This is its great virtue, perhaps dwarfing all others. We may say with the economists that private property "internalizes the externalities," or with the philosophers that it gives rise to "social justice." □

THE FREEMAN
Ideas On Liberty

Just Deserts

by Charles W. Baird

The AFL-CIO has a Web site, www.paywatch.org, dedicated to condemning what it considers to be "runaway CEO pay" in private corporations. It claims that high executive pay damages all other "stakeholders" in corporations, especially workers and stockholders. In other words, the AFL-CIO asserts that excessively paid executives and other stakeholders are locked in a zero-sum struggle.

The Web site had 250,000 hits in 1997. William Patterson, director of the AFL-CIO Office of Investment, boasts that "We put a face on runaway pay in 1997." Betsy Leondar-Wright, an official of United for a Fair Economy, a consortium of religious and activist organizations in league with the AFL-CIO, asserts, "There's nothing like this issue. This one just galvanizes people instantly."[1] Visitors to the site are invited to "fight back" by sending messages to boards of directors, using their clout as shareholders, staging workplace actions, and e-mailing members of Congress.

The site promotes enraged envy. Visitors are told that on average, CEOs make 326 times the pay of ordinary factory workers. The site offers a calculator for envious visitors to compute how long they would have to work to take in what their CEOs took in during the previous year.

The AFL-CIO's agenda is clear: to arrest and reverse the declining market share of unionized labor. Unions represented only 9.8 percent of the private-sector work force in 1997. That figure has been declining since 1953 when it was 36 percent. The site asserts that "Workers have less power in today's economy, which means that executives can take far more for themselves. That wasn't always the case. When unions represented a third of the workforce in the 1950s and 1960s, workers had an effective counterweight to corporate greed." A more powerful AFL-CIO will be able to seize the ill-gotten gains of CEOs and restore them to their rightful owners.

What's really going on with executive compensation? In Chapter 10 of their new text for MBA students, Richard McKenzie and Dwight Lee survey the literature on executive compensation and conclude that, in general, the high compensation packages paid to executives can be explained by some simple economic theory.[2] Far from exploiting workers and stockholders, high executive compensation is a means for all corporate stakeholders to benefit. It is part of a positive-sum game. The authors' explanations fall into two categories, which I call productivity and meta-productivity arguments.

The Productivity Argument

Top executives are the ones who control most resources in firms. Their decisions affect the performance of all other managers and employees. Excellent executives are scarce, and their talents are economized by putting them at the top where their productivity is

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multiplied through its effect on many others.

General Electric's CEO, Jack Welch, made 1,003 times the pay of the average U.S. factory worker in 1996. His total compensation was $27.6 million in that year. United for a Fair Economy submitted a shareholder resolution that asked the GE board to set "a cap on CEO compensation expressed as a multiple of pay of the lowest-paid worker at GE." GE responded by arguing that Welch's compensation "is appropriate in light of the value that his superior leadership, vision and dedication provided to the share owners during his 17-year tenure as chief executive officer." The total value of GE shares rose by more than $225 billion during that period.[3] Welch earned what he was paid. Moreover, increasing shareholder wealth is good for employees as well as stockholders. A successful corporation provides higher wages and salaries and offers more job security than an unsuccessful corporation.

At Scott Paper, CEO Al Dunlap rescued the firm through radical downsizing and restructuring. As a result he produced $6.5 billion in additional shareholder wealth. His compensation was only $100 million—less that two percent of what he produced. Dunlap asks, "Did I earn that? Damn right I did. I'm a superstar in my field, much like Michael Jordan in basketball and Bruce Springsteen in rock'n'roll." He says, "You cannot overpay a good CEO and you can't underpay a bad one. . . . If his compensation is not tied to the shareholders' returns, then everyone's playing a fools game."[4]

Of course, in the face of imperfect knowledge mistakes can be made, and McKenzie and Lee illustrate such failures. However, when mistakes are discovered, they usually are rapidly corrected. Corporations that allow failed executives to keep their high-paying jobs soon become ideal candidates for hostile takeovers. The market for corporate control never rests. When hostile corporate raiders gain control, they show the door to failed executives.

Sometimes failed executives leave their firms with very golden parachutes. Michael Ovitz walked away from a 14-month tenure with Disney with a $90 million severance package, and it took Gilbert Amelio only 17 months on the job at Apple to get $7 million.[5] More recently, David Coulter was dismissed from Bank of America, after two years on the job and large hedge fund losses, with over $40 million as a consolation prize. Golden parachutes like these are likely to seem excessive to everyone except the recipients, but McKenzie and Lee suggest an explanation.

A newly hired top executive is likely to be much more risk averse with respect to the activities of the firm than its stockholders are. This is because stockholders have diversified portfolios; they own shares in many different firms. If one gets into trouble, perhaps others can make up the losses. In contrast, the executive has all his human capital tied up in the firm. This one firm is the executive's sole employment, and he will be reluctant to undertake risky, but possibly high-yielding, ventures. By consenting to golden parachutes in executive hiring contracts, boards of directors may just be trying to overcome excessive executive risk aversion. On this reading, golden parachutes merely align executive and shareholder attitudes toward risk.

McKenzie and Lee report on several systematic empirical studies of the connection between executive pay and executive productivity. Consider three examples. Sherwin Rosen's research indicates that on average, when a company's rate of return increases by 1 percent, top executive pay increases by 1 to 1.25 percent.[6] Inasmuch as executive pay is a small fraction of company income, those executives earn their keep. Michael Jensen and Kevin Murphy say that on average, executives get only two cents more in cash pay and $3.25 in added wealth for every $1,000 they add to stock values. Murphy concludes that "top executives are worth every nickel they get."[7] James Brickley, Sanjai Bhagat, and Ronald Lease report that on average, stock prices increase by 2.4 percent within two months of the adoption of executive incentive pay over what they would otherwise have been.[8]

The most common form of incentive pay for top executives is stock options, which are rights to purchase shares at a fixed, low price. If the executive is successful, the market price

of shares will rise, and he will reap large capital gains. This aligns the interests of the executives and the stockholders. On average, stock options make up two-thirds of top executive compensation. That means that two-thirds is at risk. Therefore, part of the high yields received through stock options may be considered just a risk premium.

Meta-Productivity Arguments

Yet many top executives get compensation that cannot be explained by the productivity argument. They get paid more than they are worth in the narrow productivity sense. McKenzie and Lee offer three arguments to explain such "overpayments."

Discovery. Knowledge of who has the ability to become a successful top manager is given to no one. Within a firm top executives have to discover who among the ranks of lower-level managers is deserving of significant promotion. When such a person is identified and promoted, his discovery is announced to the general business community. If the promoted manager were paid only what could be justified by his direct productivity, executive raiders from other firms could easily bid for his services. In doing so, these outside bidders would be avoiding their own costs of search for executive talent. Therefore, a firm that promotes an executive is well advised to pay more than his productivity can justify to be assured of keeping the executive and conserving on future search costs for executive talent.

An interesting implication of the discovery argument is that some people who are not promoted may be just as good as those who are. They are simply undiscovered. To be discovered, it may pay for lower-level managers to acquire self-promotion and schmoozing abilities as well as basic skills for the job. It is possible, McKenzie and Lee write, to acquire "too much in the way of basic skills and not enough of, say, political savvy."[9]

Self-Monitoring. It is very difficult, and often impossible, to monitor the performance of top executives accurately. A good executive doesn't follow any prescribed routine that a monitor could observe. A good executive is alert to possibilities of turning all sorts of daily encounters, on and off the job, into profit opportunities. One may say a really successful executive is one who knows how to make it up as he goes along. The only effective monitoring of an executive is self-monitoring. An executive can be induced to self-monitor by a compensation package that substantially exceeds his opportunity cost (worth in the market). An executive who knows that shirking, once detected, means losing the difference between current compensation and what other boards of directors are willing to pay is likely to avoid shirking. This implies that the amount of the overpayment will be positively related to the difficulty of detecting shirking. The more subtle the executive's operations, the higher the necessary overpayment.

Tournaments. One way for top executives to motivate lower-level managers to work as hard and smart as they can is to make clear that rungs on the managerial ladder get increasingly narrow as it is climbed. Firms following this strategy purposefully hire many more low-level managers than they can possibly promote, and they make sure that new hires understand that this is true. Promotions are awarded to the few who can successfully compete for them. At each stage the tournament prize is a promotion and a substantial increase in pay that cannot be justified on narrow productivity grounds. Why does the pay increase have to be so large? Because the contestants will naturally discount the increase by the probability of achieving it. The higher up one is on the managerial ladder, the lower the probability of climbing still farther. Therefore, the gaps in pay must grow as one climbs from one rung to the next.

The institution of a tournament has at least two effects among the contestants. First, those who think they have little chance of winning will self-select out of the contest. Job seekers will not accept jobs with the firm to begin with, and those who are already with the firm will leave and seek more accommodating employment elsewhere. Those with substan-

tial self-confidence will remain. This increases average productivity. Second, competition among the contestants who are willing to play the game will make all of them exert more effort and avoid shirking. All contestants will be more productive than they would have been without the tournament. The "overpayments" that accompany promotion are paid from the added output of the enterprise as a whole rather than the individual productivity of the prize winners.

Gaps in compensation between top executives and average workers are increasing. The tournament model explains this. Deregulation and globalization of competition have flattened firms' managerial hierarchies. Middle-level management positions are being eliminated and replaced with floor-level team decision-making monitored increasingly by pay-for-performance schemes. These changes in organizational architecture enable firms to respond more quickly to rapidly changing market conditions. The changes also mean the managerial ladder is becoming narrower faster. Thus the probability of lower-level managers being promoted to top executive positions has substantially decreased. To keep a tournament viable under these circumstances, the gaps between top-level and average compensation must grow.

It should not be surprising that the AFL-CIO violates the Tenth Commandment's proscription against envy. Unions have never been reluctant to exploit misunderstanding of economics for their own gain. The executive pay issue is just the most recent example. The only remedy is for people who do understand economics to expose the spurious reasoning of the enemies of freedom. We should be grateful to McKenzie and Lee for having done so in this case. □

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2. Richard B. McKenzie and Dwight R. Lee, *Managing Through Incentives* (New York: Oxford University Press, 1998).
3. Rose.
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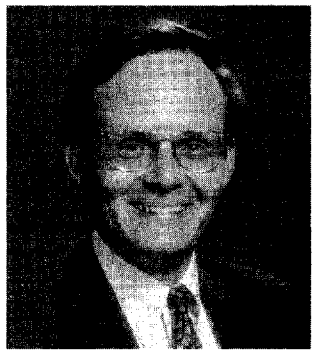
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Night of the "Living Wage"

For years, FEE has stressed the supremacy of sound economics over the political process. If people understand how markets work, and the vital link between free markets and personal liberty, they will support the right policies and the men and women in public office who implement those policies. Those who stress politics first, and concentrate their resources and efforts there, are putting the proverbial cart before the horse. Now from Detroit comes painful evidence of how true this principle is.

On November 3, Detroit voters overwhelmingly approved a so-called "living wage" ordinance that requires employers with at least $50,000 worth of city contracts or financial assistance to offer a minimum hourly wage of $7.70 if health benefits are included or $9.63 if they are not. Furthermore, the law requires that employers hire only city residents. Violators are subject to a $50 per day penalty and may have their city contract or grant revoked as well. The city's already bloated bureaucracy will get larger now because contracts will have to be monitored for compliance, which also means that businesses will be forced to reveal confidential payroll information.

This is magic-wand economics at its worst: Want higher wages? Just pass a law making it illegal to pay anything less than some arbitrary amount. Presto! Supply and demand, profit and loss, incentives and disincentives all mean nothing if you can get what you want through the force of law.

Of course, there's nothing in the ordinance that will make workers more productive, only less affordable. A city that has already driven out a million people and countless businesses with a tax burden more than six times the average for Michigan municipalities will now become even less competitive and economically attractive. David Littmann, senior economist at Detroit's Comerica Bank, estimates that the ordinance will wipe out about 7 percent of the city's jobs by the year 2000. Incredibly, Mayor Dennis Archer, who publicly supports the living-wage concept, headed to Washington within days of the vote, seeking federal assistance (that is, other people's money from all over America) to help keep businesses from leaving Detroit.

And it isn't just businesses that will be affected. Nonprofit charities will be too. For example, two Salvation Army sites in Detroit receive $300,000 from the city. Most conservative estimates put the new law's cost to the Army at $1.5 million. The Army will have to raise an additional $1.5 million, lay off workers, or become independent of the city.

Every argument against the minimum wage—long familiar to readers of *The Freeman*—applies in spades to living-wage proposals like Detroit's. The law can't make a person worth $5.15 an hour (the current federal minimum) by making it illegal to pay him any less. By mandating an even higher minimum, the living wage prices even more peo-

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ple out of work. The people who push these cockamamie ideas never seem to ask why any employer would hire someone at $7.70 if that person's services are only valued in the marketplace at, say, $5.

Moreover, by imposing more unnecessarily costly employment arrangements, the new law will require more city revenue or reduced city services. The long and short of it is this: though some workers may keep their jobs and even see their wages hiked, others will pay the price in the form of fewer jobs or higher taxes. Unemployment resulting from the law will boost the public welfare rolls in a city where the poverty rate—at 30 percent—is already the highest of American cities.

Detroit, sadly, is not the first municipality to engage in such foolishness. In 1994, Baltimore became the home of the country's first living-wage law. Portland (Oregon), Milwaukee, Minneapolis, St. Paul, Jersey City, Boston, and Los Angeles have all adopted similar ordinances. Last fall, the city council of San Jose, California, began debate on a living-wage ordinance that would set minimum hourly pay at an astounding $12.50 plus benefits for employees performing work for the city. On top of that, the San Jose proposal stipulates that any contractor who takes over a city job previously performed by another entity would be forced to hire the same people who had been doing that work before.

Who is behind these silly laws? In Detroit, the ballot language was drafted and the campaign funded by none other than organized labor. Why? Because a city floor under wages will stifle the unions' low-cost competition and make it more difficult for the city to contract out for services. This is not organized labor playing the role of Florence Nightingale. It is the cannibalization of fellow workers by greedy, self-interested union bosses.

Nationally, the living wage effort is being led by a group known as the Association of Community Organizations for Reform Now (ACORN). Like the unions, ACORN is no paragon of either altruism or intellectual consistency. Even as it was arguing for the federal minimum of $5.15 and lobbying for sky-high living wages in a number of places across the country, ACORN filed a lawsuit in California in an attempt to exempt itself from paying its own employees the state's then-current $4.25 per hour minimum wage. In its legal brief, the organization declared that "the more that ACORN must pay each individual outreach worker . . . the fewer outreach workers it will be able to hire." Hypocrisy has rarely been on more arrogant display.

Meanwhile, some people and certain business organizations in Detroit that have long viewed the promotion of free-market economics as "too controversial" for their tastes are now reaping the bitter harvest of their "moderation." In challenging the new law in the courts, they may spend far more than they ever spent on behalf of economic education. Whether they learn anything from it all remains an open question.

Too often, in Detroit and elsewhere, the schools don't teach sound economics; or worse, they teach the toxic stuff. Businessmen devote too much of their resources to politics and too little to the right ideas that can really make a lasting difference for the better. That's why living-wage nonsense succeeds in becoming law. We shouldn't be surprised at the results, and we should be ashamed if by our action or inaction we're part of the problem. □

THE FREEMAN
Ideas On Liberty

Crimes of the Mind

by Melissa Suarez

The killing some months ago of Matthew Shepard has brought to the forefront of debate the idea that a federal law is needed to protect people against "hate crimes." Proponents want the law to punish individuals who target others because of race, sex, religion, disability, or sexual orientation.

The murder of Matthew Shepard of course is tragic. That it was likely committed with hatred for his sexual orientation is indeed also tragic. A federal law against hate crimes, however, could never be constitutional nor could it protect likely victims of such crimes.

The U.S. Supreme Court has already unanimously struck down a hate-crime law. *R.A.V. v. City of St. Paul* involved a city ordinance in St. Paul, Minnesota, that prohibited the display of a symbol that arouses "anger, alarm or resentment in others on the basis of race, color, creed, religion or gender."

Several white youths were charged with violating that ordinance when they burned a cross on the property of a black family. The flaw with the ordinance was that it was neither content-neutral (concerned not with the speech's content, but where, when, or how it takes place) nor viewpoint neutral. Writing for the Court, Justice Antonin Scalia said the ordinance was invalid because "it prohibits otherwise permitted speech solely on the basis of the subjects the speech addresses."

Content and viewpoint neutrality will derail future hate-crime laws as well. The best alternative would be to heed Scalia's words, when he wrote that governments have no authority "to license one side of a debate to fight freestyle, while requiring the other to follow the Marquis of Queensbury Rules."

Campus Speech Codes

Consider how similar legislation, specifically "hate speech" codes at colleges and universities, have fared. Campus speech codes that punish students for speech, slurs, or epithets that relate to a person's race, gender, religion, or sexual orientation are prime candidates for lawsuits because they, too, lack content and viewpoint neutrality.

The most famous incident involving hate speech began in January 1993 at the University of Pennsylvania. Five black, female students claimed they were victims of racism after a fellow student, Eden Jacobowitz, who was interrupted in his studying by their boisterous behavior outside his window, yelled at them, "Shut up, you water buffalo." Jacobowitz was charged with violating Penn's speech code, which prohibited racial harassment.

The administrative judicial officer in charge of his case, in a telling question, asked him if he was "having racist thoughts" when he used the term "water buffalo," because, the administrator said, a water buffalo is a dark, African

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animal. Jacobowitz vehemently denied his remarks were racist, saying that the students' noise and not their race prompted his remark. Several scholars rushed to Jacobowitz's defense, including black professors at Penn who said there were no racial connotations behind the term "water buffalo." Others pointed out that the water buffalo is found not in Africa but in Asia.

Nevertheless, because of the code, Jacobowitz's fate depended on the black students' interpretation of his remark. They decided it was racist, so the university charged Jacobowitz with racial harassment. The university eventually dropped the charges.

Another problem that hate-speech codes have, and hate-crime laws inevitably would have, is related to their lack of viewpoint neutrality. These codes are not all-inclusive. They are usually so vaguely worded that the ban is generally on hate speech only by speakers of a certain gender and certain races, sexual orientations, religions, or handicaps.

Sheldon Hackney, who was president of the University of Pennsylvania during the "water buffalo" incident, blatantly admitted the codes' selectivity. When someone asked Hackney if "racial harassment" would include "someone [who] called a black with white friends an 'Uncle Tom' or an 'Oreo,' or if someone called a white person a '[expletive] fascist white male pig?'" Hackney said no.

Punishing Thoughts, Not Acts

A federal hate-crime law would also threaten selective enforcement. Such a law could easily be used to protect only certain groups and punish only certain crimes as hate crimes, thereby making some forms of "hate" more punishable than others.

The alternative would be to punish all hate crimes equally, which would be impossible. It would also be superfluous. For example, in Shepard's case, there are already laws against murder, and the penalties are greater than those of any proposed hate-crime legislation.

Nevertheless, many people argue that a federal law against hate crime could possibly stimulate education about racism, sexism, homophobia, and the like. It would also, they say, probably make minorities feel more protected. It's known in some circles as "thought control."

Consider the success of hate-speech codes in this area. At many institutions, students who violate the speech code are required to take classes on the dangers of prejudice and stereotypes. At UCLA, for example, violators of the university's anti-harassment policy usually must either perform several hours of community service or "become educated" about harassment. One student accused of sexual harassment had to establish a program to educate his fraternity about sexual harassment and write a paper for the dean of students on heterosexism and the origins of programs that combat sexual harassment. Similar punishments are handed down at other universities.

One wonders what kinds of "community service" and "education" violators of a federal hate-crime law would be subjected to. After the federal government charged an individual with having the wrong thoughts (which is already a blatantly unconstitutional action), would it then force him to change his mind? The last government to do that was Ingsoc, in George Orwell's *Nineteen Eighty-Four*.

Supporters of hate-crime laws also argue that federal legislation might heighten awareness about prejudices and stereotypes. More important, they say, stiffer penalties for those who commit such crimes would deter them to begin with. How could they serve as a deterrent when the act itself is already a crime?

A federal hate-crime law would also raise questions of double jeopardy. If, for instance, a black person's accused assailant is acquitted at the state level, he could be retried for the same crime in federal court under the hate-crime law.

We can never know for certain the motive behind a person's speech or action. For that and other reasons, laws designed to punish the thought behind the crime are dangerous and inappropriate in a free society. □

THE FREEMAN
Ideas On Liberty

Mises on Mexico

by Eduardo Turrent

Today should be a day of celebration for students, book lovers, and all who are interested in reflecting on the economic development of Mexico. *Mexico's Economic Problems* by Ludwig von Mises, which Bettina Greaves found in 1997 among Mises's papers, is truly a treasure.[1] Although there are obvious differences, it calls to mind musicologist Alberto Gentili's rediscovery in the 1920s of the complete works of Antonio Vivaldi, more than 200 years after the composer's death. We economic historians are more fortunate than musicians and music lovers were, since Mises's text has reappeared only 25 years after his death.

The monograph by Mises on the Mexican economy is outstanding in many respects. One particularly important aspect is that it is relevant to more than just the economic situation he found when he visited in 1942. Mises was concerned with the long-run historical context; or as one says nowadays, he focused on fundamental structural change. He was interested in uncovering the fallacies on which the principal positions and policies of Mexico's former socialist regime, as well as all socialist regimes, were based.

One of the principal points in Mises's essay was his vote of confidence for Mexico because of the capabilities of its people and the progress of the country. As he put it: "It is beyond doubt that the Mexicans are endowed with the spirit of workmanship. The achievements of the autochthonous [indigenous] craftsmen and artisans meet with the admiration of all experts. The workers in the already existing industrial plants and in the mines are not less efficient than those of other countries." And the same may be said with respect to their entrepreneurial and other skills.

Thus the problem of Mexico's development was not capital scarcity, geography (which Mises judged favorably), climate, or geology, even though the soil "in the greater part of the country is dry and barren." Development depends on the application of "an appropriate economic policy"; that is, a "wise" economic policy aimed at the "establishment of a durable system resulting in a continuous improvement of the nation's well-being."

Unfortunately, this was not the case in Mexico when Mises wrote this paper. Nor has it been the case since, especially not from 1970 to 1982, even if one considers the several forms such a "wise" policy may take.

Attack on Easy Money

Only five or six years after the publication of Keynes's *General Theory,* Mises took a well-aimed shot at the economic policies that

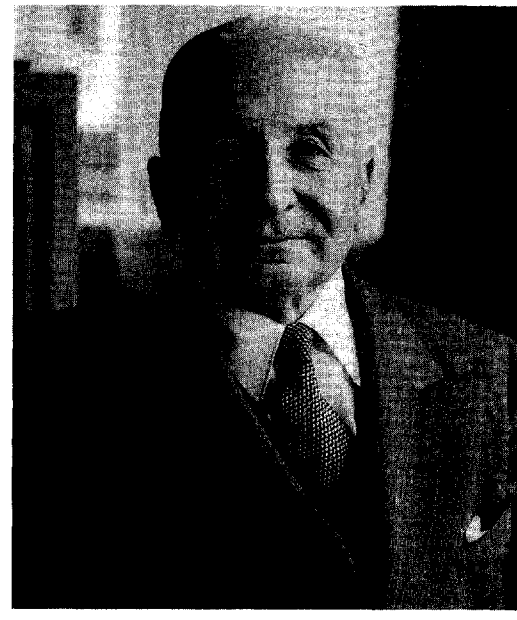
Eduardo Turrent is the historian of the Bank of Mexico. This is excerpted from a paper delivered at a conference of the Ludwig von Mises Cultural Institute of Mexico City, September 23–24, 1998, celebrating publication in Spanish of Ludwig von Mises's Mexico's Economic Problems: Yesterday and Today, *which was written in 1943 but unpublished until last year. Translated by Bettina Bien Greaves.*

stemmed from the noted English author's ideas. According to Mises, the "easy money" policies of the interwar years, policies that tended to generate inflation, had been based on the doctrines of Lord Keynes, doctrines that Mises called "fallacious." To Mises, the Keynesian dictum that "in the long run we are all dead" was no more than a new version of the cruel-hearted motto attributed to Madame de Pompadour, "After us, the deluge." Thus, every strategy that "is indifferent about the tomorrow strives after ephemeral success and carelessly sacrifices the future." Such strategies must not be considered "progressive, but parasitic." Growth may be sustained only by having fundamental policies favorable to the stability of money and exchange.

Mises said in this study, not without cause, that the monetary history of Mexico, like that of many other countries, has been "a record of failures and disasters." He hit the bull's-eye when he said that "Monetary troubles are never the inextricable outcome of conditions beyond the control of a country's government. They are always the result of a deliberate policy," which, only too often, has been "the result of erroneous monetary doctrines." Thus, with a nod to the then-current financial authorities in Mexico, Mises pointed to the need to return to a firm path toward stability.

But stability is not a goal in and of itself. "Monetary stability" must be recognized as a means, "an indispensable requirement for the formation of capital." Moreover, the consequences of applying an "easy money" inflationary policy are, and have been, economic depressions with millions unemployed and social unrest. "Easy money" policies "result for a short time in the creation of an artificial boom, but must later end in a slump and in depression."

Few of the wise observations, prescriptions, clairvoyant remarks, and even prophetic visions in Mises's text appear obsolete, not even his proposals concerning exchange. Nevertheless, one must remember that this manuscript was written years before Bretton Woods and more than a decade before the celebrated article by Milton Friedman, "Fixed vs. Flexible Exchange Rates" (1953). It should not be surprising that Mises showed



Ludwig von Mises

himself in 1942 to be an advocate of the gold standard. However, one should look at the matter from the perspective of history. Basically, what Mises wanted was not something radically different from what Domingo Cavallo introduced in Argentina, fixed exchange with a monetary policy subject to discipline.[2]

At a time when public deficits have come to be considered virtuous, Mises insisted on the advantages of fiscal health. He explained clearly that excessive public spending contributes neither to disposable income for the masses nor to the supply of social capital. If the public budget is in disequilibrium, this must be financed either by issuing central bank credit or by using internal debt. If central bank credit is used to finance the public debt, it is doubly pernicious because, in addition to leading to inflation with all its harmful consequences, it affects the balance of payments and hinders the maintenance of exchange stability. If internal debt is used to finance the public debt, wealth is simply withdrawn from the private sector and transferred to the public sector. Public spending proposals assume, also, that the government will spend resources better than individuals will. But is this by any means certain? Withdrawing purchasing power from the private sector not only reduces the total resources entrepre-

neurs will have available to invest, but it may also reduce the income and consumption of the needy.

It is possible, even likely, that in his Mexican travels under the guidance of Montes de Oca, Mises became acquainted with the Mexican historian Daniel Cosio Villegas. Mises's opinions concerning the apparent and abundant "natural wealth of Mexico and the chances of its future prosperity" were contrary to the views then commonly held. But they were remarkably similar, particularly in emphasis and approach, to those expressed by Cosio Villegas in his essay "The Legendary Wealth of Mexico." Mises's sharp observations were, and still are, particularly applicable to the agricultural capabilities of Mexico. To Mises the natural supply and quality of the land were not insuperable obstacles. Rather, he looked on agricultural policy, which was rooted in the heart of the revolutionary ideology, as the obstacle to the country's progress.

Mises cited figures to illustrate what he called the harmful effects "of the agrarian reform of the revolution." The crops of corn and wheat had been much less in 1937 than in 1907 and those of beans less than in 1897. Mises saw clearly, as did Manuel Gómez Morín and a few other illustrious intellects, that in Mexico, as in any other country, the agricultural sector could not make progress without a clear definition and absolute respect for the rights of property. The plain fact was that those rights were not well defined in the arrangement made for common land. Therefore, land was not only not cultivated with the devotion required, but investments necessary for the development of the land were not made either.

The right to property is the necessary condition for all modern productive activity. Therefore, Mises argued strenuously in 1942 against the desire of many to look to the Soviet system of agricultural collectives as the example for Mexico to follow. Granting that, however, Mises did not object to, and he even looked with favor on, other forms of collective activity even with the active participation of the state. For instance, he mentioned cooperatives that could be formed to acquire farm equipment, seed, and fertilizers, and to cover other expenses. Such cooperatives could also arrange for leasing machinery, selling farm produce, and obtaining credits for members. The government could also help with institutions to promote technological education and agricultural research. Nevertheless, every individual farmer should be "the master on his own farm."[3]

The Demographic Problem

Surely Mises was one of the first visionaries to recognize the demographic problem from which Mexico has long suffered. Mexico, he noted, is "a comparatively overpopulated country," with the surplus population living in rural areas. The potential productivity of the country was insufficient to assure a decent standard of living for these excess people. Therefore, the only viable solution was for industries to be developed to absorb that excess population. But truly productive industries could develop only in response to definite commercial opportunities.

In 1942, Mises called for something that was then strictly taboo, something that could not be undertaken in Mexico until more than four decades later: an "open door" trade policy. If the dismantling of our ancient protectionist structure in recent times provoked no few laments and rending of garments, imagine the reaction to the Austrian economist's proposal in the 1940s, in the midst of the great World War. Contrary to archaic mercantilist doctrines, Mises looked on imports as something desirable; he considered the opening of trade as the indispensable means for obtaining the best possible allocation of resources. "The advantage derived from foreign trade lies entirely in importing, not in exporting," he said. According to Mises, only by competitive industry emerging in an open environment can manufactured products be produced at prices that permit living standards in the country to rise while at the same time generating exports to pay for the nation's indispensable imports. The problem, he lamented, is that many Mexican patriots were "entangled in the neo-mercantilist fallacies" then in vogue—and I would say still in vogue among many groups.

The whole process of industrialization based on protectionism is damaging in three ways. First, protection inhibits the agricultural sector from exporting. Second, it raises the prices of manufactured consumers goods, which could otherwise be acquired by the rural inhabitants. And third, because of its high costs, industrialization based on protectionism prevents the manufactured products from penetrating international markets. It is true that, given such industrialization, many people would find employment in the protected industries. But what they would gain as employees others in other sectors of the economy would lose through the high cost of the manufactured articles. In this way any possibility of raising "the standard of living of the average Mexican" would be lost. Therefore, Mises concluded, industrialization by means of protection would lead the nation down a "blind alley" since it would perpetuate the low living standards of the people.

Although Mises argued for opening up trade gradually, he predicted that there was no need to fear that, by removing tariff barriers, "any plant will be forced to discontinue production. Some plants, it is true, will have to rearrange their lines of production in order to obtain a higher degree of specialization." But, to the great surprise of many, the visiting Austrian recommended opening up trade unilaterally—removing commercial barriers even though other countries maintained protective policies without offering commercial reciprocity.

Mises's expectations about opening the country up to trade were absolutely correct, as they were in other instances. Although the Mexican opening was not gradual and the policy adopted was unilateral in the beginning, practically no failures that could be attributed to that fact were reported.

Mises explained how the opening up of trade, with all its benefits, cannot yield its full benefits without a coherent and a compatible wage policy. Today those who think real wages can be determined by decree or by employer-employee negotiations still organize in battalions. But those who are serious know the painful consequences of such a wage policy; it directly diminishes the competitiveness of enterprises and employment, and indirectly affects inflation and economic growth. As Mises expressed it:

> There is but one means to raise Mexican wage rates: industrial expansion. Every new plant improves the standard of living of the Mexican masses by creating an additional demand for labor. But industry cannot allow higher wages than such as safeguard the conduct of business. If trade unions are anxious to enforce higher wages, they prevent the establishment of new plants and the expansion of existing plants. They succeed, it is true, in raising wage rates for a comparatively small group of workers; but they force, on the other hand, hundreds of thousands to remain in agricultural occupations, in which their income is extremely low, i.e., much lower than it would be if they could find industrial jobs.

Mises was absolutely clairvoyant in suggesting in 1942 that private initiative should participate in the production of petroleum, the management of the railroads, and the generation of electricity. He was also right in insisting that unless investment and production have confidence, they cannot thrive and thus cannot contribute to economic progress.

Railroads, Electricity, and Petroleum

More than half a century after Mises's visit, his recommendation with respect to the railroads is becoming a reality. In the case of investment in the field of electricity, there are now indications that private capital will be permitted greater participation in the future. As for the production of petroleum, we are still far from a decision; some isolated voices suggest only occasionally, rather timidly, that the matter be reconsidered.

Further, Mises was several decades ahead in predicting what would happen in Mexico between 1970 and 1976 with respect to cooperativism. In that six-year period the management of cooperatives in some sectors, like that

of fishing, was entirely given up. The results had been very disappointing; they fulfilled to the letter what Mises had written years before. "No serious economist believes that a cooperative society could successfully compete with private enterprises. The experiments have resulted in complete failure." This, he said, applied especially in the field of industrial production.

One of the themes emphasized in Mises's essay is the importance of maintaining the confidence of investors in order to improve the country's material welfare. In *Mexico's Economic Problems* there are more than ten references to this. On this point Mises was absolutely positive: "What Mexico needs most is capital, either foreign or domestic. The repudiation of the national debt and the expropriation of foreign investments deter the foreign capitalist. The methods of taxation prevent the accumulation of domestic capital."

The investor, domestic or foreign, fears every attack on property rights, lack of public safety, and arbitrariness. Strictly speaking, when we consider the situation, confiscatory taxation is aggression against the right of property. According to Mises, very high taxes "paralyze the spirit of entrepreneurship." Therefore, he recommended that Mexico distance itself from a "suicidal" tax policy of this kind. Taxes should never discourage saving or the accumulation of capital. In this same vein, personal and entrepreneurial income that is invested should be taxed at a lower rate.

Mises's essay is enlightening and clear; it refutes fallacies, destroys myths, is analytical, and advisory. When it was first written and made available in Mexico, it had practically no effect; in fact it was forgotten. Why? I venture a few theories.

First, his views were in opposition in many regards to the most widely accepted ideas of the time and the years to follow. Moreover, there was resistance from the powerful groups that were surely disturbed, or would have been disturbed, by this text. International experience reveals that one of the great obstacles to undertaking reforms is special-interest groups. And Mises's paper touched directly on many of them, especially syndicalism, the agrarian reform bureaucracy, the administrators of public enterprises that would be dismantled, the industrial beneficiaries of protectionist measures, the clientele of subsidized organizations, and even the teachers who were preaching in the schools and universities "the religion of étatism." In this connection, Chapter XI of Mises's essay, "Education," is recommended.

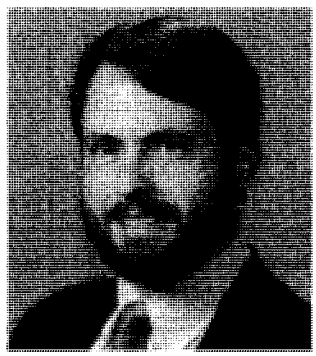
However, as Keynes said, the ideas of economists and social philosophers are more powerful than generally believed. There is a tendency to exaggerate the power of special interests as compared with the gradual penetration of ideas. And something that Keynes did not say, but which I firmly believe, is that in the long run, correct ideas will succeed in asserting themselves over the fallacies and the economic deceits. □

1. Translated into Spanish as *Problemas Económicos de México, Ayer y Hoy* by Daniel Sotelo Kucharik and Ana María de Sotelo (Mexico: Instituto Cultural Ludwig von Mises, 1998). Publication of the original English-language version is scheduled by Liberty Fund of Indianapolis in Volume 4 of *Mises's Lost Papers*.

2. Domingo Cavallo, formerly associated with Argentina's central bank, became foreign minister and then minister of economic affairs under President Carlos Saúl Menem. He was instrumental in stopping the inflation, establishing a currency board and stabilizing the exchange rate of the Argentine peso at one U.S. dollar.

3. *Editor's Note*: Mises wrote in his 1943 manuscript that "The economic backwardness of a part of Mexico's agricultural population justifies intervention on the part of the government. It is all right for the government to advise the peons how to establish and to run co-operatives. Even small subsidies for newly formed co-operatives may be advocated. But it would be a mistake to subsidize them permanently or to grant them tax privileges. It does no good to mask the failure of any institution by such measures. Mexico is not rich enough to indulge in the luxury of waste."

Government



America's Forgotten War

The war that did the most to transform the world for the worse was formally settled 80 years ago. Not World War II, which employed greater destructiveness, exhibited greater cruelty, and slaughtered greater numbers of people. But World War I, which birthed World War II, along with the greatest of the totalitarian delusions—communism, fascism, and Nazism. Yet the Great War, as it was originally called, is largely forgotten in America.

Today the United States celebrates Veterans Day on November 11, which replaced the original Armistice Day. But when Americans think of veterans they think of Vietnam, Korea, and World War II. Not so in Europe. There World War I continues to loom large.

As it should. The Triple Entente, with which America was allied, had won when the guns fell silent on November 11, 1918. But as the Versailles peace conference, which opened in January 1919, proceeded throughout the spring, the Western powers managed to lose the peace. Tens of millions in the next generation would pay for their mistakes.

And the Europeans continue to fight leftover issues of the war. For instance, last November French Prime Minister Lionel Jospin suggested rehabilitating army mutineers who had been executed during a massive soldiers' revolt in 1917. President Jacques Chirac sharply rejected Jospin's idea, however, citing the negative reaction from surviving veterans. Yet at the same time the British government allowed relatives of soldiers executed for cowardice and desertion during World War I to hold a ceremony at the Cenotaph, Whitehall's monument to the war dead.

To the extent that Americans know anything about the war, they probably think of supposed idealist Woodrow Wilson leading the fight to make the world "safe for democracy." This was pure cant. Instead, Wilson was dedicated to reforming the entire world and would have a chance to do so only if he headed a belligerent power. His high-flown rhetoric disguised the fact that he had allied America with one militaristic bloc against the other.

While Germany helped bring on the war by isolating itself and adopting a hair-trigger mobilization plan, it was not bent on war. German diplomacy after Chancellor Otto von Bismarck was maladroit and stupid, not malicious.

France, in contrast, was aggressively revisionist. It wanted to recover the provinces of Alsace and Lorraine, lost in 1871 in the aftermath of the Franco-Prussian War (which had been started by France). This required not just war between France and Germany, but a European-wide conflict, since France alone could not defeat Germany.

Austria-Hungary, Germany's ally, was also a status quo power, desperately seeking to avoid internal collapse. In contrast, Italy, which eventually joined the Entente, desired

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Austro-Hungarian territory; Russia hoped to gain influence in the Balkans at the expense of Vienna.

Most important, the blood-stained Serbian regime, built on the brutal murder of the king and queen of the previous dynasty in 1903, wanted to break apart Austria-Hungary in order to build a greater Serbia. In fact, it was the Serbian-supported assassination of Austria-Hungary's heir apparent that lit the fuse of the war. The contending alliance systems acted as transmission belts of war for all of the major European powers.

After the deaths of some ten million people, all the contending nations' goals looked downright frivolous. Washington's formal justification for war was its desire to protect the right of Americans to travel on armed British merchantmen carrying munitions through a war zone.

The celebrated *Lusitania*, sunk by a German U-boat in 1915, carried just such a mixed cargo of babies and bullets. Wilson's eloquence notwithstanding, the Germans were perfectly justified in sinking it and other such vessels. In fact, there is a continuing controversy over whether British officials, particularly then-First Lord of the Admiralty Winston Churchill, hoped the *Lusitania* would end up on the ocean floor, thereby inflaming American opinion against Berlin.

The war offers many ugly precedents. There was, for instance, the brilliant British propaganda, which convinced the world that the "Huns" were ravaging Europe. Alas, it was all false, but it helped drive America into the war. Joseph Goebbels modeled the Nazi effort after that of the British.

There was also the war against noncombatants. London imposed a "hunger blockade," denying foodstuffs to all European civilians, even though it was against international law. Britain maintained the blockade even after Germany had surrendered. Hundreds of thousands died of starvation.

Finally, soldiers were treated as cannon fodder to be slaughtered. The Western front became a static "sausage machine" once trenches stabilized positions in the fall of 1914. From then through the spring of 1918 no attack moved the lines more than ten miles.

The French mutineers about whom Chirac and Jospin quarreled represented soldiers refusing to lose their lives in useless offensives pushed by fantastically overoptimistic generals who commanded far from the front. Who could blame the *poilus* for resisting?

Especially since the politicians knew what was going on. British Prime Minister David Lloyd George admitted that people could not be told the truth about the war or they would end it the next day. He finally limited troop replacements to the front because of what he termed the generals' "reckless wastage of the manpower so lavishly placed at their disposal."

No one was immune from the effects of this reckless wastage. The carnage sparked revolution in Russia, breakup in Austria-Hungary, dissatisfaction with democratic politics in Italy, and, most important, collapse in Germany.

Unfortunately, after all this mindless bloodletting, the Allies came up with a peace that French Marshal Ferdinand Foch presciently called "an armistice for 20 years." The Allies blamed Germany for the war, dismembered Austria-Hungary and the Ottoman Empire, plundered the defeated states, awarded Third World peoples to the victors like prizes in a sporting competition, and mixed different ethnic groups in a host of unstable new nations.

A decade later Britain was embarrassed by its handiwork and refused to defend it; France lost the will to act alone. They would neither ruthlessly enforce Versailles to contain Germany nor voluntarily revise the treaty to conciliate Germany. Then came Adolf Hitler, and the Allies yielded on every point. World War II was not long in coming—followed inexorably by the Cold War.

Even today we are not free of the lingering effects of World War I. The continuing Balkan civil wars are a bloody bit of unfinished business from Versailles in 1919.

The world was full of hope 80 years ago, as Allied leaders sought to create the world anew. But they failed: not only did ten million people die in vain, but some 40 million more would perish a generation later. It is the kind of history that we cannot afford to repeat. □

Frontiers: Last, Lost, and Found

by Eric Nolte

Technological innovation is the most powerful force for improving our safety and health, but such creativity withers under government control. It flourishes in the rich soil of freedom.

Government intervention subsidizes businesses that are mediocre, obsolescent, and inept. Such firms survive not because they have won consumer dollars through the logic of superior products and voluntary trade with consumers, but because they have succeeded in lobbying for legislative advantages that hobble their betters in the marketplace and stifle the creativity behind innovation. Aviation presents many examples of this.

At one time a small factory-built light airplane could be purchased for the price of a nice automobile. No more. Those who want a little Cessna now need to raise enough money for a home mortgage, not a car loan.

While aviation electronics have seen big advances, that is largely a result of the boom in computers and consumer electronics that has proceeded mostly without government interference. But the structures, materials, and power plants used in the construction of light airplanes have not improved much for half a century. Between the huge costs of government regulation and the way tort law has been interpreted for decades, manufacturers of small airplanes have either gone bankrupt or focused on producing more expensive aircraft for business.

In 1996, Cessna announced the production of its homely model 172 for the first time in nearly two decades, thanks to the recent changes that Congress authorized to protect manufacturers from completely open-ended liability claims. This is virtually the same airplane that Cessna had produced since the late 1940s till 1978. The price? Around $200,000, three times its cost in its last year of production.

The Will to Create

The human yearning to create and improve things is like a flower that wriggles out to sun and air from under rocks. While regulation and the tort system have destroyed much innovation in small, commercially produced airplanes, a loophole in federal legislation allows average people to build airplanes at home. They buy plans and parts for simple airplanes, and network with others under the auspices of the Experimental Aircraft Association. While the name suggests an organization devoted to cutting-edge matters, their primary function is to help ordinary citizens get into the air with simple machines.

One part of the EAA's membership is devoted to advancing aviation. It produces kits that make good use of new composite materials, new power plants, and structures to produce machines that in their performance and convenience put to shame anything

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offered by today's makers of little planes. For example, the Beechcraft Bonanza, which first rolled off the Wichita production line in 1945, is still among the hottest factory-produced private airplanes in general aviation. In efficiency, speed, and comfort, it is a dinosaur compared to what home-builders can offer today.

Much attention has focused on the benefits of airline deregulation to the flying public. Airline traffic is twice what it was in 1978, encouraged by fares that are so much lower that airline travel has become the primary mode of traveling long distances.

Little known is that airlines remain among the most highly regulated industries in the country. The highly touted deregulation of 1978 merely allowed airlines the power to set rates and choose which cities to serve.

One result of regulation is that airliners today neither look nor perform much better than those introduced 40 years ago. What would airliners look like absent government regulation? And how might this contribute to advancing aviation safety?

Compare the huge leap in safety that occurred when the old piston-engine airliners were replaced by the jets that started coming online around 1960. Suddenly, instead of getting their feathers knocked off as they slogged through nasty weather systems down in the lower reaches of the troposphere, jets had the speed and range to top or circumnavigate much of the bad weather. The improvement in comfort and safety was a quantum leap over those of the old propeller-driven transports.

The technology has existed for decades that would allow a similarly dramatic improvement over the current generation of jets. But trying to use much of this technology is as hopeless as trying to compete with the post office. It's forbidden by law.

Those who are familiar with particular fields, as I am with my profession of aviation, are in a position to have some idea of what might be. Abundant technology is on hand today that would astonish you.

Air Orient Express

In my professional opinion, if it weren't for regulation, we would already have in operation, at the very least, a true Orient Express: a second generation of big, long-range, supersonic jet transports (SST) that would be quieter, environmentally cleaner, and more fuel efficient than the Concordes and similar products that were on the drawing boards at Boeing, Lockheed, and Douglas in the 1960s. But the government—in thrall to the politically connected lobbyists, Luddites, and human-haters of the time—passed legislation that killed all such efforts before the first American SST appeared even in prototype.

It is also my belief that we would have—or would shortly have—viable, reusable, single-stage-to-orbit rockets, plying the skies in low-earth orbit between Europe, the Americas, and Asia, carrying mail, people, and high-priority freight with greater safety, speed, and value than anything we have today.

The whole history of technology validates this point. And these are not the most impressive innovations that G. Harry Stine outlines in his book *Halfway to Anywhere: Achieving America's Destiny in Space*. Stine presents a sample business plan produced by experienced venture capitalists that marshals scientific and economic savvy. The plan shows how big profits are available to those who get into low-earth orbit, from where, as science fiction author Robert Heinlein put it, one has already expended the energy to be "halfway to anywhere in the solar system." Big floating space stations would serve as hotels for gawkers and well-to-do honeymooners. Factories in space (as Stine pointed out in his 1979 book, *The Third Industrial Revolution*) could exploit the unique characteristics of a zero-gravity environment that would allow the production of certain drugs and the use of some industrial processes that are simply impossible outside that environment. Earth-orbiting industries could serve as hubs for mining precious resources from the asteroid belt. Getting into space would allow human beings to transform the earth into a new garden of Eden, at a pace set by the rewards that market forces offer us for moving off the planet. (Getting into space ultimately promises an answer even to the threat that will otherwise doom human beings when our sun begins to burn out.)

More immediately, getting into space

promises a renewal of the psychological benefits long said to have ended with the closing of the American frontier a century ago. It might restore the idea of progress, the death of which has been proclaimed by the crabbed, depressed, minimalist, dyspeptic human haters and anti-technology zealots who tell us that we are merely a cancerous blight on the earth. (Some of these folks, like the misanthropic Norwegian philosopher and founder of deep ecology, Arne Naess, yearn for a new virus to wipe out the horrible curse of man.)

People need to get into space for a multitude of reasons. But we will never get there without free markets to implement the technology we already have and bring to fruition the equipment to satisfy this widespread human desire. Regulation thwarts innovation by making creativity a crime, and by punishing businesses that would otherwise be successful enough to attract the necessary venture capital.

The NASA Bureaucracy

Harry Stine offers an insider's lucid discussion of the scandalous way in which the federal government and NASA have throttled a rich vein of creativity through the bureaucratic "empire-building" of regulation, subterfuge, political back-stabbing, lying, and logrolling.

According to Stine, a group of Douglas engineers noticed that NASA's way of handling the problem of lofting payloads into space was fixed at the mentality of 1940s-style rocket artillery: the multistage booster and payload capsule. Imagine how far commercial aviation would have come, thought these few engineers at Douglas, if an airliner required a Cecil B. De Mille cast of thousands to prepare six months in advance for every trip from New York to Paris. Passengers would have to be trained for the ride weeks in advance, garbed in special, expensive tailor-made suits. When the day of the trip arrived, the vehicle would launch and proceed to jettison 95 percent of its parts, dropping these hideously expensive components into the ocean, never to be used again. And finally, arriving in Paris, the return flight would require another six months to replace the missing components, perform a major overhaul of the remains, and to engage in the same extravagant process of preparation with the same cast of thousands.

This small group of Douglas engineers embarked on an unofficial program, funded with shoestring capital that they raised almost entirely by their own efforts. By the late 1980s, they had produced and flown the first proof-of-concept prototype that would ultimately be a fully reusable single-stage-to-orbit (SSTO) vehicle able to deliver satellites and other payloads to low earth orbit (LEO) with the reliability and ease of airliners plying the sky between New York and Paris.

Despite smaller budgets than in the glory days of the moon program, in the late 1980s the space agency was still a bureaucratic, empire-building institution, quick to lunge at any threat to its health. To some of NASA's bureaucrats, the Douglas DC-X project appeared to threaten its turf. At the very least, its success was an embarrassment to NASA owing to the contrast between its tiny budget and the bloated financing of the space agency's projects. By offering Douglas money to fund the project, NASA succeeded in the time-tested ruse of hijacking it for itself. The agency turned it into another massive government program by divvying up the carcass among its many aerospace contractors (including, not incidentally, the corporate remains of McDonnell Douglas itself, now that this company had been taken over by rival Boeing).

NASA has a new, improved version of the SSTO vehicle and, a decade after the first (and to date, last) flights of the DC-X, has spent years running studies of all the various matters involved. It estimates a first flight of its spacecraft far in the future, following still more years of studies and tests.

Another Blow to State Dogma

One frequently hears that the development of aerospace vehicles is a textbook example of the kind of capital-intensive venture at which private industry could never exhibit

either the foresight or wherewithal to succeed. It is said that only the wise, all-knowing government can selflessly surmount the tawdry motive of short-term profit to focus on expensive, long-term, noble projects.

This perennial claim by freedom's enemies recently received another blow. A recent article in *Flight International* magazine reports that the Rotary Rocket Company has raised $17 million from investors and hired Barclays Capital to help it raise another $20 million in private funds in order to offer by the year 2000 commercial launches of satellites or other payloads weighing 3,200 kilograms to low earth orbit for a cost of $7 million, or $2,200 per kilogram. This is much less than today's going rate. To put this in perspective, compare the cost of launching John Glenn back into orbit, a recent publicity stunt by the attention-starved space agency: something on the order of $500 million—for a single mission.

Rotary's goal is "to herald the arrival of a new space age—the age of routine, commercial space transportation" by operating a fleet of aerospace craft called "Roton," which will be the world's first successful reusable commercial SSTO vehicle. The two-pilot Roton booster will be 20 meters high and 6.7 meters in diameter. The name of the Redwood Shores, California, company refers to the rotary pumping action of the Roton's Rocketjet engine and its free-spinning helicopter-style blades that deploy during the last phase of descent, enabling precise control for landing.

Scaled Composites is producing sections of the Roton's fuel tank. This company was founded by Burt Rutan, the designer of many highly creative aircraft, including the very popular home-builts Vari-Ese and Vari-Viggin, and the prototype of the twin-turboprop Beechcraft Starship, which may be the most advanced turboprop corporate airplane in production today. All of these aircraft use composite materials and an unusual tail-first "canard" configuration. Rutan also designed the privately created Voyager aircraft that was the first airplane to fly around the world without refueling.

Gary Hudson, Rotary's chief executive, says that Roton will begin deployments and retrievals of LEO telecommunications satellites and other cargo during the first half of 2000.

Other missions for the Roton include solar power satellites and space manufacturing of new materials. Because it is piloted, a Roton will be able to conduct a final check of satellites before their release, a service never offered before. While other commercial launchers charge clients a non-refundable advanced payment, Rotary Rocket's bill will be due only on successful delivery of the payload into orbit; any problems would result in returning the payload and launching it again with no further charge.

Rotons will also repair or retrieve damaged or "dead" satellites, which should lower insurance costs.

The Roton may well be the first profitable spacecraft. It is the product of imagination and funding that are entirely private and cost a tiny fraction of the time and money spent by its government-led competition.

Who says only the government can succeed with big, time-consuming, capital intensive projects?

Freedom is the great engine that draws out the breathtaking creativity of our human potential, because only freedom unleashes every person's desire to achieve happiness. In a free market, such achievement is advanced when we offer goods or services that please our customers, wherever they may be found on—or off—the planet. □

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THE FREEMAN
Ideas On Liberty

The Great Bequest

by Tom G. Palmer

Limited government is one of the greatest accomplishments of humanity. It is imperfectly enjoyed by only a portion of the human race, and, where it is enjoyed, its tenure is ever precarious. The experience of the twentieth century is surely witness to the insecurity of constitutional government and to the need for both courage in achieving it and vigilance in maintaining it.

Advocates of limited government are not anti-government per se, as some people would charge. Rather, they are hostile to concentrations of coercive power and to the arbitrary use of power against right. With a deep appreciation for the lessons of history and the dangers of unconstrained government, they are for constitutional limitations: government should have the delegated authority and means to protect our rights, but not be so powerful as to destroy or negate them.

The American system was established to provide limited government. The independent existence of the United States was based on certain truths:

> that all Men are created equal, that they are endowed by their Creator with certain unalienable Rights, that among these are Life, Liberty, and the Pursuit of Happiness—That to secure these Rights, Governments are instituted among Men, deriving their just Powers from the Consent of the Governed, that whenever any Form of Government becomes destructive of these Ends, it is the Right of the People to alter or to abolish it, and to institute new Government, laying its Foundation on such Principles, and organizing its Powers in such Form, as to them shall seem most likely to effect their Safety and Happiness.

On this foundation the American Founders established a system of government based on delegated, enumerated, and thus limited powers.

The American Founders did not pluck these truths out of thin air, nor did they simply invent the principles of American government. They drew from their knowledge of thousands of years of human history, during which many peoples struggled for liberty and limited government. There were both defeats and victories along the way. The results were distilled in the founding documents of the American experiment in limited government: the Declaration of Independence, the Articles of Confederation, the state constitutions, and the Constitution of the United States.

Students of History

The American Founders were careful students of history. It was Thomas Jefferson, in his influential *A Summary View of the Rights of British America*, prepared in 1774, who noted that "history has informed us that bod-

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ies of men as well as individuals are susceptible of the spirit of tyranny." Another Founder, Patrick Henry, devoted great attention to the study of history. He summed up the importance of history thus: "I have but one lamp by which my feet are guided, and that is the lamp of experience. I know of no way of judging the future but by the past." History—the lamp of experience—is indispensable to understanding and defending the liberty of the individual under constitutionally limited, representative government.

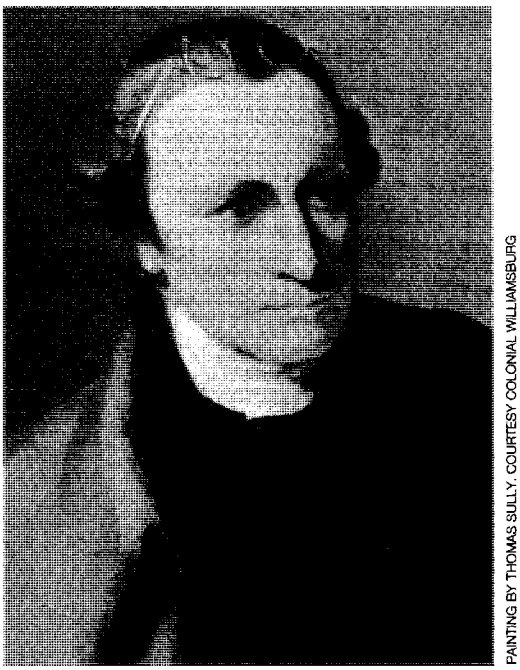
Through the study of history the Americans learned about the division of power among judicial, legislative, and executive branches; about federalism; about checks and balances among divided powers; about redress and representation; and about the right of resistance, made effective by the legal right to bear arms, an ancient right of free persons. Liberty and limited government were not invented in 1776; they were reaffirmed and strengthened. The American Revolution set the stage for the benefits of liberty and limited government to be extended to all. As John Figgis, professor of modern history at Cambridge University, noted at the turn of the century:

> The sonorous phrases of the Declaration of Independence . . . are not an original discovery, they are the heirs of all the ages, the depository of the emotions and the thoughts of seventy generations of culture.

The roots of the history of limited government stretch far back, to the establishment of the principle of the higher law by the ancient Hebrews and by the Greek philosophers. The story of the Golden Calf in the Book of Exodus and the investigations of nature by Aristotle both established—in very different ways—the principle of the higher law. Law is not merely an expression of will or power; it is based on transcendent principles. The legislator is as bound by law as is the subject or citizen; no one is above the law.

Many strands have been entwined to form the fabric of liberty:

• The struggle between church and state, which was put into high gear in the Latin West by Pope Gregory IV in the eleventh century under the motto, "freedom of the church." This movement, which created an institutional distinction between the church and the secular authorities, was the first major "privatization" of a previously state-owned industry (the church) and provided the foundation for such important institutions as the rule of law and legal accountability, federalism, and the independent and self-governing associations that make up civil society.



PAINTING BY THOMAS SULLY, COURTESY COLONIAL WILLIAMSBURG

Patrick Henry (1736–1799)

• The growth of civil society in the self-governing chartered towns of Europe, in which the guiding principle was "city air makes one free." The independent cities of Europe were the seedbeds of modern civil society—of the market economy, of personal liberty, and of the security of person and property.

• The fixing of limits on the powers of monarchs and executives through written constitutions. The Magna Carta of 1215 is the most memorable of those documents to inheritors of the Anglo-Saxon political tradition. It included the requirement that taxes could not be imposed without the consent of the "general council of the realm," which provided the

origin of the English parliament, as well as other specific limitations on the king's power, including the stipulations that no one be imprisoned, outlawed, or exiled, or his estate seized, "except by the lawful judgment of his peers or the law of the land" and that "merchants shall have safe conduct in and out of England." This was the precursor of the Petition of Right of 1628, the Bill of Rights of 1689, the American Declaration of Independence, and the American Constitution and Bill of Rights.

Those various movements reinforced each other in a multitude of ways. The assertion of the freedom of the church and even of its supremacy over the secular powers was bound up with the idea of the higher law, by which all are judged—emperor, pope, and peasant alike. As legal scholar Henry Bracton, a judge during the reign of Henry III, noted of the royal authority, "The law makes him king. Let the king therefore give to the law what the law gives to him, dominion and power; for there is no king where will, and not law, bears rule." Were the king to consider himself above the law, it was the job of the king's council—the precursor of parliament—to rein him in: "if the king were without a bridle, that is, the law, they ought to put a bridle upon him." Not only was the nascent parliament above the king; the law was above the parliament, as Sir Edward Coke noted in the seventeenth century:

> when an act of Parliament is against common right and reason, or repugnant, or impossible to be performed, the common law will controul it, and adjudge such Act to be void.

Law Supreme

The supremacy of the law over the exercise of power is a hallmark of the Western legal tradition. The rule of law is not satisfied by merely formal or ceremonial exercises, such as the publication of edicts in barely understandable form, whether in the archaic "Law French" of the king's courts or the pages of the *Federal Register*; the laws must be understandable and actually capable of being followed.

There was also widespread recognition of the principle of reciprocity between the holders of power and the general populace. Rights were spelled out in contractual form in constitutions and charters. Those rights were not gifts from the powerful, which could be taken away on a whim, but something on which one could take a stand. Tied up in the notion of a chartered right was the ancillary right to defend that right, even to the point of resistance with force of arms. The higher law, reciprocity and mutuality of obligations, written charters of rights, the right to be consulted on policy and to grant or refuse one's consent, and the right of resistance in defense of those rights are the foundations of constitutionally limited government. They were won over many centuries at great sacrifice.

Just how precious this heritage is can be gleaned from comparing it with the history of Russia, where, until very recently, there was no reciprocity between rulers and ruled, no independent power able to challenge the rulers. The principality of Muscovy and its successors were despotic to a high degree, with no charters of liberty, no power higher than the Tsar (or his successor, the Communist Party), no limits on power—in effect, no law. As Harvard University historian Richard Pipes noted in his book *Russia under the Old Regime*, "There is no evidence in medieval Russia of mutual obligations binding prince and his servitor, and, therefore, also nothing resembling legal and moral 'rights' of subjects, and little need for law and courts." The immense difficulties in establishing the rule of law, a system of well-defined and legally secure property, and a market economy are testimony to the great and vital importance of building on a tradition of stable, constitutionally limited government. They also remind us how important it is for us to maintain our heritage of limited government and the rule of law.

Liberty Versus Power

The struggle for limited government was a struggle of liberty against power. The

demands for religious liberty and the protection of property were fused in the heroic resistance of the Netherlands to the Empire of Spain in their great revolt. The Dutch became a shining example of what was possible when people were free: prosperity was possible without the guiding hand of the king and his bureaucrats; social harmony was possible without enforced religious conformity; law and government were possible without an unlimited and absolute sovereign. The Dutch inspired the English to rise up against the Stuart kings, who sought to fasten upon the English the absolutism that had made such headway on the Continent. The American Revolution was one link in a long chain of revolutions for liberty.

The story of the attempts to institute absolutism in the Netherlands and in England was well known by the American Founders, who were, after all, British colonists. One cannot understand the American attempt to institute limited representative government without understanding the history of England. What they were struggling against was the principle that the powers of the state are "plenary," that they fill up the whole space of power. King James I of England (then King James VI of Scotland) had written in 1598 that "the King is above the law, as both the author and giver of strength thereto." In 1610 James made *A Speech to the Lords and Commons of the Parliament at White-Hall* in which he railed against the notions of popular consent and the rule of law and stated that "as to dispute what God may do is blasphemy . . . so it is sedition in subjects to dispute what a king may do in the height of his power."

In other words, there are no limits to power. Distinct echoes of that view are still heard today. For example, the solicitor general of the United States, Drew Days, arguing in the case of *United States v. Lopez* before the Supreme Court, was unable to identify a single act of Congress, other than those expressly prohibited by the Constitution, that would be impermissible under the administration's expansive view of the Commerce Clause. Solicitor Days contended that the powers of Congress are plenary, that is, unlimited, unless, perhaps, specifically prohibited.

That all-too-common view turns the notion of limited government on its head. Limited government means that government is limited both to the exercise of its delegated powers and in the means it can employ, which must be both "necessary and proper." The English Revolution of 1640, the Glorious Revolution of 1688, and the American Revolution of 1776 were fought precisely to combat unlimited government. What Americans need is not unlimited government, as Days proposes, but limited government under law, exercising delegated and enumerated powers. That is how the equal liberties of citizens are protected. As the philosopher John Locke, himself an active participant in the struggles for limited government in Britain and the primary inspiration of the American revolutionaries, argued in his *Second Treatise of Government*: "*the end of Law* is not to abolish or restrain, but *to preserve and enlarge Freedom*: For in all the states of created beings capable of Laws, where *there is no Law, there is no Freedom.* For *Liberty* is to be free from restraint and violence from others, which cannot be, where there is no Law."

Unprecedented Liberty

The American experiment in limited government generated a degree of liberty and prosperity that was virtually unimaginable only a few centuries before. That experiment revealed flaws, of course, none of which was more striking and repugnant than the toleration of slavery, or "man-stealing," as it was called by its libertarian opponents, for it deprived an individual of his property in his own person. That particular evil was eliminated by the Thirteenth Amendment to the Constitution, showing the self-correcting nature and basic resilience of the American constitutional system, which could survive such a cataclysm as the Civil War.

Other flaws, however, have been revealed or have surfaced since. Among them are the following:

• An erosion of the basic principles of federalism, as the federal government has consistently encroached on the authority of the

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March 1999

Brutes in Suits

Statists on the left habitually congratulate themselves on their humanity. They croon on endlessly about peace, harmony, cooperation, community, mutual understanding, tolerance, and diversity. They profess to abhor violence and cruelty. They apparently regard candlelight vigils—featuring dozens of people swaying in unison and singing about love—as the most transcendent form of self-entertainment.

Statists on the right don't get teary-eyed at the mention of "peace" or "diversity," and most are as likely to attend a candlelight vigil as Bill Bennett is to model fashions by Dennis Rodman. But statists on the right nevertheless profess a high regard for peace and a hatred of violence.

But while their *particular* goals may differ, all statists are hypocrites. Their distinguishing mark (whether they realize it or not) is that they all advocate government-as-thuggery. Statists, whether on the left or on the right, advocate that government unleash its coercive powers in various and sundry ways, most of which would be criminal if done by private people.

The thugs in question happen to dress well, are well-coifed, and are (usually) articulate. But what makes someone a thug is not how he looks or what he proclaims to be his ultimate motive, but, rather, what he does. And most of what politicians now do is sophisticated thuggery. They're brutes in suits who sell to the highest bidders their willingness to coerce innocent people.

Here's an imperfect, but useful, way to test whether or not some government activity is thuggery. Ask: Is the activity one that ordinary people could ethically do on their own, either individually or in a group, in the absence of government? If the answer is yes, the government activity isn't thuggery. If the answer is no, the government activity is thuggery.

Consider, for example, a police officer directing traffic. This activity is legitimate; it isn't thuggery. It's legitimate because there is nothing inherently unethical about a private citizen directing traffic on a busy street. The same is true for government efforts to nab murders, rapists, thieves, and arsonists. Depending on your view of government, you might or might not trust government to perform these tasks effectively. You might also believe that even these tasks are best left to the private sector, or, instead, you might believe that it's prudent to assign these tasks to government exclusively. Either way, none of these tasks would be considered criminal or illegitimate if carried out by private persons in the absence of government. (Even legitimate activities arguably become ille-

gitimate if they are funded through coercive means, such as taxation by government. No private citizen can ethically confiscate resources from others even if these resources will be used in ways that nearly everyone approves. Recognizing that I am skipping blithely over a fundamentally important issue, I ignore here the problems created by taxation.)

Regrettably, the overwhelming bulk of what government actually does today—even apart from using taxation to fund its efforts—would be (correctly) considered criminal if private persons did these things.

Examples are legion. Here's one: minimum-wage legislation. Suppose your neighbor offers to hire at $3.00 per hour someone to work in his supermarket. Would it be moral for you to stick a gun to your neighbor's head and order him not to hire anyone for less than $5.15 per hour? Of course not. Would it be moral for you to round up several of your friends into a mob and threaten to lynch your neighbor if he insists on hiring workers for less than $5.15 per hour? Of course not.

So what makes it legitimate for government to threaten people with violence if they insist on hiring workers at less than the government-stipulated minimum wage? Nothing. Nothing at all.

Consider other activities currently pursued by government. Would it be morally acceptable for the president of Bethlehem Steel to stand on the wharves in Seattle and threaten to shoot anyone who dares to unload steel made in Asia? Obviously not. It follows that import restrictions are immoral; only thugs promote and implement them.

Would it be morally acceptable for you to burgle your wealthy neighbors' home and then give the funds to a poor family living across the tracks? Obviously not. It follows that government's efforts to redistribute wealth are illegitimate.

Would it be morally acceptable for you to imprison your neighbor and confiscate her property if she refuses to install a wheelchair ramp at her place of business?

Would it be morally acceptable for you to storm into your neighbors' house and tote them off to a jail in your garage if you find that in the privacy of their own home your neighbors smoke marijuana or Cuban cigars?

Would it be morally acceptable for you to inflict violence on Americans who refuse to obey your command that they not hire Mexican or Filipino workers?

None of these activities enjoys any legitimacy when pursued privately. Indeed, they are all considered criminal.

So why should government be allowed to do these things?

Most statists respond by intoning that democratic governments carry out the will of the people. If it's the will of the people that, say, no worker be paid less than $5.15 per hour, then the few selfish reprobates who would violate the collective will should be prevented from doing so.

Numerous problems afflict this response, not least of which is the fact that democratic government *at best* carries out only the will of the majority. One of the most pernicious myths that today plague the popular political mind is that the appetite of some mysterious phantom called "the will of the people" is justly satisfied if as few as 50% of voters plus one acquiesce in schemes concocted by a cabal of politicians who are beholden to special-interest groups.

Sadly, the very logic of modern politics is that politicians and bureaucrats use the coercive powers of the state to transfer wealth from politically unorganized groups (for example, sugar consumers) to politically powerful groups (for example, sugar producers). But whether the state is coercing the minority to bow to the will of the majority, or coercing the majority to bow to the will of politically potent interest groups, such coercion is wrong—and it gains not a smidgen of legitimacy when carried out by telegenic talking heads who work in marble-domed buildings and are dressed by Armani.

Beware of brutes in suits.



Donald J. Boudreaux
President

The March of History

What comes to mind when you think about the month of March? For many people it is the ominous-sounding "Ides of March," the day when Brutus slew the dictator Caesar, announcing as he committed the act, "Sic semper tyrannus"—"Thus always to tyrants." In recognition of the connection between March, history, and the state, we are putting four of our most interesting history titles on sale. These books will help bring new worlds to life for you—something Caesar could have used!

Leviathan at War, Edmund Opitz, ed.

Published in 1995, this anthology addresses a number of war-related topics, including the causes of war, conscription, weapons and prosperity, war and liberty, and peace and free trade. This collection contains work by Leonard Read (including his important "Conscience on the Battlefield"), Ayn Rand, Ludwig von Mises (on the economics of war], military historian B.H. Liddell Hart, and Mark Twain, among others. One of our best *Freeman Classics*, this book provides an excellent foundation for arguing against the aggressive militarism so many governments adopt.

195 pages, paper $9.95 **SALE: $4.00**

Capitalism and the Historians, F.A. Hayek, ed.*

How often do you hear that the Industrial Revolution was a disaster for workers? Many historians argue the Industrial Revolution caused wage rates and standards of living to plummet; that the movement away from farms and villages toward cities and factories was a truly dreadful development. This small book debunks these myths and provides evidence that the Industrial Revolution caused standards of living to rise, which in turn, led to a vastly improved quality of life. A great antidote to the leftist diatribes one often encounters when reading about the 19th century.

191 pages, paper $12.95 **SALE: $6.00**

The Industrial Revolution and Free Trade, Burton Folsom, ed.

More good stuff on the Industrial Revolution – one of mankind's **true** "great leaps forward." Dr. Burt Folsom brings together 22 essays that investigate the economic theories that undergirded the Industrial Revolution, the consequences of the Industrial Revolution, and the case for free trade. This book has been called "a veritable gold mine of facts about the history of free trade and of the free market." This 1996 work is great on its own or as a companion volume to Hayek's *Capitalism and the Historians*.

182 pages, paper $14.95 **SALE: $7.00**

Theory and History, Ludwig von Mises*

In his preface, Murray Rothbard says this book "provides the philosophical backstop and elaboration of the philosophy underlying *Human Action*." This neglected work includes chapters on the Philosophy of History, the Concept of Historical Individuality, and the Meaning and Use of the Study of History. It is a powerful volume that illuminates Mises's earlier writings.

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An Evening with the Editor . . .



Sheldon Richman
"Separating School and State"

Saturday, April 24, 1999, at FEE

Sheldon Richman has given a new look and fresh editorial voice to *The Freeman.* He has recruited some of the world's top journalists and renowned free-market scholars to write for FEE's monthly magazine. And his own lively "Perspective" and "Peripatetics" columns are welcome additions to the editorial mix.

Sheldon is also an informative and entertaining speaker. Get to know him better at our April Roundtable. This informal gathering starts at 5 p.m. with a reception and dinner, followed by a spirited discussion on the perils of public education. Price is $35 per person.

For reservations, call Janette Brown at (800) 452-3518.

Other Forthcoming Events at FEE

Undergraduate Seminar, March 18-20

Trustees Annual Dinner, May 16

Introductory Seminar in Economics, Politics, and History, June 26-July 1

Advanced Seminar, "The Economics and Ethics of the State," August 7-12

states. Federal criminalization of acts that are already criminalized by the states, for example, usurps state authority (as well as circumventing—opinions of the Supreme Court notwithstanding—the prohibition of double jeopardy in the Fifth Amendment to the Constitution). An even more striking contemporary example of the overreach of federal law is the continued exercise of federal controls over marijuana use in states—California and Arizona—that have legalized the medical use of that drug. The Tenth Amendment is quite explicit on this point: "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people."

• Violation of the separation of powers between the various branches of government. In article I, section 8, for example, the Constitution explicitly reserves the power to declare war to the Congress, a power that the Congress has allowed to be usurped by the executive branch and which it should retake to itself. Further, the Congress has illegally exceeded its authority by delegating its legislative powers to administrative agencies of the executive branch, such as the Food and Drug Administration and the Federal Trade Commission. In addition to violating the Constitution, that has led to the erosion of the rule of law, as such administrative agencies have burdened the population with an unimaginably complex welter of edicts; the *Federal Register* runs to some 60,000 pages *per year*, representing a degree of minute regulation that is unreasonable and burdensome and that virtually guarantees that any citizen involved in a commercial transaction, for example, will run afoul of some part of it, no matter how well intentioned or scrupulous he may be. Such a situation is an invitation to the arbitrary exercise of power, rather than the application of law.

• Inattention to the important role of the federal judiciary as a check on arbitrary and unauthorized exercises of power. Especially since the threatened Court-packing "constitutional revolution of 1937," there has been too little attention by the federal judiciary—and by the Congress in ratifying judicial nominees—to fulfilling the role of the courts in enforcing constitutional restraints on both the federal and the state governments. For example, the Supreme Court has not consistently applied the prohibitions of the First Amendment to either commercial speech or political speech (the latter in the context of campaign finance), nor has the Court rectified the novel (and specious) distinction between personal liberties and economic liberties drawn by Justice Harlan F. Stone in *United States v. Carolene Products Co.* (1938).



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Harlan F. Stone (1872–1946)

• The failure to pass a constitutional amendment limiting members of the Senate to two terms and members of the House of Representatives to three terms. Just as the president is limited in the number of terms he can serve, so should be the other elected branch of government, to guarantee the rotation in office that the Founders believed essential to popular government.

Needed Corrective

Those flaws can, however, be corrected. What is needed is the courage to place the health of the constitutional order and the

future of the American system above short-term political gain. The original American Founders were willing "to mutually pledge to each other our Lives, our Fortunes, and our sacred Honor." Nothing even remotely approaching that would be necessary for today's members of Congress to renew and restore the American system of constitutionally limited government.

The challenge facing Americans today in defending constitutionally limited government was succinctly stated by the English libertarian Herbert Spencer in 1884:

> The function of Liberalism in the past was that of putting a limit to the powers of kings. The function of true Liberalism in the future will be that of putting a limit to the powers of Parliaments. □

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Smoke Got in Their Eyes

Economics pervades life. Many people (not *Freeman* readers) will misinterpret that remark to mean that money is all that's important. And that common misinterpretation testifies to the dearth of economic education in America.

To say economics pervades life is the same as saying that choice pervades life. Everything we do volitionally requires that we choose one thing and forgo another. This is inescapable in a world where everything of value, including time, is limited.

We all understand this implicitly about our own actions. If you explain it to a child of, say, 10, he will know what you're talking about right away. He makes choices all the time.

But because economics, in this broad sense, is not taught early on to most children, and surely is not taught in schools and universities, people have a hard time applying it to most abstract matters, such as government policy. When they focus on that realm, suddenly there are no choices, and resources at any moment are limitless. Policymakers are the worst offenders.

No better example exists than the recent settlement between the tobacco companies and 46 state attorneys general. Economics was almost completely missing from the analysis of the settlement.

To recap, the tobacco companies, under the threat of pending liability suits and new government regulation, agreed to pay the states $206 billion over the next 25 years to "reimburse" them for medical expenses paid on behalf of residents with smoking-related illnesses. At first, state officials were licking their chops over what they will be able to do when the money starts rolling in. Now it is dawning on them that there might not be as much money as they thought.

The state of Arkansas is a case in point. "Is Windfall for State All Smoke, No Cigar?" asked a headline in the *Arkansas Democrat-Gazette*. The state was expecting a $20 million check from the tobacco companies by the end of 1998. But to pay that bill, the tobacco companies raised the price of cigarettes by 60 cents. The state's Department of Finance estimated that because of the price hike, cigarette sales would drop 11 percent, reducing tax revenues by $10 million in 1999. Easy come, easy go.

With the price increase comes an increase in the amount of tax smokers will pay on each pack, 2.8 cents to be exact. That led some people to believe that even if sales drop 11 percent, the state will still come out about $7 million ahead in tax revenues. Not so fast. Remember the broken-window fallacy.

At this point I must acknowledge, reluctantly, that Arkansas has a director of economic analysis and tax research who understands Bastiat's broken-window principle. "With people having to spend more for cigarettes, that money has to come from somewhere, so we look at that as a wash in sales tax," Joe LaFace said.

Good point. If smokers reduce other purchases to keep smoking as much as before,

Sheldon Richman is editor of The Freeman.

they will simply shift from one taxed item to another. There won't be an increase in tax revenue.

Aside: That, of course, is a *good* thing. I never regard it as meritorious that a policy, even the repeal of a bad policy, produces more tax revenue. What's good about government's having even more money with which to commit mischief?

Well now. The windfall won't be as large as the states anticipated. And the reason is that the tobacco companies raised prices, presumably dampening demand for cigarettes. Surely no one is surprised that the tobacco companies will pay the states from money obtained from customers. Do the companies have some other source of money? Moreover, since smokers are disproportionately low-income people, we have the Alice-in-Wonderlandish spectacle of smokers' indirectly reimbursing the states for the medical services the state ostensibly pays for on their behalf.

To truly appreciate this, let's walk through it step by step. The states, through Medicaid, pay for the treatment of low-income people with smoking-related illnesses. The states demand that the tobacco companies, which made the product that produced the illnesses, pay the states the money spent on treating their customers. The tobacco companies raise their prices in order to have the money to pay to the states for the treatment.

Wouldn't it be more efficient—not to mention honest—to cut out the middle man? But doing so would give the game away. It would be equivalent to telling low-income people that smoking disqualifies them from Medicaid. How ominous would that be? The government would be announcing that personal habits will determine eligibility for government benefits. Precedent is powerful. If that policy is adopted for Medicaid, surely Medicare is next. And as the government slowly absorbs the medical industry (the attempted quick absorption came a cropper in 1993), it will have set the stage for the general denial of medical care on the basis of personal habits. Government will be in the triage business.

So, if you have clogged arteries and a life of ham and eggs behind you, perhaps Medicare won't pay for your coronary bypass operation. If you have a cyrrhotic liver and a boozy past, you might be turned down for treatment.

But that won't be the end of it. If you're an octogenarian needing a new hip, well, maybe those resources would be better devoted to a younger person with productive years still ahead.

That's the risk we run when we let government pay medical bills.

To cover all bases, we have to entertain the possibility that higher prices won't reduce the demand for cigarettes. There were early indications of that. We can't predict how people will act in the face of new alternatives. Let's assume demand falls not at all. What happens? As we've already seen, there will be no new revenue for the states. Furthermore, since smokers don't suddenly have additional income with which to pay the higher price, they will reduce other purchases. The falling demand for other products could result in cutbacks and layoffs in those industries. Let's assume all the people laid off are nonsmokers. That leaves us with an odd outcome. People who don't smoke will be made to suffer so that people who do smoke can have their medical expenses paid for. Not exactly justice, is it?

I think we can conclude that this tobacco deal is a fiasco. It's a mass of fallacy, confusion, and dishonesty.

But it didn't begin with the states' lawsuits. It's been going on for years. When the Clinton administration came in it spoke of raising the federal cigarette tax to, first, discourage smoking and, second, pay for health care and anti-smoking campaigns. Now I'm no Rhodes scholar, but isn't there a conflict between those two objectives? If you have plans for the revenue from the cigarette tax, you'd better hope people keep smoking. That would help save Social Security too.

They never learn. President Clinton wants the states to use their tobacco windfalls for anti-smoking programs. (Some states are resisting.)

I have an idea: the government shouldn't pay for *anyone's* medical care or tax our habits or lecture us on how to live. □

THE FREEMAN
Ideas On Liberty

The "Savings Crisis"

by John Hood

It's a constant refrain among politicians and the news media: America has a low savings rate. This, it is said, has dire consequences for the long-term health of the economy. Some analysts put the personal savings rate—the percentage of disposable income that isn't consumed in a given year—as low as 2.1 percent in 1997, a 63-year low. Although this undercounts the real amount of American savings and investment, there is no doubt that the private savings rate is near an all-time low.

Why is this? Are Americans simply irresponsible? Should government force households to save more money for a rainy day, as some doomsayers have suggested?

On the contrary. America's savings crisis is almost totally manufactured by government itself. Through punitive taxation and the growth of the welfare state, big government has legislated against the habits of thrift and delayed gratification on which human progress is based. The decline in the savings rate over the course of the twentieth century isn't just a minor economic trend. It represents the threat that government expansion poses to the principles on which successful human civilization rests.

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What Is Savings?

It's worth pausing to consider the definition and origin of savings. After all, economists aren't talking simply about a bank account, or even an investment in stocks or bonds, when they address the issue of savings. For example, one's home is a form of savings, in that the value of the home usually appreciates even as one uses the home for current consumption (shelter).

Indeed, the official savings rates don't factor in the appreciating value of assets. They reflect the difference between reported income and reported expenditures. The Commerce Department, which generated the 2.1 percent rate cited above, doesn't actually track inflows and outflows of wealth. It doesn't include the rise in the value of investments in individual retirement accounts, 401(k) plans, real estate appreciation, or the rise in value of mutual funds or corporate stock. It doesn't count the implicit wealth people accumulate in pension plans. The Federal Reserve computes an alternative measure incorporating some of these factors and estimated that the 1997 savings rate was actually 7.1 percent of disposable income. Still, that's pretty small compared with the savings rates of other countries. In Asia, rates reach as high as 20 percent.

The reason the issue of savings is so impor-

tant is that deferring consumption—which is probably the best definition of savings—is essential to human happiness. That statement may seem paradoxical. How can forgoing current pleasure or satisfaction by choosing not to buy a good or service today increase one's happiness? To answer that question, it's important to look at how four closely related economic behaviors—savings, insurance, investment, and specialization—arose among prehistoric human cultures.

A Short Economic Prehistory

The earliest societies historians can identify are the nomadic hunter-gatherers who inhabited various regions of Africa, Asia, Europe, and the Americas. Throughout most of their history, these hunter-gatherers traveled in small groups of 20 to 30 related individuals—a patriarch and matriarch, their children and grandchildren, mates from neighboring groups, and other assorted relatives. They worked together both to hunt animals for meat and to gather fruits, vegetables, nuts, simple tools, and other useful objects. Because these groups were constantly on the move, their housing consisted of either portable shelters (tents, or yurts) or structures they found or could construct quickly (caves, lean-tos).

In this earliest of human societies, the line separating political, economic, and spiritual institutions was blurred or nonexistent. Few of the tools future civilizations would use to draw such lines were available to the hunter-gatherers. Their nomadic lifestyle, for example, provided little opportunity to develop or enforce private property rights, not only over land but over the products that land might produce. Private property rights are indispensable if societies are to separate the public from the private, the sphere of human activity over which political power is freely wielded and the sphere over which it is limited or excluded.

Furthermore, the small size of these societies necessarily reduced the extent to which differences in knowledge or talent resulted in the development of markets or a division of labor beyond the most rudimentary one. Finally, because they lacked any practical means of saving and transporting food of more than limited quantities, these earliest human societies provided little reward or incentive for hard work. All that was hunted or gathered was consumed relatively quickly. An individual who was exceptionally talented as a hunter or gatherer had no reason to invest much of his time performing those tasks.

Stages of Economic Discovery

Even under these conditions, however, developments occurred in economic exchange and institutions. The earliest hunting and gathering humans cooperated with each other to derive sustenance from a sometimes-forbidding environment. They had to develop terms of trade and rules of work and reward in order to put members of the clan or band to productive use. A simple division of labor did evolve, based on age, sex, and physical prowess (or infirmity). We know that these small societies, while primitive and sometimes brutal, also gave opportunities for those with different natural talents and skills. And while the invention of money was far in the future, these early humans engaged in mutually beneficial trade in valuable goods that sometimes spanned surprising distances.

Archaeologists and anthropologists divide human prehistory before metallurgy into three periods: Paleolithic (Old Stone Age), Mesolithic (Middle Stone Age), and Neolithic (New Stone Age). The names suggest a categorization based on stone technology, but the real dividing lines among these periods involve changes in geography and corresponding changes in economic technology and organization.

For the purposes of understanding economic history, the Paleolithic Period is critical. It lasted from 2.5 million years ago until about 10,000 B.C. Humans during this period include Homo erectus and archaic Homo sapiens. Early in the period, humans used simple tools made either of the core of a stone after pieces had been flaked off, or the flakes themselves. They used fire (discovered sometime between 1 million and 500,000 years ago) to drive or prod animals, to prepare food, and of course to keep warm.

Later, in the so-called Middle Paleolithic Period, flake tools were developed into a wide array of scrapers, borers, and points used to manipulate animal kills and other materials. This was the period of Neanderthal Homo sapiens in Europe and some humans even closer in appearance to modern humans. Their tools may have improved their hunting but, more important, there is evidence of extensive social cooperation not only in hunting but in storing and exchanging food. As one writer has noted, hunting is not just about killing animals. Killing animals is the easy part, whether it is by using weapons, by trapping, or by driving prey over cliffs. The difficult part lies in the organization of personnel so that they are in the right place at the right time and with the right gear to ensure a better-than-average chance of success.

Even more difficult is the task of coping with failure, weather, and the decline of animal stocks. Remember that these societies lacked effective technologies for storing food, and a diet of nuts, berries, and other gathered foods was of insufficient quantity or nutritional value to tide families and clans over in the event of a seasonal decline of game.

Humans Beings Invent Savings

It is here, in the Middle Paleolithic populated by humans whose language skills were limited or nonexistent, that economic institutions extending beyond kinship probably developed. More specifically, these Middle Paleolithic people pioneered the crucial economic behavior of managing risk—in this case, the risk of starvation. They did it with two innovations: savings and group insurance. In the former case, they learned to put stores of food in secure places in their hunting and gathering territory, and then budget them to cover subsistence needs over the lean times. In the latter, nearby small kinship groups established social networks through alliance, intermarriage, visiting, and feasting that served as regional insurance policies. A group facing a decline in game (or lack of success in hunting) could make claims on the food stores of neighbors with whom they had previously invested time, attention, or their own food. This served to spread the risk of starvation over a broader number of hunters and gatherers, thus improving the chances of survival for all.

The concepts of savings and insurance are closely related; indeed, one might think of insurance as a way of realizing the benefits of savings without 1) having to develop technologies for saving food over a long period and 2) having to wait until a stock of savings is sufficiently large to tide a family or group over during hard times. Insurance-type arrangements, if they are of large enough breadth for their members to escape simultaneous misfortunes, represent a reasonable technique for coping with risk under difficult technological conditions.

The Upper Paleolithic, beginning about 50,000 years ago in various regions, represented the appearance of humans roughly identical to us today. It also brought two additional economic innovations of critical importance: specialization and investment. The Cro-Magnon and other advanced Homo sapiens of the Upper Paleolithic, unlike their predecessors, seem to have specialized in the hunting or gathering of specific species, rather than being purely opportunistic and pursuing whatever was visible in their range areas. Like savings and insurance, specialization was a form of risk management in the sense that it usually involved careful study of particular animals with the goal of predicting their behavior—and thus increasing the likelihood of catching them. Specialization took some of the risk out of hunting and gathering by allowing for the accumulation of knowledge with which small human societies could ensure a more stable and predictable food supply. It not only required study of animal habits and movements, but also a more detailed understanding of the climate and topography of their range areas.

Accumulating such knowledge had a cost. It took a great deal of time and effort, which earlier human societies had probably devoted to less taxing and more recreational activities. Indeed, many people assume that economic progress throughout history has meant a progressive increase in leisure time, but until recently the opposite has been true. In earlier Paleolithic groups, there was little to be

gained by spending more time on hunting and gathering activities rather than on leisure activities. Hunting and gathering was such a hit or miss process that increased time and effort invested in it wouldn't have yielded much more in the way of results.

But with the introduction of specialization, increased time and effort devoted to the study of quarry and environment could pay off in higher returns. So the more sophisticated hunters and gatherers of the Upper Paleolithic discovered the value of investment—forgoing consumption or leisure in the short run for greater material benefit in the long run. Until it became practical to store information (through better language skills and specialization in a relatively narrow field of inquiry) investment would have had paltry returns.

This revolution in hunting and gathering had repercussions beyond improvements in the food supply. It was also associated with the development of larger, multi-family groups. For one thing, specialization and investment made population growth much more desirable. Additional people meant additional opportunities to gather useful information and carry out the more complex strategies required to catch more game. At the same time, the improved food supply made it possible to support larger populations. Specialization and the increased scale of human populations led to larger and more permanent settlements, and the beginnings of a territoriality that would eventually lead to concepts of private property. And both the larger populations and the increased productivity of hunting and gathering made possible a greater division of labor within the groups, allowing some individuals the option of specializing in tasks other than hunting and gathering.

Savings and Investment Create Trade

Finally, the development of larger groups with a higher level of specialization created the conditions required to inaugurate trade among unrelated groups. After all, if one group chooses to specialize in a particular form of hunting and gathering, then the occasional acquisition of game or artifacts outside the specialty becomes more attractive. It represents variety and diversion. A coastal group specializing in catching fish and gathering shellfish would have something of value to offer an inland group specializing in hunting deer, horses, or other big game. This increased value of trade would apply not only to foodstuffs but also to other goods. In both western and central Europe of the Upper Paleolithic, for example, there is evidence that several species of seashells were traded or exchanged over hundreds of miles. Similarly, there is evidence of relatively long distance trade in high-quality flints and other raw materials.

The Upper Paleolithic Period ended with the end of the last Ice Age and the impact of global warming on the environment. The initial stages of this warming can be traced back to about 11,000 B.C., and affected different parts of the Old and New Worlds at different times. The oceans rose as ice melted, forests expanded over the expanses left behind by the retreating glaciers, and portions of the globe saw climate change of cold to temperate or temperate to hot. These changes led either to human migration or to significant changes in the way humans lived in their home areas. One further note about the end of the Upper Paleolithic is that it coincides with the final settlement of every habitable continent.

The key point for our purposes is that the development of multi-family societies, and later towns and cities, was based on the invention of economic practices involving delayed gratification, or savings. The habit of savings and investment paid its greatest returns once human settlements developed around new notions of private property. Once families could work their own land or tend their own herds, the economic value of hard work soared. After all, at a very basic level, agriculture and animal husbandry were the epitome of savings and investment. Rather than literally "eating the seed corn," farmers planted it in the ground, tended it for months (perhaps nearly starving the whole time), and then reaped a far greater bounty at harvest time. With herders, delaying gratification meant feeding scarce grains and water to stock animals rather than to their own families. It meant tending, not eating, the stock. Those

who could learn to do this would, in the long run, be far better off that those hunter-gatherers who worried only about today's meal.

If one considers the broad sweep of human history, this radical revolution in how human beings live has occurred only recently. The passage of time from the last Ice Age and early human settlements to the modern day is, geologically speaking, a blink of the eye. Yet consider how radically different our lives are compared with our hunter-gatherer ancestors.

The Savings-Rate Decline

Although no data exist on the personal savings rate per se throughout recorded history, one can safely say that it was extremely high. Even as recently as the nineteenth century, most Americans still lived and worked on farms. They spent most of their waking hours saving and investing—working the land for the promise of future return. Few could afford luxury items, vacations, or other forms of current consumption.

The Industrial Revolution changed all that. Mass production, first of clothes and later of other goods, significantly reduced their cost and thus reduced the amount of time and effort consumers had to save and invest in order to afford them. Advances in transportation technology came next, facilitating trade and thus the comparative advantages in price and quality of purchasing goods from others rather than making them oneself. Finally, dramatic advances in agricultural technology and practices so increased the productivity of farming that prices fell, far more food and fiber could be produced per person, and farmers gradually found their time and effort more profitably invested elsewhere.

The purpose of savings and investment changed from acquiring basic necessities to addressing "quality of life" goals. As workers moved to cities, then to suburbs, in the new industrial economy, savings and investment became a means of purchasing a new automobile, buying a nice home, sending children to college, affording higher levels of health care, dealing with sudden disability or unemployment, and providing for a comfortable retirement.

Unfortunately, the advent of the New Deal in the 1930s, followed by the Great Society programs of the 1960s, began to suggest to Americans that these big-ticket items in their lives might be paid for by someone else. Roosevelt's Social Security and unemployment insurance promised income in case of sudden loss of employment, disability, or old age. Johnson's Medicare and Medicaid promised families that they wouldn't have to save and invest to take care of elderly relatives who needed lots of medical attention or institutional care.

At the same time, these expansions of government spending required increasing amounts of revenue. The government got this revenue in large part by taxing private savings and investment. The first permanent income taxes arose in the early 1900s. Marginal rates soared during World War I and then rose again during the New Deal and World War II. Payroll taxes were added to fund entitlement programs, taking money that families would otherwise have saved for their own needs. Today, the income tax code is strongly biased in favor of current consumption and against long-term savings. For example, a worker who earns $1,000 will pay income and payroll taxes only once on that money if he chooses to spend it immediately. If he invests it in corporate stock, however, he will likely pay income tax on the money three or more additional times, as the corporation pays taxes on earnings, the worker pays taxes on his dividends, and then pays again if he leaves the investment to his heirs.

Is it any wonder that the rise of the welfare state has coincided with what many observers, of varying political persuasions, call a new ethic of instant gratification and self-indulgence? Public opinion polls show that Americans have become convinced that government will help them through the big expenses they will face in their lives, be it unemployment, education, health care, home-buying, disability, or retirement.

This is a mirage, of course. If one thinks of the money taxed out of families and "invested" by government for these future needs as the real rate of personal savings, then it's not being invested very well. Everyone knows the

crisis that faces Social Security in the long run, as Baby Boomers retire and base their expectations of a comfortable old age on the prospect of government transfer payments from a smaller cohort of working Americans. But the problem isn't just limited to retirement. Medicare will go broke far earlier, perhaps in the next decade. Medicaid—increasingly a program of nursing-home payments for the middle-class elderly instead of an anti-poverty program—will collapse next. Unemployment insurance is already an awful deal for most workers, who are eligible to draw money only if they are terminated without cause, and even then they get paltry returns. The money Americans are forced to save and invest in education also gets poor returns, as the mediocre test scores of American schoolchildren and the declining academic standards of American universities illustrate.

So even if one defines the savings rate in the most expansive manner—as not only private savings but also the amount of money government "saves" on your behalf—there remains a savings crisis. Too little of our seed corn is being invested in long-term productive enterprise, with a promise of future harvests. Instead, government is feeding this seed corn to current beneficiaries of entitlement programs. Americans have lost the impulse that industrious human beings throughout history have maintained to work and save for the future.

This is the real savings crisis. It isn't just one of dollars and cents, but of thrift and self-reliance. The solutions are clear: end the tax code's bias against private savings and investment, and end government's false promise of saving and investing on our behalf. There is no more serious challenge facing American society and American freedom. □

(For further background, see Barry Cunliffe, The Oxford Illustrated Prehistory of Europe *(Oxford: Oxford University Press, 1994) and Mark Kishlansky,* Civilization in the West, Volume 1 *(New York: HarperCollins Publishers, 1991).*

The Foundations of Morality

by Henry Hazlitt



In this impressive work Hazlitt explores the proper foundation of morality. It would give the game away to reveal his conclusion, but suffice it to say that Hazlitt conducts a detailed and scholarly inquiry into the many possibilities.

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THE FREEMAN
Ideas On Liberty

The Bully that Acts Like a Hero

by Harold B. Jones, Jr.

In 1995 President Clinton established what he called "Operation Restore Trust," a Health and Human Services initiative aimed at wiping out fraud and abuse in the health-care industry. According to the administration, only terrorism surpassed health-care fraud as a criminal problem in this country. The initiative relied on the False Claims Act, a piece of legislation dating back to the Civil War and designed to frighten Army contractors into honest billing practices by threatening them with a substantial fine plus triple damages for every false claim.

An Operation Restore Trust demonstration project in five states supposedly identified $23 in overpayments for every dollar spent on the project, and the program was expanded. Eighty percent of American hospitals and nearly 100 percent of those participating in Medicare were targeted for investigation.

The program used demand letters that began with a reference to the False Claims Act and went on to tell hospital administrators that "It has been determined that your institution should be civilly prosecuted pursuant to that act." A statement like that is a good attention-getter. It was, however, followed at a short distance by these words of comfort: "In order to expedite and simplify this matter, we are extending to all hospitals the opportunity to settle before litigation."

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One particular hospital received such a letter on November 21, 1996. The letter stated that in the 85-month period ending on December 31, 1994, the hospital had submitted 13,726 Medicare claims for a total of $140,648,474. Of these, the government said 36 were "false claims." Of the amount that had been billed, $7,998 had been billed incorrectly. Under the terms of the False Claims Act, if the hospital had defended itself in court and lost, its penalty would have been $153,576.15, in addition, of course, to its legal expenses. It settled out of court for a fine of $12,257.

Abuse or Error?

Let's look at this case a little more carefully. The total number of Medicare claims was 13,726. Thirty-six were supposedly false claims. That figures out to be a "false claims" rate of about one quarter of one percent. The false claim dollar amount was less than one percent of one percent. To state the matter precisely, we have here the case of a complex bureaucratic process that was accurate in 99.74 percent of the cases and for 99.99 percent of the dollars involved.

This raises some questions. The most obvious is about the government's characterization of the hospital's behavior as "fraud and abuse." Could it not be more appropriately described as a simple billing error? What does this say about the honesty of our government? On the one hand, it goes to a hospital with a demand

that is probably better described as extortion than regulatory oversight. On the other, it goes to the American people with a deliberate mischaracterization of the way private institutions have conducted themselves. It acts like a bully. It represents itself as a hero.

The government's behavior in cases of this kind undoubtedly has something to do with the character of the current president, but it has even more to do with the fact that government is an organization. Organizations differ in many ways, but beneath that variety are certain common denominators of organizational behavior. Let's examine the government's regulatory activities in this light.

The Real and the Palatable

The student of organizations soon learns that there are at least two explanations for everything an organization does: an explanation that sounds good and the real explanation. (There could be several of each kind.) We learn the first by looking at the organization's statements about its purposes. We learn about the second by studying its behavior.

In his wonderful book *The Death of Common Sense,* Philip Howard looks at issues through the eyes of an attorney. He gives examples of government's stated objectives (the reasons that sound good), notes its complete failure to attain these objectives, and concludes that government is ineffective. It can be argued, however, that although it seldom attains its stated objectives, government is massively effective in reaching its real objectives. These objectives are never articulated, but they do exist, and they have been identified in the behavior of every organization ever studied. They are in fact the driving force in the life of an organization, and government is, if anything, more effective than other organizations in reaching them.

Consider the Food and Drug Administration and the Environmental Protection Agency as Howard describes them. The FDA set out in 1962 to examine the possibly harmful effects of some 200 food-color additives. The task was supposed to take 30 months. It actually took 28 years. In 1972, the newly created EPA was assigned the task of examining 600 pesticides and determining which should be removed from the market because they were hazardous. The Insecticide, Fungicide and Rodenticide Act gave the agency three years to carry out this project. More than 25 years have passed since then, and for most of this time over a thousand EPA employees have been hard at work on it. They have come to conclusions on the safety of about 30 pesticides. The rest, including those with regard to which the data indicate a significant risk, remain on the market.

If we content ourselves with believing that the actual purposes of our government and its agencies are the same as their stated purposes, we will conclude simply that the FDA and the EPA are incredibly ineffective. Something needs to be done, we will say, and we will vote for the person who claims to have a plan for doing . . . well, *something.* If we want to understand what's happening, though, we must recognize that the actual purposes of an organization are not necessarily the same as its stated purposes.

The Law of Self-Preservation

Every organization we know has sought to perpetuate its own existence. I won't say there are no exceptions to this rule. Now and again one encounters exceptions to almost everything. The case of the organization that voluntarily ceases to exist is approximately as frequent as the case of the happy, healthy, and well-adjusted man who decides to drive his car off a cliff. It is not logically impossible, but it is extremely rare.

One of the best guarantees for an organization's continued existence is a public perception that it is involved in something important. Even organizations with large endowments need public endorsement. This creates a strong incentive for organizations either to expand their missions or to draw them out. In spite of flowery statements about their purposes, organizations display mixed sentiments about actually completing whatever it is they are supposed to be doing.

The original purpose of the March of Dimes was the discovery of a cure for polio. Well, the cure was discovered. The March of

Dimes should have disbanded. Its work was done. But you already know the rest of that story.

Spinoza said everything seeks to persist in its own being. When applied to government and its agencies, this helps to explain the existence of regulatory codes that Howard says are so complex as to guarantee noncompliance. The Occupational Health and Safety Administration has estimated that at least 80 percent of all workplaces are not in compliance with the law. The reason? It's simple. Not even the most conscientious businessperson has time to keep up with four thousand detailed regulations.

Howard suggests that we need to develop more general laws that can be interpreted according to the demands of the situation and then hold people accountable. In the long history of governments on this planet, however, there have been very few changes of that kind. Almost without exception, legal systems become more detailed and complex over time.

Complexity Breeds Power

Complex legal systems increase a government's power over its citizens. The Resources Conservation and Recovery Act (known as "Rickra"), for example, requires every company that receives hazardous materials to keep track of them and eventually dispose of them. RCRA also requires a ledger showing exactly where each container is located on the premises. Federal environmental agents go into large companies that could not possibly maintain minute-to-minute paperwork on the exact location of thousands of barrels and threaten criminal indictments unless the companies pay large fines. Once again, the government's behavior is more like extortion than regulatory oversight. A complex rule has allowed a government agency to make unreasonable demands without fear of being challenged in the courts.

Organizations never represent themselves as striving for their own preservation, of course. They always appear to be seeking to advance the interests of outsiders. I don't suppose too many people would challenge me if I said that Minute Maid is infinitely more concerned about selling orange juice than about customers' health. But an ad campaign based on that truth wouldn't get very far. To succeed in advancing its own interests, an organization must represent itself as seeking to advance the interests of outsiders. (As we'll see, with private companies the two sets of interests coincide.)

This law of organizational behavior holds true across the wide spectrum of organizations and in no way depends on the personalities or ideologies of the individuals involved. Government always manifests this tendency. That has been evident in both Republican and Democratic administrations.

Antitrust Law

A good example is antitrust legislation, whose ostensible purpose is to protect consumers from monopolies that operate to restrain trade and therefore to raise prices. An examination of how the laws have been used, however, may raise some doubt. If the stated and real purposes were the same, the laws would provide a clear description of prohibited behaviors. A businessperson could use them to determine what was legal and what was not. As Ayn Rand pointed out, though, the antitrust laws are designed and have been interpreted in a way such that one cannot know whether they have been violated until after the fact. Numerous students of business ethics have pointed to this problem as characteristic of the regulatory laws in general. They are like a powerful trap with a defective trigger mechanism. Several people step over it without harm. Then all of a sudden and for no apparent reason, it takes off someone's leg.

During the 1930s, Alcoa had become an aluminum monopoly in the sense of being the only producer in its industry. But it was not a monopoly that constituted a restraint of trade. It had kept the price of primary aluminum at a level compatible with the maximum expansion of its market. At that price, profits were possible only by means of cost-cutting efficiency.

Alcoa had not entered into collusive arrangements with any other producer or with any of its customers or suppliers. It had done

nothing to dominate the aluminum industry or forcibly prevent the entry of new competitors. It had done nothing to violate the law. All it had done was attempt to maximize its profits in exactly the way that economic theory says they can be maximized, by setting its marginal revenues equal to its marginal costs. Other companies did not enter the market because at the going price it was not profitable to do so. If Alcoa had raised its prices, though, or if a cost-cutting technology had been discovered, competitors would have appeared almost immediately. Given the opportunities of a free market, innovation would have happened sooner or later.

Under the antitrust laws, a monopoly, as such, was not illegal. What was illegal was "the intent to monopolize." Under those laws, Alcoa should never have been found guilty unless there was evidence that it had tried to maintain an artificially high price by taking aggressive action to exclude competitors from the market. No such evidence was ever presented. Judge Learned Hand, however, in *United States v. Aluminum Company of America* (1945), argued that the mere fact of being so productive that competitors had no incentive to enter the market was in itself sufficient evidence of monopolistic activities. Alcoa was penalized, Ayn Rand said, not for breaking the law, but for being a well-run business. The net effect was a higher price for consumers.

Five years later, the Cellar-Kefauver Act would sprinkle holy water on this injustice by declaring that market share could be used as evidence of intent to monopolize. It was nothing but an after-the-fact justification of something that had already happened. Behavior of this kind is what the great organizational theorist Karl Weick has described as retrospective sense making. The federal government was in effect looking back at its previous actions and reinterpreting them in such a way as to make itself look good. Instead of correcting the injustice, legislators re-defined the situation in such a way as to make Judge Hand's decision seem reasonable. The legislation was not described in these terms, but that was its effect. It explained away the Alcoa case, set the Justice Department free to initiate more cases of the same kind, and provided justification for the expansion of the antitrust division through the hiring of more lawyers. The government said it was protecting the public. It was in fact expanding the area under its own control.

The laws of organizational behavior apply quite as much to businesses as to the government and its agencies. Businesses, too, offer both real reasons and reasons that sound good. Businesses, too, seek to advance their own interests and represent themselves as seeking to advance the interests of outsiders. Businesses, however, come with a safety device called competition. A business operates under the hard necessity of providing something of value to its customers because if it doesn't, they will find another place to spend their money. If Ford doesn't provide me with a good car in exchange for my dollars, there are plenty of other companies that will. Competition puts constraints on the degree to which the actual performance of a private enterprise can vary from its stated purpose.

Governments, as monopolies, do not operate under this constraint. The only thing that can constrain the behavior of a government is an informed and active citizenry.

We need to start looking at the difference between the government's stated purposes and what it actually does. It claims to be protecting us. What it is actually doing is gradually taking away our liberty. Businesses are easy targets. Ever since 1902, when Theodore Roosevelt initiated the trust-busting era with his attack on the Northern Securities Company, the government has portrayed private institutions as offenders and itself as the defender of the public interest. It does not take much thinking to see that this is a misrepresentation. We need to remember that the government's freedom to harass a business is the freedom also to harass the individual. Ayn Rand would remind us that when one citizen's rights can be legally violated, no one's rights are safe. □

THE FREEMAN
Ideas On Liberty

Philosophy 1 On 1

by James R. Otteson

It is no secret that classical liberalism receives little attention in American academic philosophy, and then generally only as a historical artifact. What one hears is something like this: "No serious philosopher today believes that people can get on without substantial, organized help from the government. The only issues are in what way the government should help and to what extent; the issue of *whether* the government should help can no longer be seriously entertained."

There are of course exceptions—Robert Nozick, David Schmidtz, and Eric Mack come to mind—but they are a decided minority and, in my experience at least, are often not considered to be within the philosophical mainstream. I have thus faced considerable difficulty convincing my colleagues that classical liberalism is worth thinking about at all, let alone worth careful examination. But a free society is worth the effort, and so I have explored many methods of opening the closed intellectual doors I have encountered, believing that if I can get others to think about classical liberalism for just a few minutes, I will find some place where it matches up with—or, if I am lucky, accounts for—a deep moral or political intuition they already have. When that happens, I have found that classical liberalism suddenly gains a footing as a position that has at least the possibility of plausibility. And that is a start.

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Connecting to Intuition

In my experience arguments for classical liberalism rarely get off the ground unless they can first make this connection to intuition. Hence the method I have settled on for extending liberty's cause in my discipline of philosophy is one that, first, seizes on a few of the adversary's deeply held intuitions and then uses those intuitions as bases on which arguments can be built. I think three intuitions in particular combine to make an initial case for the free society that almost any person, regardless of his political position, will find formidable.

Here's how I propose going about it.

Begin by asking whether there is anything wrong with rape. Now of course such a question may well shock its hearer, but a shock is sometimes necessary to get people to think hard about a different way of looking at the world. Ask your adversary to answer the question seriously. So: yes, there is something wrong with rape. Well, what is it exactly? It does not suffice to say that rape is self-evidently wrong because it might not be self-evidently wrong to everyone. The rapist, for example, might not think so.

To bring the matter into sharper focus, ask this next: Is rape *always* wrong—or might there be occasions when it is acceptable? What if raping a person would lead to some greater good? For example, should we consider whether the rapist might not receive such a degree of pleasure from the rape that it effec-

tively cancels out the pain and suffering the victim experiences? On that ground, then, should we judge each rape on a case-by-case basis, asking in each instance whether the act in question led to a net increase or decrease in welfare? This question is typically met with horror: *of course* rape is always wrong and of course its wrongness is not subject to any utilitarian calculation. It is wrong absolutely and simply so. The following suggestion will now seem quite apt and will almost always meet with approval: rape is wrong always and everywhere because a person's body is inviolable; a person has an absolute right to his (or her) body, and anyone who breaches that right is acting immorally regardless of his reasons. A person is, as it were, the *owner* of his own body, and as such he has absolute say over what gets done to it.

At this point the case for a free society has already begun to be built, though one's adversary probably does not see it. It is time to call up the second intuition, again by asking a question whose answer will seem obvious. Is there anything wrong with slavery? Well, what exactly? Again we must not allow "self-evidence" to justify our belief that slavery is wrong because many people evidently have believed and continue to believe that slavery is at least in some circumstances acceptable. Might slavery be wrong because it violates the dignity of the enslaved by treating him as a means to someone else's end? Might it be wrong because it dehumanizes the enslaved, treats him as if he were the moral equivalent of a pack animal?

Yes, that is it: slavery is wrong because it treats a man as if he were not a man; it fails to respect his inherent dignity, his inherent worth as a human being. But suppose that Congress—and congressmen, note, are popularly elected—passed legislation requiring the enslavement of some minority of the population. Suppose that to supply vital industries with much-needed cheap labor, the majority of us decided to enslave all, let us say, Irishmen. This would be democracy in action; the whole process would be strictly according to protocol in a democratic country. That would be acceptable, would it not?

Of course not! the reply will come. Slavery can never be justified, no matter how many people voted for it. And now one's adversary will believe what has already been said with almost unshakable conviction: slavery disrespects the inherent dignity in a human being and is therefore always wrong. A person may not in any way be used against his will for the sake of another person, and his sovereignty over his own life is immune from democratic (or any other) lawmaking.

Is Theft Wrong?

Now the foundations of the free society are almost entirely laid. Only one more element is required. Is there anything wrong with stealing? This matter can be a bit tricky, because there will be those who think that stealing is justified in the case of a poor man stealing from a rich man. Put that possibility off for a moment and ask the hearer to answer whether theft as a general practice is acceptable. Is it all right for anyone who wants something simply to take it regardless of who owns the thing in question? To this question the answer will be "no." But once again, why is it not all right?

Although the intuition that stealing is wrong is strong, people are often not quite sure what to say about why it is wrong. Proceed, then, with this question. Suppose Congress took a vote, and the majority, which carried the day, passed legislation licensing local police authorities to take anyone's property whenever in their judgment, and in their judgment alone, they saw fit to do so. Would there be anything wrong with that? Would the fact that such a practice had been signed into law thereby make the practice morally acceptable? Odds are that the answer to this will be "no" as well.

Make, then, this suggestion. People have a right to what they own—that is, to what they have legitimately acquired (through labor, trade, or gift); stealing violates that right and for that reason is wrong. To return to the case of the poor man stealing from the rich man: how wealthy a person is does not seem relevant to our explanation of why theft is wrong. Theft violates a right, and hence it is wrong regardless of whose right is in question. If one's

adversary wavers on this point, remind him that there is always someone poorer than oneself, and thus everyone is a "rich man" relative to someone else—so if he is willing to allow an exception for a "poor man" to steal from a "rich man," he is effectively licensing not only everyone else but also himself to be robbed. Is he still willing to make this exception?

Government Violates Rights

One can now move in for the coup de grâce: one's adversary, whether he realizes it or not, is a classical liberal. Everything the state does beyond protecting these basic, negative rights of individuals is a violation of these same rights. Conscription, for example, is a use of your body to which you did not assent. The income tax and the staggering national debt are nothing but obligations on you to labor for the benefit of someone else. Wealth transfers to the poor, subsidies to farmers, support for the arts, and Social Security are all the forcible seizure of some people's property in order to give it to others. And however noble the cause, however good the intentions, however many people voted in favor—rape, slavery, and theft are still wrong. And hence all the government programs that are merely particular instances of the principles underlying the immorality of rape, slavery, and theft are wrong as well.

One concrete example will show that the strong language of rape, slavery, and theft is justified in the case of government action. Estimated projections are that an average American born in 1999 will face an effective income tax rate of *one hundred percent* of his lifetime earnings simply to pay off the financial obligations that the American federal government will have incurred—and that is assuming that no more government programs are created. One hundred percent of lifetime earnings to make good on debts that these people played no part in creating and from which they will receive no benefit. How do you define slavery?

My genuine suspicion is that virtually all people are libertarians in their personal, everyday lives. In practice they regard anything that violates the sanctity of a person acting privately to be wrong. Certainly among my colleagues in philosophy I have met no one who would bodily assault another person (except perhaps in self-defense), who would enslave another person, or who would steal from another person. The challenge for the supporter of a free society, then, is threefold. First, he must get his adversaries to see that these three principles—the right to one's body, the right to one's labor, and the right to one's belongings—are the fundamental organizing principles of classical liberalism. Second, he must show his adversaries that they already subscribe to these principles, a fact demonstrated by their reaction to the series of questions raised above. And, finally, he must bring his adversaries to understand that these principles are binding on everyone, including those who work for the government.

This last point is especially difficult since many people are inclined to believe that the government has an authority all its own. That is, they think that if the government says something, it must be right; and if the government tells one to do something, one's sole duty is to obey. But one can summon a strong impulse to reconsider this thinking by pointing out that the government is nothing more than other people. If one would expect one's neighbors to live by the three principles of respecting others' lives, liberty, and property, then one should expect government employees to live by them as well. A person gains no special knowledge and earns no exemption from the requirements of morality merely by becoming an employee of the government.

Now I have not demonstrated that the free society is the only morally acceptable society (though I believe that it is). A philosophically sophisticated person will demand further argument for the principles underlying each of these intuitions, even if he shares them. It does not follow from the fact that one has a certain intuition about a moral matter, or even from the fact that many people have the same intuitions, that the matter is thereby settled. One's intuitions might after all be wrong.

Moreover, I have not yet shown that the moral principles that I have suggested underlie these intuitions are in fact the principles that underlie them. It is possible to construct

moral condemnations of rape, slavery, and theft—and thus justifications for the respect of life, liberty, and property—without appeal to natural rights. It might be possible, for example, to give a utilitarian or consequentialist rationale for these principles, although the sense that these principles deserve absolute recognition will be difficult to preserve within a utilitarian moral framework. It is also quite possible that one either has these intuitions or embraces these principles because one subscribes to Austrian economic thought. A follower of Ludwig von Mises or F.A. Hayek may well adhere to the sanctity of these moral principles without thereby thinking that they are made sacred because of their reliance on natural rights. Mises himself thought that the notion of natural rights was an intellectual fiction. Or one might subscribe to these principles because one is a Christian who believes that each of us, as a child of God, is sacred. A follower of Father Robert Sirico will believe that it is a violation of God's will to treat another human being as anything other than inherently valuable and inviolable, and that one cannot fulfill one's Christian duty to others unless one is radically free to choose to do so. Or, finally, one might think that man's rational autonomy presupposes allegiance to certain universal rules, among which are the principles under consideration here. A Kantian will believe he is categorically commanded to treat others as ends in themselves and never merely as means, and he might for that reason believe that the free, classical liberal society is just the Kantian "kingdom of ends."

I would not presume to resolve here which of these foundations for believing in the principles of the free society, if any, is correct. But that is not my intent. My belief is that substantially all of us share the intuitions that suggest these principles, regardless of the specific set of background beliefs we hold that lead us to accept them. My purpose rather is to galvanize adherents to a wide array of beliefs to fight for the free society by showing them that anything beyond the minimal, libertarian state violates moral principles they already hold—*whatever* the basis on which they hold them.

The Virtue of Consistency

All that would remain is to remind one's adversaries of the importance of consistency in applying these principles generally. The classical liberal society is not alien or extreme or licentious or bizarre or naïve. It is simply our own moral principles writ large; it is the manifestation and reflection of the person of dignity each of us believes himself to be.

Many years ago Hayek called on classical liberals to "make the building of a free society once more an intellectual adventure, a deed of courage" and to develop a program that would at once inspire us and serve as a blueprint for us to realize freedom under law. I think that such a program must begin by appealing to our deeply held intuitions, our pre-theoretical sense of right and wrong.

It is frequently remarked in America today that voters have a deep distrust for politicians and for politics; they are cynical about the whole political system, a fact that is regularly evinced by their exceedingly low interest in finding anything out about the people running for office. One will probably not understand this distrust and cynicism until one sees the constitutional, if perhaps unconscious, libertarianism that runs through many Americans. I suspect they distrust politicians and dislike politics because they are aware on some level that almost everything that goes on in politics is a violation of moral propriety. When the government bestows largess on them, they are by and large happy to receive it; but I suspect that most of them nevertheless harbor the perhaps vague sense that there is something wrong with this state of affairs.

Even if they think that they cannot but take advantage of the government's "free money" before someone else does, they would, if they were candid and forced themselves to reflect on the matter, admit that these are dishonorable actions. This, in part, is what stands behind Americans' general belief that politics is a sordid affair (and that politicians are little better than moral reprobates). What is required, then, is to bring into the open exactly what makes these actions sordid and dishonorable, and to discover explicitly the close connection between people's notions of

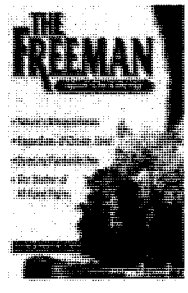
impropriety and the libertarian principles that give rise to them.

One way to begin this process of discovery is to get people who spend their time thinking about moral and political issues on a philosophical level—like philosophy professors—to begin to focus their mental energy on the philosophical underpinnings of the free society. The hope is that more and more of them will come to see the classical liberal conception of society as a compelling manifestation of some of their own fundamental moral beliefs, and, further, that they will then teach it to their students. In this way one might get people who are already prone to intellectual investigations to become intrigued with the strong intellectual appeal of the free society and to replace their perhaps present desire for a socialist utopia with a desire for a classical liberal utopia.

The free society *is* worth fighting for, and even a person in a tiny corner of human life—a person in academic philosophy, for example—can take up the cause of liberty and make a difference. The strategy I have outlined here can be an effective way to make people within academic philosophy open to the power of classical liberalism, but it can also, I believe, bear fruit with people outside philosophy. It can thus be a first step toward answering Hayek's call. I commend it to you. □

The FREEMAN goes to high school!

Thousands of intellectually curious people, young and old, each year awaken to the world of ideas. Those whose "awakening" arrives in high school often participate in speech and debate. These young men and women deserve an opportunity to consider the great heritage of Western civilization and learn the role that private property, freedom of contract, and freedom of association have played in promoting prosperity and protecting Americans from arbitrary authority.



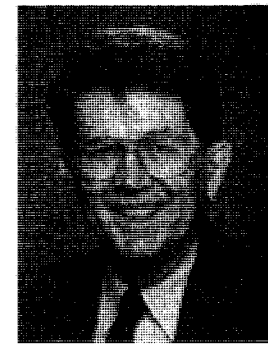
FEE's new Speech and Debate Program will make The Freeman, FEE books, and our redesigned web site valued resources for students. Our new newsletter, Freeman Notes on Speech and Debate, will be sent to over 5,000 high schools. Each monthly newsletter will promote The Freeman, encourage schools to subscribe, and feature excerpts from FEE books. FEE's publications and seminars will teach students how to apply these free-market and classical liberal concepts to speech and debate topics.

The 1999–2000 national high school debate topic will be "Resolved: That the federal government should establish an education policy to significantly increase academic achievement in secondary schools in the United States." FEE's Speech and Debate Program can play a vital role in countering statist notions, and proposing free-market reforms.

Please consider supporting this exciting new program. For further information, contact Gregory F. Rehmke, FEE's Director of Program Development (grehmke@fee.org).



Economics



Opportunities and Costs

My previous columns have been devoted to an overview of how markets work by facilitating social cooperation: providing people with the information and motivation to pursue their own advantages in ways that best create opportunities for others. My emphasis has been on the forest rather than the individual trees of economic understanding. Now I shall begin looking at some of the key concepts essential to applying economic reasoning to all human activity. I begin with opportunity cost.

Limits and Opportunities

Economics has been called the dismal science because it studies the most fundamental of all problems, scarcity. Because of scarcity we all face the dismal reality that there are limits to what we can do. No matter how productive we become, we can never accomplish and enjoy as much as we would like. The only thing we can do without limit is desire more. Because of scarcity, every time we do one thing we necessarily have to forgo doing something else desirable. So there is an opportunity cost to everything we do, and that cost is expressed in terms of the most valuable alternative that is sacrificed.

But the pervasiveness of costs suggests that the dismal reality of limits is only one side of a coin with a brighter side. The limits of scarcity create costs only when there are opportunities. Eliminate the opportunity to choose among alternatives and there are no costs. If, for example, I am forced to live in a particular house, take a particular job, marry a particular woman, and consume a set bundle of goods, I incur no costs when I do those things. So the bright side of costs is the opportunities that create them. Expand our opportunities and the costs of everything we do increase.

Although we commonly see cost as something to avoid, in fact we are better off living in an economy where we are forced to confront the cost of everything we do. I personally might be better off if I could consume products without having to consider their costs because I could shift them to others. But any advantage I could realize would be more than offset if others could ignore the costs of their activities and shift them to me. As a result, we would all lack the information and motivation to choose wisely. Only when the costs of choices are imposed on those who make those choices can we best use the opportunities available.

This is one way of explaining the advantage of market prices. The prices people pay in the marketplace reflect the opportunity costs of their choices. You cannot generally purchase a good or service in a free market for less than others are willing to pay for it, or for less than the amount spent to make it available, which is an important part of the social cooperation that emerges out of market transactions.

Dwight Lee is Ramsey Professor of Economics and Private Enterprise at the University of Georgia.

Special Interests Don't Want Costs Considered

Unfortunately, many economic decisions are made not in a market setting in response to market prices, but by government in response to political considerations. This creates opportunities for the politically influential to acquire benefits paid for by the general public. Invariably, those seeking political benefits downplay the costs in the hope of justifying larger expenditures; they commonly argue that some things are so important that costs shouldn't even be considered.

Educators argue that education is too important to be considered in terms of costs; environmentalists argue that saving the earth is so imperative that environmental programs should be implemented regardless of the costs; recipients of medical research grants argue that human health trumps any crass consideration of costs; and people supported by the National Endowment for the Arts claim that the value of "art goes to the very soul of what it means to be human" and is "contaminated when compared with dollars and cents." (That's a close paraphrase of a statement on arts funding that I heard on National Public Radio.)

All these statements are best understood as attempts by organized groups to capture more public money. To consider costs has nothing to do with exaggerating the importance of money. Money provides a convenient way of expressing costs, but money is not the cost of anything. When I put down a ten-dollar bill to pay for a meal, the money may appear to be the cost, but the real cost is the opportunity cost—the subjective value I forgo by spending the money on the meal rather than spending it on the most valuable alternative.

Silly Claims

To claim that we shouldn't consider the cost of doing some things is equivalent to claiming that we should do those things without considering the alternatives. That such a transparently silly claim continues to be used in special-interest pleading illustrates the power of deception over logic in political debate. Not considering the alternatives to doing something would make sense only if it were always more valuable than anything else. But this means that we should devote all of our resources to this one thing. If it were really true that fine orchestral music, for example, was so valuable that costs shouldn't be considered, then everyone should go homeless and hungry and spend all of their time listening to orchestras in the nude. This is obviously silly, but not one bit sillier than claiming that something is so important that it is inappropriate to consider its cost.

As soon as two or more groups claim that their program should be funded without considering costs, the relevance of costs should be obvious. Educating our youth and curing our sick cannot both be too important to consider cost, not in a world of scarcity. The cost of doing more to educate our youth is doing less to cure our sick, and vice versa. To ignore the cost of one is to treat the other as unworthy in comparison.

Of course, the reality of scarcity, and the opportunity costs that result, intrude into the political process despite the special-interest rhetoric disparaging considerations of cost. Comparisons have to be made among competing alternatives, so opportunity costs are considered in the political process. Unfortunately, imperfections and biases in the political process prevent the opportunity cost of government action from being adequately considered. The result is what one should expect when alternatives are poorly considered. Waste occurs as decisions direct resources out of more valuable and into less valuable activities, and often into activities counterproductive to the stated objectives.

Market prices do not perfectly reflect opportunity costs, but one can appreciate how close they get by considering the perversities that arise because political decisions often ignore most of the costs of a policy. I shall consider this problem next month as a way of further illustrating the importance of opportunity costs in understanding economics. □

CAPITAL LETTERS:



Vive la Différence?

To the Editor:

In her articles on "individualist feminism," Wendy McElroy is offering merely a core-feminist approach in sheep's clothing, much like "equity" feminism and "equal opportunity" feminism, both of which single women out as androgynous integers needing vindication for centuries of "brutalization," "exclusion," "mistreatment," and so forth, none of which jibes with the truth. Our grandmothers were not that helpless! If one has not studied feminism, such nuances get lost in the shuffle.

The problem with all types of feminism is that men *and* women are on this earth together, and the trick is not to focus on one or the other as feminism does (and possibly libertarianism tends to do). It is necessary to seek a *common good* felicitous to the human race, as the Founders had in mind. McElroy's approach is too one-sided and thus inevitably futile. That there were brave and active women in the past should not require our apostheosizing them now when they've already been accorded their due in the melting pot of history (Nightingale, Barton, etc.).

Whether McElroy likes the idea or not, society is not founded on activist, adventurous, manly women but on *loving, nurturing, womanly wives, mothers, housewives, teachers of the young, and so forth.* As Midge Decter has put it, feminists are merely females who balk at adult womanhood, and the idea of "individualist feminism" comes dangerously close to Tocquevillian dysfunction.

In the end, the big problem for feminism is that good women rear strong sons, and a healthy, natural division of labor serves to foster strong male leaders. Thanks to "sex equality" and bans against "sex discrimination," we're not seeing male leadership anymore. Although I am not an Objectivist, I think Ayn Rand would agree with me on this: You can't have strong men and dominant women at the same time. "Strength" for each has a different frame of reference.

—W. EDWARD CHYNOWETH
Sanger, California

Wendy McElroy responds:

It is difficult for me to tell how deeply the two of us may disagree on the issue of feminism, as I simply do not hold the beliefs you ascribe to me. Individualist feminists routinely encounter an understandable problem in today's politically correct environment: namely, the "feminist" label overwhelms the word "individualist," when exactly the opposite is true. For example, as a feminist, I oppose both affirmative action and sexual harassment laws.

Rather than deal with particulars, however, let me clarify what I consider to be the theoretical foundation of individualist feminism. It is natural rights, based upon a Lockean model. Men and women have equal rights, which should be acknowledged in the same manner by law. This means neither oppression nor privilege. It does not mean equity in the sense of redistributing wealth or power; it means equality under a system that fully reflects the natural rights of both sexes. If such a system existed—embodying neither oppression nor privilege—I would cease to actively call myself a feminist. Unfortunately, government currently treats women differently from men. It generally assumes a protective role toward women, which I believe to be as damaging as an outright denial of rights. As long as the law accords different treatment to women and men, there will be a need to oppose that difference.

Whether women should choose to raise strong sons, as you suggest, is a personal choice every woman must make for herself. My personal lifestyle is rather traditional, but my political emphasis is on choice itself in the broad sense.

I, too, look forward to a day when there is no need to discuss men and women as though two legal categories. I hope to play a small part in bringing such a society about. □

THE FREEMAN
Ideas On Liberty
MARCH 1999



Y2K and Entrepreneurial Error

"No businessman in the real world is equipped with perfect foresight; all make errors."

—Murray N. Rothbard[1]

Over the past year, I've been involved in a series of debates over the impact of the Year 2000 Problem, the potential collapse of computers—and perhaps of the economy—owing to the fact that since computer programs use two digits instead of four to indicate years, the year 2000 will be treated as 1900. On the one extreme is Gary North, who claims that the Y2K problem is so serious that it will gravely disrupt society for years. On the other end is Harry Browne, who says that enlightened entrepreneurs will avert a worldwide disaster.

What's interesting about the debate is that free-market advocates are found on both sides. North and other naysayers focus on the propensity of market players to make entrepreneurial errors and engage in shortsightedness. Browne and other optimists stress the entrepreneurs' ability to solve problems, especially when so much is at stake. (Some businesses could go bankrupt if they don't address the Y2K problem.) In short, the market works.

My concern is that the "market always works" camp comprises true believers who blindly think the market can solve all problems almost automatically. They seem to fit into the rational equilibrium-always school of economics where entrepreneurial misjudgment, imperfect knowledge, and uncertainty play little or no role.

Markets Are Not Perfect

The Austrian economists teach otherwise. Israel Kirzner, noted for his studies on entrepreneurship, attacks the model of perfect efficiency as "wholly unsatisfying." He adds that "It is most embarrassing to have to grapple with the grossly inefficient world we know with economic tools that assume away the essence of the problem with which we wish to deal."[2]

The market is characterized by profit and loss, success and failure, certainty and uncertainty. There is always room for improvement, and the entrepreneur's role is to eliminate errors and inefficiencies. Thus, it should come as no surprise that many businesses and financial institutions are making significant headway in fixing their computer programs to avert the Y2K problem.

On the other hand, it would be folly to ignore that many businesses have budgeted insufficient time and money to fix or replace their computers. Evidence is growing that most firms, especially small businesses, are

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not doing enough. Many major corporations and government agencies, both here and abroad, admit that they only have time to fix critical systems. The rest will fail on January 1, 2000.

Free-market advocates sometimes place too much faith in the market's ability to solve problems and ignore ubiquitous error in an entrepreneurial economy. Think about all the ways people make mistakes every day in the marketplace: Investors buy the wrong stock. Businessmen declare bankruptcy. Marriages break up. Consumers over-spend and over-eat, especially during the holidays. Kids fail to do homework. Drivers have accidents. Ships sink. Builders don't meet deadlines. Economists make false predictions. Entrepreneurs cut corners, deceive customers, and embezzle funds. Economic failure, stupidity, and incompetence are common to human nature. As Ludwig von Mises noted, "To make mistakes in pursuing one's ends is a widespread human weakness."[3]

The decision by computer programmers in the early 1950s to use two digits instead of four is a classic example of individual shortsightedness. To save space, they cut corners, and now, a generation later, the whole world is paying a heavy price for their blunder.

Cluster of Errors

In most cases, entrepreneurial error is random, unpredictable, and self-correcting. As Murray Rothbard stated, "As a rule only some businessmen suffer losses at any one time; the bulk either break even or earn profits."[4]

There are, however, cases of widespread error—mistakes that affect virtually every part of an industry or economy. Rothbard, in standard Austrian school fashion, explained depressions in terms of "a sudden general cluster of business errors."[5] Of course, the Austrians attribute those errors and the business cycle in general to monetary inflation by government.

Yet can't error with far-reaching harm occur in the market without government being responsible? Austrian economists don't normally discuss this possibility, but it undoubtedly exists. Market decision-makers have made shortsighted blunders that have had universal consequences. Examples of such error include asbestos in construction, pesticides in agriculture, and air and water pollution in manufacturing. The Y2K computer glitch is a particularly tough challenge because it is universal and time-sensitive. In most cases, the deadline cannot be postponed.

The Market's Self-Correcting Mechanism

Fortunately, the market has a built-in mechanism to minimize mistakes and entrepreneurial error. The market penalizes mistakes and rewards correct behavior. Business leaders know that computer problems can destroy their business; fixing the Y2K bug will avoid losses and may even be profitable. They are willing to pay the price. As Kirzner has said, "Pure profit opportunities exist whenever error occurs."[6] At the same time, the market will severely penalize businesses that have ignored the Y2K problem or have procrastinated.

Followers of free markets should take note: markets may be self-correcting, but they are not all-seeing. □

1. Murray N. Rothbard, *Man, Economy and State* (Los Angeles: Nash Publishing, 1970), p. 746.
2. Israel M. Kirzner, "Economics and Error" in *Perception, Opportunity, and Profit* (Chicago: University of Chicago Press, 1979), p. 135.
3. Ludwig von Mises, *Theory and History* (New Haven: Yale University Press, 1957), p. 268. Mises adds that "Error, inefficiency, and failure must not be confused with irrationality. He who shoots wants, as a rule, to hit the mark. If he misses it, he is not 'irrational'; he is a poor marksman."
4. Murray N. Rothbard, *America's Great Depression*, 4th ed. (New York: Richardson & Snyder, 1983 [1963]), p. 16.
5. Ibid.
6. Kirzner, pp. 132–33.

BOOKS

For Your Own Good: The Anti-Smoking Crusade and the Tyranny of Public Health

by Jacob Sullum

The Free Press • 1998 • 288 pages • $25.00

Reviewed by John Attarian

Hounded by billboards and other "public-service" exhortations, barred from lighting up almost everywhere but in their own cars and homes, and saddled with rising cigarette taxes, smokers are being treated like pariahs—for their own good, of course. The anti-smoking crusade asserts that tobacco companies concealed the dangers and addictive nature of cigarettes, and manipulated their nicotine content to addict smokers; that all tobacco forms are bad; that secondhand smoke greatly endangers others; that people, especially impressionable teenagers, smoke because of insidious advertisements like Joe Camel; and so on.

In this levelheaded and well-informed book, *Reason* magazine senior editor Jacob Sullum convincingly debunks these claims. Smoking's health hazards have been known, and openly discussed, for decades. So has manufacturers' control of cigarettes' nicotine levels. Cigars and smokeless tobacco are far less dangerous than cigarettes. No evidence exists that casual exposure to secondhand smoke is a significant danger. As for supposedly sinister old Joe, the most important factors influencing teenagers' decisions to smoke are their sense of smoking's risks and benefits, the demonstration effect of family members who smoke, and peer behavior.

Opposition to smoking, Sullum points out, is nothing new. King James I, Pope Innocent X, and others denounced tobacco as addictive, unhealthy, inconsiderate of others, and downright wicked. But people kept smoking for the benefits and pleasures they got from it, and brushed off warnings of health hazards.

The 1964 Surgeon General's report stated that smoking, linked to cancer and other ailments, was a health hazard serious enough to warrant "appropriate remedial action." This opened, in Sullum's words, "the most concerted, sustained, and successful effort in history to discourage the use of tobacco." *For Your Own Good* carefully narrates that effort. At first, public health officials realistically recognized that Americans would not abruptly kick the habit, and opted to steer them to safer cigarettes with low tar and nicotine. But gradually the objective changed to eliminating all tobacco use. The anti-smoking movement won several victories. Cigarette advertising on television and radio was banned after 1970. Increasingly blunt warnings were mandated on cigarette packs and cartons.

Feeling the pressure and terrified of lawsuits, the tobacco companies responded by criticizing the evidence of health hazards as inconclusive, sponsoring its own research into the link between tobacco and lung cancer, and introducing filter-tipped and other "safer" cigarettes. Sullum observes that this refusal to acknowledge smoking's well-known dangers "has made the cigarette business the most reviled and distrusted industry in America." The unrelenting threat of lawsuits finally broke the tobacco companies' resistance, and in 1997, to limit their liability, they offered the (in)famous $368.5 billion agreement with the federal government.

Sullum acknowledges the cancer risk and describes nicotine as "the most dangerous recreational drug." He describes the tobacco companies as "cynically dancing around the truth to ward off liability and protect [their] profits," but he adds that they "didn't fool anyone who didn't want to be fooled."

By contrast, one of the anti-smoking movement's worst aspects is its end-justifies-the-means dishonesty, which Sullum abundantly presents: twisting research to fit its agenda, attacking researchers for saying what they in fact did not say (for example, that some cigarettes are safe), and relying on hysterical rhetoric, ad hominem assertions, and outright falsehoods. Sullum himself has been smeared as being "in the pay of the tobacco industry," because R.J. Reynolds used one of his articles

in an ad campaign and a tiny fraction of the Reason Foundation's budget comes from Philip Morris contributions.

A favorite recent recourse of the smoking-bashers is cigarette tax increases. This will reduce smoking marginally, but will also spawn corruption and smuggling. Furthermore, stating that smoking is sensitive to price defeats the argument that cigarettes are irresistibly addictive. As Sullum wryly notes, "giving up cigarettes when the price of a pack goes up twenty-five cents is not the behavior of someone who is powerless over nicotine."

Indeed, addiction receives much attention. Sullum concludes that smoking is a habit difficult to break, but not impossible (America has about as many ex-smokers as smokers). Will power is crucial. Smoking bashers who assert that cigarettes are irresistibly addictive are in effect abolishing man as a moral agent; "they criticize individualism itself, because it implies that people are responsible for their own behavior."

Given the anti-smoking crusade's premises, a cigarette ban is its logical culmination. But Prohibition and the war on drugs, Sullum shows, provide a valuable cautionary tale of crime, corruption, and despotic encroachments on individual liberties.

For Your Own Good is a rare, welcome voice of reason and truth about cigarettes. If you want to make sense of the smoking war, don't miss it. □

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Star-Spangled Men:
America's Ten Worst Presidents
by Nathan Miller
Scribner • 1998 • 272 pages • $23.00

Reviewed by Gene Healy

Historians who evaluate American presidents suffer from a bias against inaction. In the conventional view, great presidents are the nation builders and the war leaders; the failures are the ones who "never did anything."

Nathan Miller, author of *Star-Spangled Men: America's Ten Worst Presidents*, shares the conventional bias. For example, he indicts Silent Cal Coolidge with Mencken's faint praise: "He had no ideas, and was not a nuisance."

Those of us who favor limited government see it differently. This would have been a happier century by far if the worst that could be said of any president was, "He had no ideas, and was not a nuisance." One (unintended) virtue of Miller's book, then, is that it reminds us of some of the forgotten men who have held America's most powerful office, yet somehow managed to leave well enough alone.

Miller picks his losers by asking, "How badly did they damage the nation they were supposed to serve?" What's strange, then, is that the presidents he selects were mostly peacetime leaders who did little perceptible damage to the Republic and its institutions.

Take Coolidge, whom Miller writes off as "a reluctant refugee from the nineteenth century." Miller fairly sneers at Coolidge's emphasis on fiscal probity and laissez faire. Unable to find much to criticize in the uninterrupted prosperity of Coolidge's tenure, Miller tries a cheap shot: Coolidge's "penny-pinching refusal to cancel [the war] debts contributed to the rise of Adolf Hitler." Well, maybe. But as long as we're doling out responsibility for Nazi atrocities, why don't we give some to Woodrow Wilson? Wilson's dragging the United States into World War I allowed the Allies to impose a punitive peace on Germany in the first place. Why, then, does Miller consider Wilson a "near great" president?

Unlike Wilson, Coolidge was never awake for long enough to do much damage; as Miller recounts, he slept 11 hours a day. During his waking hours, Silent Cal's sound instincts allowed him to hew to the presidential equivalent of the Hippocratic Oath. As Coolidge put it, "Nine-tenths of a president's callers at the White House want something they ought not to have. If you keep dead still they will run out in three or four minutes."

Miller's chapter on William Howard Taft inspires reflection on the varieties of presi-

dential obesity. Mencken saw Grover Cleveland's great bulk as indicating a kind of implacable strength. But Taft's girth reflected placidity and inaction, complementing his sedate view of the presidency: "the president cannot make clouds to rain, he cannot make the corn to grow, he cannot make business to be good." Miller rates Taft as the ninth worst, but his tenure in the White House was marked by peace and prosperity.

Warren G. Harding receives the most undeservedly rough treatment of any president examined. From a classical liberal perspective, Harding was arguably the greatest president of the twentieth century. He initiated the largest spending cut in history—a 40 percent reduction from Wilson's last peacetime budget. And Harding's good nature and liberal instincts led him to overrule his political advisers and pardon Socialist presidential candidate Eugene Debs. Debs had been jailed during Wilson's jihad against opponents of World War I, but Harding turned him and other dissenters loose; "I want [Debs] to eat his Christmas dinner with his wife," he said. The scandals surrounding Harding's administration push him near the top of Miller's hit list. But, as Miller notes, he never took "so much as a nickel" from any of his corrupt cronies.

Despite the author's depressingly conventional perspective on presidential greatness, *Star-Spangled Men* is tremendously enjoyable. Miller can turn a memorable phrase: (for example, he writes that Kissinger "looked like a Bronx Butcher and operated with the cynicism of a Renaissance Cardinal") and has an eye for the kind of detail that makes reading history fun.

Read with the proper attitude, *Star-Spangled Men* inspires reflection on what we should value in a president. □

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Fantasies of Salvation: Democracy, Nationalism, and Myth in Post-Communist Europe

by Vladimir Tismaneanu

Princeton University Press • 1998 • 216 pages • $29.95

Reviewed by David L. Prychitko

Communism is dead, but collectivism is quite alive. Vladimir Tismaneanu's book *Fantasies of Salvation* explains why. Tismaneanu, once a Romanian dissident and now professor of government and politics at the University of Maryland, argues that while the centrally planned, socially engineered visions of Marxism-Leninism are dead, the false, utopian hope of emancipation through the state lives on. The myth of socialist internationalism has now been replaced by a new myth, populist nationalism.

Communism declared that its aim was the unification and collective freedom of workers around the world, but the new post-communist vision abandons that myth for a much narrower but equally deadly one. The new political vision in many former socialist regimes is not the Western ideal of individual freedom and civil society. Instead, "the nation" is the focus of attention.

The 1990s are a stubborn and sobering reminder that classical liberalism does not necessarily replace socialism by default. Although there have been success stories—countries like the Czech Republic, Poland, and Slovenia, for example—the 1990s might be better remembered for the Bosnian war, the growing Kosovo crisis, and the return of refugee camps. Who would have thought that the collapse of the Berlin Wall would be followed by the return of ethnic cleansing?

Tismaneanu shows that the problems of post-communism remain because the fight is less about the freedom of individuals and more about the emancipation of the ethnic enclave. Throughout eastern and central Europe "the nation" is paraded as the true center of history, the source of dignity, the subject of sorrow and oppression. The author

demonstrates how this emergent populist-nationalism seeks to destroy individuality, pluralism, and democracy and instead champions unity, stability, and authoritarianism.

Tismaneanu's explanation of why collectivism has re-emerged in many post-communist states is worth quoting at length:

> The end of communism has left individuals with a sense of loss: even if they hated their cage, it offered at least the advantage of stability and predictability. Like former prisoners, they now have freedoms but do not know exactly what to do with them. Under these circumstances, they are ready to espouse the rhetoric of the tribe with its emphasis on group identity and community values. The neurosis of the transition period, the collective fear of a general collapse, the closing of the historical horizon and the anger at the new economic barons nourish sentiments of revolt, distress, and intolerance. There is need to find scapegoats, to identify those culpable for the ongoing sorrows. The political myth of lost and reconquered ethnic unity serves precisely this purpose: to explain defeats and alienation and reassure the individual that he or she has a place within the *volkisch* community.

In the face of all this, Tismaneanu remains optimistic over the prospects of the liberal intellectual dissidents in the post-communist countries and their continued resistance against collectivist nationalism. The emergence of classical liberal institutions—a market economy, a fully flourishing civil society, and constitutional democracy—remains critically dependent on them.

I highly recommend this book. Those familiar with Ludwig von Mises's *Nation, State, and Economy: Contributions to the Politics and History of Our Time* will find in Tismaneanu's book a fascinating and probing updating to *our* time. □

David Prychitko studied the former Yugoslav system on a Fulbright grant in 1989, and currently heads the department of economics at Northern Michigan University in Marquette. He is co-editor, with Nevenka Čučković, of a collection of classic articles by Mises and Hayek, translated into Croatian.

Out of Order

by Max Boot

Basic Books • 1998 • 252 pages • $25.00

Reviewed by George C. Leef

Max Boot is a journalist and editor at the *Wall Street Journal* who has made a name for himself (and a lot of enemies) with his articles exposing the despicable practices of plaintiffs' lawyers who will do almost anything to squeeze money out of "deep pocket" defendants. With *Out of Order*, he turns his considerable writing and reportorial skills toward another facet of our legal system—judges. Once highly respected pillars of the community, the ranks of the black-robed contain, Boot argues, many who have little or no regard for justice. This is a serious problem that has received too little attention. Thus this is a welcome book.

The bad-judge problem has several facets. One that Boot addresses is partisan judges, ones who have an ingrained preference for certain litigants, lawyers, or causes, so that their courtrooms are about as fair as the Stalinist show trials of the 1930s. Plaintiffs' lawyers know who they are and naturally contrive to file suits in their courts. You have probably heard of the multimillion-dollar punitive damage awards in cases where there was truly no harm at all, such as the infamous repainted BMW case in Alabama. But how do these absurd instances of legal plunder ever get to trial at all?

The answer is that some judges—elected with copious amounts of money contributed by lawyers who will have cases before them—are unwilling to serve the interests of justice by dismissing suits that are transparently nothing more than legal extortion. Boot names names and gives the nasty details.

But the harm done by rogues who play favorites is minimal when compared to the harm done by another class of bad judges—those who have aided and abetted in the unconstitutional expansion of power of government. This has mainly been the work of the Supreme Court and the lower federal courts, many of whose members have been chosen

for their philosophy that the Constitution's restraints on governmental power should be "interpreted" in such a way as to give the Congress and President virtual carte blanche. This category includes judges who insist on amending the Constitution through creative interpretations. As an example, Boot cites Justice Ruth Bader Ginsburg—long an advocate of the vague, never ratified "Equal Rights Amendment"—who managed to smuggle it into the Constitution with her opinion in the Virginia Military Institute case.

Yet another facet of the bad-judge problem is the phenomenon of judges who regard themselves as potentates, taking over prison systems, ordering busing schemes, and even decreeing that taxes be raised for their utopian visions. Consider, for example, the Kansas City judge who decided that he was going to "equalize" educational opportunity by ordering an incredibly costly program of inner-city school construction, or the New York judge who ordered the City of Yonkers to build hundreds of units of low-income housing in middle-class neighborhoods. Power always attracts authoritarians. That judges can get away with a lot of tyranny bodes ill for the future.

Given that we have a judicial system infested with judges who are partisan and judges who use their positions to coercively reshape society, what are we to do? Boot discusses several ideas for ameliorating the problem. He suggests, for example, ending the practice of popular election of judges, which has had the unfortunate effect of putting justice up for sale—read his account of a race for the West Virginia Supreme Court. That might help, but it might just as well turn out like so many other attempts to clean up the political system and merely hide the problem.

Assume that judges were chosen through some other political mechanism. The special interest groups that have been getting the judges they want through elections will not give up their quest merely because we enact some reform statute. They will simply concentrate their efforts on influencing the new judicial selection method, perhaps by getting friendly faces appointed to the judicial selection board. Under a "reformed" system, it may be even harder to identify judges who are puppets of organized labor or the plaintiffs' bar.

The bad-judge problem has the same roots as most of our other problems, which is to say, our over-politicized society. Trying to rein in partisan and Constitution-wrecking judges is, I fear, an exercise in futility as long as so many people see politics as a legitimate way of getting what they want.

But even if there is no easy remedy for the bad-judge problem, we still ought to be cognizant of it. *Out of Order* skillfully assists us. □

George Leef is book review editor of The Freeman.

A History of the American People

by Paul Johnson

HarperCollins Publishers • 1998 • xv + 1,088 pages • $35.00

Reviewed by Burton Folsom

"The creation of the United States of America is the greatest of all human adventures. No other national story has such tremendous lessons, for the American people and for the rest of mankind." So begins Paul Johnson in his upbeat and first-rate *A History of the American People.*

As a British historian and non-academic, Johnson avoids the pitfalls of so many American historians. Academic historians in particular often impose a double straitjacket on U.S. history: first, that economic issues have been paramount in shaping American politics; and second, that government intervention in the American economy has been necessary and benign. Johnson disputes both of these points.

Johnson gives due attention to economic issues, but he also highlights the crucial role of religion in shaping American history. For example, he takes the Puritans seriously as men of ideas. Later, he analyzes the Great Awakening, the religious fervor of the 1740s. "The Great Awakening," Johnson argues, "was thus the proto-revolutionary event, the formative moment in American history, preceding the political drive for independence

and making it possible." George Whitefield, its leader, "was the first 'American' public figure, equally well known from Georgia to New Hampshire."

In Johnson's history, the rise of America to world prominence is a fascinating story, full of key inventions and daring entrepreneurs. Liberty, not government, is what extended the American dream to millions of Americans, immigrants and natives alike, during the 1800s.

The 1900s might well be called the century of big government in U.S. history. "It was [President Woodrow] Wilson who first introduced America to big, benevolent government," Johnson asserts. But Wilson "was corrupted by power, and the more he had of it the deeper the corruption bit, like acid in his soul."

Johnson prefers Calvin Coolidge: "No one in the 20th century defined more elegantly the limitations of government and the need for individual endeavor, which necessarily involves inequalities, to advance human happiness." Coolidge cut taxes, promoted free enterprise, and had the lowest misery index (inflation plus unemployment) of any president in this century. "Of those who came to power at the same time as Coolidge, all the most notable were dedicated to expanding the role of the state."

When the Great Depression hit, both Hoover and Roosevelt brought bigger government to America—and much of it had negative consequences, according to Johnson. "No series of events in modern history is surrounded by more mythology than the New Deal," Johnson writes. "There was no actual economic policy behind the program." Democratic Presidents Kennedy and Johnson and Republican Nixon expanded government further. But, Johnson says, Ronald Reagan, a "conservative revolutionary," challenged the Democratic hegemony. Johnson curiously ignores Nixon's failed economic intervention, but praises him for challenging the Kennedy money and the "liberal" media.

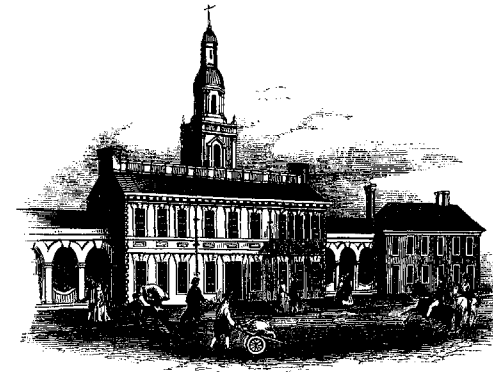
Johnson's history is a superlative achievement, not only for his knowledge and insights but also because he is an able writer and captivating storyteller. In a recent interview, Johnson showed impatience with historians who "niggle" at his work, but more niggling by his editors would have cleared up a variety of misspellings and minor errors. Zachary Taylor was a Whig, not a Democrat; it's Alfred Sloan, not "Sloane," and John W. Davis, not "Davies." But let me niggle no more.

Critics accuse Johnson of being biased, but he is in fact balanced and nuanced in his treatment of historical events and personalities. Johnson *appears* biased to other historians because so many of them are accustomed to teaching from the standard "liberal" texts that dominate the market—for example, Samuel Eliot Morison's *Oxford History of the American People.*

Where Johnson treats Coolidge with respect, Morison lashes out, calling him "a mean, thin-lipped little man, a respectable mediocrity . . . dour, abstemious, and unimaginative." Where Johnson dissects the New Deal, Morison is filled with gushing praise, saying that it was "just what the term implied—a new deal of old cards, no longer stacked against the common man. . . . Probably it saved the capitalist system in the United States."

These snippets are typical of the "history" most Americans have learned. Johnson's excellent work often stands in opposition to the conventional wisdom. It deserves a wide readership among students as well as adults, and if so, we may yet train our next generation to appreciate American history. □

Burton Folsom is senior fellow at the Mackinac Center for Public Policy. He is author of The Myth of the Robber Barons *and* Empire Builders.



Independence Hall

Economics



Illuminating the Unseen

The good effects of laws are often easily seen. The bad effects, unseen. So observed Frederic Bastiat 150 years ago. His basic insight remains true today. We live in busy times. Information bombards us. In such a world, even that which is seen is often overlooked. The unseen is that much more elusive.

If we are to make the case for economic freedom, we have to bring these unseen costs to light. Consider an increase in the minimum wage. What is seen: businesses give some of their low-wage workers a raise. The direct effects of the minimum wage—more money for low-wage workers, less money for businesses that pay them—frame the entire debate. Senator Christopher Bond of Missouri says the minimum wage is bad because it hurts small business—as he argued in his recent re-election campaign. So most people see the minimum wage as a tax on small business that helps the poor. No wonder many people think it's a good idea.

If we want to dent the consciousness of the average American, we have to talk about how the minimum wage doesn't just tax small business. We have to show how it bankrupts some firms that hire low-skill workers. That means fewer opportunities for low-skill workers. But even the firms that survive will try to reduce the hours of low-skill workers and their numbers. In short, while the minimum wage helps some low-skill workers by giving them a modest pay increase, it has a devastating effect on others, pushing them out of the work force and into the street. The minimum wage thwarts human possibility among those it tries to help. And as Bastiat understood, it is easy to see those who are helped by the minimum wage. Those who are harmed are much harder to identify.

We've done a decent job explaining the hidden costs of the minimum wage. We've done such a good job, in fact, that proponents of the minimum wage have actually tried to argue that increases in the minimum wage have *no effect* on low-skill employment. To paraphrase Orwell, you'd have to be an academic economist to find that argument compelling. But in other areas, we have a long way to go if we wish to cast light on the unseen costs of government intervention.

Free Trade and Protectionism

Here's how trade often gets discussed in the media: should we destroy jobs in America in order to have cheap imports? That's like being asked how long you've been beating your wife. Why does it get discussed this way?

Opponents of free trade want the American people to think that trade is about destroying jobs in order to get cheap foreign goods. It makes free trade look mean-spirited and mercenary. But another reason is that these are the most obvious effects of free trade. If Americans buy from foreign suppliers, people

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understand that fewer Americans will be hired in the competing domestic companies. Unseen are the jobs created to make the products we exchange with foreigners. Unseen is the impact of specialization and comparative advantage. Unseen is the power of foreign competition to induce our domestic industries to innovate.

Unless we can illuminate the unseen, making the case for free trade will be an uphill battle. Unfortunately, one of the best things about free trade is extremely difficult to see: free trade allows resources to flow to their highest use. But to make the argument compelling, we have to describe it in a way that allows it to be seen without a semester's worth of economics.

Freeing Up Opportunity

Somewhere in South Carolina, there's a high school girl whose mom works in a textile factory. This girl doesn't know what she wants to do with her life, but like most high school kids in America, she probably doesn't want to work in the same job or career as her parents. The security of the textile factory is appealing, but she might want to go to college and try something different. It all depends on her options.

That factory is threatened by Chinese competition. Should we let the factory go under or should we protect it from the cheaper Chinese imports? We could spend hours on the pros and cons and the economic impact of that decision. But let's look at the impact on that girl in high school. If we keep the factory around, we make the choice of working in the factory more appealing. If we let the factory die, we change the available options. We push her out into the world.

Exploring the world is a good thing, but that's not reason enough for letting the factory go under. What is harder to see is that the world to be explored is a more vibrant and alive place when the factory goes under. Allowing the factory to die frees up capital and management skill that can be used elsewhere. If we maintain all of the factories and all of the companies that cannot survive competition, then the American economy is a much more static place.

If we try to make everything for ourselves and be self-sufficient, we lose the opportunity to specialize in doing what we do best. Our capital gets tied up in industries that do not take the greatest advantage of our unique skills. Free trade allows a high school kid in South Carolina to inherit a world of maximum human potential, with the maximum chance for her to use her gifts, whatever they may be.

A skeptic would ask how the girl in South Carolina is going to achieve her potential if her mom is out of work. And that in turn might lead to a discussion of how past generations have managed to survive and thrive in a dynamic economy. In 1900, one-third of the American work force was in agriculture. Today the number is around 3 percent. Do you think the kids on the farms of 1900 are glad that we let agriculture become more capital intensive with fewer jobs? It wasn't a trivial transition, but in 1900, we couldn't see the industries that would arise to use the skills of the next generation. And we can't know the opportunities that will arise to help that girl in South Carolina if we let the textile factory fail. But they will arise. What they will be depends on the gifts and aspirations of the next generation.

If we want to inspire people to support free trade, we must touch their imagination. Bastiat understood that 150 years ago. Our best chance is to make the unseen, seen. Economics can bring the unseen to light, but only if we leave the jargon behind and show how free trade and other economic freedoms help transform our lives. □

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PERSPECTIVE

"Security" or Friedman

True joy is waking up to a Milton Friedman op-ed. He never quits. In January the *New York Times* published his article "Social Security Chimeras." What a breath of fresh air!

Milton Friedman begins by criticizing the increasingly common suggestion that individual accounts replace *part* of each person's Social Security benefits. "Why replace only *part* and not *all* of Government benefits?" he asks. He goes on to refute the response that the government needs the money to pay current retirees.

Friedman's op-ed really shines when he demolishes the case for a *mandatory* privatized system. As advocated by economist Martin Feldstein and others, everyone would be forced to save a minimum amount specified by the government. Feldstein says that's necessary because, "First, some individuals are too shortsighted to provide for their own retirement [and] second, the alternative of a means-tested program for the aged might encourage some lower-income individuals to make no provision for their old age deliberately, knowing that they would receive the means-tested amount."

Friedman's response:

> [T]he fraction of a person's income that it is reasonable for him or her to set aside for retirement depends on that person's circumstances and values. It makes no more sense to specify a minimum fraction for all people than to mandate a minimum fraction of income that must be spent on housing or transportation. Our general presumption is that individuals can best judge for themselves how to use their resources. Mr. Feldstein simply asserts that in this particular case the Government knows better. . . . I find it hard to justify requiring 100 percent of the people to adopt a Government-prescribed straitjacket.

Friedman ends by calling for a voluntary pension system. (In one sense, it would still be compulsory; we'd be taxed to support people

now on Social Security.) "I believe that the ongoing discussion about privatizing Social Security would benefit from paying more attention to fundamentals," Friedman said, "rather than dwelling simply on nuts and bolts of privatization." Hear, hear!

* * *

Corporate layoffs make for good, glitzy television-news reporting. The addition of jobs is dry and statistical. No wonder people have a sense that layoffs outnumber new jobs. Charles Baird looks at the facts and finds a whole different picture.

Richard Cobden once pointed out that when government touches something—he had trade and religion in mind—it's twisted into something else entirely, and not for the better. Bruce Benson demonstrates that science can be added to Cobden's list.

The energy crisis, a production of your government, is long gone, but the regulations designed to whip us into efficient energy users live on. Worse, we get new ones all the time. Ben Lieberman shows the lengths to which such inanity can go.

If you lived through that crisis, you might have thought the future would be an eternal nightmare compliments of oil sheiks and—these letters were scarier than "IRS"—OPEC. Since then the price of a gallon of gas has fallen below the price of a gallon of milk. What happened to the big bad cartel? Christopher Mayer will fill you in.

What is really happening in China? Is it going capitalist even as it defends the socialist revolution? Why is it jailing dissidents? James Dorn brings lucidity to the enigma.

The term "the tragedy of the commons" has become a cliché, useful to free-market advocates as well as statist environmentalists in promulgating their policy views on property and ecology. Bruce Yandle explores how tragedies can become triumphs.

The welfare state doesn't miss a trick. Under President Bush, the Commerce Department started a program to subsidize private companies in the development of new technology. You see, markets aren't good at that and—well, John Sparks will give you the scoop on this creative piece of governance.

During the 1920s, the monetary authority did *something* to set the stage for the economic debacle of the 1930s. But *what*? The literature is full of conflicting answers. Richard Timberlake sorts it all out in the first of a series of articles.

Labor-relations law is premised on the Marxist notion of an irreconcilable conflict between workers and employers. Economists have debunked the notion, and so have some businessmen. Daniel Hager tell us about one: James F. Lincoln.

The withholding tax is a classic case of adding insult to injury. It's bad enough the government appropriates a chunk of our income; but it does so before we even see it. Donald Boudreaux and Andrew Morriss point out that withholding is more than just an insult.

If you tell people you don't *want* government benefits you are "entitled" to, people sure look at you funny. That's what Mark Reboul found out when he was laid off.

FEE president Don Boudreaux's monthly *Notes from FEE* column moves to the front of the magazine beginning this month. In other columns, Lawrence Reed reports on a new study about high-school economics texts, Doug Bandow dissects the minimum wage, Dwight Lee exposes the "hidden technology" myth, Mark Skousen wonders about Diamond Head and property rights, and Walter Williams takes on the government schools. Roger Meiners looks at what William Weld has to say about property rights and the environment and implores, "It Just Ain't So!"

Our book reviewers examine tomes on conflicting outlooks about the future, the wealth and poverty of nations, America's role in the world, the economy ahead, misery in Africa, and the memoirs of Clarence Carson.

—SHELDON RICHMAN

Thoughts on Freedom

by Donald J. Boudreaux



Who's Progressive?

Our world is full of grotesque mislabeling—for example, politicians are called "Honorable." Few labels, though, are as inappropriate as is the term "progressive" when it is used, as it frequently is, to describe people who endorse widespread government regulation. "Progressivism" came into use in late nineteenth-century America as the label for a naïve yet ambitious program for giving the government carte blanche control over the economy. To this day, American leftists (mostly of an academic bent) snootily declare themselves and their policies to be "progressive."

But you don't turn junk into jewels by calling it pearls. No matter what they *call* themselves, statists emphatically are not progressive. The root word of "progressive" is "progress," which my Merriam-Webster defines as "to move forward" and "to develop to a more advanced stage." Under this definition, statists are *anti*-progressive; they're *re*gressive; they possess less ethical sophistication than Cro-Magnon man.

Think about it. The statists' policy prescriptions are nothing but directions for the use of force. From dealing with the poor ("force the haves to surrender some of their money to the have-nots") to the regulation of industry ("force every firm to abide by bureaucratic rules") to cultural matters ("force people to support art that they will not buy voluntarily"), the common element in all statist proposals is force—coercion, or its threat, initiated against peaceful people.

What, though, is more primitive, more backward, more *re*gressive, than relying on force as a means of organizing society? Relying on force requires no intelligence, ingenuity, insight, or wisdom. If you have more brains than a tree stump, you can visualize how to satisfy your immediate desires through force—simply grab whatever you want, standing ready to bludgeon or blast away anyone who interferes with you. And if what you want is someone else's services, simply threaten to do him physical harm unless he does your bidding.

Coercion and theft are primal impulses, and primal impulses become no more meritorious when carried out by government officials than when carried out by lone bandits.

Consent and Empathy

Compare reliance on force with reliance on voluntary, peaceful actions. A bandit—be he an independent operator or an agent of government—is interested in his victim's thoughts and desires only insofar as these determine if and how the victim will defend himself.

In contrast, peaceful people identify with—empathize with—one another. They must figure out other people's likes and dislikes, needs and turn-offs—for only by empathizing with others can they prosper in the market. They must learn what to offer in order to prompt others to exchange goods and services with

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them. The entrepreneur who stubbornly ignores the desires of consumers and insists on producing only what he, personally, likes will not long remain an entrepreneur.

This reciprocal learning in the market is continual. Far more than anything that government does, this process of being attentive to the needs of one another is what links us together into a peaceful and prosperous society.

Moreover, while force destroys, market relations create. The brute who steals my supper gives me nothing in return; his gain is my loss. And because I will not long keep producing if others keep stealing from me, coercion literally destroys wealth. But as I said, in the market people gain only by offering things of value. Human beings—brimming as we are with creativity—produce value by devising new products, new services, and new ways of doing worthwhile tasks. The more we create for exchange, the better off we all are.

Creativity, by its nature, is truly progressive. So, too, are the social conditions that promote creativity: private property rights, the division of labor governed by market prices and voluntary choice, and the rule of law under which no one is accorded special privileges or duties. While some semblance of private property rights and the division of labor has always been part of human societies, these institutions remain stunted and distorted without the rule of law. Regrettably, the rule of law has been largely absent from human history. It flowered during the Roman republic and again in western Europe during the past few centuries, reaching its historical zenith in nineteenth-century England and America.

Tragic Retreat

But we've drawn back from the rule of law during this century. Government increasingly treats us according to which groups we belong to rather than according to our individual actions. A new caste system is in the works. But pigeonholing people into various groups, and distributing legal privileges and duties accordingly, is primitive. Such obsession with status is a hallmark of the most repressive and backward of societies. The gall of the proponents of this new caste system to call themselves "progressive"!

The countless generations of human beings who lived before the industrial revolution knew very little prosperity and progress. With the exception of the nobility and a select few other fortunate dandies, people lived in uniform poverty and misery. (Indeed, even the nobility and the few fortunate dandies lived in what by our standards is deep poverty.) Hunger, disease, filth, and boredom—not to mention the deaths of spouses, siblings, and children—were routine and inescapable features of life.

Only since the protection of property rights and freedom of contract became widespread and available to the humblest person did the human race yank itself from the muck. Only then did we prosper and flourish. We did so because these institutions dramatically reduced the scope for "legitimate" force and therefore inspired us instead to create and to deal with one another peacefully and as equals, rather than as masters and slaves.

As Tom Bethell shows in his wonderful new book, *The Noblest Triumph*:

> When property is privatized, and the rule of law is established, in such a way that all including the rulers themselves are subject to the same law, economies will prosper and civilization will blossom. Of the different possible configurations of property, only private property can have this desirable effect.

Some proponents of government intervention in economic affairs fail to see that force only destroys and never creates, while others are power-hungry hooligans. None of them, however, are progressive. True progressives embrace private property rights, the free market, and the creativity and advancement that these institutions let loose. □

THE FREEMAN
Ideas On Liberty

"So-Called Property Rights"?

It Just Ain't So!

Remember William Weld? He was the Massachusetts governor (and presumed presidential wannabe), who resigned so President Clinton could appoint him to dispense advice as ambassador to Mexico. Those plans were derailed by Senator Jesse Helms, so now he makes money in Boston perhaps while planning his political future. Weld wrote an op-ed in the *New York Times* late last year that indicates why the media like this "maverick" Republican. In "Government Made Easy," Weld skewers the leading Republican and Democratic presidential aspirants because, unlike the with-it Weld, they "really don't get it."

In a couple of paragraphs, Weld tries to position himself as a thoughtful guy who understands the virtues of markets by attacking nationalized health care, wage and price controls, and collective bargaining by public school employees. He is also foursquare against slavery—really. Tough stuff in Massachusetts.

What role does he see for government? It is to appeal "to the better angels of our nature, when it contributes to a sense of community, both at home and abroad." How does it do this? By, among other things, strong environmental controls. Let's focus on only a few of his pronouncements to see the depth of his lack of knowledge of markets and law.

Weld asserts that "Individuals and businesses simply will not protect the environment for our descendants; we need vigorous government enforcement and conservation measures." He scorns "backers of so-called property rights."

He does not understand that property rights are the key to environmental protection. People, not government leaders, protect resources, environmental or otherwise. The worst abuses of the environment in the United States have come on government-controlled lands. The communists left an environmental nightmare behind in Russia and other eastern European countries.

The Virtue of Property

Weld's mistake is common. It is one that Tom Bethell discusses brilliantly in his new book, *The Noblest Triumph: Property and Prosperity Through the Ages.* Those who do not understand the virtues of liberty and markets, as exemplified by private property, believe that problems can best be overcome by having the right person in charge. Sure, dolts like Stalin and Brezhnev got it wrong and ruined the environment (and everything else); if only there had been a *good* person in charge. . . . The Russians needed someone who knew how to exploit "the better angels of our nature," as Weld says. Unfortunately, heaven on earth is not possible; Weld could not produce it in Massachusetts—good luck on a larger scale.

In any event, Weld need not worry about individuals and businesses destroying the environment—it was nationalized in the early 1970s when the EPA was created and given near total control over environmental matters. But in recent decades politicians have fared well by perpetuating the myth that centralized control of the environment is needed to save it. The Al Gores and William Welds of the world will save us from our ecologically destructive selves!

Weld thinks people can "pursue happiness" when the government is there to help them do so. Of course, it is the other way around. People naturally pursue happiness. Government "helps" that to happen not by centralized control of the use of property but by helping to protect and enforce private property rights.

Weld's lack of respect for the fundamental legal regime that allowed this nation to be so successful is astonishing. Besides deriding the fundamental liberty of property rights, he also says we should "not give ourselves over to generalized weeping about due process." Toss out the Constitution.

Weld also focuses on the need for strong antitrust laws. After all, he notes, "government is good when it safeguards our livelihoods from predatory business practices." As a former Federal Trade Commission bureaucrat, I can report that businesses often engage in "predatory business practices." Over and over, we see businesses attempting to gain market share at the expense of their competitors!

Many practices are used in an effort to lure customers from one seller to another: new product innovations, quality improvements, price reductions, and advertising. What is predation to a losing firm is usually another firm's superior service to the public. Don't like UPS? Switch to Fed Ex or DHL. Don't like the Department of Justice? Switch to, uh, well, just trust Weld to put the right person there to produce good government.

Weld's concern about "predation," which most people presume to mean really nasty business tactics—the evil stuff shown in so many television shows and movies—is belied by the dearth of cases. Even the Clinton regulators find so little to pick on that they are reduced to the foolishness of devoting public resources to beating up on Microsoft: one multibillion dollar company giving away its Web browser to lure customers from the market-dominant browser of another multibillion dollar company. They even have tape recordings of Bill Gates saying that he wants to beat the competition!

Weld hits the nail on the head when he notes that "Economic Man will take the whole pie for himself every time, if you let him." That, in straightforward language, is in fact an essential assumption in economic theory. Theory assumes that people are interested in maximizing their own well-being. Much of this has to do with obtaining wealth for personal and family comfort, but it goes far beyond that. Well-known people often derided as Robber Barons—Carnegie, Ford, and Rockefeller—earned billions! And what became of their wealth? It was mostly given to charity.

Humans are inherently competitive. That drive can be exploited largely for good and productive purposes, such as devising better products that help people, or it can be devoted to wheedling resources out of the pockets of those who worked to earn them. One can be a thief, which is clearly unproductive to society. One can also be a politician who exploits the power of government to force people to give up earned resources to those who are wise enough to support the politician.

Perhaps I have been overly harsh. Weld is not a deep thinker. Like many politicians he probably sincerely believes he can tell us what to do to live a better life. He has the same instincts as George Bernard Shaw, who believed that the Soviets were doing a great job of crafting a "new man" devoid of self-interest.

When the Berlin wall fell, the crust finally fell from most people's eyes about the real nature of central control. Not William Weld's. He still does not get it. The Mexican people can count their lucky stars.

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THE FREEMAN
Ideas On Liberty

Recycling Labor

by Charles W. Baird

In 1998 Boeing and MCI WorldCom, to mention only two, announced plans for massive layoffs. Boeing actually cut 48,000 jobs. Throughout 1998 there were many announcements of intended mergers—for example, Exxon with Mobil and Chevron with Shell—most of which included plans for substantial job cuts. Total layoff announcements in the United States in 1998 exceeded 600,000.

To those who received such announcements it must have seemed that their personal fortunes were ruined and the economy was falling apart. No one wants to leave a job involuntarily, and when one hears of it happening, one is naturally sympathetic. The perceived instability of employment in free-market economies is a major reason why many Americans support government intervention in the labor market.

Yet in any market-based economy there will always be layoffs and there will always be hires. Moreover, this is to be celebrated. It is a sign of economic health. Given the pace of change in what we know, in what is discovered to be possible, in consumer tastes and preferences, and in the extent of competition, labor, like all productive resources, must constantly be recycled.

The popular press always stresses the downside of the recycling of labor. Bad news sells better than good news and each plant closure or massive layoff is easy to capture on videotape. The upside of recycling—the hiring—is more diffuse and less visible. Nevertheless, most of the time the upside outweighs the downside.

From December 1997 to November 1998, in spite of all the layoffs and downsizing that occurred, entrepreneurs in the American economy created over a million and a half *net* new jobs. That's an average of 131,916 more jobs created than lost each month. And 1998 was not unusual. Table 1, column 2, shows this net job creation (December to November, seasonally adjusted) in each year starting in December 1992. Column 3 shows the 12-month diffusion index of employment change for the same periods. A diffusion index of 50 percent indicates an equal number of American industries adding and decreasing jobs.

TABLE 1

Year	Net New Jobs	Diffusion Index
1992	1,106,000	62.9
1993	2,293,000	69.2
1994	3,362,000	66.6
1995	672,000	63.5
1996	2,543,000	69.1
1997	2,825,000	72.9
1998	1,583,000	n.a.

Source: http://www.bls.gov/news.release/empsit.toc.htm (Bureau of Labor Statistics Employment Situation Report)

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In every year net new jobs were created, and more industries added than eliminated jobs. Clearly, layoffs and downsizing do not mean the American economy is falling apart.

Moreover, the personal fortunes of most people who receive layoff notices are not ruined. Most find new jobs at better pay after a job search and relocation. Table 2, column 2, shows the American unemployment rate, and column 3 shows the median duration of unemployment in November for each year from 1992 to 1998. Column 4 shows the private-sector employee total compensation index for the third quarter of each year. For example, in the third quarter of 1998 total compensation paid to private-sector employees was 38.7 percent higher than in the second quarter of 1989. Total compensation includes wages and salaries plus all benefits such as health insurance and paid vacations.

TABLE 2

Year	Unemployment Rate (percent)	Median Duration (in weeks)	Compensation Index (1989/2=100)
1992	7.4	9.0	114.7
1993	6.6	8.3	118.9
1994	5.6	9.1	122.8
1995	5.6	8.1	126.1
1996	5.4	7.8	129.7
1997	4.6	7.8	133.7
1998	4.4	6.7	138.7

Source: http://www.bls.gov/news.release/empsit.toc.htm

Using Bureau of Labor Statistics (BLS) data, the Employment Policy Foundation concluded that in the last five years, average annual employment growth in the highest paid one-third of new jobs was 3.2 percent. In the same period, employment growth averaged just over 1 percent in the lowest- and middle-paying thirds. This means that over 60 percent of all employment growth occurred in jobs in the top third.[1] Since 1983, job growth in the top third has been 50 percent, which is one-and-a-half times more than in the lower third.[2] It seems clear that for most people who receive layoff notices, unemployment is temporary and a bridge to a better job.

The unemployed fall into four categories: job losers, job leavers, re-entrants, and new entrants to the labor market. The job losers are those who are fired, those who receive layoff notices, and those who have completed a temporary job. Job leavers are those who choose to quit a job either to take or to seek another job. Re-entrants are people who were employed in the past but who dropped out of the active labor force for some time to pursue other activities, such as school or homemaking, and who then take up an active job search. New entrants are those who are engaging in active job search for the first time.

Table 3 shows the percentage distribution of the unemployed in each of the four categories in November in the years 1992 to 1998. Job losers are the largest group, followed by re-entrants.

TABLE 3

Year	Job Losers	Job Leavers	Re-Entrants	New Entrants
1992	55.2%	10.5%	24.0%	10.3%
1993	52.5	11.9	25.2	10.4
1994	48.0	9.5	34.5	8.0
1995	47.6	11.1	33.4	7.8
1996	45.9	11.4	34.6	8.1
1997	45.6	10.3	35.2	8.8
1998	45.0	10.7	35.4	8.9

Source: http://www.bls.gov/news.release/empsit.toc.htm

Job leavers and new entrants together make up roughly 20 percent of the unemployed. In November 1998 the seasonally adjusted number of unemployed people was just over six million. So there were about 2.7 million job losers, three-quarters of a million job leavers, over 2 million re-entrants, and over half a million new entrants. They were all actively involved in the labor recycling process.

Another way to think of employment and unemployment is as percentages of the total civilian noninstitutionalized population aged 16 or over (hereinafter, the population). The unemployment rate reported above is the

number of unemployed divided by the active labor force. The active labor force is the sum of the employed and the unemployed. Only people who are out of work and who are actively seeking work are counted as unemployed. Many people in the population are not in the active labor force. The labor-force participation rate is the active labor force divided by the population. Table 4, column 2, shows the labor force participation rate in November of the years 1992–1998. Column 3 shows the ratio of the employed to the population. The difference between columns 2 and 3 in any year is the ratio of the unemployed to the population. Those ratios are shown in column 4. In November 1998, for example, only 3 percent of the entire population was unemployed. The other 97 percent were either employed or were not seeking employment. Since 1994, when the BLS began to collect the data, only 0.5 percent of those out of the labor force were discouraged about finding work. The rest were out of the labor force by choice.[3] Typically the discouraged job seekers are those whose skills have become obsolete and who need retraining.

TABLE 4

Year	Participation Rate	Employed/ Population	Unemployed/ Population
1992	66.3%	61.4%	4.9%
1993	66.3	61.9	4.4
1994	66.8	63.0	3.8
1995	66.5	62.8	3.7
1996	67.0	63.4	3.6
1997	67.1	64.0	3.1
1998	67.1	64.1	3.0

Source: http://www.bls.gov/news.release/empsit.toc.htm

The Market Process

The labor market, like any other market, is a process of interaction between forces of demand and supply. The buyers of labor are employers, and the sellers of labor are job seekers and job holders. When employers "buy" labor, they hire the productive services of workers. Labor is employed, along with materials, supplies, and the services of capital goods, to produce output that employers in turn sell to customers. Workers supply labor services to employers in exchange for wages, salaries, and benefits.

The maximum amount that an employer is willing to pay for a worker's services is called his demand price for the labor. It depends on the increment to output that the services make possible and on the prices for which the employer can sell the additional output to customers. Suppose that employer expects that an additional worker makes possible the creation of ten additional units of output per day, and that when those units are sold, the employer will receive $120 of extra revenue net of all other incremental costs. The hiring cost is the sum of compensation paid to the worker and employment taxes paid to government. The employer would not be willing to pay $120 per day or more for the worker's services, but at any hiring cost less than $120 per day, the employer would increase profits by hiring the worker. From the employer's point of view, the lower the hiring cost the better so long as he can hire the quantity and quality of labor he wants. The lower the hiring cost, the more eager the employer will be to hire additional workers if he can get them.

If workers' productivity declines because of, for example, a change of technology that makes their services less important, or if the prices that the employer receives from customers decline because, for example, the customers decide they want to buy different products, the employer would have to cut labor costs by layoffs or by reducing rates of compensation (or both). The latter is likely to cause many workers to quit because they have no reason to think that the reduced compensation is the best they can do. Both those laid off and those who quit will begin a process of job search.

The minimum compensation that an employee will accept from an employer is called his supply price for the job. It depends on his perception of his alternative employment (and unemployment) opportunities. Other things equal, the better his alternatives the higher his supply price. If you know you can get $15 per hour from Employer X for doing a job, you will not accept anything less from Employer Y for doing the same job. If

your alternative to working for Employer X is to be unemployed (a very unlikely situation), you will have a higher supply price if your family will support you during unemployment than you will if your best alternative is to become homeless.

So there is an upper limit on what an employer will pay and a lower limit on what a worker will accept. The actual rates of compensation depend on the relative strengths of two types of competition in the relevant labor market—competition among employers to hire and competition among employees to be hired. For a given level of competition among employees, the more intense the competition among employers to hire, the greater the pay. Conversely, for a given level of competition among employers to hire, the greater the competition among employees, the lower the pay. Every hiring of every worker is an employment contract based on voluntary exchange. Every employer and every employee enter into such contracts because they expect to be better off than they would be if they did not do so.

From an individual worker's point of view, the best of all possible situations is to be the only one who can do a particular kind of work and to have hundreds of employers competing to hire someone who can do the job. Such a worker would have tremendous bargaining power, and any one employer would have almost no bargaining power. Similarly, from an individual employer's point of view, the best of all possible situations is to be the only buyer of a particular kind of labor service and to have a plethora of workers competing to do the job. Such an employer would have tremendous bargaining power, and any one worker would have almost no bargaining power. Bargaining power in any market depends on the alternatives available to the actors therein.

Enterpreneurship

Entrepreneurs are the key actors in all markets. The role of an entrepreneur is to discover and grasp profit opportunities. Every problem that emerges in a market is a profit opportunity for an entrepreneur who first notices how to solve it and undertakes the solution. Successful innovations by entrepreneurs elicit imitation, and imitation by more and more people means that, in free-market settings, problems inevitably give way to solutions. Entrepreneurs do what they do in pursuit of profit; but when they are successful, and therefore make profit, the rest of us benefit from their innovations.

Entrepreneurship involves creating new products, creating new technologies, creating new productive resources, assembling new combinations of productive resources to produce old and new products, adopting new forms of organization, and entering new markets and exiting old ones. Buyers and sellers in all markets must keep abreast of more innovation now than ever before. In today's markets, successful innovation at one place rapidly affects most other places. Entrepreneurship, and responses to entrepreneurship, lie behind the recycling of labor (and of other productive resources).

Suppose that the proposed merger of Exxon and Mobil takes place. In the face of falling prices for petroleum and its products (which itself is due to successful innovations in the discovery, production, and refining of crude oil as well as the discovery and implementation of alternative energy sources), the decision-makers in the new firm will have to cut out duplicative operations. This means that many employees of the merged firm will receive layoff notices. Perhaps some will be able to stay on by agreeing to accept cuts in compensation, but most will quite reasonably think that it is possible to find other satisfactory jobs that pay as much or more as the ones they have lost. While searching for alternatives, they will be counted by the BLS as unemployed. Some will find new employment quickly; others will not. As noted, the median duration of unemployment in November 1998 was 6.7 weeks. If after some initially planned search period, some job seekers find no satisfactory new jobs, they will reevaluate their prospects and lower their supply prices. Or perhaps they will become convinced that their best strategy is to undertake retraining so they can find different sorts of jobs.

Employers in markets for new products and products for which customer demand is rising also engage in search. They search for new

employees who can do what needs to be done. They could attract a lot of applicants right away by offering very high pay and benefits, but most will reasonably think it would be cost-effective, at least for awhile, to offer normal compensation and spend some time sampling the workers that apply. Recycling labor is not a simple matter of throwing all applicants into a common bin. They must be sorted according to abilities, interests, and costs. If after some initially planned period of search the employers do not find enough satisfactory employees, they will then offer better compensation to attract more applicants.

The key insight is that every unemployed worker who wants to work is a potential profit opportunity for an entrepreneur who discovers ways of employing him. Even workers who have a hard time finding new work are potential profit opportunities. They are likely to be available at modest levels of compensation, making it cost-effective to hire and train them. And when they are trained they acquire additional bargaining power with their employers and with potential new employers. This is why, in a market-based economy, layoffs do not usually result in a growing number of unemployed people and falling average rates of compensation. Unemployment is like a pipeline. There are always people entering the pipeline, but there are always people exiting too. Even if the number of people in the pipeline at any moment were always the same, the faces on those people would be constantly changing.

Entrepreneurs, like all people, make mistakes. Some entrepreneurs think they perceive profit opportunities and hire additional labor to try to grasp those opportunities. When losses instead of profits emerge, they have to pass out layoff notices. However, the historical record suggests that under normal circumstances, entrepreneurial successes more than make up for entrepreneurial failures. After all, entrepreneurs are self-interested and therefore keenly motivated to avoid mistakes and the losses that result.

Of course, there are occasional periods during which unemployment increases relative to employment, but these are the result of faulty government policies that cripple the labor recycling process. If, for example, the government inflates the money supply and thus distorts the price signals to which entrepreneurs respond, lots of entrepreneurs will hire labor that later, after the market corrects the distorted prices, they will have to lay off. Excessive taxation and regulation are other ways in which government can cripple the labor recycling process.

Government Doesn't Create Jobs

It is entrepreneurship in the context of freedom, not government, that creates increasing employment opportunities. Try to imagine what would happen to the labor-recycling process if entrepreneurs had to get permission from some government authority before they could enter or exit markets, expand or contract employment, create new products, change technologies, or alter their organizational structures. The pattern of production would become less and less consistent with the pattern people want. Innovation would shrivel. Lots of people would continue to be employed doing what they always did, but they would increasingly produce things for which there would be no demand. There would be few job opportunities for new people in the labor force. Production would be aimed at keeping government authorities, not customers, happy.

American presidents like to assert that they are elected to "run the economy." We should be grateful that that is merely their conceit. No one runs a successful economy. Its success depends on no one's being in charge of it all. At the same time, its success depends on everyone's being in charge of his own production and exchange activities, dealing with others on the basis of voluntary exchange. □

1. *The American Workplace 1998* (Washington, D.C.: Employment Policy Foundation [www.epf.org], 1998), p. 24.
2. *Economic Bytes,* Employment Policy Foundation, November 2, 1998.
3. http://www.bls.gov/news.release/empsit.toc.htm, Table A-10.

THE FREEMAN
Ideas On Liberty

Scientists Beware

by Bruce L. Benson

Many political commentators lament the growing apathy among the voting-age population, but I do not believe apathy keeps many potential voters away from the polls. Many of us care a lot about what politicians are doing; we just don't trust any of them.

Richard Nixon, Lyndon Johnson, Bill Clinton, and hundreds of others like them elected to federal, state, and local offices have destroyed the credibility of politicians in general. And this political disease is contagious. I regret to say that it has spread to my profession. So many economists have been pulled into the political process as government employees or paid consultants to provide "expert" opinions on virtually every side of every political debate that economics has lost much of its credibility. In fact, there are almost as many economist jokes as lawyer jokes (check out netec.wustl.edu/JokEc.html).

Economics is, of course, a social science (or in some circles, a "soft science"), so our laboratory is the complex real world and it is relatively easy to find selective evidence in support of any political position. The physical sciences (or "hard sciences") are not immune from the political disease either, however. The policy process at the Environmental Protection Agency has made this abundantly clear. For instance, last year while invalidating part of a 1993 EPA report on secondhand tobacco smoke, a federal judge concluded that the "EPA publicly committed to a conclusion before research had begun, . . . adjusted scientific procedure and scientific norms to validate the Agency's public conclusion, and aggressively utilized authority to disseminate findings to establish a de facto regulatory scheme . . . and to influence public opinion." In particular,

- A policy document, which presumably would be written after the scientific analysis was carried out and reviewed by other experts, was written before the analysis was completed.

- To provide scientific support for the EPA's predetermined conclusions, its scientists had to "cherry pick its data." The report contained a selective review of scientific literature that ignored both many relevant studies and criticisms of many that are cited. It also contained a statistical reanalysis of 11 U.S. studies, none of which provided support for the desired conclusions at standard levels of statistical confidence. By re-analyzing those studies together (using "meta-analysis") and abandoning the commonly accepted standard for statistical confidence (effectively doubling the chances of being wrong), the EPA was able to support the predetermined conclusion that evidence of a "substantial public health impact" exists.

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- The validity of the re-analysis cannot be assessed because the EPA report does not provide sufficient information about the studies and process, leading the judge to conclude that "The court is faced with the ugly possibility that EPA adopted a methodology for each chapter, without explanation, based on the outcome sought in the chapter." Furthermore, if the two most recent U.S. studies that were then available (one funded by the National Cancer Institute and one by the World Health Organization) had been included in the re-analysis, the results apparently would not have been statistically significant even at the lower level of confidence.

I could go on, but the point is that the EPA, supposedly an agency whose policies are based on valid scientific evidence, is willing to manipulate that evidence in pursuit of a political agenda. Indeed, despite this judicial decision and numerous studies contradicting the EPA's position, Administrator Carol Browner described the court decision as "disturbing" because "it is widely accepted" that the dangers alleged in the report are "very real." Apparently, wide acceptance of an idea is justification enough for a policy, whether the scientific evidence supports it or not! The possibility that the EPA's misleading report may have influenced this "wide acceptance" does not seem to matter either.

Questioning Integrity

The EPA is appealing the ruling, so it is far from final. Some agency officials have even questioned the integrity of the judge because he is located in North Carolina, the nation's leading tobacco-producing state. But the same judge ruled, only a year earlier, that the Food and Drug Administration has the authority to regulate cigarettes, despite strong protests by the tobacco industry. The judge also was not the only person to be concerned about the report. Two internal EPA documents from its Environmental Criteria and Assessment Office argued, before the 1993 Report was issued, that it was badly conceived and presented, that it overstated the alleged causal relationship, and that the conclusions were unwarranted. More important, the court ruling apparently has just uncovered the tip of the iceberg. In 1992, EPA's own Science Advisory Board lamented that the agency pays inadequate attention to peer review and quality assurance, "leaving EPA initiatives on shaky scientific ground and affecting the credibility of the agency."

More and more EPA scientists are also alarmed at how policy is increasingly made at the expense of scientific integrity. In all likelihood, scientists who work for EPA are concerned about environmental issues and predisposed to supporting strong policies. But many also care about the credibility of their agency and their scientific disciplines.

For instance, David Lewis, a research microbiologist, risked his 27-year career at EPA by writing to Browner and Vice President Al Gore deploring the deterioration of science at the agency. When he got no response, he published an article titled "EPA Science: Casualty of Election Politics" in the highly respected journal *Nature*, arguing that the agency gives "a higher priority to issuing regulations than to developing the underlying science." Elsewhere he attacked the agency's wastewater toxicity tests as being unreliable. Subsequent studies performed outside the agency support his criticisms, and perhaps as a result, the agency no longer uses the tests. But Lewis was still charged by EPA officials with an array of ethics violations. He felt the need to file a whistleblower's complaint with the Labor Department, which concluded that EPA officials had violated six federal statutes in harassing him.

Spreading Skepticism

Despite Lewis's vindication, complaints by one employee might be dismissed, but he is not alone. The increasing complexity of the EPA's own internal rules, along with a commitment to punish anyone who does not follow those rules, has given EPA management considerable discretion, which can be employed to harass whistleblowers and others who express dissatisfaction with the agency's

activities or procedures. And such harassment is becoming common. On June 10, 1998, more than a dozen career employees of the agency sent a letter to the *Washington Times* "risking our careers rather than choosing to remain silent" about the "egregious misconduct" at EPA. The letter explains that the "retaliation against whistleblowers . . . at every management level" and other "illegal or irresponsible behavior by managers" in pursuit of political agendas "jeopardize the proper enforcement of law." In other words, while these employees believe that there is a proper role for the EPA in enforcing scientifically valid environmental restrictions, they see that role being jeopardized, just as Lewis did. Some lab scientists who do not follow the "party line" are apparently even being charged by the EPA's Inspector General's office for alleged corrupt practices, although federal administrative judges are throwing out such cases and accusing the IG of carrying out investigations in bad faith. (See Bonner R. Cohen, "Polluted Agency" *National Review*, August 1, 1998, pp. 38–39.)

No matter what position on secondhand smoke or water-quality measurement or any of a number of other policy issues one might support, scientists should be concerned about the politicization of their research. When shoddy practices such as those revealed by Lewis and the federal judge are passed off as science, people begin to doubt other "scientifically justified" policy recommendations and regulatory standards. Critics of policies ranging from ozone protection to the banning of dioxin and other alleged carcinogens have done just that.

Supporters of those policies of course attack the scientific arguments of their opponents, making the physical sciences look like the social sciences—capable of providing evidence to support any politically motivated proposal. Those of us who already dismiss claims made by politicians and social-scientist "experts" on retainer in political causes are developing the same attitude about claims by biologists, chemists, and other physical scientists, at least when their research is cited in the public policy arena. If scientists do not stand up against the political manipulation of their research, their credibility will soon be similar to that of politicians, lawyers, and alas, economists. □

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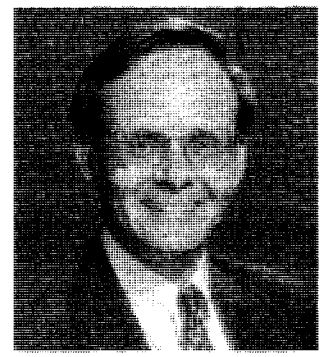
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Flunking Economics

Why should we care about economic literacy? Are we troubled by illiteracy in physics? Or metaphysics? Should we worry that most of us can't remember much of the periodic chart of the elements? Why should we worry more about economics? Because economic illiteracy is dangerous. I can ride on a roller coaster without understanding centrifugal force. In fact, even if I refuse to believe in centrifugal force and actually create a new religion on that basis, I will probably stay in the roller coaster as I careen around the corner. Physics can protect me, whether I believe it or not. But if I ignore basic economics, I could go broke. And if a country ignores basic economics, it could go bankrupt.

That's the opening paragraph of an essay titled "Hope and Danger for Economic Literacy" by economist Todd G. Buchholz, one of several fine essays published in the December 1998 issue of *The Region*, a quarterly journal of the Federal Reserve Bank of Minneapolis. The issue was devoted to what Americans know, don't know, and should know about economics.

Buchholz is right. The level of economic knowledge will make or break an individual or a nation of individuals. When people understand the subject, its principles, and its implications, they can raise the standard of living and solve problems.

When people don't understand economics, they gullibly embrace "quick fix" promises that erode the standard of living and blindly support impractical "pie-in-the-sky" solutions that make problems multiply and worsen.

So economic education is important, and Americans today need heavy doses of it. Ordinarily, it might make sense to recommend that Americans pick up a high school economics text and read it from cover to cover. Sadly, that would be very poor advice.

My colleague Burton Folsom has directed a Mackinac Center for Public Policy review (written with George Leef and Dirk Mateer and released this month) of 16 of the top-selling high school economics textbooks. Folsom found only six texts he could grade either A or B for economic accuracy. Each of the rest rated a C, D, or F. If he hadn't been generous enough to grade on the curve, more than half might have flunked.

Errors abound in the texts students are using in high school economics classes, more than an entire issue of *The Freeman* could address. What follows is a small sample of the worst ones. These statements are so inexcusably erroneous that they have no business appearing in print on any page of an economics text worthy of the name.

"*As societies become more complex, the need for government power tends to increase.*" From Sanford Gordon and Alan Sanford's *Applying Economic Principles*, this little canard is tossed out in a matter-of-fact, everybody-knows-it fashion.

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Are these guys utterly unaware of F. A. Hayek's withering critique of central planning? (Hayek and most economists would surely dismiss the statement as a "pretense of knowledge" if there ever was one.) Have Gordon and Sanford never heard of public choice, the school of thought within economics that explains the inherent defects in government action? Do they not know that one of the many reasons for the collapse of the Soviet socialist empire was the utter incapacity of the state to keep up with the information and innovations of competitive markets?

FEE's Leonard Read demolished this simplistic notion decades ago by pointing out that the impossible task of one person's planning the life of another is made even more hopelessly complex when a handful of people in government set out to plan the lives of millions. "Obviously, the more complex our economy, the more we should rely on the miraculous, self-adapting processes of men acting freely," wrote Read.

"Despite fears by some Americans that governmental tampering with the free enterprise system would be harmful, most government policies have met with success." David E. O'Connor, with a straight face, asks us to believe this statement in his text, *Economics—Free Enterprise in Action.*

Government doesn't always fail, to be sure—especially if you're not picky about what "failure" means. But the track record hardly suggests that "most" of its policies have been successful. Education? Studies show the more government spends and meddles, the worse the schools get. Money? At least seven or eight recessions, a Great Depression, and a currency worth a nickel of its value when the Federal Reserve System was established does not add up to success. Poverty? We now know beyond dispute that $5 trillion in poverty spending only exacerbated the problem. On and on it goes, but you get the picture.

"During the Industrial Revolution, 'wages were so low that sometimes entire families had to work.'" Richard Hodgetts and Terry Smart employ this assertion in their text, *Economics*, to imply to the reader that the Industrial Revolution set society back because it made many people work for the first time.

If text authors could be sued for malpractice, Hodgetts and Smart would need skillful attorneys to handle this one. Evidence by the boatload shows that life was far more "nasty, brutish, and short" in the days before industrialization boosted productivity and gave people a chance. Kids did not dance their time away around the maypole in 1400; large numbers of them died before the age of five and those that survived typically labored under appalling conditions and never heard the phrase "summer vacation."

"Under a balanced budget, the government would 'not be able to do things that many people think it should do, like building roads and providing for the needy.'" Henry F. Billings, in his *Introduction to Economics*, apparently believes either a) when government runs a deficit so that it can spend more than it raises in taxes, we get the extra goodies for free, or b) people have to be bamboozled into programs they wouldn't want to pay for.

After 30 years of nonstop deficit spending, no intelligent adult has a legitimate excuse for thinking that red ink makes anything cheaper or more readily available. A balanced budget means taxpayers pay now for what they get from government. Deficit spending simply means that today's taxpayers get the goodies and tomorrow's get the bills, plus a hefty interest charge.

How does this junk—and so much more, as documented in Folsom's study—find its way into high school economics texts? One reason is that high school teachers drive the market, and few of them who are asked to teach economics have either majored in the subject at college or have demonstrated any particular competence in the field. Publishers even assemble focus groups of such teachers; if they say, "We like the minimum wage!" then that's what the authors of texts are told to include in the books.

Another reason is the general level of economic ignorance throughout our society. It's an enduring, pandemic affliction that underscores the need for the work of organizations like FEE. □

THE FREEMAN
Ideas On Liberty

Wasting Energy on Energy Efficiency

by Ben Lieberman

Few aspects of our daily lives are more heavily regulated by the federal government than our use of energy. The cars and trucks we drive, the structures in which we live and work, and virtually every major appliance we use has been transformed by Washington's near obsession with energy efficiency. Chances are, if it runs on electricity, gasoline, natural gas, heating oil, or any other energy source, it has been substantially affected by federal laws and regulations.

The energy efficiency crusade was originally launched in the 1970s as part of the solution to the so-called energy crisis. Washington was convinced that world oil supplies were rapidly dwindling and that drastic energy conservation measures were needed. As a result, Congress enacted several laws for the purpose of reducing energy consumption. Some statutes set energy-use standards, be it miles per gallon for motor vehicles or kilowatt hours per year for refrigerators. These laws not only set initial standards but gave the implementing agencies (Department of Energy [DOE] for most appliances, National Highway Traffic Safety Administration [NHTSA] for motor vehicles) the authority to periodically tighten them without going back to Congress for approval. Several laws also created tax incentives or other inducements for individuals and businesses to reduce energy use beyond the level they would achieve on their own.

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A Second Ill Wind

The energy crisis has long since faded away. The "experts" could not have been more wrong—oil supplies are so plentiful today that the price has reached a 25-year low. Nonetheless, the efficiency agenda lives on. These same statutes and regulations, and the army of bureaucrats and activists that make their living from them, are experiencing their second wind as one of the putative solutions to global warming. If consumers can be made to use less energy, the argument goes, then less carbon dioxide, the chief anthropogenic greenhouse gas, will be emitted into the atmosphere.

Last November, when the Clinton administration signed the Kyoto Protocol, the international agreement to reduce emissions of greenhouse gases, Stuart Eizenstat, undersecretary of state for economic, business, and agricultural affairs, emphasized the role energy efficiency will play in its implementation. He announced new funding for research into more efficient automobiles and housing, and an effort to "begin setting new energy efficiency standards for major appliances." Indeed, until the Kyoto Protocol is submitted to a skeptical Senate for approval, these already existing energy-efficiency statutes are among the few tools the Clinton administration can legally use to combat energy use.

Before the nation embarks on new rounds of tougher efficiency standards for everything from washing machines to light bulbs to SUVs, it is worth examining what the first

wave of such centrally planned austerity measures has done for us. Despite the positive publicity accorded measures enacted in the name of energy efficiency, they have accomplished nothing. However, they have raised the cost and reduced the quality of affected products, and have created or exacerbated several health and safety problems.

An Ineffective Solution

Even assuming the global warming crisis is not as spurious as the energy crisis (but see Jonathan Adler, "Global Warming: Hot Problem or Hot Air?" in *The Freeman,* April 1998) and that substantial environmental benefits will accrue from reduced energy use, there still are serious limitations on how much can be achieved through federally mandated energy efficiency measures. True, if consumers use less energy, then less carbon dioxide will be emitted into the atmosphere, either directly in the case of motor vehicles or fuel-burning appliances, or indirectly in the case of electrical appliances whose energy is generated through fossil-fuel combustion by utilities. But 25 years of energy efficiency measures have failed to stem the increases in national energy use.

"People always seem to find more uses for energy," says Herbert Inhaber, author of *Why Energy Conservation Fails.* Today's refrigerators may require half the electricity of a comparable 1980 model, but people are more likely, given the lower operating costs, to own a larger one, or even have two. Better gas mileage has led to increases in vehicle miles traveled. Studies have shown that owners of high efficiency heating systems tend to set their thermostats a bit higher than others. Many consumers "spend" their savings from efficient appliances on other energy-using conveniences, like additional lighting. Ironic but true, a quarter century of federal energy-efficiency mandates has increased, not decreased, total energy use.

Ratcheting down current efficiency standards will probably have the same effect. In all likelihood, the only way for Washington to actually reduce energy use is to sharply increase energy costs. Proponents of the Kyoto Protocol are also seriously considering energy taxes or other price-raising schemes, but these cannot be enacted until the treaty is ratified, or new legislation is enacted. In addition, such options are fraught with the kind of direct adverse political consequences the energy efficiency agenda has thus far avoided.

Bad Deal for Consumers

The level of consumer satisfaction with many things targeted by the energy-efficiency crusade has declined as a result of Washington's dictates. This should not be surprising—in a free market, most technological improvements that allow efficiency gains without adverse side effects would be incorporated anyway. Manufacturers, responding to competitive forces, have plenty of incentives to provide the best available balance of price, performance, and operating costs. Efficiency mandates simply upset this balance, placing arbitrary energy-use standards above everything else. Alan Kessler, vice president of Raytheon Appliances, noted in congressional hearings on appliance standards that "from the perspective of DOE and standards advocates, the purpose of major appliances is solely to save energy," and not to provide maximum overall consumer satisfaction.

Energy efficiency, Washington-style, comes at a cost. For example, DOE estimates that the latest energy standard for refrigerators will add $80 to the cost of a new model when the standard takes effect in 2001. DOE is also considering regulations mandating certain highly efficient types of clothes washers that currently cost hundreds more than their conventional counterparts. One study estimates the total cost of appliance standards of $59 billion. True, these and other goods save on energy, but the payback periods are often very long.

Beyond appliances, studies have also shown that the sticker price of automobiles has increased because of NHTSA's Corporate Average Fuel Economy (CAFE) standards, and that energy-saving features add considerably to new housing costs.

Quality also suffers. Air conditioners rated as highly efficient under the federal standards

are less reliable than average models and some do a poor job dehumidifying the air. "I've seen state of the art, high efficiency air-conditioners in homes where there's mold and mildew on the walls," says Dave Debien, owner of Central City Air, in Houston. Many consumers are dissatisfied with the weak trickle from federally mandated low-flow shower heads. Some highly efficient refrigerators have freezer sections that don't stay as cold as they should to safely preserve foods for extended periods. Efficiency mandates often have a performance downside to go along with the energy savings.

Beyond the effect on price and quality, these standards also limit the choices available to consumers. Kessler noted that the need to meet arbitrary efficiency standards is leading to product lines "so homogenized and energy-oriented that other product innovations or features are placed on the shelf." In addition, several manufacturers have stopped producing certain products, such as the lowest priced air conditioners, because they have been rendered unprofitable by efficiency regulations. Directly and indirectly, Washington is telling us what we can and cannot have.

The efficiency crusade has also exacted a price in health and safety. The problem of indoor air pollution is in large part attributable to the government's attempts to conserve on energy used to heat and cool homes and buildings. Though the federal government does not directly set energy standards for homes and offices, it has been quite effective in doing so indirectly. For example, Washington requires that newly constructed houses meet certain efficiency requirements in order to be included in federally backed mortgage programs. The government also pays for insulation in low-income housing, and has provided tax breaks for energy-saving expenditures.

These and other efforts sought to reduce "excessive" ventilation, considered wasteful of energy. Granted, heavily insulated, weather-tight buildings and homes do save energy by holding in more of the already heated or cooled air and reducing the influx of outside air. However, there has been an unanticipated side effect—these energy-efficient structures concentrate the levels of contaminants inside. The result has been a two-decades long increase in indoor air-related health problems as people inhale higher levels of airborne pollutants, including biological contaminants from molds, mildew, microorganisms, and insects, as well as chemicals like formaldehyde and volatile organic compounds. Even the federal government has admitted this oversight. The Environmental Protection Agency (EPA) now concedes that "the current trend toward sealing off homes to conserve energy may have serious health consequences."

Perhaps most disturbing is the sharp rise during this period in the incidence and mortality of pediatric asthma, especially among minority youth. While the reasons for this increase are not fully understood, one *New England Journal of Medicine* editorial suggested "decreased ventilation after the energy crisis in the United States in the 1970s" as one possible cause of increased exposure to the indoor contaminants that trigger and exacerbate asthma attacks.

Deadly Light Cars

CAFE standards may have also cost thousands of lives. To meet the average-miles-per-gallon requirements, automakers have had to reduce the weight of cars. Studies have consistently shown that, all other things equal, lighter vehicles are less crashworthy. A 1989 Harvard/Brookings study estimated that CAFE standards have increased motor vehicle fatalities by 14 to 27 percent. This works out to about 2,000 to 4,000 lives per year. As is typically the case with the energy-efficiency agenda, such non-efficiency considerations have been almost completely ignored by the government. CAFE proponents now want to sharply raise the bar on automakers to help avert the highly speculative threat of global warming, but still deny the well-documented size-safety tradeoff.

The frequency with which federal measures to promote energy efficiency have led to these adverse "unintended consequences" has an interesting flip side. In retrospect, the levels of energy use in appliances, houses, and vehicles prior to Washington's interference implicitly included a good deal more wisdom than their

critics assumed, for they managed to avoid these problems. Once again, so-called market failures turn out not to be such failures after all. It's the efficiency mandates that have proven more regrettable.

The Future of Energy Efficiency

Federally mandated energy efficiency has been touted as a real win/win policy for consumers—we save on energy and enjoy the societal benefits from a national decline in energy use. In reality, it has been lose/lose—we must endure the negative effects of Washington's preoccupation with energy conservation while the overall policy proves pointless.

The real winners are the hundreds of energy-efficiency bureaucrats and allied activists, most of whom receive substantial federal funding for their efforts. They are frequently joined by opportunistic manufacturers who stand to benefit from federal energy policy, such as insulation producers or appliance makers who believe that their most efficient models are superior to the competition and can gain market share if a new standard is promulgated.

Thus far, these special interests have made for an almost unbeatable coalition. The energy-efficiency activists occupy the moral high ground, at least among Democratic legislators and the media, and the industry proponents provide enough lobbying clout and Republican support to win the day. The Naderites and other big consumer advocates are so smitten with the efficiency agenda that they turn a blind eye to its adverse effects on consumers; thus the battles have been mostly one-sided.

But there are a few signs that the efficiency crusade has marched too far. The 104th Congress set a moratorium on new energy efficiency standards for appliances, though it was criticized for doing so and eventually lifted it. Nonetheless, the moratorium managed to kill some truly silly regulations, like the proposed prohibition on oven windows, and delayed the implementation of several others.

Low-flow showers and toilets have been so unpopular that they sparked a grassroots backlash. In response to constituent complaints, Representative Joseph Knollenberg introduced a 1997 bill to repeal the low-flow requirements. The bill garnered 76 co-sponsors, not bad for a supposedly anti-environmental and anti-conservation measure. Knollenberg has promised to introduce a new bill in 1999.

The burgeoning backlash will only intensify if Washington embarks on new rounds of standards in the name of fighting global warming. The efficiency gains that were relatively easy to achieve have long since been used up to meet existing standards, and even those have proven quite painful. Whatever the alleged merit, additional federal micromanagement may impose an unacceptably severe impact on cost, quality, health, and safety.

Nonetheless, the Clinton administration is intent on spending more of our tax dollars to come up with new restrictions on our choices in the marketplace. Such measures will be an expensive nonsolution to an unproven problem.

Washington should stop wasting its energy. □

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THE FREEMAN
Ideas On Liberty

Paper Tiger

by Christopher Mayer

Gadflies have long been predicting the exhaustion of critical natural resources —especially oil. Despite the doomsaying, a barrel of oil is cheaper today than a pair of movie tickets.

As Daniel Yergin pointed out in a recent editorial in the *Wall Street Journal*, "prices, in inflation-adjusted terms, are at a level that has not been seen since 1973, prior to the oil embargo and the first oil crisis." In addition, the cost of exploring and developing crude is now only about $5 per barrel compared with over $21 per barrel in 1982.

Any cursory review of the history of real oil prices will show a long downward trend. It would seem oil is getting less scarce. And it would seem that there is no reason for this trend not to continue. This line of reasoning is vigorously pursued in the late Julian Simon's book *The Ultimate Resource 2*.

With oil prices at record lows, it is perhaps appropriate to reflect on the triumphs of markets and the erosion of the power of OPEC, the Organization of the Petroleum Exporting Countries. OPEC is often thought of as an Arab organization, but four of the 11 members—Iran, Nigeria, Venezuela, and Indonesia—are not Arabic. (See www.opec.org.) That's not the only misconception about OPEC.

Low oil prices persist despite OPEC's best efforts to support a higher price. In fact, market forces have made OPEC a paper tiger. Alan Abelson of *Barron's* astutely noted that years ago "In contriving to push up the price so precipitously, it inspired a frantic hunt for new deposits of oil and gas and, at the same time, set off formidable efforts at conservation. Which, of course, is the way markets inevitably work."

Services, Not Substances

Oil is used more efficiently today, and new sources are constantly being found. Importantly, substitutes for oil are also being developed and used. Remember, it is not oil itself that concerns us. Rather, it is the services that oil provides that are important. We should not care if, in a highly unlikely and theoretical scenario, we ran out of oil, as long as the service that oil yields is provided just as adequately by some substitute.

The world's experience with the energy crisis is consistent with deductive theory regarding the essential role of market prices in mobilizing economic forces to best provide for consumers' most urgent wants. As Simon wrote in *The Ultimate Resource 2*: "Heightened scarcity causes prices to rise. The higher prices present opportunity, and prompt investors and entrepreneurs to search for solutions. Many fail, at cost to themselves. But in a free society, solutions are eventually found. And in the long run the new developments leave us better off than if the problems had not arisen."

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We are better off because the market process yields more goods that cost less. Of course, for this type of activity to occur, people must have the freedom to employ their capital as they wish. The market process must be allowed to work free of government meddling. This goes against the conventional wisdom that when energy prices rise, government should induce conservation. (See the preceding article by Ben Lieberman.)

OPEC as Cartel

Can't OPEC wield cartel power? Economic theorists have long recognized the unstable nature of cartels. A cartel is an organization of separately owned producers cooperating, often through quotas on production, to achieve a price above what the free market would have chosen. On a free market, these arrangements fail because of the market forces they set into motion.

Simon pointed out that "A cartel such as OPEC, whose members have differing interests, is subject to pressures that make it difficult to maintain whichever price maximizes profit for the cartel as a whole. There is a great temptation for individual countries to sell more than their quotas."

The problems inherent in any cartel can best be illustrated by the prisoner's dilemma. Sharon Oster, in her book *Modern Competitive Analysis*, writes that in the prisoner's dilemma, "the payoffs are such that both players have individual incentives to choose strategies that together give both players a worse outcome than if both players had simultaneously chosen the other strategy."

To illustrate, say two prisoners are separated and told that if one confesses to a joint crime, both will be convicted, but the confessor will get a light sentence, say, one year, while the other prisoner will get ten. If neither confesses, they each will get two years. Individually, their incentives are to confess to serve the shortest time imprisoned. Jointly, it would be best if both kept quiet. This was a good approximation of the situation faced by OPEC, when it had a better grip on the world's supply of oil.

Some critics point to the fact that OPEC is still the low-cost producer and if oil prices continued to fall, OPEC would regain market share and its monopoly power.[1] I would first point out that the more oil prices fall the greater boon for oil consumers. Also, the fact that oil prices could fall further is a reflection of increased supply or slackening demand on the free market (ignoring money-induced changes or government price-fixing), neither of which would be cause for concern if we believe that market prices transmit valuable information regarding efficient resource allocation. We shouldn't care who produces the oil, only that we can purchase it when we need it. I am reminded of Bastiat, who made the point this way:

> Suppose someone tells you: "It is essential for a great country to have an iron industry." Answer: "What is more essential is that this great country *have iron*."[2]

OPEC wouldn't be helped by expanding to include American producers. There will always be an incentive for the better producers to cheat on the cartel.

The abundance of oil today is a testament to the ability of prices to send signals to entrepreneurs about consumers' most urgent wants. It is an illustration of the market's ability to organize and deliver goods efficiently. And finally, it shows that in a free market, there is no such thing as monopoly power, for it will not be long before the monopoly that attempts to defy the market is broken. As Horace said, "Many shall be restored that are now fallen and many shall fall that now are in honor." □

1. Ron Chernow, "No Funeral for OPEC Just Yet," (*New York Times*, January 5, 1999). Chernow makes the point that the cost of extraction is only $2 per barrel for OPEC, versus $7 per barrel for "super-efficient" Exxon on domestic oil and more than $10 per barrel on foreign oil.

2. Frederic Bastiat, *Economic Sophisms*, from the essay titled "The Little Arsenal of the Freetrader" (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1964), p. 251.

THE FREEMAN
Ideas On Liberty

China's Spontaneous Order

by James A. Dorn

This year marks the 50th anniversary of the People's Republic of China and the tenth anniversary of Tiananmen Square. The spontaneous demonstrations for freedom that took place in the heart of Beijing in May and June a decade ago met with a dramatic and tragic end when confronted with the power of the state.

It is no coincidence that the monopoly of power exercised by the Communist Party and the horrid events of 1989 are related. The party can survive only by its ultimate reliance on the use of force to prevent competition from those who would contest single-party rule. The recent crackdown on the founders of the first opposition party in the history of the PRC, the Chinese Democratic Party, attests to the insecurity of the ruling elite.

Yet, even in the face of an oppressive government, the Chinese people have made substantial economic progress since 1978. They have done so because brave individuals have been willing to challenge the planned economy and because the communist party under the leadership of Deng Xiaoping recognized the failure of planning and the value of a market system. But the party has been unwilling to abandon its vision of a "socialist market economy" and allow a true market system to evolve.

The party leaders believe that without their firm guidance, life in China would be chaotic and unstable, and the economy would grind to a halt. No one better represents that view than Jiang Zemin, China's president and chairman of the Communist Party. This past December, he celebrated the 20th anniversary of China's economic reform, and attributed its success to "unswerving adherence to the Party's basic line." By his logic, continued economic success depends on the survival of the Communist Party and on the primacy of public ownership.[1] Nothing could be further from the truth.

The Secret of China's Success

China's economy has grown by nearly 10 percent a year since 1978 because the government has gotten out of the way of the market and allowed individuals greater economic freedom—not because of strict adherence to the basic party line, which holds that the individual is a cog in the socialist state. The truth is that China's economic reforms have succeeded because some individuals were willing to risk everything to escape the iron grip of state planners and a life with no future.

The first steps were taken by farmers who resisted state coercion under the communal system and initiated what Kate Xiao Zhou, author of *How the Farmers Changed China*, calls "a spontaneous, unorganized, leaderless,

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nonideological, apolitical movement."[2] The goal was to create a market-oriented system under which farmers would have greater control over the land at their disposal and be able to profit from voluntary exchange. It was only *after* that limited, spontaneous experiment with the "household responsibility system" (*baochan daohu*) proved successful that the party sanctioned the new arrangement.[3]

As farmers gained wealth, they expanded into nonfarm production and experimented with a new form of collective ownership—the so-called township and village enterprise (TVE). Rather than actively promoting that new ownership form, party leaders cautiously observed its operation. Once success was evident, the Communist Party again was willing to permit expansion. However, it never envisioned that TVEs would far outperform state-owned enterprises. According to Deng, "Our greatest success—and it is one we had by no means anticipated—has been the emergence of a large number of enterprises run by villages and townships. They were like a new force that just came into being spontaneously."[4]

Today, the market-driven, nonstate sector, which includes TVEs, foreign-funded enterprises, private enterprises, and other firms that are not dependent on government handouts, is the dominant force in China's "socialist market economy." More than 70 percent of industrial output value is now produced outside the state sector. Most state-owned enterprises, on the other hand, are losing money and eating up China's capital—more than 50 percent of state investment funds go to these collectives.[5]

Another example of spontaneous order in China is the special economic zones. Those zones were first set up in the coastal areas, but the idea spread to other areas and took on new forms as competitive forces led some local officials to permit the growth of markets and foreign investment *before* receiving approval from the central government. Once the new institutions were successful, however, official recognition followed.[6]

China's economic success has been the result of millions of hard-working Chinese being set free to pursue a better life. The relaxation of price controls has allowed the market, rather than the plan and the party, to guide production and consumption. The continuing depoliticization of economic life has given people more time and energy to devote to everyday affairs. Personal freedom has inched forward as a consequence. People are now free to work outside the state sector and to choose their life's work, to buy from alternative sources, to invest their money, and to enjoy the infusion of new products and new ideas brought about by trade liberalization.

The real lesson from China's "economic miracle" is not that economic development depends on adherence to the "party's basic line," but that economic freedom is essential for increasing human well-being.

A Constitution of Liberty for China

The willingness of China's leaders to open the country to the outside world, to permit new ownership forms, and to abolish much of the state planning system in favor of market pricing should be congratulated. But the lack of commitment to private property rights and, therefore, to limited government and the rule of law means that China's future is unclear. So long as the market is contaminated by party politics and state planning, corruption will continue to pollute China's economic environment.

If China wishes to continue its rapid economic growth into the next century and end corruption, it must strive for institutions that are consistent with free-market principles and the rule of law. That is why Justin Yifu Lin, Fang Cai, and Zhou Li argue that "It is essential for the continuous growth of the Chinese economy to establish a transparent legal system that protects property rights so as to encourage innovations, technological progress, and domestic as well as foreign investment in China."[7]

Ultimately, economic and political reform are inseparable. To depoliticize economic life and nourish China's fragile spontaneous market order, there must be constitutional change and new thinking (*xin si wei*). The Chinese people need to understand and appreciate the

nature of spontaneous order and the institutions that underlie that order—namely, private property, freedom of contract, and limited government. Most of all they need to adopt what F.A. Hayek called a "constitution of liberty."[8] As Roger Pilon, director of Cato's Center for Constitutional Studies, stated, "If China is to preserve and expand upon its recent achievements, it will need a constitution that institutionalizes, not simply tolerates, the forces that have led to improvements there."[9]

Chinese scholars are beginning to realize the necessity of constitutional change. In 1991, Jixuan Hu argued that the market is a "living system" that cannot be designed. "By setting up a minimum group of constraints and letting human creativity work freely, we can create a better society without having to design it in detail. That is not a new idea, it is the idea of law, the idea of a constitution."[10] To accept that idea, however, means to understand and accept the notion of spontaneous order and the principle of nonintervention (*wu wei*) as the basis for economic, social, and political life.

But as Pilon explains, the development of China's spontaneous market order is being limited by the Communist Party's adherence to a constitution that turns the relation between the individual and the state on its head. Instead of protecting individuals and their property rights, the Chinese constitution makes the individual subservient to the state and narrowly circumscribes rights, allowing only that amount of freedom that does not threaten party rule. Rights are temporary and arbitrary, not permanent, and depend solely on the will of the rulers.[11]

What China needs is a government of limited powers that respects the life, liberty, and property of each individual—not 100 more years of communist rule and "public" ownership. It is not enough that China has permitted the market to develop; China must now recognize the futility of trying to plan the market and to control the lives of 1.3 billion people. A better way is to increase freedom within a constitutional setting that establishes general rules to constrain government and let people be free to choose.

Lao Tzu Thought

In considering what steps to take next, China's leaders should look to their own ancient culture and rediscover the principle of spontaneous order—the central principle of a true market system.[12] In the *Tao Te Ching* (also known as the *Lao Tzu*), written more than 2,000 years before *The Wealth of Nations*, Lao Tzu instructed the sage (ruler) to adopt the principle of noninterference as the best way to achieve happiness and prosperity:

> Administer the empire by engaging in no activity.
> The more taboos and prohibitions there are in the world,
> The poorer the people will be.
> The more laws and orders are made prominent,
> The more thieves and robbers there will be.
> Therefore, the sage says:
> I take no action and the people of themselves are transformed.
> I engage in no activity and the people of themselves become prosperous.[13]

"Lao Tzu Thought," not "Mao Zedong Thought," is the beacon for China's future as a free and prosperous nation.[14]

Truth versus Party Line

The truth is, the basic party line is inconsistent with a spontaneous market order and a free society. When push comes to shove, the party, not the individual, rules, and no dissent is tolerated. Until that totalitarian mentality is contested, China's future will be plagued by uncertainty, and the nascent market economy will be in constant danger.

The right to dissent—that is, to be different, to think, to choose—is the hallmark of a free and civil society. The party's recent crackdown on dissidents, including the harsh sentencing of Zhang Shanguang to 10 years in prison for "informing" Radio Free Asia of the protest by 80 farmers in Hunan's Xupu County against excessive taxes, is yet one more egregious example of how the party's quest for "stability" is, in reality, a ploy to protect its monopoly power.[15]

It is time for the Communist Party to abandon its top-down model of "stability" and allow the forces of freedom and individual responsibility to create a new constitutional order from the bottom up—based on the consent of the people and a respect for their natural rights to life, liberty, and property. Only then will the institutional incompatibility that now exists in China's socialist market economy disappear and a true market-liberal order emerge—based on liberty and justice for all.

The recent publication and popularity of a Chinese language edition of Hayek's classic book *The Constitution of Liberty,* now in its second printing, is a sign that the old top-down order of planning and control is slowly giving way to a new spontaneous market order of liberty and opportunity. People are beginning to recognize the need for adhering to universal principles of justice. Mao Yushi, director of the Unirule Institute in Beijing, told the *Wall Street Journal*, "We need to make everyone equal before the law and set the rules of conflict resolution." In his opinion, liberty, not democracy, should be the primary concern.[16]

The challenge for China is to allow liberty to grow by adopting constitutional constraints on government power. In the end, it must be the Chinese people themselves who will have to meet that challenge by ending the power of the party and securing the power of the people to choose their own institutions. That will not lead to chaos but to a new spontaneous order for China. □

1. "President Jiang Says China to Maintain Socialist Economy" and "President Jiang Calls for Another 100 Years of Communist Rule," Agence France Presse, in *Inside China Today*, December 18, 1998 (http://www.insidechina.com/china/business/news/98121801.html and http://www.insidechina.com/china/news/98121808.html).

2. Kate Xiao Zhou, *How the Farmers Changed China* (Boulder, Colo.: Westview Press, 1996), p. 4.

3. See Justin Yifu Lin, Fang Cai, and Zhou Li, *The China Miracle* (Hong Kong: The Chinese University Press for The Hong Kong Centre for Economic Research, 1996), pp. 132–33.

4. Deng Xiaoping, *Fundamental Issues in Present-Day China,* translated by the Bureau for the Compilation and Translation of Works of Marx, Engels, Lenin, and Stalin under the Central Committee of the Communist Party of China (Beijing: Foreign Languages Press, 1987), p. 189.

5. East Asia Analytical Unit (EAAU), *China Embraces the Market* (Barton, Australia: EAAU, Department of Foreign Affairs and Trade, 1997), pp. 10, 338. Hugo Restall estimates that "as many as 70 percent [of state-owned enterprises] are losing money" ("China's Long March to Reform," *Wall Street Journal*, September 23, 1997, p. A22).

6. See Steven Lewis, "Marketization and Government Credibility in Shanghai: Federalist and Local Corporatist Explanations," in David L. Weimer, ed., *The Political Economy of Property Rights: Institutional Change and Credibility in the Reform of Centrally Planned Economies* (New York: Cambridge University Press, 1997), pp. 259–87. According to Lewis (p. 283), "By the early 1990s, when surplus domestic capital could be moved between localities and banks more freely, and as central and local authorities began to decrease their monitoring of rural localities, thousands of non-sanctioned land development companies and 'development zones' had sprouted up around China."

7. Justin Yifu Lin, Fang Cai, and Zhou Li, "The Lessons of China's Transition to a Market Economy," *Cato Journal*, Fall 1996, p. 226.

8. F.A. Hayek, *The Constitution of Liberty* (Chicago: University of Chicago Press, 1960).

9. Roger Pilon, "A Constitution of Liberty for China," in James A. Dorn, ed., *China in the New Millennium: Market Reforms and Social Development* (Washington, D.C.: Cato Institute, 1998), p. 333.

10. Jixuan Hu, "The Nondesignability of Living Systems: A Lesson from the Failed Experiments in Socialist Countries," *Cato Journal*, Spring/Summer 1991, p. 44.

11. Pilon, pp. 334–41.

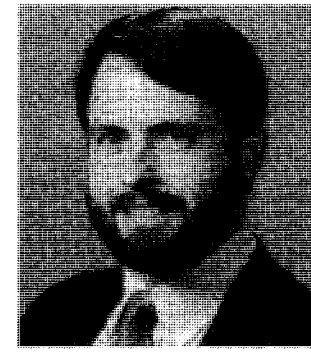
12. Nobel laureate economist James M. Buchanan has called "the principle of spontaneous order" the "most important central principle in economics." (In J. M. Buchanan, *What Should Economists Do?* [Indianapolis: Liberty Press, 1979], pp. 81–82.) It is the idea that individuals seeking their own gain in a system of private ownership and free markets bring about mutually beneficial exchanges, and that competitively determined prices coordinate economic decisions without central planning.

13. *Tao Te Ching* (the *Lao Tzu*), 57, in W.-T. Chan, *A Source Book in Chinese Philosophy* (Princeton, N.J.: Princeton University Press, 1963), pp. 166–67.

14. See James A. Dorn, "China's Future: Market Socialism or Market Taoism?" *Cato Journal*, Spring/Summer 1998.

15. See John Pomfret, "4th China Dissident Sent to Jail," *Washington Post*, December 28, 1998, p. A17.

16. "China Rediscovers Hayek," interview with Mao Yushi, *Wall Street Journal*, June 12, 1998.



Think Tank Wars and the Minimum Wage

True to form, Senator Edward Kennedy is pushing legislation to hike the minimum wage 41 percent, to $7.25 per hour by September 2002. President Bill Clinton has naturally jumped on the bandwagon, though he only wants to go to $6.15 an hour. He declared before last November's election: "We are fighting hard for the dignity of living wage [sic] in the face of partisanship that refused us last time."

But thanks to groups like the Employment Policies Institute (EPI), which regularly exposes junk research, the mirage that Uncle Sam can set wages without destroying jobs is starting to dissipate. Even some people who backed the raise three years ago are starting to have second thoughts.

Few economists doubt that artificially hiking wages lowers employment, since companies generally don't hire employees who can't earn their salaries. Scores of studies over the years have demonstrated the harmful employment effects of the minimum wage, though the magnitude of the job loss remains in dispute. Even former Labor Secretary Robert Reich acknowledged in a 1993 memo to President Clinton that "the potential effects of a minimum wage increase on employment should of course be weighed."

Four years ago Alan Krueger of Princeton and David Card of the University of California at Berkeley wrote a study arguing that a hike in New Jersey's minimum had actually increased employment. (Krueger and Card later reaffirmed their earlier conclusion, based on just three months of data after the 1996 federal wage hike took effect.) The counterintuitive study suffered from severe data problems, pointed out by EPI. Economist Finis Welch called the numbers "incredible." However, Senator Kennedy suddenly discovered the value of economic research and brandished the study at every opportunity. In 1996, an election-minded Congress raised the minimum.

In fact, it appears that the Pollyannas were wrong and the two-stage increase to $5.15 did cut employment. Overall employment has obviously increased in what remains a strong economy. But that jump came in spite of the rising minimum. The place where job losses typically occur is among the unskilled and ill educated, particularly blacks, teens, and female family heads. Alan Reynolds of the Hudson Institute found that six months after the 1996 installment took effect, unemployment rates rose in all three categories.

Moreover, EPI figures that the 1996 installment alone probably reduced the total number of jobs by about 380,000. The impact was particularly hard on teens, who found an estimated 128,000 fewer job openings. While overall employment rose, the rate for teens, especially black teens, fell. Today teen unemployment stands at about 17 percent, nearly four times the overall rate. Black teens have an unemployment rate of nearly 40 percent.

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Minimum-wage supporters reply with their own numbers, usually based on data choices that obscure employment changes. But even the most avid advocates of an increase flee from the logic of their position: if the minimum wage does not cut jobs, why not increase it by $100 an hour instead of just $2, as proposed by Kennedy, and make everyone rich? The reason, of course, is that he knows, and knows everyone else knows, that doing so would reduce jobs. Hiking the wage by less would eliminate jobs too, just not so many. A Heritage Foundation study figures that a $1 hourly increase would destroy 345,000 jobs in 2000. Overall employment would still rise, but not as much.

In fact, even Krueger now suggests caution. He explains that "David and I have said all along that there was a tipping point where a great enough increase in the minimum wage would start to reduce employment." He didn't think the economy was at that point in 1996. However, today he says, "I suspect now that another increase, coming quickly after the last one, would bring us closer to the tipping point and may even cross it." This defection has chastened Senator Kennedy—at least a little bit. "I am not ready to grant the job loss argument. But it is an argument that needs serious evaluation."

Such serious evaluation won't come from the Economic Policy Institute (EPoI), the labor-backed think tank that has long pushed for a higher minimum. EPoI's Jared Bernstein argues that raising the minimum would help "insure that low-wage workers get a fairer share of the economic growth."

How that would happen if they lose their jobs is unclear. So EPoI simply argues that wages have no impact on the employer's decision to hire. It is as if business were a charitable enterprise, hiring irrespective of productivity.

EPoI's research suffers from even more serious legerdemain than the Card-Krueger studies. In a 1997 report co-written by Bernstein, EPoI claimed that employment didn't fall after the 1996 hike. But it based that conclusion on just six months of data; researchers for the Employment Policies Institute found that adding just three more months of data reversed that conclusion. EPoI also contended that most of the gains from the 1996 minimum wage increase went to "the poorest 40 percent" of low-income working families. That sounds good, except for the fact that EPoI defined a "family" as just about anything, including a single person. And one could fall into the category of "poorest" American by earning up to $37,000. In fact, even using EPoI's curious methodology, two-thirds of the gain went to families with incomes above $25,000.

Baltimore's Preamble Center for Public Policy study, which cites the Card/Krueger and EPoI research (and which is also cited by Kennedy), is even more dubious. It allegedly analyzed a city ordinance (one of the nation's first "living wage" measures) that set a minimum wage of $6.10 (later increased to $6.60) for municipal contractors. Preamble declared that, magically, city costs fell by $500,000. Preamble relied on contracts that had been re-bid and others that were exempt from the ordinance. Had these effects been included, average costs would have risen.

There is an odd connection between these examples of bad research. Robert Reich was a member of EPoI's board before becoming secretary of labor in the first Clinton cabinet. He later hired Alan Krueger as his chief economist. EPoI's study was partially funded by the Department of Labor. EPoI and Preamble share the same research director, Mark Weisbrot, who happened to write Preamble's living-wage study. Organized labor helps fund EpoI, political supporters of the minimum wage, and living wage electoral campaigns. Indeed, it looks an awful lot like, well, a vast left-wing conspiracy.

Advocates of the minimum wage have not been able to repeal the law of supply and demand. If you make something more expensive, people demand less of it. And that includes employment.

Helping low-wage workers should be a priority. But the best way to help them would be to cut their taxes, reduce regulatory burdens on companies that would otherwise hire them, and allow them to pull their children out of failing public schools. Today Congress threatens to kill them with kindness. □

THE FREEMAN
Ideas On Liberty

The Commons: Tragedy or Triumph?

by Bruce Yandle

In the summer I watch ruby-throated hummingbirds fly and hover near a feeder that my wife, Dot, carefully fills with nectar and hangs in view of our kitchen window. The store-bought nectar is colored red, since people think that hummingbirds find that color attractive.

Business around the feeder picks up following rains that wash away the birds' naturally provided food. It is then that the feeder becomes crowded and a hummingbird struggle ensues. Almost always, there is at least one bird that attempts to control access to the feeder—what naturalists sometimes call a dominant male.

The dominant male seeking to maintain control will fly rapidly to the feeder, place his beak into the small openings for a quick draft of nectar, and then fly to a nearby perch where he vigilantly monitors the feeder. When other birds attempt to feed, he quickly tries to intercept and force them away from the stock of sweet food. But while he engages in dogfights with one bird, another often swoops in and takes its fill.

The feeder is a commons, but not just for hummingbirds. Bees are attracted to it as well, and oddly enough, they can drive off the larger hummingbirds. So even if the dominant bird is able to deflect competition from other members of the species, that is not enough to protect the nectar, and the defense itself is costly in energy burned. The feeder contents are never secure.

Hummingbirds have no way to stake a claim to the feeder. So far as we can tell, hummingbird communities have no constitution that reflects socially evolved rules for establishing a social order. Most likely, a long process of adaptation and selection has generated a hummingbird capable of living in a world where nourishment is a common-access resource, a commons. Hummingbirds live a life of flight, engaging in a constant search for nourishment to feed their high-energy lives and, at times, fighting for temporary control over valuable resources.

Human Commons

We all know the tragedy of the commons story. Wonderfully written by Garrett Hardin in 1968, the highly stylized rendering is about a pasture devoid of rules, customs, or norms for sharing.[1] It is open to all comers. In this never-never-land, shepherds logically add sheep to their flocks as long as doing so adds an increment of gain for the particular flock. Uncoordinated in their effort, and unaware of the effects of their individual actions on others, the unconcerned shepherds collectively destroy the pasture. What could be a story of

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plenty, if only the shepherds understood, turns into a story of poverty. The passive shepherds are like hummingbirds.

As Hardin artistically puts it: "Therein is the tragedy. Each man is locked into a system that compels him to increase his herd without limit—in a world that is limited. Ruin is the destination toward which all men rush, each pursuing his own best interest in a society that believes in freedom of the commons."

Garrett Hardin's words beautifully bundle aspects of an endless human struggle to form communities, accumulate wealth, and improve well-being. With that phrase—tragedy of the commons—the essence of the challenge hits us squarely between the eyes: When there are no property rights—formal or informal—that limit use of a scarce natural resource, human action leads inevitably to untimely resource depletion and destruction.

But people are not hummingbirds. People can build institutions that take the edge off frantic commons behavior. People have unwritten and written constitutions that help to establish social order. People can and do accumulate wealth. People communicate, invent lines of kinship, and develop customs, traditions, and rules of law that limit anti-social behavior. People define, enforce, and trade property rights. People can and do avoid the tragedy of the commons. Indeed, instead of living with tragedies, people triumph over the commons. But the triumphs are never perfect or complete. There is always another commons to manage.

The Ascent of Man

I wish to put forward the notion that encounters with the commons form the fundamental stimulus that yields, instead of tragedy, what we today call civilization. The ascent of man from a primitive existence with no wealth accumulation to life as we know it is fundamentally a story about triumph over, not tragedy of, the commons. Let me explain.

Our very existence as human beings is defined by evolved institutions for avoiding tragedies. We have names, which serve the economic purpose of identifying us as parties to contracts and agreements. Those names, first and last, form webs of communication that reduce the social cost of assigning responsibilities and liabilities. They enhance truth-telling and promise-keeping; they raise the cost of engaging in anti-social behavior. They limit a tragedy of the commons.

We have abstract symbols of ownership—deeds, titles, and contracts—that define spheres of autonomous behavior. We speak of our homes, our cars, our clothes, our families, and our pasture. Even language has evolved to provide a possessive form that accommodates triumph over the commons.

We write and observe contracts, wills, and marriage agreements that define relationships, identify turf, and conserve wealth. We accept evolved bodies of law and law-enforcement activities to assure the integrity of our agreements. We carry papers that enable us to acquire property, extinguish debt, cross borders, drive vehicles, and communicate effectively with strangers. And we have locks, keys, walls, fences, brands, and encryption devices, all this in an effort to avoid a tragedy of the commons.

Property rights define who we are and what we have. Property rights guard others from our unwanted advances and prevent us from contributing to a tragedy of their commons.

Avoiding a tragedy of the commons is costly. The benefits must be large.

How has it worked out? Mankind has triumphed over the path to ruin on the commons. Relative to that dewy time when nomadic tribes lived on the commons, we in the Western world live in a veritable Garden of Eden. The pastures are green. The sheep are fat. The clothes racks are full. Where property rights flourish, the choice of food is almost endless. We travel with ease to the four corners of the earth. We communicate electronically at practically no cost. Where is the tragedy of the commons?

The tragedy is found where for reasons having to do with power, intolerance, or cost, human beings have not yet defined private property rights. Or, as we shall see, where evolving property rights encouraged by man the institution builder have been destroyed. What was once a triumph can become a tragedy.

Tragedies Observed and Avoided

It is not difficult to find places where the institution builders have failed. Listen to the description of the situation of the world tiger population. "At the start of the twentieth century, wild tigers were widely distributed throughout Asia, ranging as far west as Turkey, as far north and east as southeastern Russia, and as far south as the Indonesian islands of Java and Bali. There may have been as many as 40,000 tigers in India alone, and the total population may have numbered 100,000 animals. Today, the largest estimate is that the total number of wild tigers is between 4,800 and 7,300."[2] What explains the demise? The same author provides an answer: "Command and control prescriptions for saving the tiger have largely failed because the people who actually determine the destiny of wild tigers have few incentives to save them. . . . We must convert live tigers from liabilities into assets." In short, property rights must be defined.

How might that be done? Consider the description of elephant populations in Kenya and Zimbabwe: In Kenya "poaching has reduced the number of elephants from 65,000 to 19,000 over the last 10 years. To stop the killing, conservation groups . . . called for a ban on the trading of ivory. But the evidence strongly suggests that the ban will only accelerate the destruction of African elephants. In Zimbabwe . . . where ivory trading is legal, the elephant population has thrived, growing at a rate of five percent a year."[3] Why? "In Zimbabwe the revenue from the tusks and hides and a portion of the money made from selling hunting permits go to nearby communities."[4] In short, ordinary people on the ground have a property interest in the elephants. They protect their assets.

What about fisheries? How can we avoid a tragedy of the commons there? Long before the Europeans arrived on the scene in the Pacific Northwest, Native Americans had figured it out. Small tribes in what is now Washington State had salmon fishing rights. Don Leal tells us that "in some cases, the tribe owned the rights; in others, families or individuals or a combination owned the rights."[5]

And what happened when the Europeans arrived? You guessed it. Leal tells the story this way: "Instead of recognizing the well-defined and enforced fishing rights, the U.S. government allowed newcomers to place nets across the mouth of the Columbia. This quickly depleted salmon runs, so traps and weirs were banned—only to be replaced by purse seine boats powered by internal combustion engines. The race to catch salmon moved to open waters. Ironically, from the country where private property is considered sacrosanct came a socialistic legal system driven by politics and military power."[6] What had been private property was turned into a commons. What had been an institution-builder triumph became a political tragedy.

But how can property rights to fish in the high seas be defined? Consider the story of Michael Markels, president of Ocean Farming, Inc. Ocean Farming is in the business of fertilizing the seas to enhance the growth of phytoplankton, which in turn nourishes fish production. Based on actual experiments, Markels estimates that with continuous fertilization about one thousand tons of catchable fish per square mile can be produced each year. "Therefore, 100,000 square miles of fertilized ocean should produce about 100 million tons of fish per year, about equal to the current annual world fish production."[7] So what? Is this all hypothetical?

Ocean Farming has now entered into a contract with the Republic of the Marshall Islands giving the firm an option on up to 800,000 square miles of deep ocean. "Once fish harvesting begins, Ocean Farming will pay RMI $3.75 per square mile of ocean optioned or 7 percent of the value of the catch, whichever is more."[8] In effect, 800,000 square miles of the Pacific Ocean has now been privatized. Ocean Farming can charge other companies to fish the waters, and the firm has agreed to allow artisanal fishing to continue.

Or consider the effort to conserve salmon made by Orri Vigfússon in his native Iceland.[9] Concerned about the systematic decline of the ocean salmon population in the face of rising



COURTESY PERC., BOZEMAN, MONTANA

Orri Vigfússon

demand for salmon sport fishing, Vigfússon in 1989 formed the North Atlantic Salmon Fund. Fishermen in Icelandic waters owned quota or rights to fish for salmon. Vigfússon began purchasing those rights and retiring them. His organization now owns the rights to 4,000 metric tons of quota from the high seas, which represent 95 percent of the exiting quota. The result: the demise of the salmon is ended, highly profitable sport fishing is flourishing, and the tragedy of the commons has been avoided. Oddly enough, Vigfússon's efforts to introduce a similar approach in New England, where unsuccessful efforts to restore wild salmon have been underway for 140 years, fell on deaf ears. Some might describe the New England situation as a tragedy of the commons. It is not. It is a tragedy of failed institution building.

Water and Air Pollution

What about water and air? Can the institution builders help us avoid a tragedy of the commons for these unowned resources? The answer is clearly yes, they can help, but the solutions are never perfect.

For centuries before anyone in the United States thought much about environmental quality, our common law defined and protected the environmental rights of ordinary people.[10] Enforced by judges in courts across the land, common law protected the right of downstream property owners to receive water and air in undiminished quality for reasonable use. At common law, rivers could not be treated as open sewers if doing so imposed costs on downstream rightholders. Industrial plants could not blow smoke and emissions onto the land and property of ordinary people. The record is filled with cases, here and in Canada, decided under English common-law traditions: where farmers sued industrial plants and won; where citizens of one state sued polluters in another state, and won; and where common-law judges ordered polluters to clean up or shut down. There are also cases where this did not happen, where judges turned away from property-rights enforcement and behaved as policy makers. But when the judges got it wrong, their decisions affected a small number of people, not an entire nation. This, of course, changed with the advent of legislation.

Prior to the passage of federal pollution-control statutes, every major city in the United States had taken steps to define public property rights to air quality. Many states, including California, had taken a river-basin approach to the management of water quality, this in addition to the use of common law. Multi-state compacts were forming. By the 1960s, environmental quality was improving rapidly in many locations. The property rights institution builders were on their way to avoiding a tragedy of the commons. Common law was converting the commons to private property.

This was changed with the passage of federal legislation that effectively nationalized air and water quality in the United States. What was becoming private property was made public property, almost a commons. The new system of command-and-control regulation allowed polluters to operate legally if they had a permit. With permits in hand, new polluters could enter already crowded river basins. The new regime provided political access to industries and municipalities that hoped to postpone the day of reckoning in common law courts. Environmentalists ran interference, since they typically preferred

political solutions to remedies based on property rights, markets, and the rule of law. A triumph on the commons was reversed. Tragedy once again reared its head.

On the frontispiece of Rachel Carson's epoch-making book, *Silent Spring*, one finds these words from Albert Schweitzer: "Man has lost his ability to foresee and forestall. He will end by destroying the earth."

Such pessimism expressed by such an imminent and sensitive thinker gives us pause. What was Schweitzer thinking about when he uttered those words so many decades ago? And how is it that at least so far, his damning forecast has not come true?

About a year ago, a colleague and I began an investigation of air and water quality for a sample of countries worldwide.[11] We gathered data on income, life expectancy, and property rights enforcement for 14 countries. Our results replicated previous work that showed a systematic relationship between improved environmental quality and incomes after a certain income threshold was passed. Our new finding was that where property-rights enforcement is stronger, environmental quality is better.

This work sheds light on mankind's struggle to avoid the tragedy of the commons. It tells us that at very low levels of income, what might be called stage one, human beings cannot afford to do much about property-rights enforcement and the commons. They live in a world where custom and tradition sustain them. As incomes rise and losses from the commons expand, stage two is entered. Fences go up, and rules are set for protecting the commons. Finally, in stage three, markets evolve along with rules of law that define spheres of private and public action. Private rights replace public control, and the triumph replaces the tragedy of the commons.

Life for mankind began on a commons where tragedies were commonplace and the incentive to improve was powerful. Out of the struggle to survive and accumulate wealth evolved markets, property rights, and the rule of law—a triumph on the commons.

But just as bees compete with hummingbirds in the struggle to control access to nectar, institution builders who seek to support markets and property rights compete with others who seek to redistribute wealth. Actions to redistribute wealth blunt the incentive to protect property rights and create wealth. This converts triumph to tragedy.

Human beings can and do avoid the tragedy of the commons. But doing so requires property rights and markets, which must be defended if the triumph is to continue. □

1. Garrett Hardin, "The Tragedy of the Commons," *Science* (162) 1968, pp. 1243–48; it's available at http://www.cs.colostate.edu/~heckendo/tragedy.html.

2. Michal t' Sas-Rolfes, "Who Will Save the Tiger?" PERC Policy Series, PS-12, February 1998, p. 2.

3. Terry L. Anderson and Donald R. Leal, *Free Market Environmentalism* (San Francisco: Pacific Research Institute, 1991), pp. 67–68.

4. Ibid., p. 67.

5. Donald R. Leal, "Community-Run Fisheries: Avoiding the Tragedy of the Commons," PERC Policy Series, PS-7, September, 1996, p. 4.

6. Ibid.

7. Michael Markels, Jr., "Farming the Oceans: An Update," *Regulation,* Spring 1998, p. 10.

8. Ibid.

9. Orri Vigfússon, "How Markets Save Salmon," *PERC Reports.* September 1998, p. 9.

10. Roger E. Meiners and Bruce Yandle, "Common Law Environmentalism," *Public Choice* (94), 1997, pp. 49–66.

11. Bruce Yandle and Xiang Dong Qin, *Environmental Kuznets Curves, Property Rights and Learning*" (Clemson, S.C.: Center for Policy & Legal Studies, 1998).

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THE FREEMAN
Ideas On Liberty

Economics

Second-Guessing the Market

by John A. Sparks

We commonly think of people below the poverty line as the only beneficiaries of welfare. But poor families are not the sole recipients of government money. Some of America's largest and most successful companies get welfare checks just as certainly as do millions of single mothers. General Electric, GM, DuPont, IBM, and Armstrong World Industries are just a few of the firms that have garnered government grants provided through the Department of Commerce under something called ATP, Advanced Technology Program.[1] The department has just approved another round of grants totaling $236 million for business-participants in 79 new research and development projects.[2]

The aim of ATP sounds laudable. It was created a decade ago to develop new technological ideas that could be used by U.S. businesses to make themselves more competitive on world markets. Under the program, firms file grant proposals with the National Institute of Standards and Technology (NIST), an arm of the Commerce Department. NIST selects the most promising proposals for federal money. Businesses winning grants must agree to risk some of their own money, usually an amount roughly equal to Uncle Sam's share.

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Winning Proposals

What kinds of projects command the federal cash? Here are some examples from the most recent awards. General Electric received over $1.5 million to develop "amorphous silicon devices" for use in medical imaging systems. It also got $482,000 to work on using synthetic sand to produce fused quartz, a component of semiconductors. A California outfit called DemoGraFx managed to win a $2 million grant, which it promised to use to develop systems that will help digitize motion pictures. Another business, Seaward International, Inc., will use its nearly $2 million to develop plastic railroad ties to replace the old-fashioned wooden creosote-soaked variety. Taxpayers also footed the bill for research and development work in the realms of microturbines, superfingerlings, spinal cord injuries, propane fuel cells, and a host of other endeavors.

Why do these companies need taxpayer money to further their research and development efforts? Recipient firms say that they would not be able to raise enough capital from private sources to finance such unproven ventures. DemoGraFx is typical. In its successful bid for government funds to finance research for digitizing theater films, it said that "the high-risk nature of developing a system that meets industry's needs for quality and security has deterred investment."[3] How does this claim stand up to economic analysis?

The economics of capital convertibility, which is what companies engage in when they consider new technological ideas, is relatively simple. Every kind of enterprise, from the simplest to the most complex, possesses capital goods (machines, tools, and equipment) that are based on certain technological ideas. As Ludwig von Mises pointed out, production is always being carried out with the "then prevailing ideas concerning ends and technological procedures."[4] However, new technological ideas are always surfacing that present the businessman with a dilemma: Should he continue to use existing capital goods to produce his product or service, or should he adopt the new technology and either scrap the old capital goods or use them less? Again, as Mises

argued: "The choice rests, as it always does in the market economy, with the consumers."[5] Will consumers recognize the superiority of new products promised by the advanced technology? Will they pay a price for the "new, improved" version that will be sufficient to compensate the businessman for the costs of the technological change? "The absence of a sufficient degree of superiority to make the cost of transformation possible," Mises wrote, "is proof of the fact that consumers are more intent upon acquiring other goods than upon enjoying the benefits of the new invention."[6]

Now back to the ATP applicants. Each business-applicant presumably went through its own internal review to determine if the response of consumers to the new technology would warrant the added capital investment in the idea. For example, the managers of DemoGraFx undoubtedly asked themselves how movie houses would respond to digitized motion pictures. Would they be especially attracted to the truer reproductions and to the reduction in fading over time? More importantly, would they pay enough more for the digitized copies to cover the increased capital costs? The answer to that question appears to have been no.

Undoubtedly, the other businesses that submitted requests for ATP funds went through similar calculations and came to similar conclusions. Their own boards apparently refused to use internally generated capital to bankroll the R&D projects at levels that would move them forward. If the firms then sought capital from outside investors, they too gave the research project a thumbs down—at least at the levels of funding sought.

Now, these facts reveal the first objection to ATP. Businesses that submit their ideas to NIST for financing present projects that they themselves have already determined to be *unpromising* according to ordinary market criteria.

Accelerating Development

But, counters NIST: "ATP support significantly accelerates potentially important R&D projects. . . . [A]ccelerated R&D is critical to eventual economic success in the highly competitive global market."[7] ATP does accelerate the research projects that receive the government money. However, this acceleration should not be confused with economic progress. The "acceleration" is not in response to true consumer demand. Neither is it consistent with the true costs of capital. The market counsels postponement of these projects until conditions of demand and cost are more favorable. ATP ignores this counsel and denies the true configuration of demand and capital costs. ATP nullifies the assessment mechanisms by which the rest of the business world determines which projects are worth pursuing. Therefore, ATP of necessity wastes precious capital on projects that applicants have already denominated as unripe, premature, and unsuitable for development at this time.

The second objection to ATP is related to the first. Not only is capital forced into projects that real-world conditions have branded as uneconomic, but that capital must first be confiscated from other citizens through taxation. To the extent that they win ATP grants, business firms make all U.S. taxpayers, including other small, medium, and large businesses, into unwilling investors in their shaky undertakings. The managers of the ATP recipient firms mentioned here would not think of taking funds by force directly from their fellow industrialists to help finance their research projects. Yet when they participate in ATP they are doing that by indirection and political means. □

1. Project Briefs describing each successful project by General Electric, General Motor, DuPont, Armstrong World Industries, and the other enterprises mentioned in this article can be found at the National Institute of Standards and Technology Web site at http://www.atp.nist.gov.

2. "79 New R&D Projects Selected for 1998 Advanced Technology Program Awards," http://www.atp.nist.gov/www/press/g98-74.htm.

3. "Integrated Layered Compression System Prototype: Project Brief," http://www.atp.nist.gov/www/comps/briefs/98040006.htm.

4. Ludwig von Mises, *Human Action* (New Haven: Yale University Press, 1949), p. 504.

5. Ibid.

6. Ibid., p. 508.

7. "79 New R&D Projects."

THE FREEMAN
Ideas On Liberty

Money in the 1920s and 1930s

by Richard Timberlake

One of the most enduring and troublesome mysteries in economics is money: how it is created, what sorts of institutions initiate the process, what kinds of mystique and priestcraft central bankers use in managing monetary systems, and what rules, laws, or customs limit their actions.

Perhaps the common ignorance about money is harmless. After all, the millions of people who use this money drive sophisticated automobiles and manipulate complex computers without knowing much about the technical properties of either. As long as cars, computers, and money behave themselves, can we perhaps ignore them? The answer is that we can for cars and computers but we should not for money.

For one thing, ignorance about money has side effects that are not comparable to ignorance about technical equipment. Competitive markets drive the production and sale of all household durables, but the production of money in every country in the world today (and yesterday, too) is the province of governments. Through the offices of their associated central banks, states monopolize the machinery of money. Each central bank determines within very close tolerances just how much money an economy has and the rate at which the current stock of money will change. Unquestionably and inevitably, political pressures that are rarely visible even to experienced observers influence these operations.

Because they have the power to create money without license, governments also have the complementary incentive to claim that depressions and inflations resulting from the mismanagement of money occur because of unusual and unexpected economic developments—"shocks," as they are labeled. The term implies a sense of impending and inevitable drama. No such social catastrophes result from the public's incomplete knowledge of computers and automobiles, nor of "shocks" that might affect their production and distribution. However, neither do governments monopolize that production and distribution, and therein lies the difference.

Fateful Decades

Nowhere is monetary ignorance more apparent than in bystander evaluations of the economic and monetary events of the 1920s and 1930s. Although several decades have passed, the various popular accounts continue to misinterpret the causes of the disequilibrium that occurred and also the federal government's aggravation of the problem. Government apologists of many persuasions not only argue that the massive interventions of the 1930s were necessary; they also contend that the lack of response in the private sector to the multitudinous government programs put into

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place proved that the economic system was moribund.

Nothing, they argue, could have prevented the debacle. They encourage the popular belief that the market economy zealously overextended itself in the 1920s. The boom, they contend, led to the stock market crash in 1929, and to the several banking crises of the early 1930s. These financial failures, the legend continues, provoked exhausting industrial liquidations, and the other devastations of the 1930s. The role that the central bank—the Federal Reserve System—and its managers played in the catastrophe of the 1920s and 1930s is largely unknown and therefore unappreciated.

Other observers, for example, many Austrian economists, believe that all the trouble started with a central bank "inflation" in the 1920s. This "inflation" had to be invented because it is a necessary element in the Austrian theory of the business cycle, which seems to describe most Austrian economic disequilibria. Austrian "inflation" is not limited to price level increases, no matter how "prices" are estimated. Rather, it is any unnatural increase in the stock of money *"not consisting in*, i.e., not covered by, an increase in gold."[1]

Once the Austrian "inflation" is going, it provokes over-investment and maladjustment in various sectors of the economy. To correct the inflation-generated disequilibrium requires a wringing-out of the miscalculated investments. This purging became the enduring business calamity of the 1930s.

The late Murray Rothbard was the chief proponent of this argument. Rothbard's problem is manifest in his book *America's Great Depression*. After endowing the useful word "inflation" with a new and unacceptable meaning, Rothbard "discovered" that the Federal Reserve had indeed provoked an inflation in the 1921–1929 period. The money supply he examined for the period included not only hand-to-hand currency and all deposits in commercial banks adjusted for inter-bank holdings—the conventional M2 money stock—but also savings and loan share capital and life insurance net policy reserves. Consequently, where the M2 money stock increased 46 percent over the period, or at an annual rate of about 4 percent, the Rothbard-expanded "money stock" increased by 62 percent, or about 7 percent per year.[2]

Here, Rothbard mistakes some elements of financial wealth with money. The latter two items he specifies as money are not money. They cannot be spent on ordinary goods and services. To spend them, one needs to cash them in for other money—currency or bank drafts. Increases in their quantity do not pervasively spill over into all other markets causing serious macroeconomic disequilibrium. Their appearance as financial assets in people's possession is just as likely to be deflationary as not, because their purchase and sale require money that would otherwise be used for transactions of conventional goods and services.

Apologists for central banking, by way of contrast, see stock market "speculation" instead of over-investment as the culprit. They argue that the Federal Reserve System did all it could to counteract the "inevitable" contraction that followed the 1929 stock market boom, but that its best effort could not be good enough. Since earnest and sophisticated men operated the federal government and the Federal Reserve System, something had to be wrong with the economic system itself. Markets just could not be trusted to provide full employment and steady real growth.

The Mismeasure of Money

Careful scrutiny of the monetary system and its associated monetary data reveals that neither of these views is analytically correct. Their defects result from ignorance of the flawed institutional framework within which the gold standard and the central bank generated money. Both also suffer from mismeasurement of the central bank's monetary data.

Four definable institutions created the money in use during the 1920s: the gold standard, the U.S. Treasury, the Federal Reserve System of 12 regional banks and the Federal Reserve Board in Washington, and the commercial banking system of 20,000-odd banks. These institutions were not created equal,

however. Only the gold standard and the Fed, with a notable assist from the Treasury, were important in initiating either monetary policy or the monetary happenings of the period. The commercial banks could only take what came their way from the central bank and the gold standard. They, too, created money. But their money-creating activities were all unintentional and strictly a byproduct of their lending operations.

The gold standard after World War I was anything but the autonomous, self-regulating institution that the Founding Fathers had prescribed—quite the contrary. The Federal Reserve Bank officers, particularly presidents, and the governors on the Federal Reserve Board, based then in the Treasury Building in Washington, exercised a monetary policy that often finessed the gold standard.

When gold came into the U.S. economy from a foreign country, importers deposited it in a commercial bank. The commercial bank in turn sent the gold to the regional Federal Reserve Bank to which the commercial bank belonged. The Fed Bank would credit the reserve account of this member bank, credit its own gold asset account by the same amount, and deposit the physical gold in the Treasury. If the member bank needed currency instead of an additional balance in its reserve account, the regional Fed Bank would issue its own Federal Reserve notes, dollar for dollar, based on the gold it had received. In either case, the Fed Bank was simply a monetizer of the gold. It converted the gold into dollars just as an ordinary commercial bank would have done in the absence of a central bank.

The monetary system thereafter had more dollars of bank reserves and deposits, or dollars of currency, because gold had come into the country. All other legal tender items, such as silver currency and greenbacks, were accounted in the Fed Banks in the same way as the gold. Fed Banks, therefore, were the custodians of a large fraction of the economy's basic money stock—the currency and bank reserves behind the checking accounts that households and businesses used for everyday transactions.

Blocking the Effects of Gold

Of course, the Federal Reserve System did not come into existence to be a custodian of the economy's base money and nothing else. The Fed Banks also had the legal power to create bank reserves and currency. Using the gold and other legal tender they held as *their* reserves, the Fed Banks could themselves become fractional reserve institutions. They could expand the reserves of their member commercial banks, or issue additional currency to them, by buying certain interest-earning "eligible" assets from the banks. If Fed Banks wished to block the effects of gold deposited with them to prevent the creation of common money based on the new gold, they could restrict their own lending to the commercial banks or sell off some of their interest-earning assets. Within limits, the Fed's money managers could deliberately and purposively supplement or counteract what the gold standard machinery did as a result of market forces. It was this particular machination to which Rothbard properly objected.

The Fed Banks' institutional authority derived from the Federal Reserve Act of 1913. The Act gave the Fed Banks the role of sequestering most of the banking system's gold, and the power, explained above, either to enhance or hinder the monetary effects of any incoming gold. At the same time, the congressional founders of the Fed saw the new institution only as a supplement to the official gold standard. In the Federal Reserve Act itself, they inserted a provision stating: "Nothing in this act . . . shall be considered to repeal the parity provisions [between gold and the dollar] contained in an act approved March 14, 1900." That referred to the Gold Standard Act, which made gold the sole legal tender monetary metal in the U.S. system. The new Federal Reserve System was supposed to act only within this official gold framework.

To show how the Fed's hands-on controls worked during the 1920s, I have constructed a table that summarizes the major monetary elements in the combined Fed Banks' balance sheet for the 1921–1933 period. It also includes the level of prices as measured by the Consumer Price Index (CPI).

The column labeled M1 measures the stock of common money—currency and checking account balances. From 1921 to 1929 this stock of everyday money increased on average 2.5 percent per year (compounded).[3] The column labeled "Total Fed" shows the Federal Reserve base on which this common money rested. Although this base increased slightly from 1924 to 1928, it *declined* over the whole eight-year span at an annual rate of 1.6 percent.

Fed-held gold and other reserve assets increased nominally at 1.1 percent per year primarily because of gold inflows. Federal Reserve policy prevented some of this gold from becoming a basis for new money by "sterilizing" it. That is, as the gold came into their tills, the Fed Banks allowed their holdings of other assets, which were primarily debts of the member banks, to decline: The member banks paid off some of their debts by reducing their reserve account balances at the Fed Banks. Changes in "net monetary obligations" of the Fed Banks (the column labeled "Net Fed") accurately reflects this deflationary policy. "Net monetary obligations" are total monetary assets minus gold and other legal tender reserves. This datum, which faithfully indicates the *intent* of Fed policy, *declined* at an annual rate of 8.0 percent over the eight-year period.

Fed policy successfully offset the gold inflows so that prices rose only slightly—0.5 percent per year for the eight-year period. This much of a change can hardly be labeled an "increase" because it is less than the statistical construction error of the index. One thing is certain: it was *not* any kind of an inflation. All the economic chronicles for the period, besides the monetary data, confirm that Fed policy was braking against possible gold-inspired price increases in the United States. The Fed's primary purpose was to further international monetary policies, particularly to help the Bank of England achieve and maintain gold payments for the pound sterling—but that is another story.

In their *Monetary History of the United States,* Milton Friedman and Anna Schwartz conclude their summary of the monetary events of the 1920s with this paragraph: "Gold movements were not permitted to affect the total of high-powered money [bank reserves and currency]. They were . . . sterilized, inflows being offset by open market sales, outflows by open market purchases."[4] They observe further: "The widespread belief that what goes up must come down, . . . plus the dramatic stock market boom, have led many to suppose that the United States experienced severe inflation before 1929 and [that] the [Federal] Reserve System served as an engine of it. *Nothing could be further from the truth.* By 1923, wholesale prices had recovered only a sixth of their 1920–21 decline. From then until 1929, they fell on the average of 1 percent per year. . . . Far from being an inflationary decade, the twenties were the reverse. And the Reserve System, far from being an engine of inflation, very likely kept

Money, Monetary Assets, and Liabilities of the 12 Fed Banks, and Prices (1947–49=100), 1921–1929, and 1929–1933

Years	M1	% yr.	Total Fed	% yr.	Fed Gold	% yr.	Net Fed	% yr.	Prices
1921	21.0	—	4.79	—	2.63	—	2.16	—	76.4
1929	26.2	2.5	4.25	–1.6	2.86	1.1	1.39	–8.0	73.3
1933	19.2	–9.1	5.63	8.1	3.56	6.1	2.07	12.2	55.3
($ billions, except prices)			**(a)**		**(b)**		**(c)**	**note: (a) = (b) + (c)**	

the money stock from rising as much as it would have if gold movements had been allowed to exert their full influence."[5]

Ironically, the Federal Reserve System that has provided itself in recent decades with the well-deserved label "engine of inflation" was in the 1920s an "engine" preventing gold inflation. Any gold inflation would have been very mild; so the question of whether Fed policy was proper is arguable—until we look at what happened afterward.

Given that its intervention prevented a minor gold inflation, did the Fed then reverse itself as bank failures occurred and economic contraction threatened? Following approved central bank doctrine, did it lend freely during the ensuing contraction at stiff interest rates until its remaining gold reserves would not have been enough to plate a teaspoon?[6] Let's see what happened.

Disaster Hits

As everyone knows, the following four years, 1929–1933, were a deflationary disaster. Not quite so clear is what the Federal Reserve did, or, more important, did not do during that time. Fed spokesmen have often alleged that the Fed tried "everything in its power" to turn around the contraction, and that it used its gold reserves to their utmost. Again, nothing could be further from the truth.

By 1929, the Fed's monetary liabilities—commercial banks' reserve-deposit accounts in Fed Banks, and the public's holdings of Federal Reserve currency—were $4.25 billion. These monetary items exceeded the Fed's gold asset holdings by only $1.39 billion. Put another way, the gold that came into the Fed Banks, which the commercial banks would have held in the absence of a central bank, was $2.86 billion. Federal Reserve policy actions had created the remaining $1.39 billion. By August 1929, the Fed's gold and other reserves had grown to $3.12 billion (not shown in the table). The Federal Reserve Act required half these gold reserves to back outstanding Fed liabilities, but the other half of them, $1.56 billion, were "excess" and available for whatever monetary purposes the Fed managers thought appropriate.

During the following three-and-a-half years, the Fed Banks' managers continued to build up the Fed Banks' gold holdings—even as the financial system spiraled downward as a result of three serious banking crises. By February 1933, owing to the Fed's tight money policy, the economy was in shambles and constricted to the point of monetary suffocation. The Fed Banks' gold stock had *increased* to $3.36 billion, and "excess" gold reserves were still $1.35 billion! (The higher figure in the table is for June 1933.) This damning statistic is seen in the column labeled "Fed Gold." While the Fed had enjoyed an increase of $700 million in its gold and other reserve holdings, its monetary output had increased by only $680 million: Commercial banks had $20 million *less* in reserves than they would have had with no Federal Reserve System.

This statistic, however, is not the end of the story. Since total commercial bank reserves were $2.29 billion in February 1933, the $1.35 billion of excess gold reserves Fed Banks held could have enhanced the banking system's reserves by another 60 percent—to $3.64 billion.

"Real Bills Doctrine"

The Fed Banks were truly absorbers of gold. They simply extended and intensified the tight money policy they had begun in the 1920s, but for a different reason. Instead of helping the Bank of England return to a gold standard, the Fed managers had become enthralled with the idea that production of goods and services initiates and promotes the production of money. Economists sometimes refer to this as the "real bills doctrine." While it has a grain of truth in it when a true gold standard is in place, it has no validity at all in a system dominated by a central bank. With this flawed doctrine governing their thinking, the Fed Banks' managers marked time waiting for new production to appear so that they could in good conscience expand their monetary obligations in support of the private economy.

It never happened.

The U.S. banking system went through three serious contractions and the money

stock continued to shrink. By 1933, the M1 and M2 money stocks were 27 percent and 25 percent below their 1929 levels. Meanwhile, the Fed Banks sat on their huge hoard of gold—the gold reserves legally required for their current monetary output and the "excess" gold reserves that could have provided significant monetary increases—and did . . . nothing!

Truly, when such a crisis appears, *all* the central bank's gold is excess. A proper central bank can never be faulted for "running out of gold." If the Fed Banks had followed the established (Bagehot) doctrine of the time, they would sensibly have expanded their loans, discounts, and accommodations to their "member" banks until their gold stock was a cipher.

Of course, they would not have had to run their gold reserve ratio down to zero. Long before they had expanded or used up their gold reserves, the crisis of central-bank mismanagement would have ended (or, more probably, would never have begun). The economy would have been back to normal, and none of the ugly governmental machinations of the later 1930s would have occurred. No Supreme Court conflicts would have appeared; no New Deal bureaucracies would have emerged to plague the economy; the Leviathan would have been kept in its constitutional cage. Most important, many of the freedoms we are now trying to restore would still be commonplace.

One would think that with this experience behind them, the "monetary authorities" and the congressional wheelers and dealers would have learned some lessons about U.S. monetary machinery and its relationship to the economy. They did not.

Next month I will treat the reserve requirement debacle of the mid-1930s, which added additional travail to the monetary mistakes made in the early part of the decade. □

1. Murray N. Rothbard, *America's Great Depression* (Kansas City: Sheed and Ward, 1963, 1972), p. 87. Emphasis in the original.
2. Ibid., p. 88.
3. The M2 money stock, which includes all of M1 plus time deposits at commercial banks, increased 5 percent per year from 1921 to 1929, and then fell at 13 percent per year from 1929 to 1933. No basis exists for a more inclusive money stock than M2.
4. Milton Friedman and Anna J. Schwartz, *A Monetary History of the United States, 1867–1960* (Princeton: National Bureau of Economic Research and Princeton University Press, 1963), p. 297.
5. Ibid., p. 298. Emphasis added.
6. This well-understood doctrine for central bank procedure was proposed by Walter Bagehot in his classic work, *Lombard Street*, rev. ed. (London: Kegan, Paul, Trench, Toubner & Co., 1906 [1873]).

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Inscrutable Follies

"Don't bother to examine a folly—ask yourself what it accomplishes."

—AYN RAND, *The Fountainhead*

Pardon if I sound like a character out of Dostoyevsky, but is it a sign I am mad when I am unable to understand what should be a simple newspaper article about taxing and spending in Washington?

A *New York Times* article on January 15 began: "The Clinton administration plans to propose a federal tax increase of 55 cents a pack on cigarettes to help pay for new domestic and military spending programs, White House and congressional officials said on Thursday."

The tax increase is estimated to yield $8 billion a year. Tax revenues have been rising 8 percent a year since 1992, but that's not enough for the people who spend our money for us.

That sentence was followed two paragraphs later by this: "The president has not announced how he intends to pay for these programs, promising that the details would be provided in the budget he submits to Congress on Feb. 1. But the White House has long signaled its intention to seek more money from tobacco, and officials confirmed a report in the *Wall Street Journal* on Thursday that Clinton will propose the tobacco tax, which is now at 24 cents, as part of a package of tax increases and loophole-closings that it intends to push to pay for new programs."

I guess a distinction can be made between "White House officials" saying something and a presidential announcement to the same effect. In Washington the trial balloon is a common device for testing the reaction to proposals before anyone is publicly committed to them. It makes sense to use trial balloons, considering all the surplus hot air they have there.

Nevertheless, this is unnecessarily confusing. Does Clinton favor raising tobacco taxes to pay for new government spending or not? Of course he does.

The *Times* goes on to say: "Clinton plans to discuss in the State of the Union address next week his administration's efforts to reduce smoking by teenagers, including the proposed tax increase to make cigarettes too expensive for some potential smokers."

Here we go again. Is the tax supposed to raise money or isn't it? If it discourages smoking, how can it finance new spending? The administration won't say, and the reporters don't even bother to point that problem out. They accept the contradictions and pass them along to us, assuming we won't notice.

Incidentally, if it's so terrible for tobacco companies to profit off people's lethal habits, why isn't it just as terrible for politicians to do so?

Sheldon Richman is editor of The Freeman.

The article then broadens its focus from tobacco to the budget in general: "Despite growing federal budget surpluses—Clinton announced earlier this month that the government would take in at least $76 billion more than it spends this year—the administration has been forced to scramble to come up with money to pay for a long list of initiatives that it will include in the budget proposal it will send to Congress."

Translation: The government can never have enough money. Reports of the death of big government have been greatly exaggerated. And by the way, if you exclude the Social Security accounts, there is no surplus. The budget will be in deficit at least through 2001. The surplus is the result of the onerous FICA tax (for Social Security and Medicare), which exceeds 14 percent and is applied to more and more of our income each year. The proceeds not needed to pay retirees are used for general government spending. In a couple of decades, with the retirement of the baby boomers, that surplus will turn into a deficit.

The *Times* explained that "the administration is the victim of its own success" in that Clinton and the Republicans agreed to protect the surplus pending a solution to the coming Social Security bankruptcy. "Moreover," added the *Times*, "both Congress and the administration remain bound by budget rules that presumed the government would always run deficits."

The *Times* implied the agreement not to touch the Social Security surplus was kept. Not so, as the astute James Glassman pointed out: "last year we got a good demonstration of what politicians of both parties do with a surplus. They spend it—often on pork-barrel projects such as the highway bill or on subsidies to favored groups such as farmers. . . . In his State of the Union address [in 1998], President Clinton said he would reserve 'every penny of any surplus' for Social Security. Instead, joining with Republicans, he boosted federal spending by an extra $20 billion, getting around budget rules by calling the new outlays an 'emergency.'" In other words, they lied—well, misled us.

The *Times* and Glassman both mentioned the budget rules. They deserve some attention.

From the *Times* story: "Those rules impose tight spending caps. . . ."

Obviously not tight enough if new spending can be exempted merely by labeling it "emergency." Nevertheless, the *Times* informed us that "The spending caps for next year are about $30 billion less than Congress would need to pay for all current programs—never mind any new ones [!]—and politically palatable sources of new revenue are scarce."

So the budgeters should be cutting spending, right? Guess again.

The rules, continued the *Times*, "require that any tax cuts or credits be offset by corresponding tax increases." Come again? All tax cuts must be offset by tax increases? This is where I really begin to feel I'm in the Twilight Zone. Who came up with these rules? Do they take us for fools? The state giveth, the state taketh away—simultaneously.

One more passage from the *Times* article: "In addition to the tobacco tax, Clinton plans to include a number of other proposals to close corporate tax loopholes or otherwise squeeze more revenue from the tax system, even though Republicans routinely denounce them as dead on arrival. But in the end, the proposals allow Clinton to say he is submitting a balanced budget that sets out his policy agenda."

"Closing tax loopholes" is a euphemism for raising taxes. Business, goes the old saw, doesn't pay taxes; it collects them. Thus, *we* are to be imposed on further by the government's voracious appetite for revenue. But we won't notice. And the budget will be in balance—if you hold the mirrors at just the right angle.

Government goes to great lengths to shroud its activities, and the national media are partners in the crime. They may focus on scandal and undo a rogue from time to time. But essentially they are conspirators in the building and maintenance of the consensus interventionist government requires.

Making sense of what government is up to is wearisome, which is the point. The proprietors of the budget don't want us looking over their shoulders. What shepherd ever wanted advice from his flock? □

THE FREEMAN
Ideas On Liberty

James F. Lincoln: Industrial Peacemaker

by Daniel Hager

The dichotomy between labor and management does not actually exist. Enlightened self-interest eliminates contentious factionalism in employment relations. Unfortunately, government has intervened in the workplace to convert it into a battleground and to institutionalize coercive conduct that is akin to warfare. The victims are consumers and the entire American economy.

Those were the views of an industrialist named James F. Lincoln. He applied what he termed "incentive management" in building the Lincoln Electric Co. of Cleveland, Ohio, into the world's largest manufacturer of arc-welding equipment. Lincoln Electric was a provider of top-quality products at prices that undercut the competition. Nevertheless, it paid its workers at about twice the average wages in the overall industrial sector and weathered the New Deal.

Lincoln, who died in 1965 at the age of 82 and hence was spared the Great Society's additional hamstringing of employers, was as harsh on "ultraconservative" industrialists who saw workers as adversaries as he was on misguided government. His management philosophy combined the Golden Rule with athletic metaphors. As he explained in his 1961 book, *A New Approach to Industrial Economics*, application of the Golden Rule leads to the type of cooperation that characterizes successful athletic teams, where the coaches and players are not antagonists but all pull together for the common goal of victory.

Everyone's a Manager

In any organization everybody actually embraces both management and labor functions: "All are managers when they operate a machine, an assembly line, a broom, or a punch press, or when they manage the financial, economic, and social activities of the company. All also are labor. Some operate machines, some operate assembly lines, some operate brooms, and some operate the activities with government, with sellers, with buyers, and with the public. There can be no dividing line drawn between them. All are essential to the business and are complementary in their work."[1]

Lincoln learned about individual development and voluntary cooperative accomplishment while studying electrical engineering and playing football at Ohio State University, where he captained the undefeated 1906 team. The next year, he became a salesman at the small struggling electrical company managed by his brother, John C. Lincoln, a better engineer than businessman. In 1914 at age 31, James Lincoln moved up to general manager of Lincoln Electric and later became president. He solicited employees for advice believing that no one person can know everything and that others have much to contribute.

Development of employees' talents became his goal, based on the foundation that "free-

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dom of the individual is essential. Freedom means responsibility. It means opportunity. It means pride in ourselves and the place that we have created for ourselves in the world. No free man ever allowed himself to infringe on the rights of others."[2]

His strategies excluded production speedups and even conventional profit-sharing plans, which depend on too many factors beyond the control of individuals to provide them incentives. The *New York Times* obituary quoted Lincoln's core policy: "There is no limit to the production capacity of a human being. The worker who is assured the fruits of his labor will find a thousand and one ways to increase production."[3] The workers themselves devised methods to improve productivity and reduce costs and benefited directly from their efforts.

The system of rewarded innovation worked so well that the labor required to produce a 200-amp welding machine dropped from about 113 hours in 1921 to about 16 in 1944. The selling price fell from $1,500 to $200. Between 1932 and 1943 worker productivity increased almost 13 times. Wholesale prices of manufactured goods rose more than 40 percent over that span, but prices of Lincoln's arc welders were cut in half or more.

Lincoln said that "The goal of an organization must be this—to make a better and better product to be sold at a lower and lower price. Profit cannot be the goal. Profit must be the by-product."[4] His company paid liberal dividends throughout the Depression and laid off no workers. Work stoppages were inconceivable, even in the post-World War II era when strikes by organized labor became an everyday occurrence. Lincoln Electric's productivity per worker and annual worker compensation were about double the entire manufacturing sector following the war.

Sued by the Government

During the New Deal, when corporate taxes were high and personal income taxes still low, the federal government sued Lincoln Electric on grounds it paid its employees too well. The case dragged on through the war years. Lincoln asked if the firm would have been sued if it had twice as many employees producing



James F. Lincoln

equal output at half the pay. When he was told no, he countered that the "crime" for which he was being fined was that he had freed up 2,500 people to work in the war effort elsewhere.

Government interference crimps productivity and creates poverty, as further exemplified by the Wagner Act, Lincoln noted. He described collective bargaining as "civil war." In contrast to incentive management's cooperation, under the Wagner Act "government sets up on one side of a table a group of people called 'management,' on the other side a group of people called 'labor,' orders them to fight until one or the other gives in and signs a contract dictated by the winner. . . . The fact that a conflict is forced by the philosophy of collective bargaining dooms the result to failure. . . . Cooperation is killed in the struggle and progress of the company is stopped. There has never been any collective-bargaining fight that did not end with higher cost of production. There has never been a collective-bargaining fight that did not result in a loss to the consumer."[5]

A coercion-free operation that respects all its individuals reduces costs and prices, and thereby benefits consumers, including workers. The worker who wins in a collective-bargaining war may benefit temporarily but soon needs higher wages again because lack of productivity reduces his own purchasing power. Those outside the direct scope of the bargaining war are the real victims: "Here, as is always true in war, the civilian population is overrun and suffers more than the armed forces involved in actual combat. There is no

protection for the innocent bystanders in war or in the Wagner Act. . . . As the costs of the standard of living go up and jobs decrease, as they must, unrest is sure to develop. Those at the bottom of the economic ladder suffer first. Shortly thereafter, all are involved. Government then steps in, as it must under the present philosophy of government, as a provider of a standard of living for the unfortunate. This still further upsets the economic machine, and we have still higher costs because of the increased taxes and governmental interference. There are hence still fewer jobs, more government help to the needy, and hence still more need."[6]

"The essential for success is cooperation," he wrote.[7] An orphanage can efficiently feed, clothe, and house children and may even exceed parents' abilities in those respects. But it does not succeed in rearing children as well as the home does because "the essential that is left out is the friendly cooperation that is obtained in the successful family. This cooperation cannot be commanded, it must be spontaneous. It cannot be a matter of law, it must be a matter of desire."[8]

Lincoln foresaw in 1946 that government-mandated coercion in the labor arena would deteriorate American manufacturing competitiveness and price the nation out of significant world markets. In his last two books he acknowledged the intellectual debt he owed to Rose Wilder Lane and Dr. Frank Halliday Ferris. His company has remained successful by continuing to adhere to his principles, despite the obstacle of ever-greater encroachment of government into workplace relations. □

1. James F. Lincoln, *Lincoln's Incentive System* (New York: McGraw-Hill Book Company, Inc., 1946), p. 95.
2. Ibid., p. 38.
3. *New York Times*, June 24, 1965, p. 35.
4. Ibid.
5. Lincoln, pp. 95, 97.
6. Ibid., pp. 98–99.
7. Ibid., p. 103.
8. Ibid., p. 101.

Inspired? Shocked?
Delighted? Alarmed?
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THE FREEMAN
Ideas On Liberty

Withholding the Taxpayer Hostage

by Donald J. Boudreaux and Andrew P. Morriss

How often have you heard people say with pleasure, "I got a tax refund this year!"? Americans have grown so immune to income-tax withholding that many people regard IRS refunds as gifts. Misperceptions about withholding are widespread. In fact, withholding is a regressive, costly, and furtive system for collecting taxes.

Fifty-six years ago Congress approved the current system under which a sum is withheld from each paycheck and deposited with the government, with taxpayers and the government settling accounts once a year when tax returns are filed. According to Milton Friedman, who helped create the withholding system as a young economist in the Tax Research Division during World War II, withholding was justifiable during the war because it raised revenue for the war effort that could not have been raised otherwise.

Is Withholding Justified?

What justifies withholding during peacetime? Withholding is said to have three advantages over a system in which taxpayers pay their tax bills annually in one lump sum. First, withholding guards against the threat that people will have too little money on hand to pay their taxes. Some congressmen even argued in 1942 that withholding was necessary to protect taxpayers from loan sharks at tax time! Second, because it reduces current disposable income, withholding is said to be anti-inflationary. Third, withholding smoothes the government's revenue stream, making government spending simpler.

None of these goals requires that employees who have taxes withheld not be compensated for lost interest. The government could do this simply by paying interest on the money withheld. This is not a new idea. In 1912, the federal government experimented with interest-bearing tax-anticipation notes; the secretary of the Treasury sold the first note to President Teddy Roosevelt. Flaws in the design of these notes doomed them to failure, but the principle remains correct—early payment of taxes ought to be compensated by the payment of interest.

Expensive and Regressive

Withholding costs taxpayers a great deal of money. With some back-of-the-envelope calculations based on IRS data, we estimate that since its inception in 1943 withholding has taken over $400 billion (calculated in 1995 dollars) in interest from taxpayers. In a single year withholding costs the average worker over $100 in forgone interest.

Not surprisingly, withholding also unfairly penalizes wage income relative to non-wage income. Consider two couples, Ted and

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Tammy Toiler and Pierre and Priscilla Plutocrat. Both couples have annual federal tax liabilities of $10,000, and both structure their withholding and estimated tax payments so that they legally minimize the amounts they pay to the IRS before April 15. The only difference between these couples is that the Toilers just have wage income and the Plutocrats live exclusively on investment income. Thus the Toilers have taxes withheld from their biweekly paychecks while the Plutocrats make four estimated tax payments a year. Using a 4 percent interest rate, at the end of the year the Toilers' lost interest from withholding (about $273) is 17 percent higher than the Plutocrats' lost interest (about $234). This disparity in tax treatment is caused by the government's holding more of the Toilers' money for a longer time than it holds the Plutocrats' money.

Such disparities are rampant in our tax system. Procedural quirks and unintended consequences result in radically different tax rates for similar amounts of income based on the source, the taxpayer, and, for all we know, the phases of the moon. There is no rational basis for applying a higher implicit tax to wage income than to non-wage income. A business that behaved in a like fashion, randomly charging some customers higher prices for example, would quickly go out of business. The great "advantage" of government for the tax and spend crowd, of course, is that it short-circuits the market forces which penalize irrational behavior by private businesses.

Deceived Taxpayers

The withholding tax is also a potent cause of fiscal illusion among taxpayers. Rather than write an annual check to the government for the full amount of their tax bills, most taxpayers on April 15 either send in a claim for a refund or pay only a small fraction of their taxes. In his 1989 book, *A Law Unto Itself: Power, Politics and the IRS*, David Burnham recounts a Harvard Medical School faculty member's confession that he hardly notices his paycheck deductions. Burnham reports that accountants and tax lawyers now find that large numbers of taxpayers no longer view the IRS "as a hard-nosed tax collector" but rather as "a benevolent bureaucracy that gives away money to the needy middle class." Thus, because taxpayers have become immune to the full magnitude of the tax bite, government growth is greater than it would be if there were no withholding or if withholding were less clandestine.

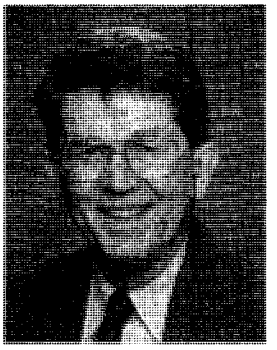
A Proposal for Reform

The best plan would be to abolish the income tax altogether. Until we can do so, however, the government ought to pay interest on money withheld as well as on estimated tax payments from the date of deposit of these sums with the Treasury. Short-term T bills provide a market rate of interest that can be easily used; a few lines of computer code can perform the calculations necessary to credit this interest to the "Amount Withheld" boxes on the W-2 forms employees receive at the end of the year.

Moving one step further to cure the problem of the disguised cost of government is almost as easy. Employers can deposit withheld tax payments (income and Social Security) into interest-bearing tax escrow accounts from which the government can borrow at T-bill rates. These accounts could then be released to employees before taxes are due. The government would be assured that individual taxpayers have the funds available to pay their taxes, while taxpayers would experience the full cost of Washington's operations. Adoption of this proposal might significantly restrain the growth of government spending by erasing the fiscal illusion caused by the current withholding scheme.

Genuine fairness requires reform of the regressive and deceptive system of tax withholding. Championing reform of the existing withholding system promises to be a good first step for politicians who regard fairness as something other than a slogan for use in class warfare. □

Economics



Opportunity Cost and Hidden Inventions

Few people think about opportunity cost as systematically as economists do, but all of us are constantly guided by the opportunity costs we face. If, as you are reading this article, you learn that someone a few blocks away is giving $1,000 to anyone who comes by, I predict with confidence that you will quickly stop reading because of the cost of continuing. Unfortunately, we commonly accept arguments that would make sense only if people ignore the opportunity costs of their decisions.

Hidden Inventions

A persistent claim is that in market economies where the profit motive reigns supreme, extremely valuable inventions are hidden to prevent their sale. Supposedly, if the inventions were available they would destroy the profits of big corporations by making their products obsolete. So these corporations buy up wonderful inventions to make sure we can't buy them.

That an amazing invention has never been found in some secret warehouse does nothing to reduce people's belief that such things exist; they're hidden, aren't they? The reality is that the opportunity cost of hiding a valuable invention is so great that inventions worth more than they cost are quickly made available. Hidden inventions exist only in economically uninformed imaginations.

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The Hidden Carburetor

A popular hidden-invention claim concerns a carburetor that would greatly increase the gas mileage of ordinary automobiles. Assume that while tinkering in your garage you develop a carburetor that allows the heaviest car to get 150 miles per gallon—your mileage may vary slightly, depending on how you drive. Would you hide this invention? Surely not, because the opportunity cost would be enormous. The cost would equal the amount someone would be willing to pay for the rights to the carburetor. And who would offer you a lot of money for your invention? When I ask students this question, the answer is, usually, a big oil company. When I ask next what the oil company would do with the carburetor, the answer is, invariably, hide it.

The trouble with this answer is that it assumes the oil company ignored its opportunity cost after buying the carburetor. Sure, if the carburetor were sold, the oil company would lose some gasoline sales. But if the carburetor proved socially valuable—costing less to produce and use than the cost of the gasoline saved—it would be profitable for the oil company to sell it anyway. Remember, with a patent the oil company could acquire a monopoly on the carburetor for 17 years and charge a price about equal to the amount the buyer saves in gasoline purchases (the present value of the savings over the life of the carburetor).

So even if only the oil company lost gas sales because of the carburetor, its revenues

would not be reduced and its profits would increase as long as producing the carburetor cost less than producing the gas it saves. Since some, probably most, of the lost gas sales would be those of other oil companies, the profits from making the carburetor available would be even greater.

Of course, once the carburetor was on the market the patent might not be enforced perfectly as competitors offer substitutes. In any event, the patent would eventually expire. Then competition would drive the carburetor price down to near the cost of production, and the oil company's profits might decrease. But trying to hide the carburetor would still be a mistake.

First, the immediate increase in profits the carburetor would generate for a few years could easily be far more valuable than the future profits lost. Second, if the oil company didn't make the carburetor available, some other company (not necessarily an oil company) surely would. Then the profits from oil sales would be lost anyway, without the offsetting profits from carburetor sales. There are real profit advantages in being the first to market a new product or invention: getting the immediate patent-protected profits and establishing a reputation for providing a quality product that is valuable after the patent has expired.

However, not all inventions that do amazing things get to market. For example, in the 1930s a Mr. Pogue invented the Pogue carburetor, which greatly increased mileage by heating and vaporizing the gas before it went into the combustion chamber. Unfortunately, the carburetor had a tendency to explode, so some of the improved mileage was straight up. This invention was more costly to use than it was worth, so there was no opportunity cost to "hiding" it.

Light Bulbs and Tires

Other inventions commonly claimed to be hidden are long-lasting light bulbs and tires. Indeed, light bulbs and tires can be made to last longer than most of those we buy. But the problem isn't that such products are hidden. For example, light bulbs can be made to last indefinitely by increasing the thickness of the filament inside. Unfortunately, the thicker filament requires a lot more electricity. So there's a tradeoff between durability and electricity usage, and the market responds to people's desire to make such tradeoffs in sensible ways. Light bulbs that are relatively easy to change do not last as long as those that are difficult to change, such as those in refrigerators and in high ceilings. Also, when it would be dangerous for lights to go out frequently, as in automobile headlights, the bulbs are built to last a long time.

Similarly, tires can be made to last longer, but they would be more expensive, less comfortable, and often less safe. The market responds to the tradeoff people choose among cost, comfort, safety, and durability, so the tires on the family car are not as rugged as the ones on heavy earth-moving equipment.

It should be pointed out that light bulbs and tires of all types last longer than they used to. Better ways of making economical light bulbs and safe, comfortable tires have been developed, and the opportunity cost of hiding those improvements in the form of forgone profits made sure they were brought to market.

Given the proliferation of new products and innovations in recent years, some of which threatened large and profitable companies like IBM and AT&T, it is hard to understand the persistent belief that valuable inventions are being hidden. If an economic system based on the pursuit of profit caused valuable inventions to be hidden, then great products unavailable to Americans should have been plentiful in the former Soviet Union, where profit didn't guide economic activity. But as everyone should realize by now, it has been the other way around. Wonderful products and innovations that Americans take for granted were unavailable in socialist economies.

This is not surprising. By suppressing profits, socialism reduces the opportunity cost of keeping new products out of the hands of the public, whether by design or by default. As long as we allow the pursuit of profits in the marketplace, the cost of hiding new socially valuable inventions will be so high that we don't have to worry that they will be hidden. □

THE FREEMAN
Ideas On Liberty

I Lost My Job—Can I Keep My Principles?

by Mark Reboul

I accidentally discovered a great party trick: Get laid off from your job, tell someone about it, listen to them decry capitalism, wait for them to observe that you're entitled to collect unemployment, and then tell them you'd really rather not.

It is incredible how indignant some people become when they hear me say that. They don't even ask why I might want to stay away from it. They just keep saying over and over again, "Mark, it's *your* money. Don't you understand, you're *entitled* to it. Your employers have been paying in for you for all the years you've been working, and now it's time for you to collect!"

If I give even a vague response like, "I don't want to deal with the government unless it's absolutely necessary to stay out of jail" or, "I really don't like filling out forms," they get madder and madder, not just as if they're dealing with a lunatic (someone who would throw away free money), but as if they're dealing with a "dangerous" lunatic—a revolutionary or something.

I skip the detailed responses, such as: I never asked the government to protect me, or, if they really wanted to help me out in an unemployed period, they would *not* have taxed my employer for this purpose and I would have gotten paid more, which I then could have saved myself or invested in private unemployment insurance—without any of the cost and aggravation of having the money run through bureaucrats' hands.

Welfare by Any Other Name

I wonder why people are so hot on collecting unemployment, but are still generally against collecting the type of welfare that the chronically unemployed receive. I think I paid in for that too. By the same logic. . .

Anyway, you get the picture.

Unfortunately, it's really hard to turn down the government's "favors" when they've enmeshed themselves in so much of the economy. If they nationalize the medical business, will I only go to black-market doctors? If they take over all business, will I choose black-market work—or homelessness—over having a job and a decent (but inconsistently principled) life?

My previous job, at a private university medical center, was largely supported by government grants. Come to think of it, I haven't moved out of my rent-stabilized apartment either. The low rent helps a lot at a time like this when I have no income.

Now I just need to find a new job soon enough that I don't have to think about compromising my principles to survive. It's impossible to be perfectly consistent, but I think it's better if you can always remain aware of your inconsistencies.

In any event, I don't judge anyone else. We all do the best we can. □

Mark Reboul is a computer programmer and musician who lives in New York City.

THE FREEMAN
Ideas On Liberty
APRIL 1999



The Battle For Diamond Head: A Case of Market Failure?

"Hawaii's great and beloved landmark . . . is too precious an asset to be sacrificed."
—*Honolulu Advertiser* editorial (1967)

Last month I addressed the theory of entrepreneurial error in conjunction with the year 2000 computer problem. This month I raise another issue dealing with the possibility of market failure: Should government protect a local landmark from commercial development? Are zoning laws and other building restrictions necessary in a free society to stop "greedy" speculators and "fast buck" promoters from creating "urban sprawl" and unsightly commerce?

Recently my family and I spent a few days in Hawaii. Walking along famed Waikiki Beach, I couldn't help noticing how a string of high-rise apartments and hotels halted abruptly along the Diamond Head shoreline. (See photo on the next page.)

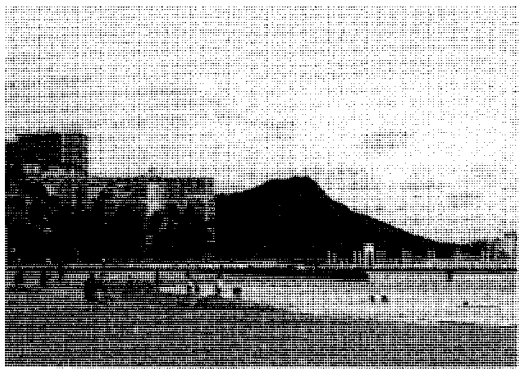
The Story of Diamond Head

Why the sudden abatement? In the late 1960s Diamond Head was the center of a fierce debate between the developers and the conservationists. Following statehood in 1959, tourists flocked to this paradise of the Pacific, and Waikiki Beach, sandwiched between downtown Honolulu and Diamond Head, became the hottest real estate market for resort hotels and condominiums. Honolulu newspapers ran photos of a rapidly disappearing view of Diamond Head, and local citizens became alarmed. A grassroots organization, Save Diamond Head Association, was formed in 1967 and demanded a halt to building any more skyscrapers along the shoreline.

Why save Diamond Head? In the nineteenth century, British sailors found crystalline rocks on its slopes and mistook them for diamonds. Conservationists argue that Diamond Head is a symbol of paradise, the mid-Pacific's most famous beacon. One visitor wrote during the debate, "I found Diamond Head, which has been declared a state monument, in imminent danger of turning into a monument for the fast buck, its craggy profile threatened with disappearance behind a palisade of tall concrete buildings."[1]

Here's the conflict: Hawaii's natural beauty and delightful climate attracted millions of new tourists in the 1960s. The tourist boom in turn created a rush in real estate development. But the high-rise buildings—along with enormous billboards—were blocking out the natural beauty that attracted tourists in the first place. What to do?

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Diamond Head today:
Should development have been halted?

The fight between the developers and environmentalists came to a head in December 1967. After a packed four-hour public hearing, five members of the nine-member city council voted against further commercial development. The other four members abstained. In 1968, Diamond Head was designated an official national landmark.

Is There a Market Solution?

Could the market properly plan for a growing Hawaii without destroying its natural beauty and aloha spirit, or must government intervene?

Sometimes the market faces a difficult choice between two conflicting goals. In the case of Diamond Head, it was the battle between development and a landmark symbol. Unfortunately, it's events like these that give capitalism a bad name. Could private developers have done better? Could it have been in their own self-interest to limit the height of hotels and condos and preserve Oahu's historic skyline while still making a profit? Can progress and profit go together?

What do free-market economists have to say about zoning and building codes? In *The Constitution of Liberty*, F.A Hayek notes that local governments have often done a poor job of city planning, sometimes amounting to "administrative despotism."[2] He cites rent controls, zoning regulations, and excessive taxation as examples. Nevertheless, he does support "some regulation of buildings permitted in cities," including minimum building codes.[3]

Economists have often been critical of zoning laws as an infringement of property rights. In a recent book on the subject, Tom Bethell asserts that zoning laws hurt the poor, cause urban sprawl, and invite political corruption. He points to Houston as an example of a dynamic city which has grown without zoning regulations.[4]

If conservationists really wanted to save Diamond Head, why didn't they buy the shoreline property and keep developers out? Instead of running to the City of Honolulu, Save Diamond Head Association should have raised the capital to stave off builders. Since 1953, Nature Conservancy, a nonprofit environmental organization with 900,000 members, has been buying and preserving land and habitats (now totaling over 10 million acres in the United States). Of course, such a plan would have been costly, with Waikiki property prices around $1 million an acre in 1967–68.

Property rights should include the right to be left alone from noise and air pollution. Should these rights also include the right of original owners to view Diamond Head? □

1. Kenneth Lamott, *Holiday Magazine*, July 14, 1967, quoted in Helen Geracimos Chapin, *Shaping History: The Role of Newspapers in Hawaii* (Honolulu: University of Hawaii Press, 1996), p. 268. Chapter 26 of Chapin's book, "Above Ground: The Battle for Diamond Head," summarizes the history of this conflict through the eyes of two local newspapers, the *Star-Bulletin* and the *Advertiser*.

2. F.A. Hayek, *The Constitution of Liberty* (Chicago: University of Chicago Press, 1960), p. 355. Hayek devotes an entire chapter to "Housing and Town Planning," an area often ignored by economists.

3. Ibid., pp. 354–57.

4. Tom Bethell, *The Noblest Triumph: Property and Prosperity Through the Ages* (New York: St. Martin's Press, 1998), pp. 297–99.

BOOKS

The Future and Its Enemies
by Virginia Postrel
The Free Press • 1998 • 265 pages • $25.00

Reviewed by George C. Leef

"At G.E., progress is our most important product." So ran the concluding line from dozens of General Electric ads from the 1960s. Back then, progress was *revered* in the United States. For the last few decades, however, there has been a rising tide of doubt. Today, we are more likely to hear hand-wringing lamentations over the destruction of the planet supposedly wrought by our exploitation of resources, or frightful predictions that technology is driving us headlong into dystopia. As the late Robert Nisbet wrote in *The History of the Idea of Progress*, "The skepticism regarding Western progress that was once confined to a very small number of intellectuals in the nineteenth century has grown and spread to not merely the large majority of intellectuals in this last quarter of this century, but to many millions of other people in the West."

The battle between those who want progress to continue and those who want to stop or even reverse it is the subject of this clarion call by *Reason* magazine editor Virginia Postrel. *The Future and Its Enemies* fills a desperate need. It's a book that illuminates the anti-progress philosophy (although that is too dignified a word) and tactics of, as she calls them, the "stasists." The inroads that the enemies of progress have been making in the United States should throw readers of this magazine into a cold sweat.

Stasists are not a homogeneous lot, but they all share a fear of change. Their camp includes violent technophobes like the Unabomber; "small is beautiful" intellectuals who pine for a simpler, more "natural" existence (not just for themselves, but for everyone); and opponents of particular innovations that might cause them losses—labor unions for instance. They are well funded, resourceful, and intent on locking in their view of the ideal world.

We have always had enemies of progress, but for most of American history, they couldn't really do anything except complain. Government had virtually no power to prevent individuals and firms from trying new products, technologies, and techniques. On the contrary, government power was committed to the defense of liberty and property rights. Coercive interference with others' experiments would land you in prison.

Jefferson warned, however, that the natural order of things is for liberty to yield and government power to gain. That has certainly been the case, especially in the last 70 years. As state power has grown, so has the ability of the stasists to put it to their ends, delaying or prohibiting changes that don't fit into their vision. Postrel correctly observes that the United States today "provides numerous opportunities for resourceful reactionaries: urban planning and endangered species laws to keep out Wal-Mart and new housing; environmental impact statements to limit business development and, if used by someone as clever as [Jeremy] Rifkin, to bar genetic engineering; Food and Drug Administration reviews to deter high-tech medical products . . . and on and on."

This constant growth of government has changed the rules of the game. People with new ideas can't just go ahead and give them a try. Often there is some board or commission whose approval must be obtained first. Even if not, we now have many vague statutes that provide cover for harassing lawsuits. Government power is of no use to innovators, but it means everything to the stasists, for the change they fear can only be halted by its use. Issuing scary manifestoes against, for example, biotechnology, won't stop it—but regulations and lawsuits can.

Postrel mentions Joseph Schumpeter's famous prediction that capitalism would collapse because of its very success, creating so much wealth and leisure that it would spawn a large class of idlers who would spend their time decrying its imperfections and destroying its foundations. Postrel puts a new twist

on Schumpeter's gloomy prediction. He feared the ascendancy of the *redistributionist* intellectual, but she shows that the greater menace is turning out to be the *anti-progress* intellectual.

But this isn't just an attack on the stasists. It is also a powerful argument in favor of the dynamic world-view. Postrel quotes Hayek's line that dynamism represents "the party of life, the party that favors free growth and spontaneous evolution," and then backs his assertion up.

If I have any criticism of this exceptional book, it is that the wake-up call isn't even louder and longer. It would have had a stronger impact had it gone into more detail on instances of stasist obstructionism. But of course, you can't say everything in a book. *The Future and Its Enemies* is, in my opinion, the most important book of the year. It needs to be widely read and discussed. □

George Leef is book review editor of The Freeman.

The Wealth and Poverty of Nations: Why Some Are So Rich and Some So Poor

by David S. Landes

W.W. Norton & Company • 1998 • 650 pages • $30.00

Reviewed by Randall G. Holcombe

Economic historian David Landes explains in this book why some nations are rich and some poor by appealing to the historical record. The history is fascinating, and Landes does a good job of relating the facts.

His explanation of the wealth and poverty of nations is simple: rich nations are once-poor nations that developed market economies; poor nations are once- and still-poor nations that did not. Market economies require governments that do not interfere with people's economic affairs except to protect property rights. Landes builds his case by recounting the history of world economic development.

Landes maintains that western European, and especially British, culture is superior to others at promoting people's well-being. He makes the same case for the virtues of Protestantism. The Roman church found truths about nature in the scripture, so new ideas were potentially subversive. Protestant culture gave individuals more freedom to think for themselves, to innovate, and to keep the rewards of their successes. The notion that one culture is as good as another is wrong, Landes argues, at least if one judges a culture by its ability to enhance the well-being of its practitioners.

This is a big book, so as you might expect, his argument is far more involved than this. Landes notes that geographical factors played a large role in the patterns of development, and that some areas had advantages due to climate and natural resources that enabled them to develop sooner than others. But he also argues that geographical advantages, in the long run, can be disadvantages, because if wealth comes too easily, people do not have as much incentive to work hard and to use their wealth productively. When the Europeans began settling the Americas, for example, the Spanish and Portuguese gained easy wealth through territory rich in gold and silver, whereas the British territory required more work and investment. That investment, however, produced a much greater long-run payoff. Similarly, Landes argues that the oil-rich countries in the Middle East today are squandering their wealth because they came by it too easily.

The same argument applies to the industrialization of Britain, which had some natural advantages, such as coal deposits, but lacked others and in any event could capitalize on its advantages only by hard work and innovation. Before the Industrial Revolution, many areas of the world were at least as wealthy as Britain and had developed at least as much scientific and technical knowledge. China, in particular, was far ahead of Britain in many respects, but the British had one crucial advantage over the Chinese—a culture that encouraged commerce, risk-taking, and innovation. The British culture produced the Industrial Revolution, and Landes argues that no place in the world was able to industrialize without British influence.

Landes's argument is generally convincing, but not entirely so. For example, he notes that the Japanese culture once lacked the work ethic of western Europe and was hampered by an institutional rigidity and isolationism similar to China's. But Japanese culture changed, permitting industrialization, economic growth, and wealth. Thus, culture is not unchangeable. Moreover, "religious" aspects of culture are not tied to particular religions. The Japanese adopted the Protestant work ethic without adopting the religion. Landes's view of culture appears tautological; the culture he champions really amounts to any one that leads to the adoption of market capitalism.

Europe was characterized by many governmental jurisdictions, creating an environment of intergovernmental competition, whereas China and Russia were vast regions without that competition. Landes notes this fact, but fails to see its importance. Is it not plausible that industrialization developed first in Europe because governments faced the prospect of losing people and capital to rival governments, thus tempering the rulers' interference with freedom? Culture has some explanatory power, but it shouldn't be regarded as the only factor determining the extent to which the market is free to work.

Landes's conclusion that the ultimate path to wealth is the adoption of a market economy is unassailable. Despite his questionable assertion that culture is the key determinant in the choice between the market and government domination, his book has much to offer in its recounting of the history of world economic development and its insights on the differences among nations and cultures. □

Randall Holcombe is DeVoe Moore Professor of Economics at Florida State University.



From Wealth to Power: The Unusual Origins of America's World Role

by Fareed Zakaria

Princeton University Press • 1998 • 199 pages • $29.95

Reviewed by Robert Higgs

Throughout history strong nations have often expanded beyond their borders, establishing military or trading outposts, exerting influence on other nations, and sometimes pushing out their own borders by subjugating neighboring peoples. The United States, which began as a union of 13 small states east of the Mississippi River, pushed to the Pacific and ultimately took control of extensive overseas territories, provides a clear example. For a quarter-century after the Civil War, however, the United States exhibited little interest in expansion, and that peaceful interlude seems anomalous to Fareed Zakaria, who finds it "a highly unusual gap between power and interests."

From Wealth to Power began as Zakaria's dissertation, and its origins still show, especially in the repetitious commentary on its theoretical underpinnings. Without these trappings, an already short book could have been even shorter with little loss of substance. Still, the author, managing editor of *Foreign Affairs* magazine, writes well, and readers will have no difficulty understanding his argument.

Zakaria regards his study as a contest between two theories of international relations. "Classical realism" asserts that a nation expands whenever it can. Rich nations have many resources, which they use as the means of expansion—for example, by supporting large armies engaged in foreign conquest. "Defensive realism" asserts that a nation seeks security rather than influence and therefore expands when it perceives an external threat. Rich nations expand only when threatened by potentially powerful aggressors. Zakaria tweaks classical realism to create what he calls "state-centered realism," positing that rich nations do not necessarily expand but do so only when their central governments have sufficient strength to extract from soci-

ety the resources required to support the expansion.

From 1865 to 1889, Zakaria argues, the U.S. central government had little strength. The executive branch, where foreign policy initiative normally resides, played second fiddle to Congress; and the state and local governments took responsibility for many more functions and took in much more revenue than the national government. In those circumstances the United States declined to act on numerous opportunities for foreign expansion. Of 22 cases considered by Zakaria, only six resulted in expansion, the most important of those being the acquisition of Alaska in 1867 and the beginning of the construction of a blue-water navy in the 1880s. In other words, our relatively weak government was a hindrance to those who wanted to spread American power globally.

By the 1890s, however, the national executive branch had begun to exert itself more forcefully vis-à-vis Congress and the states. That enhanced power gave rise to greater international expansiveness beginning as early as Benjamin Harrison's administration (1889–93) and culminating in Theodore Roosevelt's flaunting of his Great White Fleet. Between 1889 and 1908, of 32 cases considered as opportunities for foreign expansion, 25 resulted in expansion, the most important of those cases being the annexation of Hawaii and the taking of Puerto Rico, Cuba, and the Philippines from Spain in 1898.

Although Zakaria's argument is interesting and suggestive, it is less than compelling. Surely, to mention just one piece of conflicting evidence, the robustly expansionist administration of James K. Polk presided over a far weaker national government than did, say, Grover Cleveland (even in his first term, 1885–89). Nor will Zakaria's shaky command of economic history reassure readers. He makes a number of outright factual or conceptual mistakes, for example, asserting that the Civil War tariffs were reduced or eliminated after the war, and confusing the national government's debt with its annual budget deficit or surplus.

Zakaria views his study as representative of the "bringing the state back in" school of social studies. "Nations," he insists, "do not formulate and implement foreign policy and extract resources to those ends; governments do." He does not seem aware that some of us, backed by generations of intellectual forebears, have appreciated that reality and based our analysis on it for a long time.

Obviously, the ability of a central government to appropriate the requisite resources is a precondition for external expansion. But whether a nation-state *will* project force abroad depends on the dominant ideology of those who control the government. Classical liberals have always understood that limited government, peace, and free trade form a coherent policy assemblage. To sacrifice any one of those elements is to jeopardize the others. □

Robert Higgs is a senior fellow in political economy at the Independent Institute, a visiting scholar at Seattle University, and the editor of The Independent Review.

American Abundance:
The New Economic and Moral Prosperity
by Lawrence A. Kudlow
Forbes-American Heritage • 1997 • 212 pages • $22.95

Reviewed by William H. Peterson

Over the last 15 years, the U.S. economy has experienced a 3 percent real average rate of growth in gross domestic product (with only one minor recession), declining inflation, falling interest rates, and a stock market since 1982 that has increased in value sixfold in real terms.

Still, good times usually give rise to a cottage industry of pessimism. Browse through a bookstore or peruse the newsletters of some investment gurus and you will find chilling predictions of the imminent collapse of an economic house of cards.

Or you could read Larry Kudlow's *American Abundance*. This book is as robustly bullish as anything in the economic soothsaying literature.

Kudlow was one of Reagan's budget economists. These days he devotes his time to fre-

quent TV appearances, always wisely and wittily defending the superiority of the free market, and to writings that blast gaping holes in the plans of the interventionists to improve our lives through increased government spending and control. He also serves as chief economist to an investment advisory group.

Surveying the economic landscape, he comes to some very optimistic conclusions about our future. Despite the obvious falsity of the notion that "the era of big government is over," Kudlow sees irresistible forces at work to advance America's market society. The era of the *growth* of big government may be over.

One reason for his optimism is the fact that over 40 percent of the population—almost the same number as in the work force—are in the stock market through employee stock ownership plans, brokerage accounts, bank deposit plans, IRAs, Keogh Plans, 401(k) plans, mutual funds, variable annuities, and other private retirement systems. Kudlow reasons that this "investor class," a vast and growing army of corporate owners, is bound to prevail on Washington and push it toward free-market policies.

Contrary to the predictions of Marx, the workers have become capitalists—owners of the means of production. In the contest between the invisible hand of the market and the clenched fist of Marxism, as Kudlow says, "It was Marxism that withered away."

The idea that spreading investment via pension plans will cause the masses to jettison their anti-capitalistic biases is appealing, but there are grounds for skepticism. The investment trend has been going on for decades, but where's the growing opposition to Social Security, Medicare, "public education," subsidies, import restrictions, rent control, and the rest? Most people are too ill informed to see the connection between government interventionism and the size of their portfolios.

Kudlow courageously calls for wiping out more than a trillion dollars of federal spending, including the abolition of the Environmental Protection Agency, the Commerce Department, and other worse-than-useless agencies. That certainly would be good, but I fear that instead of foreseeing gains in their investments from lower spending and interventionism, the typical American would fall for the rhetoric of the politicians and their spinmeisters that the sky would fall if we didn't continue squandering money on such follies.

Kudlow also sees a big plus in the great technological wave that has been sweeping the economy, boosting productivity (which he thinks is understated in official statistics). Thanks to revolutionary knowledge and information technology—microchips, microprocessors, cell phones, personal computers, fiber optics, bioengineering and so forth—we are entering a Second Industrial Revolution, he maintains.

There is no denying that technology has given the economy a tremendous surge and will probably continue to do so as long as we can keep the government from upsetting the apple cart. The forces of "green" reactionary statism dislike technological progress and will do everything they can to slow or stop it.

In the course of the book, Kudlow pays homage to several of the great economists of the twentieth century, including Ludwig von Mises, Joseph Schumpeter, F. A. Hayek, and Milton Friedman, whose philosophies, he believes, will help make the 21st century one of growth—both economically and morally. "We are in a period of great change and transformation," he writes. "Our evaporating inflation rate and our rising economic growth rate are mirrored in the phenomenal increase in the stock market, which is a metaphor for our times. We can look forward to improving social, spiritual values; an era of global peace and prosperity is upon us."

Whether Kudlow's optimism about America's future is warranted; whether American attitudes will move back toward individual liberty and free enterprise, only time will tell. Stay tuned. □

William Peterson, a Heritage Foundation adjunct scholar, is the Distinguished Lundy Professor Emeritus of Business Philosophy at Campbell University in North Carolina.



Africa in Chaos

by George B. N. Ayittey

St. Martin's Press • 1998 • 399 pages • $35.00

Reviewed by Mwangi S. Kimenyi

George Ayittey is one of a few African scholars committed to advancing the ideals of classical liberalism. This is clearly demonstrated in his previous books, *Indigenous African Institutions* and *Africa Betrayed.* In *Africa in Chaos*, Ayittey advances the arguments made in those books, provides a detailed report on the chaos in Africa, and proposes various reforms to deal with the crisis. It is an excellent chronicle of events that have led to the demise of civil society in Africa.

A clear indicator of the chaotic state of affairs is the economic condition of Africa. The continent—more specifically sub-Saharan Africa—is richly endowed with some of the most valuable natural resources. Its potential for economic growth is enormous, yet countries in this region have the lowest standard of living in the world. Malnutrition and even starvation are widespread. African countries rank lowest in all measures of economic well-being, such as the proportion of population below poverty, infant mortality, life expectancy, and caloric intake. Infrastructure, which includes government buildings, roads, railways, and telephone and electricity facilities, is in a sad state of disrepair. The evidence shows that political independence has not advanced the material well-being of Africans in general.

What explains this dismal condition? Ayittey's book provides a detailed account of government policies that stifle the functioning of markets. Instead of building on indigenous markets that prevailed in the past, African leaders adopted policies that involved heavy-handed intervention. The primary result of government intervention has been to undermine the incentive to produce. In many countries property rights are insecure and leaders often engage in arbitrary expropriation. While many Africans remain destitute, political allocation of resources has provided rulers with copious opportunities to get rich.

Another reason for Africa's economic crisis has been the mistaken belief that large modern projects are equivalent to progress. Supported by foreign governments and international organizations, numerous capital-intensive projects divert resources from consumer-driven purposes. Further contributing to the instability has been the reliance on the many public enterprises that are inefficient and largely dependent on subsidies.

But if political independence has done little to advance the material well-being of the majority of Africans, it has proven disastrous for their liberty. Ayittey demonstrates that independence in Africa has been characterized by some of the most oppressive governments in history. The first wave of civilian leaders adopted oppressive laws that prohibited political competition and empowered rulers to detain opponents without trial. These "leaders" were replaced in many instances by military officers who were even more corrupt and tyrannical. With every coup, things have usually gotten worse.

To compound the problems, many countries have experienced internal conflicts. Armed clashes such as those in Somalia, Zaire (Democratic Republic of Congo), Liberia, Uganda, Rwanda, Burundi, Angola, Sudan, and many others have resulted in millions of casualties. Internal conflicts are exacerbated by the fact that government is geared more to plunder than to protecting rights and keeping peace.

Ayittey is critical of the commonly proposed solutions to the crisis in Africa. He argues that foreign aid and loans such as those advanced by the international organizations have no benefit in the long run. Ayittey proposes reform policies that key on the restoration of civil and economic liberties, building on traditional African systems of governance.

In sum, *Africa in Chaos* is informative, well written, and rich in detail. This book advances our understanding of African institutions and should be particularly helpful to those "development experts" who prescribe policies to Africans and yet have limited understanding of the continent. □

Mwangi Kimenyi is associate professor of economics at the University of Connecticut.

Swimming Against the Tide

by Clarence B. Carson

American Textbook Committee • 1998 • 562 pages • $29.95

Reviewed by Norman S. Ream

No one who has regularly, or even periodically, read *The Freeman* for the past 40 years will be unacquainted with Clarence B. Carson. In this book, subtitled "Memoirs and Selected Writings," one can discern how Carson's philosophical position has developed through the years, from the time he departed his birthplace in Alabama, through his teaching career, and eventually to his connection with the Foundation for Economic Education.

The title of this volume is eminently appropriate, for all through those years he certainly was swimming against the tide of popular and academic opinion. Clarence Carson is a pithy opponent of all your standard left-wing fads and fantasies, but also finds himself in disagreement with some of his allies. His economic and political philosophy is firmly grounded in the moral and ethical principles the author derives from his Christian faith. Because of that faith, Carson takes issue with Ludwig von Mises and other heroes of the free-market movement for their purely secular defenses of private property and the market order. Agree or disagree, Carson stands his ground.

The first section of the book is purely autobiographical and may be a bit too detailed for the average reader. Born and educated in the South, with advanced degrees from Vanderbilt and Auburn, Carson spent the major period of his life teaching in several colleges. During his early education he had moved toward what is today called "liberalism," but by the time he earned his Ph.D., his doctoral dissertation was titled "Embattled Individualists: The Defense of the Idea of Individualism, 1890–1930."

Although Carson was a college professor by vocation, he was mainly interested in writing and has published over 19 books, many of them designed to be textbooks. Three of his books, *Basic Economics, Basic Communism,* and *Basic American Government* have been main selections of the Conservative Book Club. His six-volume *A Basic History of the United States* is certainly his magnum opus; it is an excellent survey of American history without, of course, any hint of the common leftist biases.

Carson began contributing to *The Freeman* in 1961. Forty of his articles became a book entitled *The World in the Grip of an Idea.* The author describes it as follows:

> I believed that in my studies and writing I had reached a plateau above and beyond the ideologies of the 19th century which had fueled the conflicts of this century. I saw, or believed I saw, the underlying similarities and failings of these ideologies. I saw those things about Communism, Fascism and gradualist socialism. But I believed I saw the role and weaknesses of corporate capitalism as well. . . . What all these ideologies had in common was the justification of the use and abuse of organizations to control men's minds and actions to their own ends. Every one of these collectivisms fails to grasp the fact of the superiority of the individual in all constructive activity and fails to understand that collectives are only superior in the use of destructive force on individuals.

Most of Carson's wide-ranging memoir is taken up with stories, essays, articles, philosophical musings, economic ruminations, and more. A brief sampling: "The Constitution of Paper Money," "The Dilemmas of Public Education," and "Beyond the Christmas Story."

The author has strong opinions and deep convictions. As noted, he objected to Mises's secularism. Yet perhaps surprisingly, he includes a fine memorial to Ayn Rand.

The book has its weaknesses. The autobiographical section was not adequately edited and contains numerous errors of punctuation and sentence structure. Also, the volume would have benefited from an index. Still, *Freeman* readers old and new will find a lot of provocative and enjoyable writing in this book. □

Norman Ream, a long-time Freeman *contributor, is a retired minister living in Estes Park, Colorado.*

The Taxman Cometh!



T.S. Eliot was right: April really is the cruelest month, and not because of its wrenching mix of memory and desire but, instead, because of the discouraging annual ritual of filling out our 1040 forms. Rather than calling to mind "chestnuts in blossom," thoughts of April are much more likely to focus on hours hunched over our desks, desperately sorting receipts. Although we may (for now) be stuck with the Byzantine system, this doesn't mean we can't rail against it. This month's sale offers books that investigate taxation and money. We hope they'll provide relief from the stresses and strains of tax preparation.

What Has Government Done to Our Money? by **Murray Rothbard**, 4th ed.

Bad enough that one quarter to forty percent of our incomes are taken in taxes, but to add insult to injury, the people in charge of the money supply often debase it by turning the printing presses on full steam. This small book discusses why groups of people come to rely on money – rather than cows, for example – as a medium of exchange. After considering what a free market in money might entail, Rothbard discusses the many ways in which government officials meddle with money. Finally, he investigates how the international gold standard of the 19th century broke down in the wake of the Great War. Very interesting from both a historical and theoretical perspective.

119 pages, paper $7.95 **Sale: $4.00**

Taxation and Confiscation, a *Freeman Classic*

This anthology of articles provides an excellent overview of the general issue of taxation. Taxes may be used as the means to a number of different ends: filling the purses of the politically powerful, redistributing income to achieve some alleged equity, or encouraging or discouraging some particular behavior (sin taxes). These articles examine taxation as a means to the ends of social justice and social reform. Tax rates have an important impact upon what is produced and when. Five essays look at this problem. Finally, a number of essays discuss taxation as a destructive force. This is a lucid investigation of an issue intimately connected to liberty.

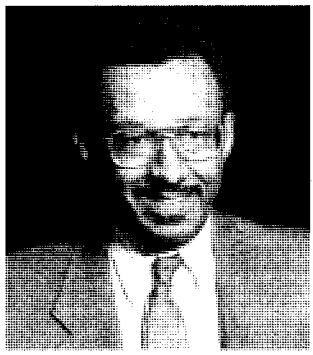
206 pages, paper $12.95 **Sale: $6.00**

Death & Taxes by **Hans F. Sennholz**

Should people's property be taxed at their death? Presumably, the property was taxed at least once during their lifetime, so why should these assets be taxed again? This book takes a brief general look at taxes and the justifications offered for their continuation. Focusing on estate taxes, Dr. Sennholz investigates the claim that death taxes are a wealth equalizer. He looks at the effects such taxation has on predecessors and successors, why people avoid these taxes, and how trusts minimize tax burdens. The volume concludes with suggested reforms.

105 pages, paper $5.95 **Sale: $3.00**

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What American Education Needs

For over four decades the public education establishment has delivered one educational disaster after another. "Solution" after "solution" has fallen far short of promises. The education establishment's perennial answer to our education problems is more money. Educational expenditures have skyrocketed (more than doubling every 20 years since 1960) and yet SAT scores plummet.

National Assessment of Education Progress (NAEP) test results partially demonstrate our dismal education picture. Of 17-year olds taking the test: 47 percent could not express 9/100 as a percent; only 5 percent could calculate the cost per kilowatt on an electric bill that charged $9.09 for 606 kilowatts; 26 percent did not know the U.S. Congress was part of the legislative branch of government; 43 percent of high school juniors could not place World War I within the period 1900 to 1950; 75 percent could not place Abraham Lincoln's presidency in the era 1840–1880.[1]

The education establishment's latest "solution," supported by President Clinton, is massive federal expenditures to hire 100,000 additional teachers. This they claim will reduce class sizes and thus improve academic performance. The United States already has smaller classes than countries where student academic performance is much greater than ours. For example, Japan averages 41 students per class compared to 26 in the United States. In mathematics, where their students run circles around ours, their average math class size is 43 compared to our 20.[2]

Breaking the education monopoly will solve most of the nation's education problems. A way to achieve this is through education vouchers or tuition tax credits. With education vouchers, state and local governments make direct payments to parents, in the form of vouchers that are used to pay tuition at public or nonpublic schools.

Tuition tax credits give parents a credit against their income taxes for tuition expenses. For example, if parents spent $3,000 in tuition to send their kid to a nonpublic school, all or a percentage of the tuition would be subtracted from their tax liability. Tuition tax credits are far preferable to vouchers because we would not run the risk of government intervention in the form of state Departments of Vouchers.

Opponents interested in maintaining the monopoly of education have advanced arguments against greater competition in the education of America's children. These arguments seem to be plausible; however, upon a little reflection they are simply baseless.

If a voucher or tuition tax system is instituted, public schools will be destroyed. This charge amounts to a tragic confession that public schools are so inferior that given a choice, all parents would opt out. The fact of the matter is some public schools are doing a satisfactory job; those schools would survive. Schools doing a poor job would have to either improve or perish.

Walter Williams is the John M. Olin Distinguished Professor of Economics and chairman of the economics department at George Mason University in Fairfax, Virginia

If there is a voucher or tuition tax credit system, private schools would skim off the best students leaving public schools with the least motivated students. Assume for a moment this might happen. To object to parental choice for that reason is callous arrogance and cruelty. It differs little from saying that parents who want better education prospects and a brighter future for their children should be held hostage until some undetermined time when public schools have improved. While the education establishment is willing to hold parents hostage, they want choice for themselves. Public school teachers enroll their own children in nonpublic schools to a much greater extent than the general public.

Vouchers or tax credits will lead to school racial segregation. Most voucher and tuition tax proposals prohibit racial discrimination. The major thrust for school choice programs has come from black parents, most likely to be served by poor schools. Moreover, most large city public schools are already racially homogeneous. For example, in Manhattan, public schools are nearly 90 percent black or Hispanic, while private schools are 80 percent white. While there is a smaller overall percentage of blacks in private schools, private schools are more racially heterogeneous. Therefore, if racial diversity is deemed desirable, school choice would contribute to that goal.

Even if school choice is a good idea, there are not enough nonpublic schools. This is an absurd criticism and reflects ignorance of markets. In the 1970s, there were no computer software stores and few video rental shops. Would you have argued back then that the manufacturing and marketing of computers and VCR machines should be held up until software and rental shops were in place? Consumers having purchased computers and videos created the demand for those shops. We would expect the same with private schools. If parents had vouchers or tax credits, one can rest assured that entrepreneurs, in the pursuit of profits, would emerge to meet the demand for private schools.

Parents, particularly those who are low-income, are incapable of making wise choices. This is a demeaning attitude toward the poor and it also reflects ignorance of how markets operate. People have little direct information about the quality of most goods and services they use. They depend on indirect information such as word of mouth, consumer reports, advertisements, and so forth. I know that Lafite-Rothschild is an excellent Bordeaux not because of my wine-tasting skills but because of the testimony by others who spend their lives studying wine. Markets generate information about quality, and information would be generated about K through 12 schools just as markets already provide information about colleges and universities.

Even if parents made mistakes, it is inconceivable that parents, particularly black parents, could choose schools worse than the schools already serving them. On occasion I have put the matter more starkly saying that if the Grand Wizard of the Ku Klux Klan wanted to sabotage black academic excellence, he could not devise a more effective way of doing so than the schools serving most black children.

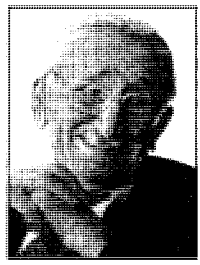
Education vouchers and tuition tax credits face another source of criticism. It comes from those fearful of government control of nonpublic schools through regulations that might accompany vouchers and tax credits. I share that concern and urge strong measures be taken to minimize that likelihood. The question I pose to these critics of vouchers and tuition tax credits is: which is the more serious and costly risk, that associated with the prospect of increased government intervention in nonpublic schools that might accompany vouchers and tax credits, or continued educational destruction of the nation's youngsters, particularly its black and Hispanic youngsters? □

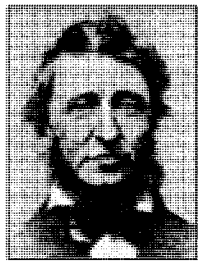
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PERSPECTIVE

Two Powerful Words

Last year Israel Kirzner, one of the economists I most enjoy, said something during a lecture that was at once simple, true, and deceptively powerful. How powerful I did not appreciate immediately. But in the ensuing months, I have come to see how much was packed into that statement.

Professor Kirzner said that the market economy can be reduced to two words: private property. At first glance that may seem so obvious as to be uninteresting. At second glance it might summon an objection along these lines: No, private property isn't enough. The market also requires individual liberty, the rule of law, limits on government, respect for contracts, and more.

But as I understand the matter (and Professor Kirzner), all those things are subsumed by "private property." A society characterized by private property will necessarily have the other features we typically associate with free markets.

Property, for example, *is* a limitation on government power (one's property of course includes one's person) because it necessarily entails rules governing how people may be treated, whether by other private individuals or state officials. (See Bradley Smith's book review this month.)

Property helps to separate the wheat from the chaff in the matter of civil liberties, such as privacy and freedom of speech. Take the issue of falsely shouting "fire" in a crowded theater. This is traditionally used to demonstrate that freedom cannot be "absolute." But as Murray Rothbard long ago pointed out, it does nothing of the sort. On the contrary, it affirms property and its extension, contract. If a theatergoer shouts fire, he violates the property rights of the theater owner. If the theater owner does the shouting, he violates his contract with the patrons.

Privacy issues, which modern law and the American Civil Liberties Union have so badly muddled, can only be sorted out when the right to privacy is understood as rooted in private property. For example, contrary to the

ACLU, it is not a violation of privacy for an employer to refuse to hire smokers, even if they smoke only at home. It is simply a matter of freedom of association, which is an extension of private property.

If you're ever asked to stand on one leg and sum up the free society in two words, you now know how to do it.

* * *

The great pyramids of Egypt fascinate tourists, real and vicarious, by the millions. Yet few, unfortunately, appreciate the tragedy they represent. Christopher Mayer contemplates what might have been and looks at one of our own modern pyramids.

President Clinton's impeachment crisis has ended. His legacy is now set. Calvin Beisner fittingly revisits another leader whose problem with truth-telling got him into hot water.

Many philosophers have offered definitions of freedom. Perhaps the most pernicious has been "freedom from want." James Bovard looks at the implications of that twisted definition.

Much of the steam of the interventionist environmental movement has been provided by certain horror stories that everyone has heard and everyone believes. What if those stories are grossly exaggerated or untrue? Roger Meiners trains his magnifying glass on the Green Scare.

Anyone who puts his mind to it can be a spokesman for the freedom philosophy. A ready platform exists wherever you are. The Internet is one method, but, as John Landrum explains, the old-fashioned way still affords ample opportunities.

F.A. Hayek, one of the twentieth century's greatest advocates of the free society, was born 100 years ago this month. Richard Ebeling surveys the long and fruitful career of the 1974 Nobel prize winner.

The U.S. government has gone to a lot of trouble redesigning the money to thwart counterfeiters. George Leef says there's a better way to accomplish the objective.

Richard Timberlake continues his series on monetary policy in the fateful 1920s and 1930s. In this installment he looks at the Federal Reserve's gold policy after the Great Depression hit.

The political philosophy at the root of the American Revolution was a novel mixture pestled in the mortar of a remarkable historical moment. Joseph Stromberg leads a tour through the compound.

In the columns department, FEE President Donald Boudreaux celebrates the birthday of his hero, F.A. Hayek. Lawrence Reed lampoons corporate welfare. Doug Bandow reminds us that the era of regulatory government is not over. Dwight Lee writes of the need for costs to be revealed. Mark Skousen concedes he was wrong about Japan and Germany. And Charles Baird looks at the labor policy of the British Bill Clinton. Roger Garrison reflects on Paul Krugman's belief that Hayek and Austrian business cycle theory are insignificant and protests: It Just Ain't So!

We proudly announce that Thomas Szasz will join us six times a year with a new column, The Therapeutic State. For about half a century Tom Szasz has been the chief and at times only opponent of the medicalization of morality, particularly through the alliance of Psychiatry and State. His regular contributions to *The Freeman* will cover an area too often neglected by advocates of freedom. The inaugural column skewers the strangely selective professional skeptics.

In the book department our reviewers pass along their impressions on such topics as neosocialism, the arts in a market economy, the politicization of nonprofit health organizations, a classic on the "humane economy," higher education, property in American legal thought, and political philosophy.

—SHELDON RICHMAN

Thoughts on Freedom

by Donald J. Boudreaux



Hayek Turns 100

Economics captivated me from the moment that I first saw on a chalkboard a supply-and-demand graph. That was in January of 1977. I was then an 18-year-old college freshman at Nicholls State University in Thibodaux, Louisiana. I immediately took to pestering my economics professors for suggestions on what to read in economics.

One of my professors, Bill Field, told me about Milton Friedman. I began reading Friedman's *Newsweek* columns and was immediately struck by his logic and passion. (One of these articles, in particular, really resonated with me; I believe that its title is "Free not Fair," in which Friedman argued that government attempts to engineer fairness succeed only in restricting our freedoms.) Soon thereafter I read Milton and Rose Friedman's *Capitalism and Freedom*. Its power floored me.

I was deliriously happy with my newfound intellectual friend, Milton Friedman.

Introduced to Hayek's Works

One afternoon, after reading something or other by Friedman, I wandered in to Bill Field's office—a place, incidentally, where I was always welcome—and announced that Friedman must be the world's greatest living economist.

"Nope. In my opinion Friedman is the world's *second* greatest living economist," Bill replied matter-of-factly.

"Second greatest?" I sputtered. I didn't believe what I'd just heard.

"Who is it?" I asked. "Which living economist can possibly be greater than Friedman?"

The name came. It was the first time I'd ever heard it. "Hayek. F.A. Hayek."

The name meant nothing to me. "Never heard of him," I responded.

"Here," Bill said. "Take this book and read chapter four. It's an article entitled "The Use of Knowledge in Society." You haven't studied economics long enough to grasp it all, but give it a try." Bill lent me his copy of Hayek's 1948 book *Individualism and Economic Order*.

That night I read "The Use of Knowledge in Society," an article that originally appeared in the September 1945 issue of the *American Economic Review*.

Bill was right; I grasped only very little of it. But I did grasp the main point that markets allow everyone to benefit from everyone else's knowledge. This insight was so profound that I knew right then that I had before my eyes the product of a mind so deep and so wise that I could never call myself an economist without knowing the full range of this man's works.

"Do you understand what Hayek says in that article?" Bill asked the next day. He and I then proceeded on the first of what became countless afternoons of reflecting upon Hayek's work. Later, Bill introduced me to the writings of other luminous economists—P. T. Bauer, James Buchanan, Israel Kirzner, Ludwig von Mises (Hayek's teacher), Joseph Schumpeter. I relished their works; I learned from them all. But to this day, Hayek remains for me the premier economist of this century.

Hayek's Revolutionary Ideas

Even in the late 1970s—still active and more than a decade away from his death in 1992—pictures of Hayek revealed a very old man. Here, after all, was a man who once challenged Keynes for the position of most prominent economist of the 1930s. Here was a scholar whose most famous book, *The Road to Serfdom*, was published fourteen years before I was born.

And yet whenever I read his words, I felt understanding being poured lavishly into my mind. These weren't the words of an old man, a man whose time had long ago passed. No, these words conveyed deep and timeless insights into the nature of economics, law, and politics. These were revolutionary words, for to understand Hayek is to understand not only that government cannot improve upon the operation of free markets, but also that government cannot even be relied upon to supply money and law—the very stuff that most economists unthinkingly assume can be supplied *only* by the state. Moreover, Hayek's explanations of government's inherent limitations—and of the market's marvelous ability to peacefully coordinate human activity into a productive powerhouse—are all grounded upon enduring truths rather than upon clever algebra or bumper-sticker maxims.

Finding Hayek was, for me, finding the most superb intellectual guide that I could dream of.

By my junior year I'd already devoured several of Hayek's books and essays. It was then that I tackled what I still regard as his finest work, the three-volume *Law, Legislation and Liberty*. In this work, Hayek most clearly and fully develops his idea of spontaneous order.

In *Law, Legislation and Liberty*, Hayek also explains why common-law methods of law making are far better than legislative methods. To this day, following Hayek's example, I cannot bring myself to use the word "law" to describe legislation. The latter is fundamentally distinct from the former, and, because of Hayek's influence, I believe that our loose habit of calling legislation "law" gives to legislatures an authority that they do not deserve. Legislators are *not* law makers; if accuracy is to be served, far better to call legislators "law breakers" rather than "law makers." Legislation disrupts the common-law rules that embody patterns of expectations built into the law over the years and through long practice. And why do legislatures upend this law? To plunder the politically weak for the benefit of the politically strong.

Hayek wrote enduring treatises in economics and political and legal philosophy. But he also wrote short, laser-like articles focused on dispelling prevailing nonsense. One of Hayek's best-known articles of this kind is his 1961 answer to John Kenneth Galbraith's notion of the "dependence effect." Galbraith argued that in modern society consumer wants are created by advertising. Hence, because these wants are artificial, the market ought not to be applauded for satisfying them.

Hayek skewered Galbraith's argument, pointing out that nearly *all* of our wants—with or without Madison Avenue—are greatly influenced by our cultural environment. There is nothing unique or sinister about Madison Avenue that renders as unworthy of satisfaction the desires that it helps to shape. Indeed, said Hayek, far better to have lots of producers use advertising to compete for consumer patronage than to have government coercing people to spend their incomes according to the fancy of the political elite.

On May 8 I will celebrate—along with all friends of liberty and truth—the centennial of Hayek's birth. First I'll call my old professor, Bill Field, and thank him again for introducing me to Hayek's works. Afterward, I'll reread "The Use of Knowledge in Society" and reflect on the ocean of knowledge that this one Austrian-born British citizen contributed to the cause of human freedom.

Happy birthday, Professor Hayek. □

THE FREEMAN
Ideas On Liberty

Hayek Made No Contribution?

It Just Ain't So!

"[I]f one asks what substantive contributions [F. A. Hayek] made to our understanding of how the world works, one is left at something of a loss. Were it not for his politics, he would be virtually forgotten."

This assessment was offered up late last year in the online magazine *Slate* by Paul Krugman, 1991 winner of the prestigious John Bates Clark Award.

A few weeks before Krugman wrote that, Gene Epstein, economics editor of *Barron's*, profiled this Yale-bred, MIT-based economic theorist. Epstein's article was largely positive and wholly respectful. But in a mildly critical tone, Epstein wondered if Krugman hadn't committed an error of omission. His writings on recessions seemed to suggest that he knew little or nothing about Hayek's theory of the business cycle, a theory built on the cumulative efforts of Carl Menger, Eugen von Böhm-Bawerk, and Ludwig von Mises. Krugman conceded that he wasn't familiar with the Austrian theory.

One is reminded of the notorious episode in which John Maynard Keynes reviewed Mises's *Theory of Money and Credit*, which was published in German. He faulted Mises for failing to offer anything original and then later remarked that when he read German, he understood only what he already knew. If we get our appreciation of Hayek through Krugman, we can credit Hayek for very little. Unlike Keynes, though, Krugman cannot invoke language as an excuse. Hayek did not get the Nobel Prize for his political views; he got it for his work on business-cycle theory. Why would Krugman not be completely familiar with Hayek's contributions? Stay tuned.

Clearly not a follower of Austrian theorizing, Krugman is, if anything, a quick study. On the same occasion in which he denied Hayek any standing as an economic theorist, he launched a vitriolic attack on the Austrians and their "hangover theory" of recessions. "I regard [their theory] as being about as worthy of serious study as the phlogiston theory of fire." Though he failed to identify the *Barron's* article or its author as the spark that set off this firestorm, he was clearly reacting to Epstein.

"Hangover theory" is a term obviously intended to denigrate the Austrian account of the unsustainable boom. Yet it is descriptive of many—if not most—modern business-cycle theories. The idea that booms lead to busts as drinking binges lead to hangovers is at home in both Monetarism and New Classicism. Even our sophomore-level college textbooks feature a stilted version of the hangover theory. In the late 1970s, the analogy between the abuse of monetary tools and the abuse of illegal substances became so well understood in the financial world that the argument by analogy was nearly reversed. A memorable cartoon of the period showed a balding Wall Street banker having a heart-to-heart with his errant teenage son: "Think of it this way, Timmy: Taking drugs is kinda like increasing the money supply. . . . "

The Austrian hangover is unique. The misallocation of resources during the period of artificially cheap credit has the feel of genuine growth, but these good feelings are followed by bad ones. The commitment of too many resources to projects that will yield output only in the remote future has as its counterpart an undue scarcity of resources for producing output in the near and intermediate future. In time the misallocation becomes apparent, after which follows a period of liquidation and reallocation—in a word: a recession.

None of this is to deny that a sharp increase in money demand (or a collapse in the money supply) can seriously retard recov-

ery—as certainly happened in the 1930s. But Krugman would have us believe that monetary disequilibrium is the whole story: People, for some reason, want to hold more money than currently exists. Accordingly, his solution is simply to print the money up and let them hold it.

Krugman's view of recessions is best put in perspective by comparing it with the contrasting views of Keynes and Hayek. These arch-rivals of the 1930s were in agreement that the increase in money demand, the "scramble for liquidity," was a secondary aspect of the downturn but in disagreement about what the primary problem was. Keynes thought it was investment demand, which in a decentralized economy is prone to collapse. Hayek thought it was malinvestment induced by shortsighted or politically motivated actions of the central bank. [Editor's note: See Richard Ebeling's article, p. 28.] Krugman elevates what both Keynes and Hayek saw as a secondary aspect to the status of the primary problem. And then, creating difficulties for the historian of thought, he attributes the high-money-demand theory of recessions to Keynes himself.

Presumably rejecting all hangover theories, Krugman pronounces the Austrian variety "intellectually incoherent"—largely on the basis of a telling question: "[How can] bad investments in the past require the unemployment of good workers in the present?" Krugman's implicit answer: They can't—and therefore we needn't pay any attention to Hayek. (The question itself is a good one and is likely to find its way onto macro exams at Auburn University.)

Emphazing the time element in the economy's capital structure, a Hayekian would argue that investment involves the employment of resources in a particular sequential pattern. During the downturn, good workers are out of work because the capital they need to work with is in short supply, having been committed to long-term projects now in need of liquidation. Krugman's response ("Well, fine. Junk the bad investments and write off the bad loans.") is all too facile. His advice is well taken, but the market process that implements it is time-consuming. During the junking and capital restructuring the demand for much of the labor force (labor whose capital complement has not yet been recreated) is low. And low demand translates into unemployment—except under the decidedly un-Austrian assumptions of instantaneous wage-rate adjustment and near-infinite labor mobility.

Recognizing that in Austrian theory the unemployment is somehow related to capital restructuring, Krugman poses another question: "Why doesn't the investment boom—which presumably requires a transfer of workers in the opposite direction [from short-term projects to long-term projects]—also generate mass unemployment?" Gottfried Haberler asked the same question in his 1937 book, *Prosperity and Depression*. The answer is that during the cheap-credit boom, there is a net increase in labor demand. And because of the low interest rate, many workers are bid away from jobs in the late stages of production and into jobs in the early stages. During the downturn, however, there is a net reduction in labor demand. As liquidation gets underway, workers are released from the higher stages and (eventually) reabsorbed elsewhere in the economy.

Both of these future exam questions have been answered by drawing on Hayek's contributions. Significantly, both answers involve heavy doses of capital theory, which serves as the underpinning of the Austrian theory of the business cycle. One seemingly permanent effect of the Keynesian Revolution was to tear macroeconomics loose from these underpinnings. Today, capital theory simply has no standing in mainstream macroeconomics. Accordingly, Hayek has no standing in the eyes of Krugman and other modern mainstream macroeconomists. It is a pity.

—Roger W. Garrison
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A Modern Pyramid

by Christopher Mayer

In *Anything That's Peaceful*, first published in 1964, Leonard Read took aim at U.S. efforts to put a man on the moon.[1] He was right on target. His powerful comments have tremendous relevance today in light of the government's aim to build an international space station. The project is expected to cost more than one hundred billion dollars over its lifetime.

In discussing the moon project, Read wrote: "What its ultimate, useful purpose is I cannot imagine. But putting aside personal prejudices against this multibillion dollar project, it is obvious that it would not, at this time, emerge from the free market."

Read also took note of all the specialized labor, machines, time, and money being poured into the project. Those workers supported themselves with money provided by the government. However, that income was not earned in the normal sense. In the market, wages are earned by providing a service or good that others are willing to pay for. Ultimately, wages are money that entrepreneurs advance to workers now in exchange for a greater amount generated later from the sale of the product. Of course, entrepreneurs make mistakes, and it may turn out that the product is sold for less than anticipated. A loss is a signal that an entrepreneur must either redirect his resources to a good more highly valued by consumers or he will continue to suffer losses and be driven from business. His resources would then fall into more capable hands and be more efficiently deployed (or left idle).

No Response to Consumers

As Read pointed out, exploring the moon "is not bound into the economy by mutual consent as reflected by willing exchanges in a free market; it is bound into the economy by the exertion of governmental force or coercion." The efforts of NASA are possible because the government forcibly collects taxes from it citizens. Read coined a term to refer to work that would not be supported by the free market: "To the extent that government intervenes in free action to that extent is *unnatural specialization* brought into play." (Emphasis added.)

The harm of unnatural specialization can be seen through Read's example of policing. Most everyone agrees that it is the government's role to keep the peace, to ensure and protect individual freedom and property, and to forcibly restrain fraud, violence, and other similar crimes. However, citizens must be vigilant about government's role even here, lest that worthy goal be corrupted. Employing too many police officers and soldiers places a drain on the economic system. What if everyone were forced to become a police officer or soldier? We can easily see the folly of such a scheme. Too many takers, not enough producers.

Christopher Mayer, a loan officer at a Maryland bank, is studying for his MBA at the University of Maryland.

Garet Garrett, a wonderful writer with a gift for symbolism, surely must have agreed with Read. He would have called exploring the moon or building an international space station a "pyramid." In his essay "The Anatomy of a Bubble," first published in 1932, Garrett used the imagery of the pyramid to denote a dead asset, an unproductive expenditure of human labor.[2] The pyramids were built through the power of the pharaoh, who wished to build a monument in honor of himself.

Garrett wrote that "it is believed that on the Cheops alone 100,000 men were employed for 20 years. And when it was finished, all Egypt had to show for 600,000,000 days of human labor was a frozen asset. . . . People could not consume what their own labor had produced. That is to say, they could not eat a pyramid, or wear it, or live in it, or make any use of it whatever. Not even Pharaoh could sell it, rent it or liquidate it."

Had they not been forced to build the pyramids, the laborers might have improved Egyptian agriculture, built homes, and made clothing and other goods that their fellows would have enjoyed and willingly paid for. They might have developed and expanded trade. They might have invented innovative products. As Garrett said, they could have insured "Egyptian civilization a longer competitive life." Instead, they made a large pile of bricks.

Once spent, the labor, capital, and time were gone forever. The Egyptians could not unmake the pyramid.

A Pyramid in Space

What's the difference between the Pharaoh's pyramid and our government's intent to build a space station? The money spent on the station can't be unspent. It is gone forever. And what will we have for our efforts? We cannot eat the station, we cannot wear it, live in it, rent it, or likely liquidate it. The station is a modern pyramid.

Advocates of the space station say it will provide important benefits. But the promises are vague, even if chock full of noble-sounding humanitarian goals that seem beyond reproach. They begin with the mission "to enable long-term exploration of space and provide benefits to the people of Earth." They include promises "to accelerate breakthroughs in technology," "to maintain U.S. leadership in space," and "to inspire our children." NASA also claims that "every dollar spent on space programs returns at least $2 in direct and indirect benefits." Nowhere is this claim substantiated. In fact, NASA's Web site (www.nasa.gov) never mentions costs. If every dollar yielded two dollars in benefits, why isn't this a private initiative? That kind of return would attract big-time money, money that would make Bill Gates blush. The reason is that individuals in society have other things they would rather do with the money.

Ludwig von Mises wrote in *Human Action* that "A project *P* is unprofitable when and because consumers prefer the satisfaction expected from the realization of some other projects to the satisfaction expected from the realization of *P*."

As Mises pointed out, many fail to recognize the fact that all action involves tradeoffs. Projects have a cost because factors of production are scarce. The money to subsidize a project must come at the expense of the taxpayer and the sacrifice of other wants.

The concept of a pyramid is a useful symbol for any number of government projects. Because of Garrett's analysis, I will never look on the pyramids with admiration and amazement. I will see only that they are the product of a tyrant and a symbol of the wasted effort emblematic of other public works projects. I'll wonder what the Egyptians would have built in their stead had they been free.

And I'll have similar thoughts every time I read about the space station. □

1. Leonard E. Read, *Anything That's Peaceful* (Irvington-on-Hudson, N.Y.: The Foundation for Economic Education, 1998 [1964]).

2. Garrett's essay was reprinted in *Where the Money Grows and Anatomy of a Bubble* (New York: John Wiley & Sons, Inc., 1997).

THE FREEMAN
Ideas On Liberty

"Must I Not Be Believed?"

by E. Calvin Beisner

It was mid-November 1688. King James II of England, heir to his father's and grandfather's beliefs in royal absolutism, was desperate. Nobles and gentry of his kingdom had invited his son-in-law Prince William of Orange to intervene for the preservation of a free parliament and the Protestant religion. James was meeting with a group of bishops of the Church of England. It was his last chance to influence these clerics, and they were the last men who might possibly persuade the English people to support James against William, who with a force of 15,000 men had just landed at Torbay.

All the king asked of the bishops was that they make a public statement that, contrary to William's declaration, they had not taken part in the invitation to William. (In fact, one of them had.) But the bishops refused on the grounds that the declaration alleged to be William's might be a forgery and that even if it were genuine, it was unfair to press them alone to disavow it, since that would raise suspicions that they were uniquely suspect. King James was beside himself. "Must I not be believed?" he asked in frustration. He desperately needed his people to believe that William had no support among the country's leaders.

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One of the bishops suggested that since they already had denied to him privately any involvement in the invitation to William, James could simply report that denial publicly. "No!" cried the king. "If I should publish it, the people would not believe me!"

Credibility Lost

That was precisely the point. James had lost credibility with his people for two reasons. First, he had been caught in manifest lies time after time. Second, he had declared himself above the law, even packing a court to ensure that it would rule that "the laws of England are the laws of the King of England. . . . [T]he king of England or any sovereign prince upon urgent occasions & necessities may dispense with any penal laws of their dominion. . . . [T]he king is sole judge of the necessities & urgency of these occasions upon which they may dispense with the laws. . . . [T]he king's power is in himself independent of any & not entrusted of any & not entrusted to them from the people of England."

Now, with William's invasion, James more than anything else needed credibility. The survival of his reign depended on it. His troops' willingness to fight for his reign depended on it. Lacking it, he watched as regiment after regiment of the army, ship after ship of the navy, either simply refused to fight or actually changed allegiance and joined William. Within a month, and with hardly a battle fought, James—who had begun with superior

forces—found himself stripped of all ability to defend himself and his kingdom, and was forced to abdicate, fleeing to France. The "Glorious Revolution" of 1688 was brought on, and consummated, by the simple fact that the people of Great Britain did not trust their king.

When President Bill Clinton, one day before a scheduled House vote on impeachment, ordered air attacks on Iraq, some Republican congressional leaders, like millions of American citizens, broke with the tradition of supporting the president in foreign military action and clearly spoke their own incredulity at both the policy and its timing. Nothing Clinton could say could eliminate the doubts. Why?

Because, like King James II, President Clinton had lost his credibility. Repeated lies, even under oath, and his attempts to use "executive privilege" to shield himself from the normal application of the laws had combined to demonstrate that he was not—and is not—to be trusted. That is why it is tragic that the impeachment process was not permitted to end in a bona fide trial. Such a trial, unlike the sham proceedings that took place, was necessary to either exonerate the president of the charges against him and restore his credibility or to convict him and remove him from office so that a new president can govern with credibility. As it turned out, we are left with a president crippled by his own dishonesty—and a nation potentially crippled along with him. □

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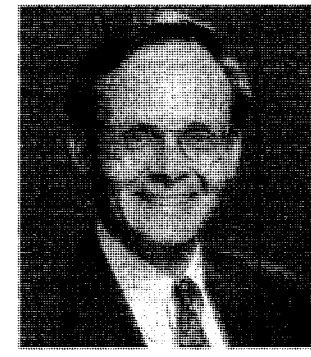
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Ending Corporate Welfare as We Know It

Corporate welfare is one of the toughest nuts to crack in Washington. While almost everyone says he is opposed to it, Congress hasn't done much about it. Maybe, just maybe, that has something to do with the fact that many congressmen are on the dole too—in the form of campaign contributions from corporate welfare recipients. A new approach is needed if American taxpayers are ever to get this monkey off their backs.

The Cato Institute estimates that direct subsidies from the federal treasury to businesses big and small, cash-rich and bankrupt alike, amount to at least $80 billion annually. (No doubt state and local governments dole out a few billion dollars more on top of that.) Companies (most notably Archer Daniels Midland) defend the handouts as being good not just for them but for the economy as a whole.

That's not an argument that was ever given much credence in debates over welfare for individuals. Most people seemed to understand that taking from A to give to B doesn't stimulate anything but B's spending at A's expense. Aid to Families with Dependent Children (AFDC) and other welfare programs for individuals were defended primarily as necessary and helpful to the recipients, rarely as a general economic stimulus. Then came overwhelming evidence that these programs were actually harmful to the recipients themselves—producing lifelong slothfulness and demoralization, intergenerational dependency, and the breakdown of families. Reforms at the federal, state, and local levels are now aimed at getting people off welfare and into work.

It seems reasonable that what's good for individuals ought to be good for companies too, especially since companies are nothing but collections of individuals anyway. Perhaps we'd be more successful at ending corporate welfare if we made it plain that it's only fair to apply the same welfare reforms to businesses that we apply to individuals. Sort of a twist on the old canard, "What's good for General Motors is good for the country."

Following this prescription, here's what corporate welfare reform might look like (and I'm being only a little bit facetious).

Declare an end to any and all "entitlements" to corporate welfare.

President Clinton signed a historic bill in 1996 that ended individuals' legal entitlement to federal subsidies. He should put businesses on notice that they are not owed anything either, except for the same common defense and other constitutional functions intended by the Founders for all of us. States should follow suit.

Put time limits on corporate welfare.

If we can't get rid of all these business handouts forthwith, then Congress should at least do what a growing number of states are doing with families formerly on AFDC: limit any company's time at the trough to five years.

Lawrence W. Reed is president of the Mackinac Center for Public Policy (www.mackinac.org), a free-market research and educational organization in Midland, Michigan, and chairman of FEE's Board of Trustees.

Impose a "family cap" on corporate welfare recipients.

New Jersey was the first state to deny additional aid to any families having more children while on welfare. Businesses should be advised that while on the corporate welfare rolls, they cannot get an increase in assistance if they hire additional employees.

Start drug testing for CEOs.

Governor John Engler of Michigan, regarded as a national leader in welfare reform, wants to deny welfare payments to individuals found to be abusing drugs. Taxpayers should not be required to subsidize corporate CEOs who abuse drugs either and there's only one way to find out if they are: if they're gettin' handouts, test 'em.

Get tough with work requirements.

To one degree or another, states now require welfare recipients to show evidence of conscientiously searching for gainful employment or doing volunteer work in their local communities. Corporate executives on the dole should also be required to prove that they are trying to straighten out their lives and develop a serious work ethic.

Require attendance at welfare-to-work counseling sessions.

Columnist Paul Gigot describes ethanol as a mixture of corn and your tax dollars. There's no reason why Dwayne Andreas, the longtime head of the Archer Daniels Midland Company and recipient of massive ethanol subsidies, shouldn't have to sit through the same social worker lectures that other welfare recipients have to endure.

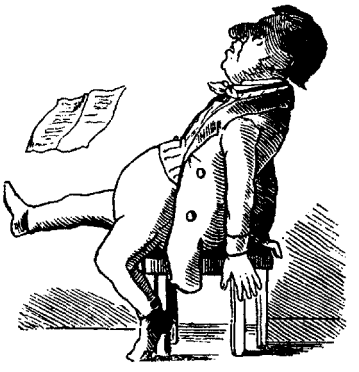
Put a "LearnFare" program in place.

Wisconsin was the first state to cut welfare benefits to parents if they couldn't keep their kids in school. Companies should be cut off if they can't keep their executives in remedial economics classes taught by economists who can explain the importance of the free economy, property rights, and keeping your hands in your own pockets.

Create incentives for the bureaucracy to discourage corporate welfare.

Wisconsin was also among the first states to reward welfare department employees for helping recipients leave the welfare rolls or stay off them in the first place. Early retirement with handsome severance packages for federal and state bureaucrats who lop corporate clients off the rolls might save us a lot of money in the long run.

President Clinton pledged in 1992 to "end welfare as we know it." He did not qualify the statement with anything like "it depends on what you mean by the word 'welfare.'" So let's call his bluff and ask him to end *all* welfare, as we've known it and as many of us would like to forget it. □



THE FREEMAN
Ideas On Liberty

Bogus Freedom

by James Bovard

"Freedom from want" is one of the most frequently invoked notions of freedom in our time. However, it is a bogus freedom that politicians and socialists offer to lull people into accepting policies that destroy true freedom. Freedom from want has been most loudly advocated in this century by those who favored removing almost all limits from government power.

For example, Sidney and Beatrice Webb, two of the founders of British socialism and authors of *The Soviet Union: A New Civilization?*, asserted in 1936: "Personal freedom means, in effect, the power of the individual to buy sufficient food, shelter and clothing."[1]

The Webbs did not specify how many millions of people government should be permitted to kill in the name of "freedom from want." But during Stalin's bloodiest decade, they asserted that for government economic planning to succeed, "public discussion must be suspended between the promulgation of the decision and the accomplishment of the task" and that any criticisms of the master plan should be treated as "an act of disloyalty, or even of treachery."[2] For government to be able to liberate people with food and clothing, it must have the power to execute anyone who criticizes the official economic plan. After visiting the Ukraine, the Webbs endorsed Stalin's war on the kulaks (the least impoverished peasants), commenting that "it must be recognized that the liquidation of the individual capitalist in agriculture had necessarily to be faced if the required increase of output was to be obtained."[3] (Output plummeted.)

Equating liberty with satisfactory living standards became far more common as the twentieth century went on. "Real freedom means good wages, short hours, security in employment, good homes, opportunity for leisure and recreation with family and friends," wrote Sir Oswald Mosley, the most prominent British supporter of Nazi Germany, in his 1936 book, *Fascism*.[4] James Gregor noted in his book *The Ideology of Fascism* that fascism aimed at "restraints which foster the increased *effective* freedom of the individual."[5] President Franklin Delano Roosevelt noted in 1937 that "even some of our own people may wonder whether democracy can match dictatorship in giving this generation the things it wants from government."[6] University of Chicago professor Leslie Pape noted in 1941 that "democracies readily admit the claims of totalitarian states to great achievements in the cause of positive freedom."[7]

British historian E.H. Carr, writing in 1951, observed that, for the modern era, "freedom from the economic constraint of want was clearly just as important as freedom from the political constraint of kings and tyrants."[8] Carr justified the array of economic controls in postwar Britain: "The price of liberty is the restriction of liberty. The price of some liberty for all is the restriction of the greater liberty of some."[9] However, with this standard,

James Bovard is the author of Freedom in Chains: The Rise of the State and the Demise of the Citizen *(St. Martin's, 1999), from which this article is adapted.*

there is no limit to the amount of freedom that government can destroy in the name of creating "greater liberty for some." The British Labour government that Carr championed advanced freedom by conscripting labor for the coal mines and empowering the Ministry of Labour to direct workers to whatever employment was considered in the national interest—empowering over 10,000 government officials to carry out searches (including of private homes) without warrants—prohibiting restaurants from serving customer meals costing more than 5 shillings (less than $2 in 1947)—and fining farmers who refused to plant the specific crops government demanded.[10] The government also "nationalized all potential land uses in the United Kingdom, permitting only continuation of existing ones and requiring 'planning permission' for any others," as law professor Gideon Kanner noted.[11]

The Labour government offered freedom via the solidarity of standing in the same rationing line—liberation via deprivation. (A 1998 *New York Times* article cited the Labour government's postwar food rationing, which continued into the 1950s, as a contributing factor to the long-term decline of British cuisine.[12])

The more politicians promise to give, the more they entitle themselves to take. Carr, serving in 1945 as chairman of the UNESCO Committee on the Principles of the Rights of Man, declared that "no society can guarantee the enjoyment of such rights [to government handouts] unless it in turn has the right to call upon and direct the productive capacities of the individuals enjoying them."[13] Thus, the price of government benefits is unlimited political control over people's paychecks and work lives.

Once freedom is equated with a certain material standard of living, confiscation becomes the path to liberation. Thus, the more avidly a politician raises taxes, the greater his apparent love for liberty. In the name of providing "freedom from want," the politician acquires a pretext to destroy the basis of private citizens' independence. "Freedom from want" becomes a license for politicians, rather than a declaration of rights of citizens.

Anyone who does not have certain possessions is assumed not to be free—and in need of political rescue. President Johnson, justifying a vast expansion of government social programs, declared in 1965, "Negroes are trapped—as many whites are trapped—in inherited, gateless poverty. . . . Public and private poverty combine to cripple their capacities."[14] Vice President Hubert Humphrey defined a poor person as "the man who for reasons beyond his control cannot help himself." This perspective on poverty and self-help mocks all of American history. It implies that any individual who earns less than $7,890 a year (the official poverty line for a single person) is incapable of any discipline or resolution.

While advocates of positive freedom insist that government must intervene so that each person "can be all that they can be," government aid programs are notorious for rewarding people for making the least of themselves. President Roosevelt warned in 1935 that "continued dependence on relief induces a spiritual and moral disintegration fundamentally destructive to the national fiber."[15] President Clinton declared in 1996: "For decades now, welfare has too often been a trap, consigning generation after generation to a cycle of dependency. The children of welfare are more likely to drop out of school, to run afoul of the law, to become teen parents, to raise their own children on welfare."[16] A rising tide no longer lifts all boats when the government rewards people for scuttling their own ships.

Faith in freedom from want depends on a political myopia that focuses devoutly on only one side of the ledger of government action. This is measuring freedom according to how much government does *for* people, and totally disregarding what government does *to* people. Government provides "freedom" for the welfare recipient by imposing tax servitude on the worker. Federal, state, and local governments collected an average of $26,434 in taxes for every household in the country, or an average of $9,881 for every U.S. resident in 1998, according to the Tax Foundation.[17] In an age of unprecedented prosperity, government tax policies have turned the average citizen's life into a financial struggle and insured that he will likely become a ward of the state in his last decades.

Some statists insist that taxation is irrelevant to freedom. According to sociologist Robert Goodin,

> If what the rich man loses when his property is redistributed is described as a loss of freedom, then the gain to the poor must similarly be described as a gain of freedom. . . . No net loss of freedom for society as a whole, as distinct from individuals within it, is involved in redistributive taxation. Thus, there is no basis in terms of freedom . . . for objecting to it.[18]

What does Goodin mean by "freedom for society as a whole"? By this standard, slavery would not reduce a society's freedom, since the slave's loss of freedom would be equaled by the slave owner's gain. Nor is there any difference, vis-à-vis freedom, between permitting people to retain their earnings and spend them as they choose, and government confiscating their money to hire more regulators, inspectors, and informants to better repress the citizenry.

What are the practical results of the modern "freedom from want"? Economist Edgar Browning, writing in 1993, examined the marginal cost of redistribution—defined as "the ratio of the aggregate loss to the top four quintiles of households to the aggregate gain to the bottom quintile of households."[19] Browning estimated that the marginal cost to the most affluent 80 percent of households of increasing the income of the poorest 20 percent by $1 was $7.82.[20] The marginal costs of redistribution are much larger than people might presume because of reduced incentives to work, both among the taxpayers and recipients. Also, as Browning noted, "marginal tax rates must be increased very sharply relative to the amount of income that is redistributed." Combining Browning's analysis and Goodin's definition, confiscatory redistribution destroys almost eight times as much "freedom" as it creates.

Once the notion of "freedom from want" is accepted as the pre-eminent freedom, it becomes a wish list justifying endless political forays deeper and deeper into people's lives. Princeton professor Amy Gutmann, in her 1980 book, *Liberal Equality*, declared: "Liberal egalitarians want to say that freedom of choice is not very meaningful without a right to those goods necessary to life itself."[21] Gutmann's elaboration of "necessary goods" reveals how government would be obliged to control almost everything: "Supplying the poorest with more primary goods will be insufficient if their sense of self-worth or their very desire to pursue their conceptions of the good is undercut by self-doubt."[22] By this standard, freedom is violated when people suffer self-doubt, and the government is obliged to forcibly intervene to guarantee that all people think well of themselves.

Political scientist Alan Wolfe, a self-described "welfare liberal," asserted in 1995 that "people need a modicum of security and income maintenance, underwritten by government, in order to fulfill the ideal of negative liberty, which is self-sufficiency."[23] Government dependency is the new, improved form of self-reliance: dependency on government doesn't count because government is a better friend to you than you are yourself. But the more dependent people become on government, the more susceptible they are to political and bureaucratic abuse. Freedom from want is conceivable only so long as people are allowed to want only what the government thinks they should have.

Freedom from want supposedly results from government taking away what a person owns so that it can give him back what it thinks he deserves. The welfare state is either a way to force people to finance their own benefits via political-bureaucratic bagmen, or it is a way to force some people to labor for other people's benefit. In the first case, government sacrifices the person's freedom to the fraud that government must tax him to subsidize him; in the second, government sacrifices the person's freedom in order to "liberate" someone else—often someone who chooses not to work. If someone pays the taxes that finance the government benefits he receives, he is less free than he would otherwise have been.

Some "freedom from want" advocates imply that government is a great benefactor when it promises citizens "three hots and a

cot"—the old-time recruiting slogan of the Marine Corps. But trading freedom for a full belly is a worse bargain now than ever before. As economist F.A. Hayek observed, "As the result of the growth of free markets, the reward of manual labor has during the past hundred and fifty years experienced an increase unknown in any earlier period in history."[24] The average worker in industrialized countries can purchase the bare necessities of life with fewer hours of labor than ever before. Comparing current wages and prices with those of 1800, economist Julian Simon found that the average American worker today needs to labor less than one-tenth the time to earn enough to purchase a bushel of wheat than his predecessors did two centuries ago.[25] While the real price of food has plummeted (in spite of government farm policies), the "real price" of political servitude has not diminished.

It is understandable that some well-intentioned people assume that "freedom from want" is the most important freedom. It is difficult for many people to conceive of enjoying anything (much less their freedom) if they lack food, clothing, or shelter. However, freedom is not a guarantee of prosperity for every citizen; the fact that some people have meager incomes does not prove that they are shackled. It is a cardinal error to confuse freedom with the things that free individuals can achieve or produce, and then to sacrifice the reality of freedom in a deluded shortcut to the bounty of freedom. Freedom is not measured by how much a person possesses, but by the restrictions and shackles under which he lives.

Throughout history, politicians have used other people's property to buy themselves power. That is the primary achievement of the welfare state. The danger of government handouts to freedom was clear to some political writers hundreds of years ago. The French writer Etienne de la Boétie, in his 1577 *Discourse of Voluntary Servitude*, noted of ancient Rome: "Tyrants would distribute largess, a bushel of wheat, a gallon of wine . . . and then everybody would shamelessly cry, 'Long live the King!' The fools did not realize that they were merely recovering a portion of their own property, and that their ruler could not have given them what they were receiving without having first taken it from them."[26]

"Freedom from want" is not possible unless the government is allowed to control all things people want. Americans must beware of Trojan-horse definitions of freedom—definitions that, once accepted, allow bureaucrats to take over everyone's life. Government handouts insinuate political power into the deepest recesses of a person's life. And when the time is ripe, politicians take command where they previously lavished their gifts. □

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The Green Scare

by Roger E. Meiners

During the Cold War, anti-communist activists were accused of using Red Scare tactics. They were parodied along these lines: The communists were everywhere, maybe even under your bed, so support the politicians who would spend massive resources, and perhaps strip away a few liberties, for the greater good of saving the nation, and especially the children, from a horrible fate. Politicians such as Senator Joseph McCarthy rose to prominence by "revealing" the threat the nation faced. Some stories were false, some exaggerated, and some true, but sensible national policy should never be based on horror stories by charlatans.

In recent years politicians have gotten good mileage with a Green Scare campaign. Vice President Al Gore wrote *Earth in the Balance,* a book filled with green scares, most of dubious merit, far overblown, or simply false, but all requiring central control of property and the economy. Environmental horror stories are so widely accepted that political opponents are chary of sneering about them. It's worth reviewing the facts about some famous Green Scare stories, most of which are still repeated as gospel.

Common Law Co-Opted

Some readers may recall the sight of flames leaping from the Cuyahoga River in Cleveland in 1969. An oil slick on the river caught fire, which lit wooden train trusses. There had been fires in the river before; the Cuyahoga, an industrial sewer, was biologically dead. A few years before the fire, a real estate company had sued the city for allowing the river to deteriorate to such a condition. The trial court ordered the city to investigate the causes of the pollution and ordered "such nuisances . . . to be abated." The supreme court of Ohio reversed, holding that the river was under the control of state authorities. Common-law protection had been erased by the Ohio Water Pollution Control Board, which had granted permission for various industries to discharge wastes into the Cuyahoga and, thereby, Lake Erie. When regulation takes precedence over common-law rights, the result can be destructive to the environment.

DDT Defamed

The book *Silent Spring* is referred to as a sacred writ of environmentalism; but it is more of a totem than a useful source of information since the book is filled with incorrect information and half-truths. The single chemical most bewailed by Rachel Carson was DDT, which was alleged to have caused massive destruction of birds (thereby leading to the silent spring when chirping would no longer be heard). As a result, DDT was banned. Yet it had saved millions of lives. Paul Hermann Müeller, its Swiss creator, won the Nobel Prize for the chemical, which con-

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trolled mosquitoes and, thereby, malaria, in many parts of the world.

Before large-scale DDT programs were introduced in 1962 in Ceylon (now Sri Lanka), there were some two million cases of active malaria reported for the country.[1] During the DDT program, the number of new active cases fell to 17 in 1963. In 1964, pressures from Western nations brought an end to the use of DDT. By 1969, 2.5 million people in Sri Lanka were suffering from the disease, partly because it was not politic to admit that wise leaders do not know their environmental science and are willing to inflict massive suffering on tens of millions of people in lesser-developed nations.

Of course there can be too much of a good thing; the federal government was so DDT-happy after World War II that it dumped huge quantities from bombers, despite objections from farmers who resisted such "help." In one case the concentration was so high from a U.S. Department of Agriculture dump that it killed a herd of cows.[2] Despite Carson's assertions, there was then and still is little evidence that individual farmers, paying for DDT, sprayed it in such massive quantities that it caused environmental damage. The relationship between DDT and damage to bird eggs is no longer the certainty that was presumed. Scientific evidence is in order before assertions are accepted and policy conclusions are reached, but politicians have little incentive to rely on science.

Air Pollution Solution

The air in Los Angeles is much cleaner today than it was in the 1950s and 1960s, despite the large growth in population and number of vehicles on the road. It is not certain that the federal Clean Air Act and the Environmental Protection Agency deserve the credit. By the time the 1970 Clean Air Act was enacted, every state had some sort of air-pollution control legislation, as did 81 counties and 107 cities.[3] Citizens of L.A. had little choice but to find a solution to the smog problem, which at the time even the best scientists could not explain well. British insurance companies holding Los Angeles municipal bonds were so concerned about the city's future prospects that they indicated the bonds would be called unless effective action was taken to clear the air.[4] Market pressure required city leaders to act. Scientists at the California Institute of Technology were paid to research the problem, and one received a Nobel Prize for identifying the photochemistry of smog. State restrictions on automobile emissions followed.

California and the rust-belt states with sooty coal-fired electric generators and steel mills knew that as they took costly steps to deal with their peculiar or worse-than-average air pollution problems, they would face competitive disadvantages. So California pressed for the rest of the nation to be forced to implement the same kinds of emission controls that made good sense for it to impose. California and the rust-belt states patched together what should have been seen as an anti-environmental alliance in crafting many provisions of the Clean Air Act. The filthiest places were given less responsibility to clean up than were the clean-air areas, and the cleanup mandates were expensive, special-interest driven measures.[5]

Since passage of the 1970 Clean Air Act, progress on air quality has been made, but it was being made before that time, perhaps more rapidly, and certainly in a more cost-effective manner designed to address local problems.[6] The billions mandated by statute to be spent on outdated technological and command-and-control solutions, to comply with standards that have little to do with scientific evidence of harm, force the consumption of many resources that could have been devoted to other worthy endeavors.

Unloved Canal

The granddaddy of all Superfund sites is Love Canal. In 1980 it generated horror stories of chemicals seeping from an abandoned toxic dump site run by Hooker Chemical Company (Occidental Petroleum). Publicity about the site helped spur public support for quick passage of the Superfund toxic-cleanup law, the Carter administration's final major "gift" to citizens before leaving office.

Love Canal was a failed entrepreneurial canal built in the 1800s. In 1941, Hooker Chemical bought the 3,000-foot long trough, which was 8 to 16 feet deep and 60 to 80 feet wide, to use to dump toxic waste from its plant on the outskirts of the City of Niagara Falls, New York. The canal soil was hard clay, so it made an excellent disposal site that did not appear to cause water contamination. In the 1950s, the city, which had been fully informed of what was under the soil, essentially condemned the Love Canal property and, over company objections, later built a public school on the grounds and allowed housing to be constructed there. Eventually, Hooker had to pay to clean up the site under the Superfund law.

Hooker was also sued in tort by citizens and various governments. The federal court judge in 1994 provided exhaustive findings in the case *U.S. v. Hooker Chemical.* The government requested punitive damages from Hooker, but the court rejected the request. Nevertheless, Hooker was held negligent, primarily for not coming forward with more information about the dangers of various chemicals in later years. "While the Company should have made greater efforts to keep local residents off the property," the judge ruled, "it violated . . . no legal obligation in failing to do so. It responded to complaints about odors, fires, and exposures to chemicals whenever notified, and there was no evidence of injury during the disposal operations that would have signaled a compelling need to provide more protection."

Love Canal is notorious. One environmental law textbook asserts that hundreds of people suffered terrible injuries there. No doubt the hysteria caused by EPA workers in space suits hustling people from their homes may have caused distress. Yet the court's review of injuries from chemical exposure shows only "relatively minor noticeable injury." That is, the Love Canal Superfund site, the stuff of environmental legends, was found, on careful examination, to be associated with little harm to human beings at the time and no lasting harm. But the company was liable for what minor harms it negligently inflicted on residents. No harm at all would have likely ever occurred had the city not demanded the property from the company and built on it, tampering with the soil cover on the chemicals.

These horror stories, the stuff of the Green Scare, have achieved the status of Official Truth. But each is grossly distorted in the service of interventionist environmentalism. Here's yet another example of the old saying that it's not what we don't know that hurts us. It's what we know that isn't so. □

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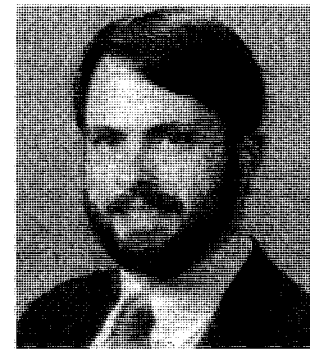
4. See Bruce Yandle, *The Political Limits of Environmental Regulation* (Westport, Conn.: Quorum Books, 1989), pp. 65–66.

5. Robert Crandall, *Controlling Industrial Air Pollution: The Economics and Politics of Clean Air* (Washington: Brookings Institution, 1983).

6. Indur Goklany, "Empirical Evidence Regarding the Role of Nationalization in Improving U.S. Air Quality," in Roger Meiners and Andrew Morriss, eds., *The Common Law and the Environment* (Bozeman, Mont.: PERC, forthcoming).

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Congressional Lost Opportunities

Although Republicans retain the control of Congress that they won in 1994, they have done little good with their power. President Bill Clinton, despite his crippling scandal woes, retains the initiative in making policy. Not only does he push for new spending programs, but his administration also continues to pour forth a flood of intrusive regulations—8,645 in the last two years alone.

Of course, people have been suffering from runaway bureaucratic rule-making ever since Congress began creating agencies. Federal regulations cost us $670 billion annually, according to Thomas Hopkins of the Rochester Institute of Technology. That's about $7,000 per family—and doesn't count lost economic growth.

For years constitutional scholars have decried Congress's "excessive delegation" of power to the hundreds of departments, agencies, and bureaus that fill Washington. Average citizens have complained too—after being fined by OSHA, penalized by the IRS, sued by the SEC, or otherwise abused by one or another alphabet-soup bureaucracy. But legislators have been unwilling to give up this tool to expand their power. After all, it would take real work for them to fill in all the blanks created by their own statutes. Equally important, doing so would allow voters to hold them responsible.

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Cases are legion where bureaucrats have created rules essentially out of whole cloth. For instance, the entire regulatory web governing wetlands grows out of the Clean Water Act, which never mentions wetlands. Yet under these rules people find their property effectively seized; an unfortunate few even end up in jail.

The Clinton administration made a similar power grab through the Food and Drug Administration's proposed controls over the tobacco industry. Such rules were never thought to be within the purview of the FDA. Nevertheless, the agency unilaterally declared its authority to ban advertising, control tobacco production, and monitor cigarette sales.

Even where the authority exists, agencies often act irresponsibly to achieve ideological ends. For example, the Clinton Environmental Protection Agency developed air pollution rules, allegedly to protect children, which offered minimal health benefits to justify their enormous cost.

Yet the GOP Congress did nothing. Republicans were unwilling to make any effort to explain why rules that sounded superficially appealing were actually environmentally as well as economically destructive.

The Clinton regulatory flood continues. As Angela Antonelli of the Heritage Foundation points out, the number of pages in the Federal Register, which catalogues federal rules, peaked under President Jimmy Carter at 87,012. It was still a too-high 53,376 pages in 1988, President Ronald Reagan's last full year in office. Last year the Federal Register was

back up to 64,549 pages. The Center for the Study of American Business reports that spending on 61 different regulatory agencies will hit $17.9 billion this year, the highest ever. Staffing is also up, to 127,927 employees (full-time equivalents).

Congressional deregulators should push an aggressive agenda. They should start by killing agencies. There is no evidence that OSHA has had any impact on workplace deaths and injuries, but plenty of evidence that its nitpicking rules cost far more than any benefits they provide. By slowing the flow of drugs to market, the FDA has killed far more people than it has saved. And so on.

Legislators should stop delegating near plenary power to regulatory bureaucracies and allowing informal "nonlegislative rules" to be binding. Congress should undertake systematic oversight of federal regulatory activity.

Regulation can be lethal. A half dozen rules—for chloroform at pulp mills, for instance—are estimated to cost literally trillions of dollars per life saved. Yet a 1994 Harvard University study figured that 60,000 people die each year as a result of today's regulatory complex, which diverts tens of billions of dollars from productive uses to fighting just such trivial risks.

Congress could at least say no to bad regulations before they take effect. Until 1996 that wasn't easy, since both houses of Congress would have had to pass a new law—over the President's veto, if necessary. Congress did create a one-chamber veto, which was later voided by the Supreme Court.

But three years ago Congress approved the Congressional Review Act (CRA). It requires all agencies to submit their rules to the Senate, House, and General Accounting Office (GAO). Legislators then have 60 days to use an expedited lawmaking process (easing the discharge of resolutions from committee, for instance) to pass a joint resolution disapproving the regulations. Already agencies have been resisting the act's requirements, just as they have sought to thwart earlier attempts to restrict new regulations. The departments of agriculture and transportation, in particular, simply refuse to submit some rules to the GAO. The GAO has done little to implement the law.

Meanwhile, Congress has not yet blocked even one rule. It may be that all 8,645 rules approved by the Clinton administration in 1997 and 1998 advanced the public interest. But it's not likely.

Past regulatory reform legislation has had little effect. For instance, the Paperwork Reduction Act and Unfunded Mandates Reform Act were both weakened before being passed in 1995 and have had only minimal impact. Other reform measures, such as property rights protection, regulatory budgets, and requirements for risk assessment, failed to become law. Throughout most of U.S. history, Congress was viewed as the strongest branch of government. But regulation has given presidents the power effectively to make law. For the sake of liberty and the Constitution, Congress needs to act aggressively to curtail agency rule-making. □

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THE FREEMAN
Ideas On Liberty

Fighting Back

by John Landrum

I have always envied "how-to" writers and secretly hoped to become one. This is my latest essay into the field. I want to bestir *Freeman* readers to make more noise in the mainstream media.

I'll offer some quick background, hoping to convince you that, if I can do it, you surely can. Until roughly three years ago, I was what Ayn Rand would have called a "contemptible middle-of-the-roader." I tended to dismiss those who talked about political issues in terms of principles, thinking them poor compromisers. I thought that we could never make democracy work if everyone insisted on his own starting position. I was well meaning and sincere. And I was like almost everyone else I knew.

Then a friend introduced me to the writings of Henry Hazlitt (*Economics in One Lesson*), Frederic Bastiat (*The Law* and *Economic Sophisms*), and Ludwig von Mises ("Economic Calculation in the Socialist Commonwealth"). Suddenly, I got it.

Reading these writings, and since then many others, I was struck by the question: why was all of this such a revelation to me? I almost never encountered even cheap imitations of these writers in any newspaper—including "conservative" newspapers.

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It occurred to me that anyone who was convinced by this stuff and took it seriously should make some racket. And writers such as Bastiat and Hazlitt gave wonderful examples of how this could be done.

Last year I found my first chance—a newspaper article in the New Orleans *Times-Picayune*—and wrote a letter to the editor in response. (A reader of my letter sent a copy to *The Freeman*, which in turn invited this article.)

I imagine I'm less well educated in free-market principles than most *Freeman* readers. So I share this story in the hope that it inspires others who may not consider themselves authorities to write confidently when they see free markets challenged.

Think of this as *The Complete Idiot's Guide to Defending Liberty*.

Unappealing Competition?

The *Times-Picayune* is the only major newspaper in New Orleans. Last May, it ran a page-one article headlined "Crawfish peelers losers in trade war." Crawfish are a favored source of protein in Louisiana. In the short season—roughly March through April—restaurants and markets sell them freshly boiled, with shells on. During the entire year, stores and restaurants buy them shelled and frozen for inclusion in sauces and stews. For this market, crawfish peelers remove the shells by hand.

The *Times-Picayune* explained that in the past few years Chinese exporters have begun to produce and peel crawfish in large quantities and sell them in Louisiana. Chinese prices are considerably lower than local ones, presumably because of the lower cost of labor in China.

The article made clear that peeling crawfish is one of the least desirable jobs imaginable, with low wages, unpleasant conditions, utter monotony, unpredictable demand for work, and frequent hand lacerations and abrasions. Nevertheless, the article called local peelers "the latest victims in the trade war with China." The federal government had slapped a tariff on Chinese crawfish imports, but according to the newspaper, that was not enough to create a "level playing field."

Local buyers were interviewed about the seeming ethical dilemma posed by the prospect of putting local workers out of jobs by buying the cheaper foreign crawfish. In reading the article, I could imagine readers writing angry letters to their congressmen urging stronger action against the insidious Chinese.

Stealing Bastiat

After reading Bastiat's *Economic Sophisms* one time through, I knew the rebuttals to the philosophical arguments implicit in the article. My letter to the editor quoted the news article's salient passages, then stated that we are no more "at war" with crawfish peelers from China than we are with wheat growers from Kansas, poultry men from Arkansas, cattlemen from Texas, automakers from Detroit, or anyone else who produces the things we need more cheaply than we can produce them ourselves. In the same way, should a French pharmaceutical company discover a low-cost cure for cancer, we would not be at war with the French, even though the cure might "threaten" the local cancer-treatment industry.

Still following Bastiat, I argued that the purpose of an economy is to create an abundance of the things we need and want, rather than to create jobs. If the essential point were to create jobs, then I could help the economy by hijacking truckloads of peeled crawfish—or better yet, blowing up roads and bridges.

I mentioned that confusion of these objectives underlay opposition to free trade. Protectionists assume that foreign producers' success can only come at the expense of local jobs in the mistaken belief that economics is a zero-sum game; they fail to recognize that trade and innovation create new wealth, with attendant new capacity and demand.

I concluded with the observation—which the *Times-Picayune* omitted—that the front page of the same edition had a long article celebrating the lowest unemployment in a long time.

I was motivated by principle, but I did fall prey to something of a stunt. One paragraph near the end of my letter stated: "Protecting uncompetitive, labor-intensive industries is a losing game. Bangladesh promotes jute production because it creates so many jobs, even though alternative materials made jute uneconomical long ago. Bangladesh is not my idea of a good economic model to follow."

My motive was to hit the "street smart," practical reader who would not easily be swayed by Bastiat's logic. My source was P.J. O'Rourke's *All the Trouble in the World*—a must-read for anyone interested in an effective challenge to people who want you to worry.

Like Shakespeare, very little of my content is original.

A Better Approach

Read, or re-read, Bastiat's *Economic Sophisms*. You'll get the clear impression that the author is having a marvelous time—luxuriating in the falsehoods of protectionists, like a porpoise sporting in the surf. The wonderful thing about the free-trade controversy is that the potential opportunities for *reductio ad absurdum* are unlimited.

After the *Times-Picayune* published my letter, it occurred to me that my article could have included an entirely different approach. Namely, if it is a good idea for Congress to protect Louisiana crawfish peelers, what American producers is it *not* a good idea for them to protect? (I suppose that we could

spare *uncompetitive* foreign imports, since presumably no local producers would lose business to them.)

And if protecting American producers from all foreign competition helps the U.S. economy, then it should also be true that in each of the 50 states, protecting in-state producers from out-of-state competition would help the state economy. That is, Arkansans as a class would presumably be richer if they could only buy from fellow Arkansans; Texans as a class would be richer if they only bought Texas-produced goods and services; and so on.

And if protecting in-state businesses from out-of-state competition would enrich each state, then it would stand to reason that a law requiring each of us to buy only from vendors located in our own *counties* would only compound the positive effect—necessitating a local producer for everything that we need.

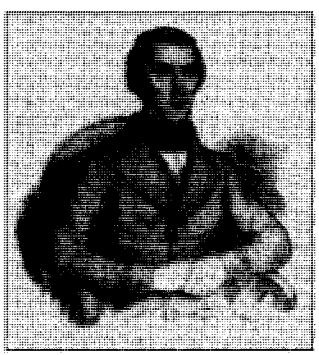
And if it would enrich everyone to insist that we buy from inside our home counties, then logically it should enrich us most to prevent us from buying from anyone—to legislate that we have to meet all of our own needs ourselves. We would certainly have full employment.

But as countless free-market advocates have pointed out, the total elimination of specialization would also restore us to the economic condition of savages.

This approach would have been a good line to pursue. I haven't seen any articles with a protectionist slant in the *Times-Picayune* since the crawfish feature and began to despair of a chance to try it. Then last fall, *USA Today* offered a debate between its editor arguing against protection (thank goodness!) and a steel industry spokesman trying to "protect American jobs." I mailed the letter immediately.

Any *Freeman* reader can do what I've done. I encourage you all to try it.

See you in the papers. □



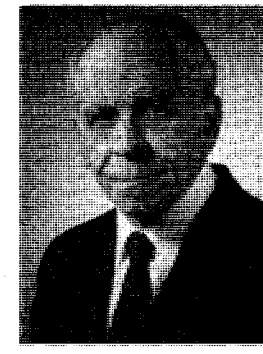
Economic Sophisms

by Frederic Bastiat

First published more than 150 years ago, these essays have come to be recognized as among the most persuasive refutations of the major fallacies of protectionism—fallacies that are still with us today and that will continue to crop up as long as the public remains uninstructed: "The introduction of machinery means fewer jobs"; "Protective tariffs keep domestic wages high"; "We need laws to equalize the conditions of production"; "Imports must be restricted to restore the balance of trade"; "High prices mean a high standard of living"; "There are no economic laws or absolute principles"; "Free trade places us at the mercy of our enemies in case of war"; and so on. The great lesson that all these essays teach, in one form or another, is the necessity of always looking at economic questions from the point of view of the consumer, rather than that of the producer. *Sophisms* contains the brilliant "Petition of the Candlemakers" (a parody of special-interest group pleading), as well as such gems as "The Negative Railroad" and "The Physiology of Plunder." This edition also contains an introduction by Bastiat's great admirer Henry Hazlitt.

291 pages, *paperback* **$7.95**

Gullible Skeptics



". . . the reason why liberty, of which we Americans talk so much, is a good thing is that it means leaving people to live out their own lives in their own way, while we do the same. If we believe in liberty, as an American principle, why do we not stand by it?"

—WILLIAM GRAHAM SUMNER (1840–1910)

Webster's defines a skeptic as "one who doubts . . . a person marked by skepticism regarding religion or religious principles." Similarly, the *Oxford English Dictionary* states that a sceptic is "One who doubts the validity of what claims to be knowledge in some particular department of inquiry (e.g., metaphysics, theology, natural science, etc); . . . an unbeliever in Christianity, infidel."

Webster's and the OED both emphasize that skeptics are likely to be especially skeptical about matters pertaining to religion. Why should this be so? Because skeptics, like most Americans, think they love liberty and seek to "liberate" people from what they regard as "religious oppression." However, as the OED also states, a skeptic is a person who is skeptical about "some particular department of inquiry"—hence, he may not be skeptical about some other department of inquiry. Indeed, we could not go through life without being unskeptical about many things, accepting them on "faith value"—for example, that diabetes is better treated with insulin than with aspirin.

I want to show that although contemporary skeptics pride themselves on disbelieving the theology of traditional religions, most of them ardently believe the theology of the Therapeutic State—the alliance of Medicine and the State—epitomized by Psychiatry. Although most educated people doubt what they regard as false claims, they do not call themselves "skeptics." Most self-styled or professional skeptics (Skeptics) are not only obsessed with agitating against what they regard as false religious claims but also act as if such doubting were a daring, modern attitude.

Actually, skepticism about religion is as old as religion itself. Adherence to religion A implies skepticism about religion B, and vice versa. Since the Enlightenment, the debunking of religion, especially Christianity, has been a veritable growth industry. Nevertheless, religious belief remains widespread. In the United States, support for religious belief as "truth" and as a political agenda is associated with the so-called Christian Right.

Skeptics are best viewed as the Christian Right's dialogic partners and political adversaries. By targeting the Religious Right, the Skeptics ally themselves—sometimes tacitly, often explicitly—with the Psychiatric Left. The result is that Skeptics are among the leading supporters of the dominant "religious" fraud and oppression of our age, Psychiatry.

The United States has a National Institute of Mental Health, but it has no National Institute of Religion. Every state has mental health laws, but none has religious health laws; indeed, none has physical health laws. Each year, hundreds of thousands of Americans are deprived of liberty on psychiatric grounds; not a single American is deprived of liberty on religious grounds. I will not belabor my view that mental illnesses, like ghosts, are nonexistent entities and that psychiatry, like slav-

Thomas Szasz, M.D., professor of psychiatry emeritus at SUNY Health Science Center in Syracuse, New York, is the author of many books including The Myth of Mental Illness *and the forthcoming* Fatal Freedom.

ery, rests on the state-sanctioned coercion of innocent individuals.

Persons engage in actions. There is no psychiatry without psychiatric acts: the paradigmatic psychiatric acts are civil commitment and the insanity defense, both euphemisms for depriving people of liberty. Civil commitment is preventive detention of the innocent. The insanity defense or, more precisely, the insanity disposition, is the punitive detention of criminals classified as "mentally ill" in prisons called "mental hospitals."

One need not be a devout skeptic to doubt that John W. Hinckley, Jr., is really innocent of attempting to assassinate President Reagan (although such is his official "diagnosis") or that he is really being treated for a bona fide illness (in a building "diagnosed" as a hospital). I submit that Hinckley's non-existent illness and psychiatric torture is emblematic of a large class of phenomena that Skeptics are not eager to be skeptical about. In the Therapeutic State, the person skeptical about religion is acclaimed as humane and scientifically enlightened, whereas the person skeptical about psychiatry is reviled as a heretic denying science and a cruel reactionary to boot.

As there is no psychiatry without psychiatric acts, so too there is no madness without mad acts. Acts we deem "mad" are either noncriminal, like depression, in which case the Skeptic rationalizes imprisoning the person in a mental hospital as saving his mind (as the inquisitors rationalized burning the heretic as saving his soul); or such acts are criminal, like murder, in which case the Skeptic basks in self-approval by demanding that the offender be "treated," not punished. In short, the Skeptic clings to the idea that mental illnesses are "real diseases" that the "sufferers" would want treated if only they recognized their true interests.

Why are so many Skeptics gullible about psychiatry? Mainly, I surmise, because psychiatrists tend to support the Skeptics' claim that religion is an "illusion." Which raises the rhetorical question, Are Skeptics more interested in the differences between true and false beliefs or the differences between consensual and coercive actions?

Psychiatry is an instrument of the coercive apparatus of the state. Separate Psychiatry and the State, and Psychiatry as we know it would melt like snow under the hot sun. Skepticism about psychiatry would then become as politically correct as skepticism about religion is now.

Consider the contrast between freedom of religion and unfreedom from psychiatry. Religion as false belief—religious relations between consenting adults—harms no one, except possibly the believer, who "deserves" to be helped or harmed by the exercise of his free choice of self-regarding religious conduct. Only Religion as political power—as violence against others masquerading as help (and the use of tax money to support Religion)—is dangerous to others. We have no religious health laws; hence, Religion is not a danger to anyone.

Mutatis mutandis, Psychiatry as false belief—psychiatric relations between consenting adults—harms no one, except possibly the believer, who "deserves" to be helped or harmed by the exercise of his free choice of self-regarding psychiatric conduct. Only Psychiatry as political power (and the use of tax money to support Psychiatry)—as violence against others masquerading as help—is a danger to others. However stubbornly true believers in Psychiatry insist that "mental illness is like any other illness," the truth is that we have no physical health laws, but we do have mental health laws. Hence, Psychiatry is a danger to everyone.

Organized religion qua religion is separated from the American State by the Constitution as well as by custom. Organized psychiatry is not: Religion qua Psychiatry is the danger that now faces us. It is Psychiatry—not Christianity—that is lavishly supported by the State and is empowered to use its coercive apparatus. It is Psychiatry—not Christianity—that is the grand deception of our age. It is Psychiatry—not Christianity—that Skeptics ought to unmask, ridicule, condemn, and combat. □

THE FREEMAN
Ideas On Liberty

Friedrich A. Hayek: A Centenary Appreciation

by Richard M. Ebeling

In 1967, English economist Sir John Hicks published an essay titled "The Hayek Story" in which he said that:

> When the definitive history of economic analysis during the nineteen thirties comes to be written, a leading character in the drama (it was quite a drama) will be Professor Hayek. . . . Hayek's economic writings . . . are almost unknown to the modern student; it is hardly remembered that there was a time when the new theories of Hayek were the principal rival of the new theories of Keynes. Which was right, Keynes or Hayek?[1]

In February 1931, Friedrich August von Hayek had arrived in England from Vienna, Austria, to deliver a series of lectures at the London School of Economics. The lectures created such excitement and sensation that he was invited to permanently join the faculty of the LSE.[2] In the early fall of 1931 these lectures appeared in book form under the title *Prices and Production* and began the "drama" to which John Hicks referred. Indeed, in the years between 1931 and 1935, Hayek was the third-most frequently cited economist in the English-language economics journals. (John Maynard Keynes and his Cambridge University colleague Dennis Robertson came in first and second.)[3]

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But by the 1960s, when Hicks wrote the passage quoted, the general opinion among economists and policy-makers would have been almost unanimous. The "New Economics" of Keynes dominated the economics profession and was the guiding star for macroeconomic policy. Hayek was only known to those who took an interest in the economic ideas of the earlier decades of the twentieth century. Thirty years later, however, it is Keynesian economics that is now merely a passing episode in the history of economic ideas. And it is Hayek's ideas in economics, political philosophy, social theory, and the methodology of the human sciences that have gained increasing attention and relevancy as the twentieth century draws to a close.

One War, Two Doctorates

On May 8, 1899, F.A. Hayek was born in Vienna. The occasion of his centenary serves as an appropriate opportunity to appreciate the man and his contributions to the cause of liberty and the free-market economy. Hayek had briefly served in the Austrian Army on the Italian front during World War I. Shortly after returning from the battlefield in 1918 he entered the University of Vienna and earned two doctorates, one in jurisprudence in 1921 and the other in political science in 1923. While at the university, he studied with one of the founders of the Austrian school of economics, Friedrich von Wieser.

But perhaps the most important intellectual

influence on his life began in 1921, when he met Ludwig von Mises while working for the Austrian Reparations Commission. It is not meant to detract from Hayek's own contributions to suggest that many areas in which he later made his profoundly important mark were initially stimulated by the writings of Mises. This is most certainly true of Hayek's work in monetary and business-cycle theory, his criticisms of socialism and the interventionist state, and in some of his writings on the methodology of the social sciences.

In 1923 and 1924, Hayek visited New York to learn about the state of economics in the United States. After he returned to Austria, Mises helped arrange the founding of the Austrian Institute for Business Cycle Research, with Hayek as the first director. Though Hayek initially operated the institute with almost no staff and only a modest budget primarily funded by the Rockefeller Foundation, it was soon recognized as a leading center for the study of economic trends and forecasting in central Europe. Hayek and the institute were frequently asked to prepare studies on economic conditions in Austria and central Europe for the League of Nations. When Hayek moved to London in September 1931, Oskar Morgenstern became the institute's director until the Nazi annexation of Austria in March 1938, when it ceased to operate as an independent organization. Beginning in 1929, Hayek was also a *Privatdozent* (an unsalaried professor) at the University of Vienna.

Hayek and the Great Depression

Hayek remained at the London School of Economics until 1949. During that time he published a large body of work that established his international stature as one of the leading economists of his time. It was during this period that he became the greatest challenger to the emerging New Economics of Keynes. In *Prices and Production*; *Monetary Theory and the Trade Cycle* (1933); a series of articles reprinted in 1939 under the title *Profits, Interest and Investment*; and *The Pure Theory of Capital* (1941), Hayek argued that business cycles had their origin in the mismanagement of the monetary system. Also, in 1931–1932, Hayek wrote a lengthy two-part review of Keynes's *Treatise on Money* for the journal *Economica*. It was considered a definitive critique of Keynes's work.[4] The Great Depression served as the backdrop against which Hayek explained his own theory and criticized Keynes.

Hayek argued that in the 1920s, the American Federal Reserve System had followed a monetary policy geared toward stabilizing the general price level. But that decade had been one of major technological innovations and increases in productivity. If the Federal Reserve had not increased the money supply, the prices for goods and services would have gently fallen to reflect the increased ability of the American economy to produce greater quantities of output at lower costs of production.

Instead, the Federal Reserve increased the money supply just sufficiently to prevent prices from falling and to create the illusion of economic stability under an apparently stable price level. But the only way the Fed could succeed in this task was to increase reserves to the banking system, which then served as additional funds lent primarily for investment purposes to the business community. To attract borrowers to take these funds off the market, interest rates had to be lowered. Beneath the calm surface of a stable price level, interest rates had been artificially pushed below real market-clearing levels. That generated a misdirection of labor and investment resources into long-term capital projects that eventually would be revealed as unsustainable because there was no savings available to complete and maintain them.

The break finally came in 1928 and 1929, when the Fed became concerned that prices in general were finally beginning to rise. The Fed stopped increasing the money supply, investment profitability became uncertain, and the stock market crashed in October 1929. Hayek argued that the economic downturn that then began was the inevitable consequence of the investment distortions caused by the earlier monetary inflation. A return to economic balance required a writing down of unprofitable

capital investments, a downward adjustment of wages and prices, and a reallocation of labor and other resources to uses reflecting actual supply and demand in the market.

But the political and ideological climate of the 1930s was one increasingly dominated by collectivist and interventionist ideas. Governments in Europe as well as the United States did everything in their power to resist these required market adjustments. Business interests as well as trade unions called for protection from foreign competition and government support of various types to keep prices and wages at their artificial inflationary levels. International trade collapsed, industrial output fell dramatically, and unemployment increased and became permanent for many of those now out of work.

Throughout the 1930s Keynes presented arguments to justify activist monetary and fiscal policies to try to overcome the imbalances the earlier monetary manipulation and interventions had created. This culminated in his 1936 book, *The General Theory of Employment, Interest and Money*, which soon became the bible of a new macroeconomics that claimed that capitalism was inherently unstable and could only be saved through government "aggregate demand management." Hayek and other critics of Keynesian economics were rapidly swept away in the euphoric belief that government had the ability to demand-manage a return to full employment.

But while seemingly "defeated" in the area of macroeconomics, Hayek realized that what was at stake was the wider question of whether in fact government had the wisdom and ability to successfully plan an economy. This also led him to ask profoundly important questions about how markets successfully function and what institutions are essential for economic coordination to be possible in a complex system of division of labor.

Debunking Central Planning

In 1935, Hayek edited a collection of essays titled *Collectivist Economic Planning*, which included a translation of Mises's famous 1920 article, "Economic Calculation in the Socialist Commonwealth." For the volume, Hayek wrote an introduction summarizing the history of the question of whether socialist central planning could work and a concluding chapter on "the present state of the debate" in which he challenged many of the newer arguments in support of planning. This was followed by a series of articles over the next several years on the same theme: "Economics and Knowledge" (1937), "Socialist Calculation: The Competitive 'Solution'" (1940), "The Use of Knowledge in Society" (1945), and "The Meaning of Competition" (1946). Along with other writings, they were published in a volume with the title *Individualism and Economic Order* (1948).[5]

In this work Hayek emphasized that the division of labor has a counterpart: the division of knowledge. Each individual comes to possess specialized and local knowledge in his corner of the division of labor that he alone may fully understand and appreciate how to use. Yet if all of these bits of specialized knowledge are to serve everyone in society, some method must exist to coordinate the activities of all these interdependent participants in the market. The market's solution to this problem, Hayek argued, was the competitive price system. Prices not only served as an incentive to stimulate work and effort, they also informed individuals about opportunities worth pursuing. Hayek clearly and concisely explained this in "The Use of Knowledge in Society":

> We must look at the price system as such a mechanism for communicating information if we want to understand its real function. . . . The most significant fact about this system is the economy of knowledge with which it operates, or how little the individual participants need to know in order to be able to take the right action.[6]

In elaborating his point, Hayek wrote that "The marvel is that in a case like that of a scarcity of one raw material, without an order being issued, without more than perhaps a handful of people knowing the cause, tens of thousands of people whose identity could not be ascertained by months of investigation, are

made to use the material or its products more sparingly."[7]

Hayek added: "I am convinced that if it [the price system] were the result of deliberate human design, and if the people guided by the price changes understood that their decisions have significance far beyond their immediate aim, this mechanism would have been acclaimed as one of the greatest triumphs of the human mind."[8]

It was in this period that Hayek applied his thinking about central planning to current politics. In 1944 he published what became his most famous book, *The Road to Serfdom*, in which he warned of the danger of tyranny that inevitably results from government control of economic decision-making through central planning. His message was clear: Nazism and fascism were not the only threats to liberty. The little book was condensed in *Reader's Digest* and read by millions.

In 1949 Hayek moved to the United States and took a position at the University of Chicago in 1950 as professor of social and moral science. He remained there until 1962, when he returned to Europe, where he held positions at various times at the University of Freiburg in West Germany and the University of Salzburg in Austria.

Undesigned Order

The realization that something so significant—the price system—was *undesigned* and not *intended* to serve the purpose it serves so well became the centerpiece of Hayek's writings for the rest of his life. He developed the idea in several directions in another series of works, including, *The Counter-Revolution of Science* (1952); *The Constitution of Liberty* (1960); *Law, Legislation and Liberty* in three volumes (1973–1979); in various essays collected in *Studies in Philosophy, Politics and Economics* (1967) and *New Studies in Philosophy, Politics, Economics and the History of Ideas* (1978); and in his final work, *The Fatal Conceit: The Errors of Socialism* (1988).

His underlying theme was that most institutions in society and the rules of interpersonal conduct are, as the eighteenth-century Scottish philosopher Adam Ferguson expressed it, "the result of human action, but not the execution of any human design."[9] In developing this idea, Hayek consciously took up the task of extending and improving the notion of the "invisible hand" as first formulated by Adam Smith in *The Wealth of Nations* and refined in the nineteenth century by Carl Menger, the founder of the Austrian school of economics.[10]

Hayek argued that many forms of social interaction are coordinated through institutions that at one level are unplanned and are part of a wider "spontaneous order." Language, customs, traditions, rules of conduct, and exchange relationships have all to a large extent evolved and developed without any conscious design guiding them. Yet without such unplanned rules and institutions, society would have found it impossible to progress beyond a rather primitive level.

Another way of expressing this is that in Hayek's view, the unique characteristic of an advanced civilization is that no one mind (or group of minds) controls or directs it. In a small tribal society all members often share basically one scale of values and preferences; the chief or leader can know the potentialities of each member and can assign roles and duties so that the tribe's physical and mental means can be applied more or less successfully to the common hierarchy of ends.

However, once the group passes beyond a simple level of development, any further social progress will require radical revision of the social rules and order: the complexity of social and economic activity will make it impossible for any individual to master the information necessary to coordinating the members of the group. Nor will the members continue to agree on preferences and values; their actions and interests will become more diverse.

An advanced society, therefore, must always be a "planless" society, that is, a society in which no one overall "plan" is superimposed over the actions and plans of the individuals making up the society. Instead, civilization is by necessity a "spontaneous order," in which the participants use their own special knowledge and pursue their own individually chosen plans without a higher will or mind guiding them.

"Social Justice"

The very complexity that makes it impossible to know all the information required to guide society, Hayek reasoned, makes it equally impossible to judge the "justice" or "worthiness" of an individual's total actions. As a result, the popular call for "social," or "distributive," justice is inapplicable in a free society. Social justice requires not merely that individuals receive what is rightly theirs in general terms, but that individuals and groups also receive some stipulated distributional share of the society's total output or wealth. However, Hayek showed that in the market economy, distributions of income are not based on some standard of "deservedness," but rather on the degree to which the individual has directly or indirectly satisfied consumer demand within the general rules of individual rights and property.

To attempt to distribute income shares by "deservedness" would require the government to establish some overarching standard for disbursing "social justice," and would necessitate an economic system in which that government had the authority and the power to investigate, measure, and judge each person's "right" to a share of the society's wealth. Hayek suggested that such a system would involve a return to the mentality and the rules of a tribal society: government would reimpose a single hierarchy of ends and would decide what each member should have and what should be expected from him in return. It would mean the end of the free and open society.

In October 1974, Hayek won the Nobel Prize in economics (along with Swedish welfare-state economist Gunnar Myrdal). In explaining its reasons for choosing Hayek for this highest of awards, the Nobel Committee drew especial attention to his contributions to monetary and business-cycle theory and to his work on alternative economic systems.

By the time Hayek died on March 23, 1992, at the age of 91, an answer could finally and clearly be given to Sir John Hicks's question: "Who was right, Hayek or Keynes?" Hayek was right, regarding both Keynesianism and socialism.

And thanks to his ideas, the 21st century may very well be a freer and more prosperous place to live. □

1. Sir John Hicks, "The Hayek Story," in *Critical Essays in Monetary Theory* (Oxford: Oxford University Press, 1967), p. 203.

2. Lord Robbins, *Autobiography of an Economist* (New York: St. Martin's Press, 1971), p. 127.

3. Brian Snowdon and Howard R. Vane, "The Development of Modern Macroeconomics," in Brian Snowdon and Howard R. Vane, eds., *A Macroeconomic Reader* (New York: Routledge, 1997), pp. 4–5.

4. Hayek's review essay of Keynes's *Treatise on Money* as well as Keynes's reply are reprinted in Bruce Caldwell, ed., *The Collected Works of F. A. Hayek*, Vol. 9: *Contra Keynes and Cambridge* (Chicago: University of Chicago Press, 1995). See also my review of this volume in *Freedom Daily*, September 1995, pp. 43–48.

5. Hayek's two contributions to *Collectivist Economic Planning*, his 1940 essay "Socialist Calculation: The Competitive 'Solution,'" and other related essays by him on the theme of socialism and planning have been reprinted in Bruce Caldwell, ed., *The Collected Works of F. A. Hayek*, Vol. 10: *Socialism and War* (Chicago: University of Chicago Press, 1997). See also my review of this volume in *Freedom Daily*, January 1998, pp. 43–48.

6. F.A. Hayek, "The Use of Knowledge in Society" (1945), in *Individualism and Economic Order* (Chicago: University of Chicago Press, 1948), p. 86.

7. Ibid., p. 87.

8. Ibid.

9. See Hayek's essay, "The Result of Human Action But Not of Human Design" in *Studies in Philosophy, Politics and Economics* (Chicago: University of Chicago Press, 1967), pp. 96–105.

10. Carl Menger, "The Theoretical Understanding of Those Social Phenomena which are not a Product of Agreement or of Positive Legislation, but are Unintended Results of Historical Development," [1883], in Richard M. Ebeling, ed., *Austrian Economics: A Reader* (Hillsdale, Mich.: Hillsdale College Press, 1991), pp. 183–211.

THE FREEMAN
Ideas On Liberty

The New Money

by George C. Leef

By now you have probably received and spent some of the U.S. Treasury's new currency. Starting with the hundred-dollar bill in 1996, the Treasury has redesigned all three of our larger denomination bills, and plans to redesign the smaller bills in the future. Treasury Secretary Robert Rubin, on release of the new twenty-dollar bill in 1998, said that each new bill "marks a new stage in the government's assault on would-be counterfeiters."

The new money certainly does contain an impressive array of features that seem to make it more difficult for anyone to produce a bill that would pass careful inspection: color-shifting ink; security threads; microprinting; fine line printing patterns; larger, more detailed portraits; and other security features designed to foil counterfeiters.

While the new currency is being put into circulation, the old will not be recalled. A reason, if not *the* reason, for not recalling the old currency is that so much of it is abroad. Upwards of two-thirds of all U.S. currency is held in foreign countries, and the Treasury feared disruption of those economies if the old money were declared to be invalid as of a certain date. So the old currency will continue in circulation alongside the new for years to come.

This has led some people to question whether the introduction of new bills will really do much to defeat counterfeiting. The old U.S. currency, according to experts, was among the easiest of all currencies to counterfeit. It had remained unchanged since 1929, giving counterfeiters a lot of time to hone their skills. Moreover, scanners and laser printers can do a very good job of reproducing the old bills. Other nations have updated their currency over the decades. The Australians, for example, produce their currency on plastic with clear windows, making counterfeiting difficult. But the old U.S. bills relied on what was the state of the art in 1929. So even if the new bills are hard to counterfeit, there currently isn't any need to try.

Edward J. Green and Warren E. Weber, economists with the Federal Reserve Bank of Minneapolis, sought to evaluate the prospects for success of the Treasury's policy of printing new bills, but honoring the old and only gradually removing them from circulation in "Will the New $100 Bill Decrease Counterfeiting?" (Federal Reserve Bank of Minneapolis *Quarterly Review*, Summer 1996). After a sophisticated analysis, they conclude that they can't say: "Although we do not show that the current policy will necessarily be effective in the near term, we do show that a long-term failure cannot be taken for granted." As federal programs go, that is actually not too bad.

A Question of Incentives

People, including government officials, generally act in accordance with their incentives. Where they stand to make a significant gain (or avert a significant loss) from taking

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action, they can be counted on to do so. As public choice economists have been saying for a long time, we should not expect that government officials will do things just because they are in "the public interest." The interests of the state do not often coincide with the interests of the ordinary citizen. Counterfeiting is a species of fraud and should be illegal. But government officials devote their efforts and resources to fighting the crimes that do them the most good.

If violent crimes are on the increase, politicians take notice and will at least take some grandstanding measures so that opponents won't accuse them of being "soft on crime." If tax evasion is on the increase, politicians will really take notice, since tax evasion reduces their ability to spend money on the programs that voters like (or at least think they like). Counterfeiting, however, does not have much impact. Competition in the production of money is definitely not welcome, but if the unlucky citizen occasionally gets stuck with a bogus twenty-dollar bill, the loss is his. The political incentive to combat counterfeiting isn't very strong compared to other goals and it should not surprise us that it has not been a high priority.

Furthermore, we may wonder if the attack on counterfeiting won't turn out to be more a matter of bravado than of effect. Printing the new bills may deter some counterfeiters who conclude that it is too costly to produce new bills that will pass, but it is not going to keep creative people who want to augment their incomes from trying to make and pass bills. In fact, shortly after the introduction of the new twenty-dollar bill, I read an article in my local newspaper about an unsuccessful attempt to pass a very poor counterfeit bill. It was two sheets that had been copied and glued together—upside down! A store clerk easily identified the bill as a fake.

Store owners and everyone else taking money in exchange for valuable goods and services have a strong incentive to see to it that they are paid with genuine money (or checks or credit cards). They will take what they believe to be the optimal degree of precaution against accepting counterfeits, and if you observe the behavior of bank tellers, retail clerks, vendors, and others who handle a lot of money, you conclude that the optimal level of precaution is very low indeed. They rarely examine the money they receive with any care.

The new currency has features that make it possible for the average person to tell a real bill from a high-quality counterfeit with a good deal of certainty. Listen to Secretary Rubin: "If you tilt the note back and forth, you will see the color-shifting ink change from green to black, and back again. And by holding the note up to the light, you will see a watermark on the right, and a security thread on the far left with its own tiny lettering and graphics. These are simple things each and every one of us can and should do." Sure, but how many money-handlers are going to take the time to look for those features unless a bill is printed badly enough to arouse suspicion?

Private Enterprise Versus Counterfeiting

The problem of counterfeiting is not unique to government currency. Businesses stand to lose money if people are able to counterfeit their products, and for that reason have a strong incentive to search for the most cost-effective means to prevent or detect counterfeits. Consider, for example, the credit card industry.

When bank credit cards were first introduced in the early 1970s, the issuers suffered large losses due to counterfeiting. It was easy for criminals to create and use phony plastic cards. The resulting losses were not diffused among the general public, but were felt by the card issuers, who realized that they had to find a solution.

The solution was the hologram. MasterCard pioneered the use of holograms in 1983 and since then they have become almost ubiquitous. Because hologram technology was not widely dispersed, this innovation dramatically reduced the amount of fraud through counterfeiting.

However, just as offense tends to catch up to defense and vice versa in war, eventually criminals found out how to produce them and get back into the card fraud game. But the

card issuers, with a constant eye on the bottom line, continue to work to minimize losses. Some cards now bear a photo identification, and cardholders are also required to confirm receipt of new or replacement cards via telephone, which has proved effective in cutting down on theft.

Counterfeit software is also a financial problem for software makers. The new Windows 98 booklet has an elaborately printed certificate of authenticity and says in fine print: "IS IT GENUINE? If you believe this certificate or the software you obtained with your system is not legally licensed and/or may be counterfeit, please e-mail Microsoft at piracy@microsoft.com." It is safe to conclude that Bill Gates has his executives constantly on the lookout for the most effective means of dealing with software counterfeiting.

Yes, credit cards, computer software, and many other items continue to be counterfeited, as does our money, old and new. The key difference is in the incentives of the people responsible. While business people who stand to lose money are always alert to the problem of counterfeiting and thus search for the optimal methods to deter it, government officials do not have such a direct, powerful incentive. After doing nothing innovative for decades, the Treasury has come up with an anti-counterfeiting program about which the best that can be said is, to repeat Green and Weber, "its failure cannot be taken for granted."

Private Money?

Back in 1976, the Nobel laureate economist F. A. Hayek published a provocative essay entitled "The Denationalization of Money." He argued that it was a grave mistake to allow governments a monopoly on money and that we should do away with legal tender laws and permit individuals to trade in whatever media of exchange they think best.

His reason for advocating this idea was not the problem of counterfeiting, but rather the problem of stability of value. Money issuers, private and governmental, would have a strong incentive to maintain the value of their money if they faced competition in the monetary marketplace. Depreciating money would be as undesirable as foodstuffs that rapidly rotted. Subjected to the test of the marketplace, good money would drive out bad money. (No, that is not contrary to Gresham's Law, which says that artificially overvalued money tends to drive out of circulation artificially undervalued money; in a free monetary market, government cannot artificially overvalue anything.)

A good side effect of monetary competition, however, would be that it would also bring into play the market's incentives to combat counterfeiting. Private issuers would compete in many respects, among them the reliability of their products. The firms that have already ventured into the realm of electronic money (e-cash) have taken pains to assure customers that accounts will be secure. Producers of tangible money would have the same strong incentive to see to it that their users had confidence in the genuineness and worth of their money.

We are used to thinking that the production of money is one of the core functions of government, but there is no reason why the production of money must be a governmental monopoly, or even a governmental function at all. There were private money producers—mints—in operation in America during the colonial period and also well into the nineteenth century. They had to pass the test of the market, unlike federal mints, and when they did so, they thrived. (For an interesting history, see Brian Summers, "Private Coinage in America," *The Freeman*, July 1976.)

Marketplace competition provides the optimal incentives for maximizing consumer welfare—giving people the greatest value for their money. That applies to money itself. The next time you receive some money, new or old, you might think about that. □

THE FREEMAN
Ideas On Liberty

Gold Policy in the 1930s

by Richard H. Timberlake

Between 1929 and 1933, the Federal Reserve System, which is the central bank of the United States, monetarily starved the country into the worst economic crisis it has ever experienced. Markets, and the market system generally, did not fail, and nothing was inevitable about the collapse that occurred. Rather, the monetary system was so mismanaged that even a healthy and vigorous market system could not correct the disequilibrium that resulted.

The popular application of "market failure" to describe the economy during the years of the Great Contraction, 1929–1933, is wrong. Market actions in that era made the politically inspired crisis less severe than it otherwise would have been. Furthermore, "market failure" is a term people often apply to events when they cannot understand the complexities of economic processes that result from ill-conceived government policies. The operations of just about any monetary system, and especially one with a central bank, are always puzzling to the layman. Consequently, when things go wrong owing to monetary mismanagement by central bankers or some other political intervention, the instigators can ring in "market failure" as an excuse for their personal failures to make the right decisions.

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Failure in other aspects of human endeavor often generates learning that subsequently leads to correction and eventual success.[1] Federal Reserve policy failure in 1929–1933, however, led only to federal legislation that *increased* the number and power of federal government agencies. The Republican Hoover administration, for example, initiated the expensive Reconstruction Finance Corporation in 1932 to carry out lending policies that the elaborately structured Federal Reserve System had failed to undertake. The Roosevelt administration then took control of the political machinery in 1933 and began a program of federal intervention and bureaucratic propagation that is mind-boggling even today.

Two items of Roosevelt-era legislation markedly affected the U.S. banking and monetary system. The first was the so-called Gold Reserve Act of 1934. This legislation gave the president the unconstitutional power to call in all privately owned gold for deposit in the U.S. Treasury. It also gave him the unconstitutional power by his fiat to *revalue* the price of gold (*devalue* the dollar) by as much as 60 percent.

Congress's constitutional power to "regulate the value of money" was a power that could *not* be delegated to the executive. Furthermore, "regulate" did not mean a massive change in the monetary values of either gold or silver. Its sole purpose was to provide a means for congressional housekeeping control over the coinage system. Properly used, it allowed Congress to make incremental

changes in the legal tender value of either gold or silver so that both metals would stay in circulation. It was put into the Constitution to counteract Gresham's Law. Otherwise, changes in the market value of one or the other metal would result in what had now become the cheaper metal going to the mint and the other, dearer, metal going into the markets as a commodity.[2]

A New Central Banking Measure

The other piece of legislation, the Banking Act of 1935, was more momentous than the original Federal Reserve Act passed in 1913. In fact, the Act of 1935 might better have been labeled "The Central Banking Act of 1935," because it virtually rewrote the earlier Act.

A central bank, like a gold standard, can assume many institutional forms that differ markedly from one another. The 1913 Fed Banks, for example, were regionally autonomous; the Board in Washington was relatively powerless. Board members were treated and paid on a scale similar to government employees in the U.S. Treasury, while the presidents of the regional Fed Banks commanded salaries comparable to those of executives heading major corporations. The Fed Banks' gold reserves severely restricted their lending policies, as was proper under an operational gold standard. Finally, the real bills doctrine was supposed to furnish the grounds for Fed Banks' accommodation of credit to their client member banks.

The Banking Act of 1935 changed the whole paraphernalia of monetary control. It vested the Federal Open Market Committee (FOMC) with complete discretionary control to determine the stock of money in the United States. Regional Fed Bank presidents still had five of the 12 seats on the FOMC, but the Board was now a seven-man majority. From that time on, the FOMC has fashioned monetary policy by authorizing the purchase (or sale) of U.S. government securities in the open market, an operation that the Fed Bank of New York conducts week by week.

When the FOMC buys the U.S. securities that the Treasury has previously sold to pay the government's bills, it does so by creating money. This new money is either commercial bank reserves or Federal Reserve note currency. Clearly, if a 12-person board is determining the quantity of money that exists, the quantity of gold in the system has little or nothing to do with the money. Either a gold standard specifies the quantity of money in the economy, or a central bank does. A marriage of the two never lasts longer than an unhappy weekend.

The Gold Reserve Act of 1934 was the final divorce decree between gold and the monetary system. After January 31, 1934, no private household, bank, or business was allowed to own or hold more than a trivial amount of gold. Gold coin was forbidden for monetary purposes. This Act also authorized the president, Franklin Roosevelt, to raise the price of gold by 60 percent. Roosevelt, however, did not use all the power given him—only 98 percent of it. In early 1934, he increased the official mint price of gold, which had been $20.67 per ounce for 100 years, to $35 per ounce. The Treasury gold stock, valued at $4,033 million in *January* 1934, became $7,348 million in *February* 1934, an increase of $3,405 million by the decree of one man.[3] The federal government had also, unconstitutionally, repudiated all gold clauses in its contracts and debts, so it did not have to share any of its newfound wealth with the private sector. In one month Congress and Roosevelt, by their legislative and administrative fiats, created seigniorage revenue from gold equal to one year's ordinary tax revenues. In contrast, the federal government of 1834–1837, when it realized one year's extraordinary revenue from land sales, returned that surplus to the state governments to be used or distributed as those sovereign governments saw fit.[4]

President Roosevelt rationalized this usurpation of private property rights in gold in one of his notorious fireside chats. "Since there was not enough gold to pay all holders of gold obligations," he claimed, "the Government should in the interest of justice allow none to be paid in gold."[5]

This rationalization of government confiscation was fatuous pretension. Gold in banks

was then and had always been a *fractional* reserve against outstanding obligations. When the banks were on their own, they had adequate means to protect their reserves—gold, silver, or other legal tender. The Fed Banks and the U.S. Treasury—government institutions—also held only fractional reserves against their outstanding currencies. Use of gold as a recognized fractional reserve always precluded immediate liquidation of all monetary obligations into gold. So in effect Roosevelt was saying, "Since there was not enough gold to pay all holders of gold obligations, . . . *the federal government should expropriate and keep all of the gold.*"

The increase in the dollar price of gold, though other countries had gone off the gold standard or had also raised the price of gold in their own currencies, started a massive inflow of gold to the United States. Political apprehension in Europe and elsewhere also contributed to the U.S. accumulation. By 1940 the U.S. gold stock totaled $20 billion, or almost 20,000 tons! The contrast was notable between a government awash in gold and a depressed economy denuded of money and functioning with a shell-shocked banking system.

Fed Banks and the Treasury still accounted new gold coming into the U.S. system as though the gold were a monetary asset. The Treasury issued "Gold Certificates"—currency notes in $100,000 denominations—accounted at the new gold price of $35 per ounce, which it "deposited" in Federal Reserve Banks. Fed Banks then debited their "Treasury deposit" liability account, and credited their "Gold Certificates." Whoever had received a check for the gold from the Treasury, however, had by now deposited that check in a commercial bank that in turn sent it to the Fed Bank for clearance. The Fed Bank cleared the check against the "Treasury deposit" account and debited the deposit-reserve account of the client bank by the same amount. No one could get the gold out of the Treasury, or touch it, or see it, or use it. (It was now a criminal act to use gold for monetary purposes!) Nonetheless, the gold provided an accounting medium for increasing the basic money stock of bank reserves and Federal Reserve note currency.

The Treasury in Control—The Fed Plays Ball

With all of the new gold coming into the system, the FOMC did not need to use its newly legislated powers. From 1933 to 1936, the M2 money stock grew at annual rates of 9.5, 14.0, and 13.0 percent.[6] In fact, so much gold was coming into the Fed-Treasury's coffers that sentiment in both the Fed and Treasury leaned toward monetary restriction.

The Fed had active hands-on control of monetary policy. Not only did it have the power to initiate open-market operations in government securities through the FOMC, but the Banking Act of 1935 also gave the Fed Board extensive control over member bank reserve requirements. Prior to the Banking Act, reserve requirements were statutory at 7, 10, and 13 percent—not based on the size of the bank, but on the size of the city in which the bank was located. The larger the city the higher the legal reserve requirement.[7] The Banking Act of 1935 used the existing set of reserve requirements as the lower end of a new *range* of requirements: 7–14, 10–20, and 13–26 percent. Board of Governors' decisions in Washington were to specify the precise set of requirements in force at any time. Thus Fed policy could be restrictive by mandating an increase in requirements.[8]

Banking Act or not, the Treasury was still very much in the monetary picture. Treasury Secretary Henry Morgenthau, Jr., had recommended to President Roosevelt the appointment of Marriner Eccles to be chairman of the Federal Reserve Board. Eccles outspokenly favored lots of federal spending and fiscal budget deficits. By his stance, he effectively signed over monetary policy to the Treasury. (Morgenthau had recommended Eccles for this reason.) The upshot of the arrangement was that Morgenthau ran the show. Both men favored a dominant fiscal policy that had Federal Reserve support. Although the new Banking Act took the secretary of the Treasury off the Fed's Board of Governors (he had been the ex officio chairman), he now had a surrogate as chairman. He was more than satisfied to see his purposes served from behind the throne.

Even a surrogate position was not enough for Morgenthau. The realized seigniorage from the gold devaluation had given the Treasury a $2 billion windfall, accounted in an Exchange Stabilization Fund, that the Treasury was supposed to use to "stabilize" the dollar price of foreign currencies. The Treasury thus had a gold "position" and license for conducting gold policy.

Federal Reserve policy directed the first increase (50 percent) in reserve requirements in August 1936—from 7, 10, and 13 percent to 10½, 15, and 19½ percent. A few months later the Treasury initiated its own gold sterilization policy—the same policy the Fed had fostered in the 1920s. Its purpose was "to halt the inflationary potentialities [sic]" of all incoming gold. Beginning December 22, 1936, the Treasury placed its gold purchases in an "inactive" account. Instead of issuing gold certificates and depositing them in Fed Banks to raise the necessary credit balance to pay for the gold, the Treasury paid for the gold by selling government securities in financial markets. By this means, it carried out its own open market operations—sales in this case—with its own "FOMC." This way the gold remained stockpiled but unmonetized in the Treasury.

Besides neutralizing the gold inflows, the policy was further deflationary because it brought more government securities into markets to compete with consumers' and investors' dollars. It thereby tended to raise interest rates as it inhibited general spending. In March and May of 1937, the Fed complemented this generally deflationary policy by increasing reserve requirements to the maximum allowable percentages: 14, 20, and 26 percent.

Fed-Treasury policy makers had acted deliberately and purposively. They believed in human management of the monetary system. Just before he was appointed Fed chairman, Eccles had boldly stated that the Fed should "support expansionary fiscal policy through discretionary monetary policy."[9] Unfortunately, the discretionary monetary policy now being practiced was anything but expansionary. It was, in fact, extremely repressive.

Unprecedented Depression

However, the rest of the economy, unlike politically prosperous Washington, was moving at an unprecedentedly slow rate. Never before had a recession-depression been so tenured or so intense. By late 1936 business was picking up, but the price level was still 18 percent below its 1929 value, and unemployment was still 16 percent of the labor force. Nonetheless, the great concern in the Treasury and Federal Reserve was the danger of inflation! Fed and Treasury officials looked at the overhang of excess *legal* reserves in the banking system and imagined what would happen if the commercial banks expanded all those reserves into an avalanche of checkbook money. Monetary mismanagement had just provoked the most disastrous hyper-deflation in history. Yet, before all the foreclosures had been properly settled, the government's monetary managers were contriving to counteract the inflationary potential that they had systematically built into the monetary machinery.

Secretary Morgenthau announced in a press release, dated December 20, 1936, that Treasury gold policy was coordinated with the Fed's reserve requirement increases.[10] By mid-1937 "inactive" gold in the Treasury was $1,087 million, or about 9 percent of total Treasury gold.

Meanwhile, the banking system and the private economy foundered in a new recession. If one were to write a script that chronicled the end of free-enterprise capitalism, the events of 1929–1938 would logically serve the purpose. Since few people understood the nuances of Fed-Treasury monetary policies, the common perception was that the Recession of 1937–1938 posed yet another failure of the market system. Dozens of tracts, novels, plays, and newspaper editorials reflected this notion.

The appearance of the depression-recession evidently convinced Morgenthau that the "danger of inflation" was passed. In September 1937 he released $300 million of gold from the inactive account thereby restarting the machinery of gold monetization. Gold certificate accounts at Fed Banks responded

and gave rise as usual to increases in monetary base items in Fed Banks' balance sheets. Finally, on April 19, 1938, Morgenthau announced the discontinuance of the inactive gold account altogether.

The time span of the Treasury's gold policy was 16 months—December 1936 to April 1938, while the Fed's reserve requirement increases occurred in August 1936 and March–May 1937, and continued in force with little change until after World War II. Treasury policy cut off new gold at the initial point of monetization; Fed policy effectively smothered the money-creating potential that old gold had already provided. For the next three years the economy stagnated. By 1941 the price level was still 14 percent below its 1929 value, and unemployment was still 10 percent of the labor force. Treatises appeared analyzing "the stagnant industrial economy." The Keynesian notion of less-than-full-employment equilibrium seemed documented beyond reasonable doubt.

Fed-Treasury methods in the mid-1930s reflected the prevailing notion of the times—that someone had to run the show, that operations without the rule of men were destined to be "chaotic." Economists and financial gurus were just as convinced of this argument as politicians and political scientists. One economist, Gove Griffith Johnson, commented in his contemporary book on Treasury policy: "One may be skeptical of the wisdom with which monetary instruments will be used, *but the possibility of abuse extends throughout the whole sphere of governmental activity and is a risk which must be assumed under a democratic or any other form of government.*"

The Treasury's gold policy, Johnson continued, "was an essential instrument for producing desired political aims." Congress had given over the Fed's powers of monetary regulation to the Treasury because the central bank had proven ineffectual. These powers had become more democratic because "they were now exercised by politically responsible officials . . . [and] would eventually be subject to review by the electorate. . . . In large part," he concluded, "the [Federal Reserve] System has served merely as a technical instrument for effecting the Treasury's policies."[11]

Clearly, the awesome monetary powers the Fed-Treasury had wielded were not the product of either "wisdom" or scientific analysis. They were simply discretionary, seat-of-the-pants responses, sometimes politically motivated, by political authorities who faced no responsibility for their decisions. Furthermore, the "risk of abuse" did not need to be "assumed" under a democratic government suitably restrained by the rule of law. Finally, the electorate knew less about these policies than it knew about Sanskrit, and it had no power at all either to pass judgment on them or to change them .

Under a true rule-of-law gold standard, the Treasury would not have had a "gold policy." The gold standard *itself* would have been the gold policy and would have been self-regulating through the concerted actions of thousands of households and businesses that bought and sold goods and services in hundreds of markets. The gold, more important, would not have been stockpiled in Treasury vaults unavailable and illegal for human use, like some dangerous drug or weapon. It would have been in commercial banks primarily, serving its conventional function of securing bank-issued money.

The monetary mismanagement chronicled here should serve as the all-time example of the failure of discretionary monetary policy. Although a gold standard was still on the books, it was nothing more than a façade for Fed-Treasury manipulations. First the Fed by itself in the 1920s, then the Treasury ten years later, simply fit this "gold standard" into their other hands-on policies. Both agencies saw to it that the gold was safely tucked away where it could do no one any good. Approximately seven thousand banks failed in the early 1930s for want of reserves while the stockpiling went on. Congress then gave the executive the power to enact an unprecedented increase in the price of gold, and added as well significant new powers to the Federal Reserve's authority. By 1936 the Fed-Treasury managers, fearing they had overdone monetary expansion, decided to put on the brakes by again sterilizing gold and doubling bank reserve requirements. The result was a virtual paralysis of the monetary system and the economy.

Had the banks held their own reserves or had them available in their own clearinghouses, as they did before the coming of the Fed, bank and clearinghouse executives (who were often the same people) would have parlayed the gold into strategic trouble spots where it would have prevented failures of healthy banks and general monetary destruction. Gold to be effective cannot be declared illegal and buried in the ground where no one can get it. If that is the best that civilization can do, we might as well have left the gold in California, the Klondike, Australia, and South Africa. □

1. See, Dwight R. Lee and Richard McKenzie, *Failure and Progress: The Bright Side of the Dismal Science* (Washington, D.C.: Cato Institute, 1993).

2. For further discussion of this issue, see Richard H. Timberlake, *Gold, Greenbacks, and the Constitution* (Berryville, Va.: The George Edward Durell Foundation, 1991), pp. 8–9.

3. Board of Governors of the Federal Reserve System, *Banking and Monetary Statistics* (Washington, D.C.: Government Printing Office,1943), p. 537.

4. See my *Monetary Policy in the United States: An Intellectual and Institutional History* (Chicago: University of Chicago Press, 1993), chapter 5.

5. James D. Paris, *Monetary Policies of the United States* (New York: Columbia University Press, 1938), p. 18.

6. Milton Friedman and Anna J. Schwartz, *A Monetary History of the United States, 1867–1960* (Princeton: National Bureau of Economic Research and Princeton University Press, 1963), p. 544.

7. This pattern of law reflected the flawed notion that banks in larger cities were more subject to "speculative" influences and were more likely to make risky loans than banks in the "country."

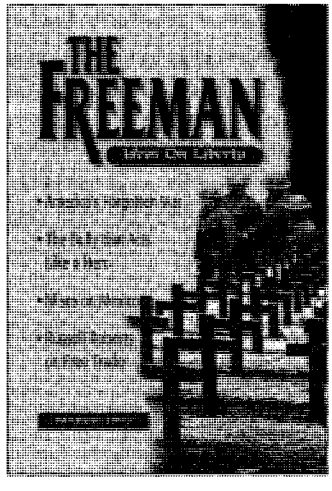
8. In next month's issue of *The Freeman*, I will treat the reserve requirement episode in more detail.

9. Donald F. Kettl, *Leadership at the Fed* (New Haven: Yale University Press, 1986), pp. 48–53.

10. U.S. Treasury, Press Releases, nos. 9–20, December 20, 1936.

11. Gove Griffith Johnson, *The Treasury and Monetary Policies, 1933–1938* (Cambridge, Mass.: Harvard University Press, 1939), pp. 205–11, 223; emphasis added.

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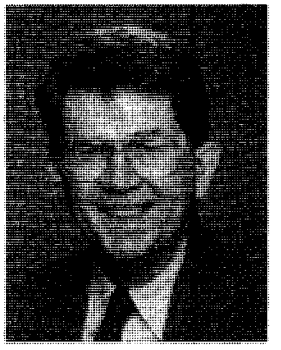
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Economics



Costs Should Be Revealed, Not Concealed

Making sound economic decisions is impossible without information about opportunity costs. Thinking about the cost of doing anything is crucial; it amounts to considering the value of the alternatives.

A major advantage of the market process is that it gathers up information on costs and transmits it to market decision-makers through prices that cannot be ignored. In contrast, the political process fails either to transmit cost information to political decision-makers or to motivate the proper use of this information. It fails partly because organized interest groups want to ignore the costs of their pet projects, and partly because political institutions are unable to acquire and communicate information on cost. Markets promote wealth-creating decisions by revealing costs, while politics promote wealth-destroying decisions by concealing costs.

Revealing Lots of Little Costs

The costs of doing anything—for example, buying a pencil—result from tiny sacrifices made all over the world. Leonard Read's primary point in his justly famous 1958 article "I, Pencil" is that making something as simple as a pencil requires the coordinated efforts of thousands (probably millions) of people with a wide range of specialized knowledge that no one person could ever possess. This coordinated effort is possible only because of the guidance provided by market prices. Read's example also illustrates how the opportunity costs incurred by everyone involved in getting a pencil to the consumer (both in terms of the value of their time and other resources) is incorporated into its price. The consumer is thereby implicitly aware of the value of every tiny sacrifice made in producing it.

All prices reveal a similar collection of diffused costs to consumers. Therefore, each product is consumed only to the point where consumers value another unit by an amount equal to the value sacrificed to make it available. As I've emphasized before, the market generates a pattern of cooperative interaction by people pursuing their own advantages in ways that take into account the concerns of others. If only the diffused costs of government action could be collected through the political process and revealed to decision-makers with the same compelling clarity as in the marketplace! That the costs of government decisions are commonly ignored goes a long way in explaining the perversities of so many public policies.

Concealing Lots of Little Costs

When the costs of government action are spread wide, as they commonly are, they are generally ignored. For example, a tariff that protects a domestic industry against foreign competition will cost consumers far more in higher prices than it benefits the industry. But

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while the benefits are easily attributed to the tariff and concentrated on a relatively small number of people, the costs amount to only a few dollars a year for each of millions of consumers, few of whom will notice the extra costs or the connection with the tariff. And even if a consumer does know of these costs, his share is so small that it doesn't pay him to actively oppose the tariff.

The benefits of any special-interest proposal are communicated through the political process loud and clear. The costs, however, are borne in silence and therefore largely ignored by politicians. Organized interest groups are aware that lots of small, widely diffused costs are difficult to register through the political process, and they aggressively exploit this fact to capture benefits at others' expense. But the inability of the political process to collect and concentrate diffused cost would result in popular support for perverse public policies even without interest-group lobbying.

For example, after an airplane crash in Sioux City, Iowa, in the late 1980s, in which an infant was killed when torn from his mother's arms, pressure arose for the federal government to require that all infants have their own airplane seats. The benefit to children on planes was obvious; they would be safer. But what was the cost? The cost of an extra seat is obvious. Other costs, however, were less obvious because they were diffused and remote. If families with infants faced higher costs for airline travel, more infants would travel in cars instead of airplanes. This would result in more infants being killed in automobile accidents than would be saved in airline accidents, since car travel is many times more dangerous per passenger mile than air travel. Several studies suggested that the cost of saving one child with the seat requirement would have been the lives of four to six children lost in car accidents. Fortunately, the requirement never became law, but that it was seriously considered illustrates the difficulty the political process has perceiving widely dispersed costs and concentrating them on the relevant decision-makers.

The Cost of the 55-MPH Speed Limit

Enactment of the 55 MPH speed limit on the grounds that it saves lives also shows the tendency of the political process to conceal rather than reveal costs. We have all heard that the speed limit reduced traffic fatalities, which then increased when it was raised. But what were the costs of the 55 MPH limit? One cost was the additional time people had to spend on the highway, a cost that came to billions of hours per year (20 extra hours a year on the road for 200 million people is 4 billion hours). Evaluated at the minimum wage, this amounts to $21 billion. Because this cost was spread over the entire population, it was largely ignored.

Unfortunately, an even greater cost—also politically ignored—was the cost in lives. The claims that traffic fatalities were reduced by the speed limit are based on fatalities on the interstate highways, which, because they are multilane divided highways, are the safest roads. But when the limit was imposed, traffic was diverted to two-lane state roads that are far less safe. This diversion occurred because the speed limit of these roads became relatively higher than before, and they were not policed as effectively as the interstates. The result was an overall increase in traffic fatalities even though interstate fatalities decreased. It has been estimated that when states were allowed to raise the speed limit on interstates outside the cities, fatalities on all roads declined by 3.4 to 5.1 percent. (See Charles Lave and Patrick Elias, "Resource Allocation in Public Policy: The Effects of the 65-MPH Speed Limit," *Economic Inquiry*, July 1997, pp. 614–20.)

If the market did as poorly as government at collecting information about dispersed and fragmented costs and imposing them on those responsible, we would live in an impoverished economy. Governments are tempted to meddle precisely because of their ability to conceal costs, and their inability to reveal them. That's why the benefits from government action are low and the costs high. □

THE FREEMAN
Ideas On Liberty

Tensions in Early American Political Thought

by Joseph R. Stromberg

According to the eminent historian of political thought J.G.A. Pocock, republican theory (or "civic humanism") was the most significant current of eighteenth-century English and American political philosophy. In the form of "country ideology," republicanism gave "left" and "right" critics of government policies a framework and believable rhetoric for their arguments. The so-called "radical Whiggism" of the American Revolution was itself, on this reading, merely an extreme and consistent version of the republican ideas of the English opposition.

From 1656, when James Harrington published a definitive statement of English republicanism in *Oceana*, down to the Americans' secession from the empire, republicanism furnished ideas for Tory party dissidents around Viscount Bolingbroke and their magazine, *The Craftsman,* and for various "commonwealthmen" and True Whigs on what we could perhaps call the original Left.

Civic humanism was an outlook grounded in the renewed classicism of the Renaissance. Niccolò Machiavelli (1469–1527) was its major prophet in his *Discourses.* His ideas rested on a view of ancient Greek and Roman political life that came to him via Aristotle, Polybius, and Titus Livy. For these writers, the ideal state had a "mixed constitution" that combined the virtues of monarchy, aristocracy, and commonwealth ("republic" in the narrow sense), and thereby avoided the degeneration into tyranny, oligarchy, and democracy (mob rule) inherent in unmixed systems. A substantial "middle class" was needed to provide stability by preventing exploitation of the masses by a narrow oligarchy or, alternatively, the plundering of the wealthy by a great mass of desperate poor. This middle class was not "bourgeois," or commercial, but a class of independent landed yeomen.

In Machiavelli's republicanism, the monarchical element lessens as emphasis on the social "balance" grows. Machiavelli's English interpreter, Harrington, stressed that the key to preserving a republic was for "the soldiers [to] be citizens and the citizens soldiers."[1] The independent landed proprietor of small or middling fortune, able to bear arms on his own account, was the ideal citizen and the guarantor of the republic.

Reading the English Constitution

Pressed into the service of many causes, this ideal was at the heart of country ideology, or republicanism. An important difference over the interpretation of English history separated Harrington himself from later thinkers who were in other respects his disciples. The point of contention was the nature of England's "Ancient Constitution," which—allegedly—included the common law, Parliament (which thereby gained many centuries in

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antiquity and traditionalist prestige), fee simple tenures, and various rights and customs from "time out of mind." Aware of the feudal basis of medieval English society, Harrington knew that the Constitution was the work of recent times and sought its origins in the passing away of the "Gothick" (i.e., feudal) balance of power and property. Royal encroachments had overborne real feudalism and its basis in military tenures (great estates held by nobles in exchange for their bearing the costs of providing military forces for the King). A new social "balance" thereby came into being, one nearer to the republican ideal and one reflected in the political struggles of the seventeenth century.

Later "Harringtonians" inverted his analysis, arguing that the old order had corresponded to the proper balance and that *later* developments unbalanced state and Constitution. They were thus able to say that the Ancient Constitution—from as far back as Alfred the Great—had embodied republican liberty and that this libertarian inheritance was now under attack. The King's "standing army"—made possible by the financial revolution (in effect, the invention of national debt)—was the instrument of anticonstitutional forces. Hence the fundamental political division was between "Court" and "Country."

Court and Country

The Court was the clique of stockjobbers, placemen, pensioners, and courtiers who made policy by means of high taxation, monetized national debt, and all manner of "corruption" (in the narrow sense). Their program undermined the Constitution (the larger "corruption" in republican thought) by overthrowing the republican balance of "classes," property, and power. The Country, by contrast, consisted of the public-spirited opponents of such state-capitalism, or mercantilism. Over time, the concept of a Country party came to stand for an ever broader range of independent property owners, finally taking on board—in the radically altered American context—every farmer and planter on the land.

As Pocock sees it, republicanism influenced the English opposition from the seventeenth century onward, so that "there can be traced a major movement of Country ideas into the radical-democratic tradition; not only much of the Chartist program, but a good deal of its ideology as well, can be shown to possess a history continuous since the days of Shaftesbury."[2] An important strand of country ideology appears in the writings of the early eighteenth-century Tory leader Henry St. John, Viscount Bolingbroke, and his allies (including Jonathan Swift). Tory in his basic principles, socially conservative, and not at all opposed to a strong monarch as such, Bolingbroke nonetheless expounded a sort of "Tory populism." Championing limited free trade, defending small craftsmen against state-sponsored monopolies, and attacking Court corruption, Bolingbroke and his circle often took positions that overlapped those of the growing pro-commercial and anti-monopolist "bourgeois" opposition.

His attacks on social upstarts and economic change separate his views from those who criticized state grants of privilege as *impediments* to the market and the rise of new men. Thus this "right-wing" opposition would have opposed an unsettling laissez-faire political economy almost as much as the unsettling "growth" made possible by Court-sponsored mercantilism and rent-seeking. Many historians who deal with these questions muddy the waters by lumping together all opponents of Court policies as "agrarians" and throwing all others together as "capitalists" (or, for U.S. historians, "industrialists"). The groups on both sides of the water that were pro-commercial but anti-mercantilist and pro-laissez faire thus fall by the wayside.

Bolingbroke's group—dedicated to preserving an older England of gentry (large landholders below the ranks of the nobility) and retainers, ready to defend old established freedoms but seemingly radical in its assaults on the Court party—had an influence on the American colonists, however ambiguous. Certainly in the South, the conservatism of this kind of republican thinking proved attractive. (Jefferson, for one, had read his Bolingbroke.) The overlap between Bolingbrokean and bourgeois versions of republicanism made it easy for American radicals to treat the

broad stream of English opposition ideas (including those of John Locke) as a unified inheritance.

Levellers, Locke, and Libertarians

Something must be said now about the relationship of classical liberalism to republican theory. Republicans idealized the independent armed proprietor as citizen and basis of the social balance, which in turn preserves the constitution. They worried little about the origin and justification of the state (which Locke sought to supply), but provided a world-outlook and language useful to various property-owning opposition movements. If pressed, a knowledgeable republican thinker might have fallen back on Aristotle, who rooted the political community in man's social nature.

For liberalism (by which we mean classical liberalism) the point of departure is different. The liberal begins with the "natural" individual in full ownership of his natural rights who cooperates with others in "civil society" before the creation of any government (state). The liberal is not unaware—as is so often suggested—that families and social relations exist, but *has* noticed that only individuals can act.

Already in the Puritan Revolution, 1642–1658, so-called "Levellers" like John Lilburne and William Walwyn developed a radical program based on individuals' ownership of themselves, natural rights, and equal access to unappropriated resources. (They did not actually want to "level men's estates"—as their enemies charged—but merely wished to open up the market.) Unlike Locke, these "Lockeans before Locke" *did* appeal to history; but theirs was not the conventional "Country party" argument from an Ancient Constitution of Liberties but a denunciation of the "Norman Yoke" fastened on the free Saxons at the Conquest in 1066 and which must be swept away.

In the *Second Treatise of Government* John Locke derived individual rights from natural law and made a case for government by consent that stood independent of historical specifics. Men's rights in a "state of nature" included self-ownership, acquisition of property by "mixing" one's labor with resources ("homesteading"), and the right to defend oneself and one's justly acquired property from aggression by others. With the "invention" of money by tacit universal consent (a notion that anticipates Ludwig von Mises's "regression theorem"), a wider division of labor and bigger marketplace comes into being that allows inequalities to arise but only along the lines of differing natural ability. Owing to the inconvenience of each man's being judge in his own cause, these pre-political individuals establish government mainly to overcome the lack of judicial services and common defense of their properties. This is the "social contract." Men do not actually give up their natural rights for all time, but merely put them in trust. Property and self-ownership cannot be transferred for Locke even by conquest and change of regime. (One doubts he had the Irish case in mind.)

The "applied" portion of Locke's system is less liberal than his discussion of pre-state civil society. From the high ground of reason and justice we arrive at the actual distribution of property in England. Locke persuasively sketches out a highly libertarian theory of property rights and then pretends that the actual distribution of English properties rests on labor title (homesteading) rather than on conquest, enclosure, force, fraud, and (frequent) expropriation of real homesteading peasant farmers. (Marx, of course, pointed this out before wandering into his own erroneous conclusions.) As Murray Rothbard observed, it is critical when applying the Lockean theory to criticize pre-existing titles in the light of the theory. The difference is between apology for a semifeudal status quo, as in England, or assertion of popular rights to property as in revolutionary North America.[3]

Whatever the limitations of Locke's writings, liberal ideas were broadly compatible with republicanism, and the new English opposition that arose after the Revolution of 1688 (which Locke's writings served to justify before the fact) employed both sets of ideas rather interchangeably. Republicans and liberals believed in property rights, however they

derived them, and Locke's pre-state proprietors looked a lot like the ideal republican citizen, armed and on his own land. In the end, natural and historically prescriptive rights ("the rights of Englishmen," the Common Law, and even Saxon freedoms) coexisted with little difficulty in the minds of Anglo-American radical Whigs on both sides of the water, and led to the same program of republican politics, freer markets, and (potentially) revolution. English opposition writers—the "Commonwealthmen" or "True Whigs"—placed side by side, and began mixing, two separate traditions into a potent new outlook: liberal republicanism. The writings of Algernon Sidney, John Trenchard, and Thomas Gordon (the latter two writing under the name "Cato") made their way across the Atlantic in a broad stream alongside those of the Tory Bolingbroke and early liberals like Locke, Richard Price, and Joseph Priestley. Stifled by moderate Whigs who turned to political capitalism once the Catholic Stuarts were deposed, liberalism and republicanism took on new meaning and life across the water. English opposition ideology entered into and helped frame the debates that preceded the American Revolution. George III and his ministers, by their intrusive policies, unwittingly set fire to this ideological tinder.

The American Revolutionary Synthesis

According to American Revolutionary thought, political life is a constant struggle between Power and Liberty. The former is inherently aggressive, constantly attempting to escape its constitutional bounds. Society is therefore best served when people guard their liberty jealously.

People have rights—by nature or by English law—and continued violation of their rights by government justified armed revolution and the institution of new forms of government. Justification of popular revolution against governments that fail "to secure these rights" was, after all, the central message of Locke's *Second Treatise*, and many passages in the American Declaration of Independence come directly from Locke.

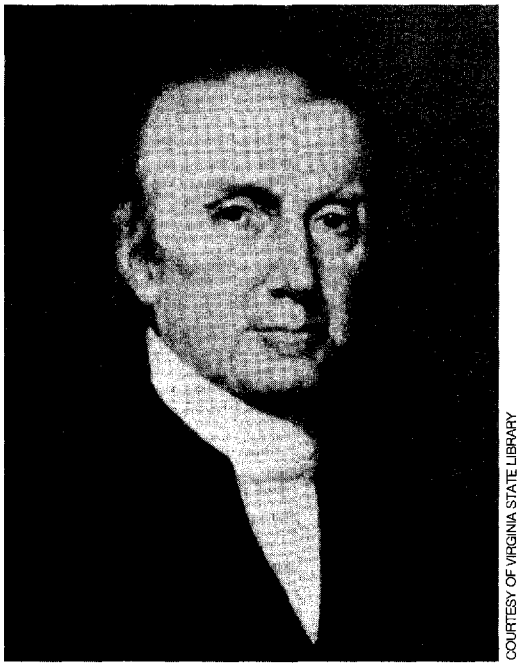
The American colonists, whose leading figures were deeply read in the whole Radical Whig tradition, were primed to fear the overthrow of liberty by a Court clique using standing armies and abusing the power to tax. Royal policies after 1763, rather harmless by present-day standards,[4] were ideally fitted to touch the radical nerve of the Americans. English and Roman history and current events in Turkey, Denmark, England, and elsewhere, as understood by the colonists, prepared them to expect the worst from kings and ministers: corruption, overthrow of constitutional forms, military rule, public debt, standing armies. . . . (They also understood that they were expected, by consuming and paying taxes on tea, to make good the East India Company's losses in the inflationary South Sea Bubble scandal.)

Working within a framework that drew from both liberalism and republicanism, the colonial radicals believed that the minimum practical content of natural law was already embodied in the "rights of Englishmen." Imperial acts infringing on these rights necessarily excited resistance. The republican idea that the safety of the republic rests in the hands of virtuous property-holders able to bear arms held a central place in the Americans' theory and practice. The differences between American social reality and that of England had democratized the concept. Broader ownership of property and firearms gave Country party ideas greater appeal and relevance in the colonies. The notion of an armed people was of great importance in a revolutionary war in which the militia may have played a decisive—if still underappreciated—role.[5]

Pocock comments on the absence of an appropriate "bourgeois" (that is, modern and commercial) ideology in the eighteenth century. As a result, he says, radicals fell back on republicanism, which they developed along new lines. In America, both the rural gentry and yeomen, as well as urban strata, were therefore in hock to pre-bourgeois ideas. Thus revolutionary statesmen such as Sam Adams, John Adams, and Thomas Jefferson returned again and again to a pre-modern concern over

the negative results of prosperity ("luxury" and "effeminacy": dreaded nemeses of republican virtue), something over which more economically oriented leaders like Thomas Paine and—a bit surprisingly—John Taylor of Caroline showed little concern.

Paine, Taylor, and many others set out a kind of libertarian republicanism, which completed the synthesis begun over the water, and which was certainly far more compatible with market relations ("capitalism") than Pocock would care to admit. Americans used republican ideas alongside classical liberal ideas, and this synthesis became "the transforming ideology of the American Revolution."[6] Liberal republicanism became the common American political language within which later struggles over mercantilism and laissez faire and slavery and emancipation would take place.



COURTESY OF VIRGINIA STATE LIBRARY

John Taylor of Caroline (c. 1753–1824)

A Unique Balance

In the American Revolution "classical republicanism" underwent considerable change as its key ideas were intertwined with those of liberalism. Gone was the concern with balancing the three classical forms of government. Instead, as Robert Shalhope writes, a "unique frame of mind emerged," which dealt with the balance between the people and their rulers. Americans went into their Revolution with "a negative view of government."[7] With the substitution of people versus government for the older contrast of Country versus Court, the stage was set for characteristically American debates in which each side claimed better to protect the people's rights against the rulers' power.

Shalhope adds that the wide acceptance of liberal/republican ideas made political stability possible after the Revolution. The debates over the ratification of the second U.S. Constitution (the Articles of Confederation being the first) underlines the point. Acting in the best Radical Whig tradition, the misnamed Anti-Federalists opposed the new charter as creating uncontrolled power. Gordon Wood has shown how the Constitution's proponents, the Federalists, justified creating a stronger federal government while staying within the theoretical confines of revolutionary thought. In effect, they made an end-run around the Anti-Federalists by suddenly becoming more democratic. Attributing a general "sovereignty" to the people (carefully avoiding the question of who were the people—the people as a whole or the people as thirteen states), the Federalists assimilated popular will to the new federal regime. So doing, they "created a distinctly American political theory but only at the cost of eventually impoverishing late American political thought."[8]

Be that as it may, what we may loosely call early "liberalism" (with some of this coming out of English law and not from Locke) and republicanism run all through the Constitution, especially if the Bill of Rights is taken into account. The provisions about freedom of religion, speech, and assembly, search and seizure, and so forth reflect the liberalizing thrust of the English political battles of the seventeenth century, while the Second Amendment enshrines the ideal republican citizen armed on his own land. (A complete account of American Revolutionary ideology would have to trace how trends in English law ran parallel with liberalism and individual rights, as did the Protestantism of the thirteen colonies.)

It seems fairly clear that the two separate doctrines—liberalism and republicanism—were fused together by the English opposition writers and the American revolutionaries because together they made for a stronger, and reasonably coherent, worldview. Liberalism, as such, had no theory of government. The French physiocratic school of laissez-faire liberal economists had no better political theory or plan than simply to get the King to sweep away barriers to trade. Republicanism, as such, had no theory of individual rights. Writers like Rousseau showed how unalloyed republicanism can easily justify militaristic and authoritarian rule on the model of ancient Sparta or the Roman Republic. (The "radical phase" of the French Revolution teaches this lesson very well.) By combining the two ideologies, the Anglo-Americans forged a powerful outlook favorable to liberty and limited government.

Some recent writers have tried to ride the renewed interest in republicanism, set off by the work of Pocock, Bernard Bailyn, and others, to the left. They hope to find in American republicanism a charter for state interventionism, mercantilism, or communitarianism. This is futile precisely because revolutionary American republicanism was a unique outlook that thoroughly blended republicanism and liberalism. (Anyway, there are plenty of "foreign" ideologies they can work with.) As regards the Second Amendment, for example, Stephen P. Halbrook makes clear that the founding generation saw no conflict between an individual right to bear arms and defense of the larger society through a militia system.[9]

Liberal Republicanism Reappears

American liberal republicanism as defined here did not die out after the adoption of the Constitution, however, but kept reappearing in slightly different guises. The asserted right to resist abusive rulers who corrupt the constitution or trample on the people's freedom found expression in the Whiskey Rebellion, the Kentucky and Virginia Resolutions of 1789, the Hartford Convention (1815), the Nullification controversy (1833), and even in



Henry David Thoreau (1817–1862)

Southern secession and creation of an alternative confederation (1860–1861). The Jeffersonian and Jacksonian political movements, in particular, carried with them the ideas and language of the revolutionary generation. Inevitably, Northern and Southern heirs of liberal republican thinking diverged more and more from their original common ground. Already from the beginning there had been differences of emphasis.

In the North, some successors to liberal republicanism—Henry David Thoreau, Lysander Spooner, Stephen Pearl Andrews, and others—developed the logic of natural law and rights all the way into individualist anarchism.[10] In the South, the felt need to defend Southern interests and culture (and not merely slavery, the relationship being more complex) led first John Taylor and, later, such figures as John C. Calhoun, Jefferson Davis, and Alexander H. Stephens to assert the South's right of resistance to federal innovation and intrusion. Ironically, slavery itself may have contributed to Southerners' assertion (for whites) of an extreme degree of personal liberty. Liberty for some and slavery for others reinforced one another

on several levels, and all attempts at consistent resolution of the intellectual dilemma foundered on the problem of race. The painful evasions on the part of Jefferson and Taylor were characteristic.[11]

In this connection it might be said that the slavery question, among others, led to a partial unraveling of liberal republicanism. Southern thinkers became very good republican theorists indeed—but somewhat at the expense of the liberal elements of the American synthesis. By the same token, Northern abolitionists (at least those working with liberal, contractual thought rather than with post-Puritan religious ideas) focused rather exclusively on the individual rights and liberties found in liberalism and English law.

The Southern Confederacy was the embodiment of a consistent, if socially conservative variety of republican theory and its defeat could be taken as a sort of last stand of the Anglo-American Country party. We might equally well take the Spanish-American War (1898)—with its leap into the uncharted and unrepublican territory of overseas empire—as the final step in the marginalization of real republican thought (as well as real liberalism).[12] American participation in World War I, on that view, made the steps taken in the 1860s and in 1898 nearly irreversible. All the same, the "Founders"—Federalist and Anti-Federalist alike—appear to have had a better grasp of human nature and the notions of responsible power (that is, power "answering to" those with whose rights and safety it is temporarily entrusted), liberty, and the rest, than do either of our existing post-republican factions called political parties. □

1. Quoted in J.G.A. Pocock, "Machiavelli, Harrington, and English Political Ideologies in the Eighteenth Century," *William and Mary Quarterly*, October 1965, pp. 549–83.

2. Ibid., p. 582.

3. Murray N. Rothbard, *Conceived in Liberty*, vol. I (New Rochelle, N.Y.: Arlington House, 1975), p. 123, note.

4. As Bernard Bailyn writes, "The condition of British America by the end of the Seven Years' War [that is 1763] was therefore anomalous: extreme decentralization of authority within an empire presumably ruled by a single, absolute, undivided sovereign" (*The Ideological Origins of the American Revolution* [Cambridge, Mass.: Harvard University Press, 1967], p. 204). George III and Lord North wanted to tighten up this loose structure and collect enough revenue to make it pay for itself. The Americans were quite happy to be neglected by arbitrary officials across the water.

5. See John Shy, "The American Revolution: The Military Conflict Considered as a Revolutionary War," in Stephen G. Kurtz and James H. Hutson, eds., *Essays on the American Revolution* (Chapel Hill, N.C.: University of North Carolina Press, 1973), pp. 121–56, and William F. Marina, "Militia, Standing Armies, and the Second Amendment," *Law and Liberty*, II, Spring 1976, pp. 1–4.

6. See generally Bailyn, especially chapter 5, "Transformation," pp. 160–229.

7. Robert E. Shalhope, "Toward a Republican Synthesis," *William and Mary Quarterly*, January 1972, p. 65.

8. Gordon S. Wood, *Creation of the American Republic, 1776–1787* (Chapel Hill: N.C.: University of North Carolina Press, 1969), p. 562.

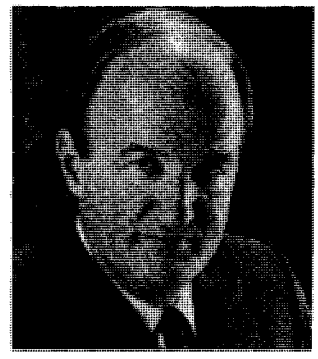
9. While the Constitution can be read—as by William Appleman Williams—as a partially "merchantilist" document, the Americans' reading of such Scottish Enlightenment figures as David Hume and Adam Smith and French economists like J. B. Say (popularizer of Smith, but more importantly, someone possessed of many "proto-Austrian" insights) pushed their liberal republicans in a direction in which laissez faire became a real option. On the Second Amendment, see Stephen P. Halbrook, *That Every Man Be Armed* (Albuquerque: University of New Mexico Press, 1984). See also Robert E. Shalhope, "The Armed Citizen in the Early Republic," *Law and Contemporary Problems*, Winter 1986, pp. 125–41.

10. See Staughton Lynd, *Intellectual Origins of American Radicalism* (New York: Pantheon, 1968), pp. 100–48, and James J. Martin, *Men Against the State* (Colorado Springs, Colo.: Ralph Myles, 1970), for the connections between abolitionism and individualist anarchism.

11. For the paradoxes of liberty and slavery in the South, see Edmund S. Morgan, *American Slavery, American Freedom: The Ordeal of Colonial Virginia* (New York: Norton, 1975); on Jefferson's and Taylor's grapplings with the problem, see Robert McColley, *Slavery and Jeffersonian Virginia* (Urbana, Ill.: University of Illinois Press, 1973) and Duncan J. MacLeod, *Slavery, Race and the American Revolution* (New York: Cambridge University Press, 1974), especially pp. 89–94.

12. For a classical liberal and republican critique of our *fin de siècle* adventure, see Joseph R. Stromberg, "The Spanish American War as Trial Run, Or Empire Its Own Justification" in John V. Denson, ed., *The Costs of War* (New Brunswick, N.J.: Transaction Publishers, 1997), pp. 169–202.

THE FREEMAN
Ideas On Liberty
MAY 1999



America Is Number 1 Again

"By the year 2000 Japan may well be enjoying the highest standard of living of any industrialized country."
—Economics textbook, 1987[1]

In 1991, I prepared an advertising campaign for my book *Economics on Trial* (Irwin). The headline was: "Japan and Germany Win World War III," followed by the subtitle, "Their formula multiplies wealth so rapidly that they will achieve their goal of world domination by the year 2000." In this ad, I referenced the sound economic model that had transformed war-torn Germany and Japan into economic powerhouses in one generation and vulcanized their stock markets. These principles were high savings rates, low taxes on capital and investment, low inflation, balanced budgets, and free markets.

Friedman Sets Me Straight

I sent a copy of my ad to the Nobel laureate economist Milton Friedman, who wasted no time debunking it: "This prediction is a bunch of nonsense," he wrote to me. "I will not live long enough to see it falsified, but you will. In the [year 2000] as in 1991, the U.S. standard of living will be higher than the Japanese."

It wasn't long before Professor Friedman was proven right. (He has set me straight on a number of occasions.) My prediction of German and Japanese dominance went awry. Not because the market formula for growth is wrong, but because Germany and Japan abandoned their model of success. Germany adopted high-cost labor-union controls, imposed anti-business regulations, and dramatically increased taxes to pay for a unified Germany. Japan exacted substantial tax increases (including a capital gains tax), propped up inefficient banks, and imposed a severe tight money policy in the early 1990s (following an excessive liberal monetary policy in the 1980s that created a bubble in real estate and stocks). Japan is still trying to recover from these devastating anti-market measures. Easier money and a higher national sales tax haven't helped. If Japan and Germany want to regain their fast-track status, they need to embrace a healthy dose of supply-side tax cuts and deregulation (known as Reaganomics in this country).

Meanwhile, the good ol' USA is rolling right along. The tax increases in the early 1990s are being reversed (long-term capital gains are now taxed at only 20 percent). Corporations have downsized and labor remains wage-flexible and productive. We lead the world in technology and employment creation, among other categories.

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Friedman (and others) convinced me to turn bullish on the U.S. economy and stock market in the early 1990s. In January 1995, I made a major prediction in *Forecasts & Strategies*, arguing that America was on the comeback, and would lead the world in stock market performance. So far it has.

How Does the U.S. Rank?

Recently I came across a delightful book that confirms my view that America is once again on top of the world: the fourth edition of *The Illustrated Book of World Rankings*, edited and compiled by George Thomas Kurian.[2] Out of some 100 positive listings, the United States received top billing in 33 categories. Among them:

- Most powerful nation (based on military manpower and economic capacity), way ahead of number 2 Russia.
- Largest gross domestic product (GDP), way ahead of number 2 Japan and number 3 Germany.
- World's highest per capita income based on purchasing power parity (though number 6 based on exchange rates), ahead of number 2 Switzerland.
- World's biggest exporter and importer, ahead of number 2 Germany and number 3 Japan.
- World's leader in retail sales.
- Leader in production of electricity, timber, and milk.
- Number 1 in airline travel, passenger cars, and commercial vehicles.
- Primary country of destination based on tourist expenditures.
- Number 1 in mail, telephones, faxes, and e-mail addresses.
- Tops in number of scientists and engineers, patents in force, and Nobel Prize winners (three times more than number 2 United Kingdom).
- Number 1 in televisions and radios per capita, number of movie theaters, museums, botanical gardens, and zoos. (India produces more films per year, but the United States dominates in movie revenues.)

The United States was edged out by Canada for number 1 in the Human Development Index (longevity, educational achievement, and standard of living). Japan is number 3.

Lest you think America can do no wrong, the United States is also ranked number 1 in several negative categories: teen pregnancies, divorce rate (among industrial nations), sulfur and carbon emissions and nuclear wastes, AIDS cases, and number of prisoners. However, it is way down the list in several crime statistics.

Debunking the Pessimists

A new book confirms America's lead in the world. In *Myths of Rich and Poor*, Michael Cox and Richard Alm highlight a slew of facts demonstrating American prowess and denying economic decay since the mid-1970s: real wealth has skyrocketed, the poor have not gotten poorer, corporate downsizing has created jobs, and the trade deficit suggests the United States is the "best place to invest."[3]

What about the future? Another fascinating book argues that the United States has a monopoly position on future technology. In *Probable Tomorrows: How Science and Technology Will Transform Our Lives in the Next Twenty Years*, Marvin Cetron and Owen L. Davies compile an exhaustive list of possible technological breakthroughs in engineering, manufacturing, computers, communications, energy, space, and medicine, noting which countries are likely to produce these innovations.[4] The United States was named the likely choice in 95 percent of the cases.

No wonder so many people from abroad want to come here. Their best alternative: invest in U.S. stocks, businesses, and real estate. □

1. Richard G. Lipsey, Peter O. Steiner, and Douglas R. Purvis, *Economics*, 8th ed. (New York: Harper & Row, 1987), p. 735.
2. Sharpe Reference, 1997.
3. See chapter 5, "Still on Top of the World," *Myths of Rich and Poor* (New York: Basic Books, 1999), pp. 91-108.
4. St. Martin's Press, 1997.

BOOKS

America's 30 Years War

by Balint Vazsonyi

Regnery Publishing • 1998 • 285 pages • $24.95

Reviewed by Clarence B. Carson

As a child of eight, Balint Vazsonyi experienced National Socialism (Nazism) when the Germans took control of his native Hungary during World War II. In 1948, the Communist Party came to power, followed by Soviet occupation and the elimination of all opposition. Those events left a lasting impression on him, and he concluded that Nazism and communism were branches of the same socialist plant, differing only slightly in the details.

Vazsonyi was able to escape to the United States in 1959. A virtuoso pianist with a strong interest in philosophy, he has been a keen observer of the American scene ever since. He concludes that for at least 30 years a struggle (he terms it a war) has gone on between those who would transform the United States into a socialist nation and those who would preserve—or perhaps we should say restore—the principles of the Constitution. This book expresses his observations on the course of that war.

The frame in which he encloses his argument is original, and his insights into how the United States is being transformed (which is to say that the war is not going well) are worth studying. Vazsonyi's early experiences with the twin evils of Nazism and communism make his book all the more compelling.

He argues that the war is really between two different ways of looking at the relationship between man and government: what he calls the "Anglo-American" view that individual rights are prior to government and that government must be constitutionally restrained to protect those rights, and what he calls the "Franco-German" view that government needs to be absolutist and wield enormous power to bring about the best possible society. These peoples are the only ones, in his view, who have produced political theories worth attending to.

This way of characterizing the opposing sides may well produce more heat than light. Neither the French nor the Germans are apt to be pleased at being credited with a series of disastrous, discredited ideas; nor have the Anglo-Americans been pure defenders of the ideas of individual liberty and limited government. England has as good a claim to the title "birthplace of evolutionary socialism" as any.

It is not at all clear to me that ideas have a native habitat and that there are national traits in political philosophy. We do ill, I think, to attribute the liking for or antipathy to various political arrangements to whole peoples. Vazsonyi would have done better to avoid pinning a national label on the contending theories.

That aside, Vazsonyi provides many clear insights into how socialist thought has mutated through hard experience to become more dangerous to America. He writes, for example, "The appetite to manage all corporations, large and small, has given way to the realization that a combination of threats, restrictions, and controls will provide access to the fruit, without ever having to plant the tree, buy the fertilizer, or perform any of the ongoing chores that go with production." This is the triumph of the fascist (Nazi) side of socialism, the realization that you encounter less resistance and get "better" results by insinuating the state into a position to take key decision-making power away from private owners, rather than trying to expropriate those owners directly.

Having lived under the control of the commissars, Vazsonyi is able to clearly see current trends in the United States. He can see how our own bureaucrats are increasingly resembling those commissars in their control over our lives. Rightly, he understands that the environmental movement and its accompanying hordes of bureaucrats are erecting a structure for a vast expansion of government authority. Since almost every use of land or activity could be said to have some impact on the environment, we are moving toward a future in which government officials will have enormous control over us.

Vazsonyi also correctly sees that piecemeal opposition to the modified socialist program is a losing game. If we argue over the "right" amount of government control, each time hoping to negotiate a somewhat better deal from the socialists than they initially propose, we are certain to see a continuing erosion of our freedom. He argues strongly in favor of an uncompromising return to our original constitutional principles, and to that I shout "Bravo." □

Clarence Carson, a contributing editor of The Freeman, *has written and taught extensively, specializing in American intellectual history.*

In Praise of Commercial Culture

by Tyler Cowen

Harvard University Press • 1998 • 278 pages • $27.95

Reviewed by Donald J. Boudreaux

For most of this century, capitalism was regularly accused of not delivering the goods as efficiently as could socialism. Today, this accusation packs as much persuasive force as do claims that ouija boards foster communication between the living and the dead. Even capitalism's most strident critics today admit that capitalism can't be beat at satisfying people's material needs. "In fact," bark the critics, "that's the real problem with capitalism: it's too responsive to consumers!" Capitalism's unparalleled capacity for delivering new 'n' improved things to satisfy the vulgar needs of the masses supposedly results in a shallow culture, whose dumbed-down denizens recognize Ronald McDonald's mug more readily than they recognize Mozart's music.

Unlike the productivity-based criticisms of capitalism, the cultural criticism of free markets comes not only from the left, but also from the right. When the likes of hyperfeminist Catharine MacKinnon are joined in their crusade against free markets by influential conservatives such as Pat Buchanan and William Kristol, the resulting coalition might well turn out to be fatal to capitalism.

The menace of this left-right alliance against the alleged cultural inadequacies of capitalism is reason alone to applaud—loudly, while standing!—Tyler Cowen's *In Praise of Commercial Culture*. But this book's virtues go well beyond the assistance it delivers in the intellectual battle against those who would substitute the whims of a political elite for the wishes of individuals. Cowen's book is also a wellhead of information about art, music, and literature, brimming with economically inspired insights into the patterns of culture and people's responses to those patterns.

Cowen, a professor of economics at George Mason University, uses as a springboard in his book the continuing debate between "cultural pessimists" and "cultural optimists." He casts his lot squarely with the (outnumbered) optimists. His case for cultural optimism is woven skillfully from sound economics and a careful study of cultural history.

One element of Cowen's argument grows from his exploration of the sources of cultural pessimism. Many pessimists are simply unimaginative old coots—as Cowen writes, they "identify great culture with what they know and have learned to love." If you spend, say, the first 40 years of your life listening only to the music of baroque composers, when you first hear the music of romantics such as Tchaikovsky, it sounds barbarous. In economic terms, you dislike post-baroque music because you haven't yet developed the human capital required to appreciate it.

Cowen also exposes the self-centeredness of many cultural pessimists. If the masses can enjoy a new work immediately, cultural pessimists haughtily pan it; but if the cultural pessimists themselves are baffled by the work, they dismiss it as illegitimate. Each pessimist regards his or her own unique accumulation of cultural human capital to be the only legitimate accumulation.

Another source of cultural pessimism that Cowen identifies is fear of the future. Many people truly fear for society when they see its cultural basis changing. This fear, however, owes far more to lack of imagination than to any evidence that cultural change necessarily portends social dry rot or disintegration. The culture of 1990s America differs from that of

1950s America—but is it really worse (as many people believe)?

Workers' greater productivity today means that they have more time to enjoy cultural amenities. Musical recordings of all types are more readily available than ever, as are broadcast performances and videotapes of dance, opera, and theater. The recent advent of book superstores brings to most Americans a selection of books that as recently as a decade ago was available only to residents of a few large cities. Far from destroying culture, the free market is bringing it within reach of more people than ever.

Mention of these bookstores points to a third source of cultural pessimism—interest-group agitation. Among those who wail about the cultural Armageddon allegedly foretold by book superstores are smaller book retailers. Those retailers naturally don't like the efficiencies that characterize Barnes & Noble and Borders. But it's uncouth to complain honestly about these new merchants ("I don't like 'em because they're better than I am at selling books!"). So smaller booksellers instead ominously prophesy cultural damnation if the book superstores aren't stopped. Cowen's discussion, replete with examples, of how cultural pessimism has been used through the centuries to mask attempts at undermining consumer choice is fascinating.

My only complaint is that Cowen is too easy on those who support government funding of the arts. Given the wealth of evidence assembled here on how markets promote a vibrant culture, he could easily have called for the abolition of the National Endowment for the Arts, but does not.

Reading Cowen's book is itself an act of cultural betterment; it is learned and sophisticated without being pedantic. It complements nicely the economics of the late Julian Simon, as well as the work of *Reason* editor Virginia Postrel. The message of each of these authors is that we should welcome, not fear, the results of freedom. □

Donald Boudreaux is president of the Foundation for Economic Education.



CancerScam: Diversion of Federal Cancer Funds to Politics

by James T. Bennett and Thomas J. DiLorenzo

Transaction Publishers • 1998 • 189 pages • $32.95

Reviewed by John Hood

Perhaps the most critical chapter of *CancerScam*, a slim but effective exposé of the politicization of America's health-care charities, begins with this famous quotation from Thomas Jefferson: "To compel a man to furnish contributions of money for the propagation of opinions which he disbelieves is sinful and tyrannical." This statement has properly been used to criticize taxpayer funding of political campaigns, of obscene art, and of various advocacy groups and lobbies.

In *CancerScam*, economists James Bennett and Thomas DiLorenzo apply Jefferson's maxim to critique the phenomenon of major health charities, such as the American Cancer Society, using taxpayer money to lobby for laws or ballot initiatives restricting the freedom of tobacco smokers. A case in point was the 1988 passage of a California initiative raising cigarette taxes and using some of the proceeds to subsidize tobacco control, research, and "public education" (read: lobbying) programs run by these very charities.

The American Cancer Society, the American Lung Association, and the American Heart Association all spent time and money pushing for approval of the initiative. They were rewarded by receiving at least $8 million a year from the cigarette tax increase to promote anti-tobacco education programs.

Bennett and DiLorenzo quote one journalist sympathetic to the tobacco-control movement, who wrote that the formerly "'starved for funds' movement . . . found itself awash in California gold."

The money-grubbing aspect of the health charities' involvement was underscored by the legislative history of the initiative. A cigarette tax hike would likely have been passed by the California legislature in 1988, but because of a constitutional spending limit, much of the proceeds from the tax would have had to be

refunded to taxpayers. Instead of pushing for the tax hike legislatively—which would have accomplished the anti-smoking activists' purported goal of raising the price of cigarettes and thus discouraging smoking—the activists pushed for and got a tax hike written into the state constitution. This may have been a bizarre way to raise a tax, but it was the only way to route the new revenues to the charities themselves.

This story is replicated several times as Bennett and DiLorenzo chronicle the growing involvement of anti-smoking health charities in the political process. The book, not surprisingly, spends a fair amount of time rebutting claims made by these anti-smoking forces on such issues as the risks of secondhand smoke, the impact of smoking on government budgets, and how smokers perceive the risks of their habit.

There's little new here to a reader already familiar with the debate, but it will help other readers put into perspective the pervasive sense of moral rectitude that the anti-smoking zealots exhibit when criticized about their taxpayer-funded lobbying efforts.

Bennett and DiLorenzo don't focus only on the smoking issue. They argue that the corruption of charitable institutions—their seduction onto the government dole and into the political game—is a trend with far-reaching negative consequences. A free society is based, in part, on drawing clear lines between various social institutions, be they businesses, governments, families, or charities. Governments have a unique role to play in our lives, as do the other institutions. Corruption sets in when businesses act like governments (for example, the Mafia), governments act like businesses (for example, providing rail transportation), governments act like families (for example, giving food stamps and subsidized day care), and so on.

CancerScam tells a cautionary tale. To pervert government public health spending—which in any event should be limited to combating communicable diseases and other immediate threats to innocent bystanders—into a means of supporting political causes is to erase the lines that protect individual liberty and the market process. Jefferson understood this. He would see no justification for forcing anyone to finance campaigns against the right of smokers to do what they want with their own lives and property, and neither do Jim Bennett and Tom DiLorenzo. □

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A Humane Economy
by Wilhelm Röpke
Intercollegiate Studies Institute • 1998 • 350 pages • $24.95

Reviewed by George C. Leef

This volume is a beautifully prepared new edition of Wilhelm Röpke's 1957 classic defense of the market economy and non-interventionist government. Röpke (1899-1966), a renowned German economist, lecturer, and writer, stood with Ludwig von Mises, F.A. Hayek, and a few other intellectuals in the middle decades of this century to warn against the perils of what he called "centrism." By this term he meant not what it means to most Americans (political namby-pambyism), but rather the tendency toward concentration of power in the hands of a few.

Röpke feared the crushing effects of big government, big business, and big labor on the forgotten, statistically insignificant individual. Reading this book of over 40 years ago reminds one of another great 1957 book, Ayn Rand's *Atlas Shrugged*. Although poles apart on some questions (especially religion), Rand and Röpke both clearly identified the ominous social and political trends that were deforming the world, and both are worth revisiting.

The subtitle of Röpke's book is *The Social Framework of the Free Market*. He seeks to show that the network of voluntary economic relationships we call the market requires a certain social framework. He writes, "Even if we conscientiously credit the market with certain educational influences, we are led back, therefore, to our main contention that the ultimate moral support of the market economy lies outside the market. Market and competi-

tion are far from generating their moral prerequisites autonomously."

What the author has in mind, for example, are moral constraints on the means by which people go about trying to get what they want. Röpke writes, "A spirit of ever alert and suspicious rivalry, not too particular in the choice of its means, must not be allowed to predominate and to sway society in all its spheres, or it will poison men's souls, destroy civilization, and ultimately disintegrate the economy." He argued that what any society needs, if it is to protect the moral norms that make the market possible is a *nobilitas naturalis*, a natural "aristocracy of the public spirit"—that is to say, men and women whose integrity and moral authority would lead most others to follow their example.

I suspect that there is much truth in this breathtakingly politically incorrect idea. The support for the ethical basis of market dealings needs to come from moral authority figures. Without that support, we will slowly sink into barbarism. Unfortunately, Röpke's thesis means that America is in grave danger. The way most Americans are educated today makes them almost impervious to any sort of leadership except by the idols of sports and popular music. Moreover, where does one see respected men and women emphasizing the importance of, say, the freedom of individuals to enter or decline to enter into contracts?

Röpke was a keen observer and elegant writer. Most of what he said is still true today, if not more so. Consider this attack on the tendency to turn economics into a branch of mathematics: "[S]uch concepts as the 'elasticity' of supply and demand, the 'multiplier' . . . and so on . . . simulate a scientific and mathematical precision which does not really exist. They are not physical constraints like . . . gravity, but relations dependent upon the unpredictable behavior of men." Or this observation about left-wing moralists: "The moralist, with his lofty admonitions, becomes an intolerant hater and envier, the theoretical pacifist an imperialist when it comes to the practical test, and the advocate of abstract social justice an ambitious place-hunter."

Sadly, the book also contains some sections that prove useful to enemies of freedom. Röpke was a population worrier. He emphatically did not want to see government in the family-planning and resource-planning business, but his alarmist statements are ammunition for those who do. And sometimes he sounds like an early Earth Firster: "We violate nature at every turn, even to the total disappearance of the countryside. . . ." Röpke would not have taken kindly to the Environmental Protection Agency with its blatant hostility to private property rights, but rhetoric like that almost inevitably promotes the "centrism" he deplored.

It is easy to ignore foibles like that, however, in a book having such an abundance of clear thinking. Over and over again, *A Humane Economy* reminds us of what is at stake in the battle between those who consistently defend freedom and those who won't: "Once the mania of uniformity and centralization spreads and the centrists begin to lay down the law of the land, then we are in the presence of one of the most serious danger signals warning us of the impending loss of freedom, humanity, and the health of society." □

George Leef is book review editor of The Freeman.

All the Essential Half-Truths about Higher Education

by George Dennis O'Brien

University of Chicago Press • 1998 • 244 pages • $19.95

Reviewed by George Roche

George Dennis O'Brien, retired president of Bucknell University and the University of Rochester and author of *What to Expect from College*, has addressed himself to a vitally important subject—the many myths and misconceptions surrounding American higher education. Although he identifies serious problems and sometimes makes telling observations, the book ultimately proves to be maddening because the author will not for the life of him make hard decisions. His proposals are always safe and temperate. O'Brien's book circles at 30,000 feet over the major issues

confronting universities and the reader exclaims, "Land somewhere! Take a position! Offer a solution! Act in some principled way even if it might create some enemies!"

At almost every turn, O'Brien takes the safe road, trying to keep establishment friends happy through equivocations and conciliation. One example: "If faculty are to administer—as I believe they should. . . ." This is a "respectable" position, but one that I view as entirely mistaken. The faculty should no more administer the institution than the players should manage the team. Many schools started to go horribly wrong when they tried mixing teaching and administration. But the author declines to challenge this conventional idea.

In another place O'Brien writes, "I think that multiculturalism is dead wrong." The reader earnestly hopes for a tough position and suggestions for curing this intellectual cancer (or at least halting its spread). But no, he does not want to offend his politically correct colleagues and thus adds, "However, if multiculturalism is bizarre in astronomy, it is not so in the area of the lost moral curriculum. It starts in the right place." He thus criticizes without really criticizing at all. This reminds one of Yogi Berra's saying, "When you come to a fork in the road, take it." O'Brien usually follows this advice and manages to take both paths.

Near the end of the book, O'Brien writes, "The issue that faces higher education is whether current faculty expectations and education will allow them to join in with administration or cause them to fight a generally losing battle against the social and economic forces that have created the need for decisive institutional direction." Indeed, we might wonder how the largely overpaid and underworked faculty of the typical American university will react when confronted with the need for "decisive . . . direction," but exactly what this "decisive . . . direction" must entail, the author will not hazard to guess.

A book that is to deal sensibly with the many problems of higher education in the United States must inquire about the *real* causes of exorbitant college costs, high dropout rates, the dumbing-down of academic standards, the perversion of the curriculum, the short-changing of students in universities where teaching takes a back seat to "research" (which often means abstruse writings that are never read and no one would voluntarily pay for), and of the spreading politicization of courses, to mention just the top of the list. It must then propose solutions.

Unfortunately, *All the Essential Half-Truths about Higher Education* comes up short. O'Brien says that his purpose "has been to raise issues." He does raise a number of them (nine "half-truths"), but misses others and, more important, semantically skirts the issues without offering any real solutions. And he unwittingly tells the reader why he adopts this inoffensive approach, when he writes, "The political cost of changing entrenched interests is staggering."

That is unquestionably true, and anyone who proposes more than minor, cosmetic tinkering with higher education will certainly incur the wrath of the entrenched interests, comfortable as they are with the status quo. O'Brien, sad to say, is like so many in the education establishment who readily sacrifice principle and correct action to popularity.

A reading of this book will give one who knows little about the terrible state of higher education some familiarity with the issues, but for deep analysis and tough solutions, it is a disappointment, reminiscent of Matthew Arnold's description of the poet Percy Bysshe Shelley: "a beautiful and ineffectual angel, beating in the void his luminous wings in vain." □

George Roche is the president of Hillsdale College and author of The Fall of the Ivory Tower.



Commodity and Propriety: Competing Visions of Property in American Legal Thought, 1776–1970

by Gregory S. Alexander

University of Chicago Press • 1997 • 486 pages • $39.95; $25.00 paperback

Reviewed by Bradley A. Smith

To discuss the meaning of property is, in many ways, to discuss the meaning of liberty. If property is an individual right, secure from encroachment by government, then government power is necessarily restricted by the existence of property. If, on the other hand, property is merely a private basis for creating a public good, then government has a right, and at times even a duty, to dictate or regulate its use.

In *Commodity and Propriety*, Cornell University law professor Gregory Alexander chronicles the history of this debate in America. Alexander argues that in colonial America, most lawyers, if not most citizens, believed that the role of property was to provide for the "public good." Property, especially land, filled this role by anchoring the citizen to his "rightful" place in society, thereby promoting social stability.

What individuals gained from holding property was not independence from government, but rather independence from the swings and roundabouts of the marketplace. With this independence, however, came a duty to use property to further alleged societal interests. If one failed to properly use his property, the state could compel him to act for the public good. This is the "proprietarian" view of property.

During the American Revolution, views on the role of property shifted dramatically. A new conception of property, as an alienable market commodity, took root. In this "commodity" conception, property serves to define the "legal and political sphere in which individuals are free to pursue their own private agendas and satisfy their own preferences, free from government coercion or other forms of external interference." Alexander suggests that the last 200 years have been marked by an ongoing dialectic in which the proprietarian and commoditarian views are continually refined in response to concrete legal and social issues of the time.

To trace this history is an enormous task. Alexander reviews 200-plus years of thinking from David Hume, Adam Smith, and John Adams, through F.A. Hayek, Michael Harrington, and Justice William Brennan. In doing so, he offers up some controversial propositions. For example, while classical liberals have usually turned to Thomas Jefferson for political inspiration, Alexander portrays Jefferson's antagonist Alexander Hamilton as the true father of the individual rights-oriented, commodity view of property in America. It was Hamilton, not Jefferson, who recognized and promoted property rights in intangible objects such as securities and even vested interests. It was Hamilton who envisioned America not as a stable, agrarian society of individuals tied to the land, but as "a society of great wealth and power whose life blood was the class of enterprising merchants [with] none of the vestiges of feudal society to inhibit [their] entrepreneurial strivings."

On the other hand, modern liberals, who like to point to slavery as a great evil of laissez-faire capitalism, will find Alexander correctly demonstrating how the philosophy of slavery reflected proprietarian views of property. The abolition of slavery was a triumph for the classical liberal, commoditarian view.

Despite such triumphs, the commoditarian view has never vanquished the proprietarian view. The common perception that property in America has always been considered a basic individual right, to be held free from the powers of government, is simply not true, says Alexander. Readers of this magazine may wish it were so, but a quick look at recent EPA regulations in the Federal Register demonstrates his point.

Still, the strength of the commodity vision has been such that in the late twentieth century those who favor the activist state have sometimes abandoned proprietarian rhetoric and attempted to put their theories into commodity terms. This is seen in efforts to define a commoditarian type "right" to welfare, health care, or other government benefits.

What Alexander's book lacks is a sense of passion. Though describing a great clash of ideas, there is little sense of drama or energy in these pages. Alexander reports the theories as equals, with little seeming interest in which view ought to prevail, or even in evaluating the merits of the arguments he describes. It must fall to others to demonstrate why and how a classical liberal view—the commodity conception of property rights—promotes prosperity, peace, and liberty. □

Bradley Smith is associate professor of law at Capital University Law School, Columbus, Ohio.

Against Politics:
On Government, Anarchy, and Order
by Anthony de Jasay
Routledge • 1998 • 256 pages • $75.00

Reviewed by Butler Shaffer

While studying political philosophy in college, I often pondered: why should my preferences for liberty have to depend on philosophical principles rather than my personal will? Why should it not be sufficient simply to declare that I do not choose to be coerced by a political system? Such a proposition did not seem to me to be so out of the ordinary—after all, the marketplace operates on such voluntaristic assumptions with obvious success.

That inquiry led me to other questions, such as, "Why isn't personal liberty the presumed condition in human society, with the burden of proof placed on those who would restrict it?" The "social contract" theorists' answer that we have agreed to the state's restrictions on our liberty rang hollow in the face of the tyrannical and butcherous regimes that had come to represent the modern world of nation-state politics.

To those who share this love for liberty, and who have likewise been troubled by such questions, Anthony de Jasay's book will prove worthwhile. In a lucid and intellectually invigorating manner, he challenges the classic justifications that have been offered on behalf of state power: from social contract theory to the public goods and economies-of-scale rationales, he thoughtfully analyzes, and casts doubts on, the case for the authority of the state.

De Jasay's explorations of the concept of "limited government" reveal an awareness of the difficulties inherent in all forms of collective behavior: namely, that "collective choice is never independent of what significant numbers of individuals wish it to be." In any kind of political system—including a democratically constituted one—it is impossible for political authority to remain "limited" except by imposing on it a higher sovereign authority, whose own actions must, in turn, be supervised by an even higher sovereign power, *ad infinitum*. The United Nations, for example, has been given some measure of authority to control the excesses of nation-states, but what will control the United Nations?

"Limited government with popular sovereignty," de Jasay tells us, "is precarious," dependent on widespread acceptance of certain philosophical propositions. The case for liberty, in other words, is never stronger than the insistence by each of us that it be preserved. Liberty must crumble when its philosophical foundation does.

De Jasay has no sympathy for such traditional fictions as "the common good" as a basis for state power. Noting that "[n]inetenths of practical politics is the making of nonunanimous decisions by some, which hurt others," he proceeds to explain how an alleged "common good" need not, in fact, "be good for, nor desired by, any individual, past, present, or future." The result is social engineering, which he defines as "a series of political decisions making people allocate their efforts and wealth otherwise than they would if allowed to do it as they saw fit." Even Hayek comes in for criticism for his treatment of "public goods." Hayek's vision of "social order," de Jasay explains, would make "the state's place in society . . . ad hoc, open-ended, [and] indeterminate."

In a politicized society that no longer distinguishes between positive law that is imposed by the state and common law that arises out of human customs, practices, and expectations, de Jasay's resurrection of the

distinction is not only refreshing, but essential to the case for nonpolitical systems of social order. The cult of state power appears to be in retreat in the minds of increasing numbers of people, and de Jasay's analysis is most useful in sweeping aside the dust-laden assumptions and faithfully chanted doxologies on which such power has rested.

Economic and systems analysis, "chaos" theory, and a growing spiritual revulsion at what state collectivism has wrought in this century alone have combined to fuel a resurgent interest in the processes of "spontaneous" order. Such order depends on a concept of "rights created by voluntary contracts," which, de Jasay tells us, are derived from property which, in turn, is not a "right . . . but a liberty to act upon owned objects."

Those who understand the distinction between "rights" and "liberties," and of how "property" and "liberty" are inextricably intertwined, will appreciate de Jasay's analysis. To those who wish to challenge the foundations of all systems of collective authority, his book will be of great value in confronting the arguments that have been historically offered on behalf of such systems. The author's title is, in the end, perfectly descriptive, for the book indeed makes the case *against politics* and in favor of liberty as the means of establishing order in human society. □

Butler Shaffer is professor of law at Southwestern University School of Law and author of Calculated Chaos: Institutional Threats to Peace and Human Survival (1985) *and* The Redistribution of Authority: Privately Owned Property as a System of Social Order *(forthcoming).*

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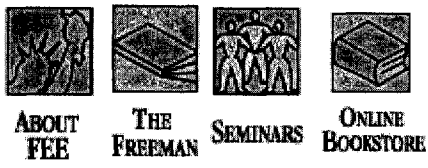
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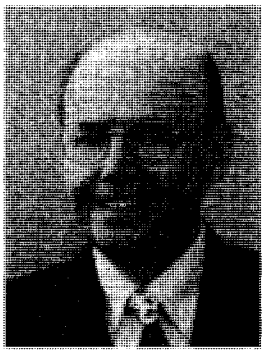
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Tony Blair and "Fairness at Work"

Tony Blair, prime minister of Great Britain, heads the "New Labour" Party. The old Labour Party was a wholly owned subsidiary of the Trades Union Congress (TUC), the umbrella organization for most British unions. In 1976 Labour Prime Minister James Callaghan asserted that "no modern government can govern against the trade unions." During the 1978–79 "Winter of Discontent," the TUC and its constituents assaulted Britain with crippling strikes, violence, and sabotage. The electorate then elected Margaret Thatcher, who set about taming the unions through a series of statutes designed to make them subject to the ordinary rule of law and to protect workers against predatory union bosses.

In the early 1990s Blair began to repackage the Labour Party. New Labour would no longer take its orders from the TUC. It would favor entrepreneurship in the private marketplace, continue with the Conservative policy of privatization, and work in the interests of the increasingly affluent British middle class. Like his friend and mentor, Bill Clinton, Blair was a successful salesman. In 1997 he defeated John Major and became the first Labour Prime Minister in almost 18 years.

Blair resembles Clinton in another way—he favors compulsory unionism. In his foreword to a May 1998 White Paper titled "Fairness at Work," Blair assured his readers that "There will be no going back. The days of strikes without ballots, mass picketing, closed shops and secondary action are over." The purpose of the White Paper, he said, is "to replace the notion of conflict between employers and employees with the promotion of partnership."

In the post-Thatcher status quo, there is no statutory requirement that employers recognize any union or even bargain with any union on the subject of recognition. Recognition is a matter of voluntary negotiations between employers and unions. Government doesn't intervene in labor relations except to uphold the rule of law.

Fair-Weather Voluntarists

British unions supported this voluntary system of labor relations when they enjoyed the privileges and immunities granted to them in the Trade Disputes Act of 1906. From then until the 1980s British unions were exempted from all claims for damages arising out of labor disputes. Employers were subject to the rule of law, but unions were not. Unions used "blacking" (violence-enforced boycotts) and mass picketing to force employers to agree to closed-shop collective bargaining. Now that the Thatcher reforms have removed their privileges and immunities, the unions no longer like voluntarism. They want the Labour government to force employers to recognize and to bargain with them. Blair proposes to do exactly that—American-style.

Exclusive representation and mandatory collective bargaining are central to American

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labor-relations law. Exclusive representation is the imposition of union recognition on the basis of majority vote among workers. A union that wins such an election at a firm represents all the employees eligible to vote, even those who vote against the union. Mandatory bargaining means that an employer is forced to bargain with a union certified by majority vote, and during bargaining the employer must compromise with the union.

Apologists for exclusive representation argue that it is merely workplace democracy. The will of the majority rules in politics; so, they argue, it should also rule at the workplace. Mandatory bargaining is necessary because the whole purpose of union recognition is bargaining. Recognition without bargaining is meaningless.

Freedom of Association

These apologists conveniently forget that democracy is a form of government, not a rule for private decision-making. The classical liberal principle of freedom of association requires that in their private lives (1) all individuals (even employers) be free to choose to associate with other willing individuals for legal purposes, and (2) all individuals be free to choose not to do so. Exclusive representation and mandatory bargaining violate freedom of association. To be represented by a union is to associate with it. To have a union as a bargaining agent is to associate with it. To bargain with a union is to associate with it.

So what is Blair up to? Chapter Four of the White Paper explains that the Labour government will propose legislation to force an employer to recognize a union "where a ballot shows that a majority of those [workers] voting and at least 40% of those eligible to vote are in favour of recognition." Moreover, a union so recognized will represent all the workers in the "appropriate bargaining unit"—that is, all the workers eligible to vote. This is American-style exclusive representation. The White Paper also states, "Recognition will cover pay, hours and holidays." In other words, recognition implies mandatory bargaining on those subjects.

In Annex 1 of the White Paper the authors explain that the Central Arbitration Committee (CAC), a government agency, can determine whether a union has majority support among workers without a ballot. Once a bargaining unit is defined by the CAC, and if the employer does not voluntarily recognize a union seeking recognition, the CAC can compel recognition "if it is satisfied, having examined carefully suitable evidence from the union and, if he wishes, from the employer, that more than 50% of the bargaining unit are members of the union seeking recognition." The CAC doesn't have to consider evidence from the employer; it may compel recognition solely on the basis of union-provided evidence. The ballot procedure is used only when the CAC is unwilling to compel recognition without a ballot. The union evidence on which the CAC is to make its determination "might take the form of membership records or a petition signed by a sufficient number of employees."

American unions have long tried to get Congress to amend the National Labor Relations Act to compel employers to recognize unions on the basis of signatures. Why? Union organizers collect signatures on a face-to-face basis, and they are not known for their gentle manners. It is much more difficult for workers to resist face-to-face organizers than to vote no in a secret ballot election.

However, the White Paper does not propose to adopt American "union security." American workers in unionized firms may be forced to pay union dues and fees as a condition of continued employment. This coercion is excused by saying that since a certified union must represent all workers in a bargaining unit, every worker should be forced to pay a share of the union's operating costs, otherwise many workers would be free riders.

In the 1930s Senator Robert Wagner, the principal author of the National Labor Relations Act, advocated a "camel's nose under the tent" strategy. First, make a few changes in the law, then a few more, and so on. Eventually your goal will be reached—the union-free tent will collapse. Given his affinity for the American model, could it be that Blair will impose union security once forced bargaining has been digested? □

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PERSPECTIVE

When Bullies Take Power

Life is Beautiful, winner of Academy Awards for best foreign language film and best actor (Roberto Benigni), is a remarkable movie. This story about a Jewish father's attempt to shield his son from a Nazi concentration camp is perhaps the most powerful movie ever made about the Holocaust. The movie makes a stunning impression precisely because it focuses on one family's ordeal and juxtaposes horror and humor.

I'd like to know what audiences are thinking when they leave the theater. I suspect the standard reactions are along these lines: The Nazis sure were bad. Or, hate and intolerance are terrible. That's fine, as far as it goes. But it doesn't go nearly far enough.

I wonder how many people came away thinking: Government certainly is dangerous. How can we limit its power so it will never engage in systematic mass murder again? Too few, I fear.

Murderous hatred was certainly a necessary condition for the Holocaust. But it was hardly a sufficient condition. How many Jews could Hitler and his thugs have killed had Germany had a strong classical liberal tradition undergirding a constitutionally limited government. The question answers itself.

Murder on the scale perpetrated by Hitler, Lenin, Stalin, Pol Pot, Idi Amin, et al. requires a *state*; that is, a *legitimized* machinery of force. Only a state can concentrate the resources (thanks to taxation) necessary for such a monstrous feat. More important, only a state has the mystique (thanks to its schools, among other things) to command the sort of allegiance required to induce large numbers of people to cooperate or at least to stand by and let it happen. A dictator is just a bully with a state at his disposal.

Hate and intolerance are likely to be features of the social landscape for quite some time to come. Trying to avert future systematic mass murders by abolishing hate and intolerance is naïve and futile—especially if government accumulates new powers in the process. A more efficacious and feasible

course (albeit still extremely difficult) is to institutionalize strict limits on government power. When that's achieved, aspiring dictators will have difficulty achieving office higher than neighborhood bully.

* * *

Thanks to a passel of government programs, Americans are increasingly getting the message that parenthood can't be left to amateurs any longer. A century and a half after responsibility for schooling was lifted from parents' shoulders, is the state ready to relieve them—starting with low-income people—of the rest of the job of rearing children? Susan Orr doesn't like what she sees.

Programs such as Head Start are often defended as "investments" in children that promise to avoid later social problems like crime and dependency. John Hood looks at the data and isn't impressed.

No matter how the advocates of gun control try to evade it, America's founding generation was avidly pro-gun and not just for sporting purposes. Joseph Stromberg explores the relationship between firearms and the philosophy on which the United States was established.

The federal government did many things to turn what might have been a short recession into the Great Depression. In his series finale, Richard Timberlake explains that one of those things was the manipulation of the banking system's reserve requirements.

One of Franklin Roosevelt's first acts was to outlaw the possession and monetary use of gold. It was an assertion of executive power that would have far-reaching consequences, writes James Bovard.

The Department of Justice and the Federal Trade Commission get upset when a company achieves a dominant share of a market. Are consumers at risk from a dominant firm? Christopher Mayer ponders the question, showing that "market share" is not the simple concept that regulators think it is.

Is the market order compatible with authoritarianism? Even some champions of capitalism reluctantly believe so. John Marangos disagrees, arguing that economic freedom holds the seeds of political freedom.

Francis Hirst is virtually unknown today. But in his time, he was a prominent advocate of individual liberty and opponent of state power, both the welfare and warfare variety. Mark Brady introduces us to this forgotten English champion of freedom.

A government-controlled education system that only sought to teach children to read would have been bad enough. But what about a school system designed to recast society in a collectivist mold? Daniel Hager profiles an old proponent of such a system, George Counts.

Our columnists once again find provocative topics to chew on. FEE President Donald Boudreaux reminds us government isn't a god, then looks at a claim that workers are being forced to work without pay and responds, "It just ain't so!" Lawrence Reed sees differences between taxes and user fees. Doug Bandow explores President Clinton's Balkans folly. Dwight Lee illustrates that even gifts entail opportunity costs. Mark Skousen thinks economic growth could double and go on indefinitely. Russell Roberts warns that nothing is free.

Our reviewers render verdicts on books about money, the welfare state, Mugwumps, the classics, secession, and the work of a major public choice economist.

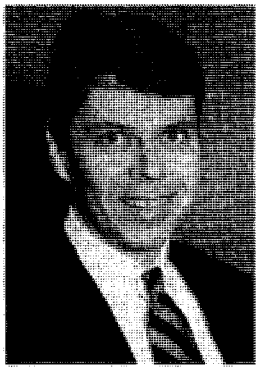
—SHELDON RICHMAN

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Thoughts on Freedom

by Donald J. Boudreaux



Government Is No God

Assume you need surgery to remove a brain tumor. Two physicians in your town offer to perform this operation. Dr. Smith specializes in neurosurgery; it's his sole occupation. Dr. Jones, however, divides his time among a variety of occupations. Along with performing neurosurgery, he practices dentistry, gynecology, podiatry, and radiology. He also spends part of each day teaching political science at the local college, and another part of each day as an investment counselor.

Which surgeon will you use?

If your brain tumor hasn't yet seriously diminished your capacity for rational thought, you'll choose Dr. Smith—the specialist. Dr. Jones might well be more brilliant than Dr. Smith, but common sense correctly tells you that even the world's smartest person can never master a complex task if that person spreads himself too thin. Mastery requires specialization.

In our everyday lives, we all grasp this fundamental truth about the importance of specialization. Each of us is trained—through schooling, experience, or both—to do a particular job. None of us grows his own food, weaves his own cloth, brews his own beer, mixes his own toothpaste, *and* works as a CPA or a pipefitter. In fact, none of us even *thinks* to try to do all these things. Nor do we purchase goods and services from non-specialists—with one big exception.

The exception is politics. Judging from any ordinary day in the life of the president of the United States, politicians fancy themselves to possess near-godlike capacities for mastering a vast array of issues and disciplines. It's typical to hear Bill Clinton—in a single day!—speak with seeming authority on the merits of school uniforms, on plans for bringing peace to the Middle East *and* to Kosovo, on the consequences of higher tax rates, on the benefits of V-chips for televisions, and on how to reduce the number of illegitimate births among inner-city teenagers. No social issue seems beyond his grasp.

Perhaps more astonishing is that virtually no one looks askance at such absurd pretensions. While almost everyone would (properly) regard as crazy a physician who attempted to work also as an accountant, farmer, and political philosopher, most people don't think twice about a politician who not only expresses opinions on countless complex subjects, but also meddles in each of these matters. Indeed, many people positively *demand* that politicians each have a hand in an oceanic array of human activities.

Why? Why are politicians—unlike people in other occupations—widely presumed to possess sufficient expertise in almost any subject that catches their fancy? Why don't people howl with laughter, rather than nod their heads seriously, whenever Bill Clinton, Al Gore, or Trent Lott discourses on some matter about which he has neither experience nor expertise? Why do people swallow the ludicrous promises and proclamations of politicians—promises and proclamations that are typically sillier than the assertions of a third-rate fortuneteller with a traveling circus?

Donald J. Boudreaux is president of FEE.

The answer to these questions, I fear, is that most people regard the state as a superhuman institution. Most people regard government (or, at least, democratic government) as somehow free of the limitations that beset human beings in nonpolitical activities. In short, too many people deify the state. But regardless of your political views, it is impossible seriously to deny that government is a human institution. Just as General Motors, Sun Microsystems, the Ford Foundation, the Kiwanis Club, mom-and-pop retailers, and every other profit and not-for-profit organization you care to name is run by human beings, so too is government. The state is no more capable of superhuman feats than is any other human institution.

Few people dispute this fact when it is stated so baldly. Nevertheless, people routinely *act* as though they do in fact believe government to be (at least semi-) godlike.

Why Is the State Deified?

The question then becomes: Why do people deify the state?

Part of the answer is that politicians shamelessly encourage this deification. They do so directly by promising to perform all sorts of impossible miracles—using prohibition to eliminate drug use, keeping Social Security solvent without imposing crushing taxes, using campaign-finance reform to exorcise interest-group demons. The fact that these schemes always fail seldom poses a problem, for politicians are unscrupulous and clever about blaming others for these failures.

Politicians' direct efforts to encourage deification of the state would come to naught, however, without their myriad indirect efforts.

Probably the most effective of these indirect efforts is government-run schooling. By failing to educate American children, government schools each year spew out platoons of young people who are not taught to think critically and reason carefully. Instead, they learn only to parrot bumper-sticker slogans and to value the emotion du jour over evidence and rational analysis.

Yet another source of support for politicians seeking to deify the state is a popular press that reports on government actions and agencies as though their names accurately describe their actual effects. For example, Congress's claim that the recent Small Business Jobs Protection Act will do just that goes largely unchallenged—despite the fact that it raises the minimum wage!

It's no surprise, then, that Americans too seldom question the motives and the abilities of government officials who regularly claim to possess far wider expertise than could have been acquired in a lifetime by a legion of Leonardo da Vincis.

My objection can't be parried by pointing out that the president gets advice from specialists of all kinds. How does he know whom to canvass for that advice? If he seeks advice on whom to seek advice from, the problem is merely pushed back a step.

It cannot be repeated too often: government is no god. Its employees are no more ethical or expert than employees in the private sector; nor are government employees—including the president and members of Congress—immune to the cognitive limitations that naturally afflict the rest of us.

I refer anyone who is tempted to fantasize that government possesses unlimited intelligence and abilities to these wise words from F.A. Hayek's *Road to Serfdom*:

> [I]t is impossible for any man to survey more than a limited field, to be aware of the urgency of more than a limited number of needs. Whether his interests center round his own physical needs, or whether he takes a warm interest in the welfare of every human being he knows, the ends about which he can be concerned will always be only an infinitesimal fraction of the needs of all men.

Anyone seeking power who denies this truth is a devil, not a god. □

THE FREEMAN
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Workers Exploited?

It Just Ain't So!

The late Nobel laureate economist George Stigler rightly insisted that anecdotes are not reliable data on which to base judgments about the state of the world. Labor lawyer Thomas Geohegan either never heard or ignores Stigler's wise warning. Geohegan relies on a handful of anecdotes to argue in the January 24, 1999, *New York Times* that American workers are increasingly exploited by their employers ("Tampering with the Time Clock").

The thrust of Geohegan's argument is that employers are forcing more and more workers to work more and more hours "off the books." "Go anywhere," he asserts, "a supermarket. A nonunion hotel or club. Any nursing home. There's a very good chance that the staff is working for nothing some of the time." The consequence, Geohegan asserts, is that the American worker now suffers "longer hours, less vacation, more stress on the job."

His apparent solution for this problem is stronger labor unions and stricter government-enforced work rules. For example, he wants the government to require that time-and-a-half be paid not only to hourly employees who work overtime (which is the current rule) but also to workers at the professional and managerial levels.

Record-Setting Leisure

Geohegan's facts are mistaken—not surprisingly, given his reliance on anecdotes—and his economics is gobbledygook. First the facts. Today's American workers enjoy more leisure—both at work and at home—than any previous generation of workers. Since the Great Depression, the number of hours worked per week by the typical American worker fell from 44 in 1938 to 38.6 in 1960 to 36.9 in 1973 and to 34.4 today. Moreover, the number of vacation days rose from six in 1938 to seven in 1960 to eight in 1973 and to 10.5 today. The number of holidays and personal days during this period increased even more dramatically.

Geohegan would question these data, arguing that Americans work ever-more hours off the books. Presumably, employers are reducing the number of hours that employees are formally required to work, while increasing the number of hours—without pay—that employees are in fact required to work. But again, aside from some anecdotes, where's the evidence?

The same consistent and substantial decline in hours worked that marks the modern workplace also marks the modern home. Holier-than-thou pundits routinely condemn capitalism for turning out excessive quantities of gadgets and gizmos. But the fact is that these gadgets and gizmos relieve us of many of the monotonous household tasks that burdened our parents and grandparents. Automatic dishwashers cut the number of hours we spend at the dreary task of cleaning up after dinner; microwave ovens reduce the amount of time necessary to prepare meals; no-iron fabrics mean less time caring for clothes; Jiffy Lube and Pep Boys now change our cars' oil in minutes; improvements in health care and household sanitation diminish the amount of time that we are down with illnesses; on-line shopping enables us to spend less time in stores. These and countless other advances brought to us by the free market have slashed the number of hours that we must give over to household chores.

All told, say researchers W. Michael Cox and Richard Alm, "In 1996, an average lifetime's waking hours devoted to work, both on the job and at home, stood at an all-time low of 21.8 percent, compared with 24.8 percent

in 1973." (See *The Myths of Rich and Poor*, Basic Books, 1999.)

Our greater leisure time isn't spent idly. We spend this time—and larger portions of our income—on entertaining activities. For example, there are today five times more adult softball teams than there were in the mid-1970s. The proportion of the population that today attends professional sporting events is almost twice what it was in 1970. The same is true for live symphonies and operatic performances. And the number of pleasure trips we take today is three times higher than it was back then. Finally, the proportion of Americans who donate some of their time to volunteer efforts is today double what it was in the mid-1970s.

Government Can't Help

The facts show overwhelmingly that American workers are not only paid more today than at any time in the past, but that the amount of leisure time we have to enjoy our higher incomes is at an all-time high. But let's suppose for the sake of argument that the facts are opposite of what they really are; that is, let's suppose that Geohegan's picture of the American worker's lot is accurate. Would increased government regulation of the workplace—both directly and through special privileges granted to labor unions—improve matters? Hardly.

Government mandates of pay, fringe benefits, and working conditions inevitably worsen the lot of the typical worker. The reason is that government-mandated pay and working conditions are substitutes for what workers themselves prefer.

The classic case is minimum-wage legislation. When government mandates that no worker be paid less than $5.15 per hour, all workers who are worth less than that to employers, but who would prefer to work at some lower wage rather than be unemployed, are forced by this legislation out of their jobs. They are made worse off. Identical logic applies to government-mandated fringe benefits—including worker leave and improved working conditions. At best such mandates merely change the compensation package to one that workers prefer less than the package that would be offered in the absence of the regulation.

Employers compelled by government to offer more employee leave will offer employees less of other forms of pay, such as wages, pension contributions, or employee discounts. The number of possible adjustments is countless. And to the extent that employers cannot offset the costs of any government mandate, the consequence for many workers is devastating: unemployment. When government piles mandates atop mandates, it artificially and unnecessarily raises firms' costs of hiring workers. Firms that would have hired 1,000 workers now hire only 850; firms that would have hired 100 workers now hire only 70; firms that would have hired ten workers now hire only nine—and some firms that would otherwise have sprung to life now are never formed; they are snuffed out in advance by reckless government regulation of the conditions of employment.

So even though Geohegan's statement of the "facts" is a sham, it is also dangerous. The danger lies in people's believing what he says and, in response, endorsing the destructive policies he proposes.

Genuine data, however, belie the gloomy and sinister picture painted by Geohegan. These data are nowhere better collected, reported, and interpreted than in Cox and Alm's book, as well as in the many books of the late Julian Simon. Almost any single chapter from the works of these scholars proves that Geohegan's argument just ain't so.

—DONALD J. BOUDREAUX

THE FREEMAN
Ideas On Liberty

The Professionalization of Parenthood

by Susan Orr

What do the following things have in common? The child-care initiative, foster care, Head Start, and the child-abuse prevention effort "Healthy Families." All are programs for children and all receive government funding, most at the federal level. They also share an insidious assumption: most people, particularly the poor, are unable to be good parents without the help of professionals.[1] Is such an assumption warranted? And if not, why not?

Parents increasingly complain about how difficult it is to raise their children in a wholesome atmosphere. In *The Assault on Parenthood*, Dana Mack tapped into that sense of frustration. Parents, she says, find that the "communal supports for the child-rearing work of even the best families are crumbling. . . . In fact, parents see the decline of social supports and the breakdown of families as symptoms of a larger phenomenon: the sudden and rapid decay of those stable social values that once fostered a protective culture of childhood."[2]

Recognizing the need for community support does not necessitate turning over parenting to a professional class, particularly one subsidized by the state. But the two things are not unconnected. As anyone could tell who monitored last year's debate over child care, the White House conference on early childhood development, or the latest proposal to triple funding to schools that make after-school programs available, the Clinton administration is more than willing for government to step in to "help" parents.

Caution Warranted

Americans should exercise caution before embracing such assistance. One has only to look at the results of the government "help" extended to the poor over the last several decades. Since the war on poverty began in the sixties, an unintended consequence of government policy has been to treat the poor as if they were incapable of living responsibly, particularly when it comes to raising their children. This shows up most clearly in education and child-welfare policy.

The easy answer over the years has been to spend more money on government programs. If we are feeling guilty about the plight of the urban poor, then increased funding for Head Start (the preschool program for poor children that is supposed to help them enter grade school on a par with their more affluent peers) is the easy solution. Increased spending requires only our money, not our time or effort. Simply spending more money also has the added advantage of appearing nonjudgmental. We don't have to say that children do better with both a mother and a father or that neglectful parents are bad. Instead, we ignore the underlying problem, hoping that more education will inoculate children against their

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upbringing. In practice, this has meant turning the problem over to professionals.

Only occasionally do we get hints that professionalized child rearing might be problematic. Only occasionally is anything made of the fact that Head Start, now in its fourth decade, might be little more than a salve for our consciences. A recent GAO study confirms what earlier research has consistently pointed out, i.e., there is scant evidence that Head Start has any long-term beneficial effects for children.[3] Yet the program now routinely recruits three-year-olds. There is also a "0 to 3 initiative," because age three was deemed too late for a sufficient head start. This initiative, as its name implies, works intensively with young mothers, teaching them about child development and encouraging them to rear their children responsibly. Yet as the program grows more expansive, there is little indication that children fare any better and some signs that they do not. (See John Hood's article, page 11.)

The Comprehensive Child Development Program, a similar federally funded initiative geared toward low-income families, released its evaluation results last year with little fanfare because the study revealed that participating families fared no better than their less pampered peers and sometimes even did worse. At some time we have to admit that there are limits to what professionals can do. By failing to insist on responsible parents, we ask educators to take on an extra burden and are shocked when they fail.

In many respects, education policy has been driven by the disasters plaguing the child-welfare system. Just a glance at recent statistics tells us that something is dreadfully awry. Child protective agencies looked into the lives of over three million children in 1996 (the latest year for which we have data).[4] This number reflects more than a 300 percent increase in reports over the last 20 years.[5] In under one-third (28 percent) of the cases, a caseworker determined that a child had been hurt by his parents; of that number, 15 percent were considered to be in sufficient danger to be removed from their homes and put into foster care.[6] While no official count exists, experts estimate that there are at least 500,000 children in foster care today.[7] Unfortunately, over 30 percent of all children sent back home to their families eventually re-enter foster care because of further abuse or neglect.[8]

But who are these children and why don't we hear about them? The children caught in the web of the child welfare system are overwhelmingly poor and without fathers.[9] Most Americans are horrified when confronted with these statistics, but are unaware that they are predictably the direct result of policies that do not hold parents accountable for their behavior. Not surprisingly, the children of those irresponsible parents are the ones who end up in Head Start.

Perverse Incentives

The pervading problem is that the child-welfare system is riddled with perverse incentives that undermine personal responsibility and reward destructive behavior. Social workers understand themselves as providing remedies in the guise of therapeutic treatment. Child abuse is not regarded primarily as a violation of justice, but as either a symptom of illness or the result of economic deprivation, depending on which theoretical model of abuse the social worker follows: the medical or ecological model. Parents, according to either theory, are not at fault. Because abuse is not seen as a moral problem, it should be susceptible to professional help. It is therefore not surprising to find reluctance to ever pronounce any given parent irredeemable.

Mirroring the science of modern medicine, child-welfare professionals are trained to look at human behavior as a doctor would look at disease. Just as doctors strive to eradicate cancer, child-welfare professionals work to end all strife within the family. Even the tools of their trade are couched in scientific terms. If someone beats a child, he is in need of treatment, even if treatment is a parenting class. Caseworkers use "risk assessment tools" to decide whether a child can safely remain in the home, as if by application of a checklist one could do more than guess who will choose to do evil. Such tools lessen the dignity of all involved: they fail to take into

account, and in fact attempt to replace, the free will of the parent and the judgment of the caseworker.

The profession continuously speaks of creating "systems of care" to protect children from the harm caused by bad parents, thus attempting to restore the broken family through social engineering. If a system fails, one needs simply to tinker with the machine, not find fault with the human beings involved. Finding fault is made more difficult because any agency intervention is cloaked under the secrecy of confidentiality laws and treated as utterly private. Since child-welfare agencies are lodged within the state, however, their actions cannot be private: citizens do not have a choice about when the agency enters into their lives.

That cases of abuse and neglect are subject to intervention is not a problem in and of itself; rather, it is the manner in which such intervention is carried out. Child welfare professionals were long ago successful in persuading state legislatures to decriminalize most cases of child abuse and neglect. By forsaking the courts of criminal law, in which determinations of justice and injustice are made and punishments meted out, social work took on the much larger task of attempting to heal family members who have gone wrong. The therapeutic regimen is carried out by providing various services from things as simple as housekeeping to as complicated as residential drug treatment for both the drug-addicted mother and her children.

Healthy Families America, embraced by politicians across the spectrum, is only the latest government-funded fad directed at preventing child abuse. Healthy Families, sponsored by the National Committee to Prevent Child Abuse and funded by most states, is popular because it is advertised as voluntary. This home-visiting program screens parents with newborns in the hospital for risk factors for abuse; then paraprofessionals visit parents deemed to be high-risk and provide them with advice and information on child development. Its effectiveness is unclear: in Arizona, for example, the first-time mothers in the control group had a lower incidence of abuse than the group in the program.[10] After several decades of social experimentation, one thing is clear: yet another government program will fail to make parents better; we do know it can make things worse, however.

It is the poor and marginalized citizens who are hurt most by current policy. If we want parents to raise their children in a manner fitting to a free society, we must remove the incentives for irresponsibility. Overcoming desperate circumstances requires good character, especially that virtue which is the foundation of all the other virtues: self-control. When virtue is not rewarded, but is instead treated as one of many equally worthy lifestyle choices, the poor are disproportionately harmed. It is more than time to insist that all parents be responsible for raising their children. □

1. This may indeed be true of foster care, where the state steps in and physically removes a child from a dangerous parent.

2. Dana Mack, *The Assault on Parenthood* (New York: Simon and Schuster, 1997), p. 17.

3. U.S. General Accounting Office, "Head Start: Research Provides Little Information on Impact of Current Program," April 1997. See also Nina H. Shokraii and Patrick F. Fagan, "After 33 Years and $30 Billion, Time to Find Out If Head Start Produces Results" (Washington, D.C.: Heritage Foundation), July 15, 1998.

4. U.S. Department of Health and Human Services, Children's Bureau, *Child Maltreatment 1996: Reports from the States to the National Child Abuse and Neglect Data System* (Washington, D.C.: U.S. Government Printing Office, 1998), p. 2–1.

5. Patricia A. Schene, "Past, Present, and Future Roles of Child Protective Services," in *The Future of Children*, Spring 1998 (Los Altos, Calif.: The Center for the Future of Children, David and Lucile Packard Foundation), p. 29.

6. *Child Maltreatment 1996*, p. 2–3.

7. The Voluntary Cooperative Information System (VCIS) is the most complete aggregate data on children in substitute care. It is collected by the American Public Human Services Association (APHSA), formerly known as American Public Welfare Association, in Washington, D.C. The last estimate available is for 1995, which puts the number of children in foster care at 483,000. However, APHSA projects a 3–4 percent increase each year, which would put the estimate at 527,787 for 1998. See American Public Human Services Association's Web site at: http//: www.apwa.org/faq/quest7.html.

8. U.S. Department of Health and Human Services, Children's Bureau, *National Study of Protective, Preventive and Reunification Services Delivered to Children and Their Families* (Washington, D.C.: U.S. Government Printing Office, 1997), p. 3–11.

9. U.S. Department of Health and Human Services, National Center on Child Abuse and Neglect, *Executive Summary of the Third National Incidence Study on Child Abuse and Neglect* (Washington, D.C.: U.S. Government Printing Office, 1996), pp. 8–10.

10. Robert Franciosi, "Get 'Em While They're Young: The Second Childcare Revolution and the Expansion of the Nanny State" (Phoenix: Goldwater Institute, 1998), p. 20.

THE FREEMAN
Ideas On Liberty

Children's Real Enemy

by John Hood

An ounce of prevention is worth a pound of cure," or so the old saying goes. For the past three decades, politicians and policymakers attempting to close the gaps in educational achievement and social well-being among American children have taken this sentiment to heart. From the creation of Head Start in 1965 to various preschool and child-care programs today, government at all levels has attempted to ameliorate or eliminate social problems such as poverty, illiteracy, crime, drug abuse, out-of-wedlock births, and welfare dependency by "investing" in early childhood education. The case for such programs has been seductive. Why not inoculate youngsters against these social pathologies with a preschool program, much as public-health departments inoculate youngsters against viral or bacterial pathologies?

In reality, the public-health model has little relevance for early childhood development. The wide range of influences on young minds has proven resistant and sometimes impervious to government alteration. Head Start and other preschool programs aren't "miracle drugs" that can overcome the effects of poor parenting, poverty, and educational malpractice in the public schools.

Nor is an institutional setting the preferred means of caring for preschoolers in most American families. Census data show that nearly three-quarters of all preschoolers are still cared for by parents or relatives at home, rather than in the day-care centers that benefit most from the new government initiatives. It is, in other words, impossible for preschool models, day-care subsidies, provider training, and new regulations to improve the early childhood development of the many children who will never set foot in a day-care center or preschool. What they and other children need are not new government programs but tax relief to allow families to keep more of what they earn and to make their own investments in their children's development.

Head Start

The granddaddy of the government preschool movement is Head Start, a federal program that provides educational, medical, and social services to disadvantaged preschool children. The program originated in 1965 as an eight-week summer program of the U.S. Office of Economic Opportunity. Over the next three decades, it grew into a $4 billion year-round program providing grants to local organizations to operate programs for about 800,000 poor preschoolers.

There are four major components to Head Start: (1) education, (2) health care, (3) parent education, and (4) social services. Local programs provide these services in surprisingly different ways and levels of quality. Indeed, reports by the Inspector General's Office in

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the U.S. Department of Health and Human Services have found that many programs fail to deliver the services for which they are paid. Many children fail to receive scheduled immunizations despite spending two or more years in Head Start.

Even given the spotty nature of local Head Start performance, few analysts dispute that children who leave Head Start and enter elementary school exhibit some advantages over their non-Head Start peers in academic and socio-emotional measures. Unfortunately, these benefits do not last long. By the third grade, according to the federal government's own analysis of Head Start studies, the benefits "fade out." That is, disadvantaged youngsters with Head Start experience become indistinguishable from disadvantaged youngsters without such experience. Whatever Head Start is, it does not qualify as inoculation against educational or social maladies later in life.

Still, defenders of Head Start and similar government programs continue to argue that an early taxpayer investment can save significant costs in the future. They base their case not on Head Start itself but studies of a handful of university experiments. The most famous of these is probably the Perry Preschool in Ypsilanti, Michigan. In 1962 the preschool selected 123 poor children. Half the group was given two years of preschool instruction and services, two-and-a-half hours a day, five days a week. The other half took part in no preschool program. Both groups of children were then tracked throughout their academic careers and into adulthood. The Perry students demonstrated not only significant short-term gains, as do typical Head Start participants, but also long-term gains. About two-thirds of the Perry group graduated from high school, compared to 50 percent of the control group. Similarly, while 51 percent of the control group had been arrested by age 19 for some crime, fewer than a third of Perry graduates had.

When the Perry results were first reported in the mid-1980s, they made a huge public relations splash. Child advocates began arguing that a dollar spent on preschool would save taxpayers $5 in future economic, education, welfare, and crime costs—all based on the Perry experiment. Even as pressure mounted to expand Head Start, and several states began their own early childhood initiatives, few bothered to ask why the Perry results differed so radically from those of Head Start programs themselves.

In fact, studies of the Perry Preschool and a couple of other university experiments don't offer much guidance about the probable efficacy of government preschool. "These programs were conducted under ideal circumstances," wrote Congressional staffer Ron Haskins in a seminal article in *The American Psychologist*. "They had skilled researchers, capable staffs with lots of training, ample budgets. . . . It seems unwise to claim that the benefits produced by such exemplary programs would necessarily be produced by ordinary preschool programs conducted in communities across the United States."

Another major difference between Perry and Head Start is obvious: studies of the Perry project and a few similar projects track only a relative handful of students, a few hundred, through their academic and early adult lives. Studies of Head Start, on the other hand, involve hundreds of preschool programs and thousands of children. When dealing with complex issues such as child development, researchers and policymakers must do better than hype a few best cases.

Smart Start and Success by Six

Fueled by Head Start's public-relations successes in the mid and late 1980s, several states began designing their own early childhood development initiatives in the early 1990s. With names such as "Smart Start" and "Success by Six," these programs mixed a variety of approaches to assisting families with preschoolers, including grants to local service providers, day-care subsidies, home visitation by nurses or social workers, child-care referral activities, and parent-education efforts. In a 1998 report, Columbia University identified eight states as having the most "comprehensive" initiatives in the early childhood area. They included Colorado, Georgia, Minnesota, North Carolina, Ohio, Oregon,

Vermont, and West Virginia. The Smart Start program, created by North Carolina Governor Jim Hunt in 1993, serves as a useful case study for how these programs have developed and what impact they have on children's lives.

Hunt made Smart Start the centerpiece of his election campaign in 1992. He promised not a traditional entitlement program but a public-private partnership to link preschool children with service providers in local communities. Very quickly, however, it became clear that Smart Start was in fact a government program paid for almost entirely by taxpayers and routing most dollars to service providers rather than parents. When fully funded, the program is expected to cost nearly $350 million a year—larger than entire departments of North Carolina's state government. Just to put that in perspective: Smart Start will consume more resources than the state's law enforcement budget and almost as much as the state's entire judiciary.

Smart Start may well be the most successful public-policy initiative ever hatched in North Carolina—if one defines success as getting good press. Not just in North Carolina but nationally, the program has received lavish praise for making an investment in the future of the state. Most recently, the program was the recipient of the 1998 Innovation in American Government Award from Harvard University and the Ford Foundation. "North Carolina is making an effort for early childhood education that includes county by county, group after group, and business after business, and is making significant headway," said selection committee chairman David Gergen, former Clinton aide and editor-at-large for *U.S. News & World Report*. Other kudos for Smart Start have come from national magazines such as *Working Mother* and *Good Housekeeping*.

After such heady praise, many state leaders seem to have conveniently forgotten the purpose of Smart Start—to make a long-term impact on the education and social development of children. With only four years of operation under its belt, Smart Start cannot yet be judged conclusively on this criterion. Indeed, it is striking how many plaudits the program has received without a shred of evidence that it is achieving its stated goals. Like Head Start, Smart Start has been successful on a political level without establishing a demonstrable record of success.

The Early Evidence

Unfortunately for its boosters, the early evidence that does exist does not bear out Smart Start's reputation. Two studies, neither conducted by critics of the program, have found it not to be the public-private partnership Hunt promised in 1993, nor is it likely to be a successful "investment" in early childhood development.

In August 1998, North Carolina State Auditor Ralph Campbell released a "Special Report on the Smart Start Program," which included financial data for FY 1995–96 and 1996–97. While Campbell's office found some areas of improvement, particularly in the number of management problems at local partnerships, it concluded that Smart Start still operates without a uniform fund accounting system, without a uniform contract management and monitoring system, and without sufficient oversight by its nonprofit parent, the N.C. Partnership for Children.

Perhaps most significantly, the audit found that Smart Start continues to fail to meet its private fundraising goals. For 1996–97, the program received $3.9 million in cash and in-kind contributions, far less than the $6.7 million in private funds required by the state legislature in exchange for past increases in taxpayer support. Even this standard wasn't particularly high; the legislature mandated only that Smart Start raise $1 in private funds for every $10 in taxpayer funds. Given the early rhetoric about Smart Start not being a government entitlement program and instead being a public-private partnership, the failure to meet the legislature's low fundraising target represents a major disappointment. Indeed, the N.C. Partnership for Children says it has exceeded the fundraising goal for 1997–98—but only after liberalizing the definition of fundraising to include gifts made directly to day-care centers, not to Smart Start itself. How much private support would flow to the centers anyway? It is impossible to tell.

With regard to the benefits of the program, only one study provides any useful information. It was conducted by the Charlotte-Mecklenburg Public Schools and Smart Start of Mecklenburg County and was released in July 1998 by the N.C. Partnership for Children. In examining the educational impact of Smart Start on kindergartners in Mecklenburg County, the state's most populous county, it surveyed 5,715 parents. It used different assessments to provide educational data. One, the Kindergarten Awareness Profile (KAP), is given to incoming students to identify potential learning difficulties. The other, the Kindergarten Assessment in Reading and Mathematics (KARM), is a periodic observation of academic achievement given by classroom teachers. The results are combined at the end of the year and serve as a measurement of student achievement.

In brief, no statistically significant relationship was found between the KAP and KARM results, on the one hand, and participation in the Smart Start program for fewer than three years, on the other. That is, preschoolers who spent a single year in a Smart Start-supported day-care center or simply received a Smart Start-sponsored vision or hearing screening did not perform any better on the KAP screening or the KARM achievement assessment than preschoolers who did not. For those who spent three years in a Smart Start-supported center, the study did find a statistically significant—but small—difference. On the KAP screening, long-term Smart Start kids scored an average of 93.35 (on a scale of 0-102) versus 91.05 for kids without that experience. On the KARM, the point difference was similar: 32.18 versus 29.83.

Smart Start proponents trumpeted that last result as evidence of the effectiveness of the program. "Smart Start is working in Mecklenburg County and this study proves it," said Ashley Thrift, chairman of the N.C. Partnership for Children. He is mistaken. The Head Start experience shows that the difference between participating and nonparticipating preschoolers will shrink as both groups go through the same schools. A large gain in early educational outcomes for participants might be sustained over time, but a tiny one—two points on a test—is unlikely to persist. It is certainly not a worthwhile return on the huge investment that North Carolina taxpayers have made in the Smart Start program since 1993.

Even the small jump in scores for long-term Smart Start participants may be suspect. After all, it is difficult if not impossible to rule out "selection bias" in such a study. That is, parents with other characteristics likely to improve student performance are probably more likely to get their children involved in Smart Start-type programs than are their peers. This effect may be small, but it would not take much to eradicate the small outcome differences the study found.

A Different Approach

There is no great mystery as to why government programs like Head Start and Smart Start don't provide the long-term benefits they promise. Two or three years of preschool are unlikely to make an indelible impact on children who will spend far more time with their parents and in what are often mediocre (or worse) government schools. There is no magic wand that can wish away the effects of poverty, family breakup, and educational malpractice. There are no shortcuts in tackling these problems, nor are many of them amenable to government solutions at all.

On this point, the comments of four academic researchers who support Head Start are particularly salient:

> If we wish to "close the gap" between advantaged and disadvantaged children, educational services need to go beyond the provision of short-term interventions. Policy decisions that support the expansion of preschool programs without addressing the more fundamental question of trying to alter what happens to disadvantaged children in our nation's public schools are shortsighted. (Valerie Lee, et al., "Are Head Start Effects Sustained?," *Child Development*. vol. 61, 1990, p. 505)

Furthermore, there is no reason to believe that government involvement or oversight of

preschool and child-care arrangements will improve their quality. It is not obvious, for example, what specific factors make an early childhood program effective, so governments have little to go on in trying to mandate improvements. As the National Research Council stated in 1996, researchers do not know what constitutes the "basic ingredients" of high-quality child care. The council observed that "what is developmentally beneficial for one child may not be so beneficial for another."

The few studies that do exist suggest that the impact of day care and preschool, positive or negative, on a child's readiness to learn is difficult to demonstrate. Only 1.3 to 3.6 percent of differences among children in cognitive and language performance has been significantly linked to child-care factors; the vast majority of such differences among students when they enter school can be linked to factors such as family income, mother's vocabulary, and family environment.

If policymakers really want to help all children grow and develop, the most important task is to alleviate the tax burden on families. □

Remember loved ones with a Tribute Gift

It's the time of year when many of us are thinking about Mother's Day or Father's Day gifts. Likewise, many people are busy celebrating wedding anniversaries. Are you puzzling over what to give? Why not consider something really unusual: a Tribute Gift in honor of a parent, husband or wife, or other loved one?

Tribute Gifts allow you to celebrate the life and vision of someone you hold dear, while also helping FEE to achieve its vital mission of promoting liberty and economic understanding.

To give a Tribute Gift, simply contact us with the name of the person you are honoring, your name and address, and the name and address of anyone else to whom you would like an acknowledgment letter sent. Your contribution may be in the form of check, credit card transaction, securities, or other property.

This year, forget the flowers or the tie — and give a gift that really means something!

THE FREEMAN
Ideas On Liberty

The Second Amendment in the Light of American Republicanism

by Joseph R. Stromberg

The "transforming" ideology of America's revolutionary period saw the chief conflict in society as one between liberty and power. That ideology synthesized themes from several sources.[1] Given the differing origins and jumping-off points of classical liberalism and classical republicanism (the two most important elements), the American "synthesis" might be expected to undergo some unraveling when up against the harder problems of political life. What is striking, however, is the surprising tenacity and coherence of American republicanism over the long haul, the persistence of its language, and the continuing relevance of its key ideas down to the present.

One of these key ideas is the notion of the individual properietor on his own land, capable of bearing arms in defense of himself, his property, his family, *and* the republic. In his role as defender of his free society, the armed citizen served with his fellows in the militia, which republican thinkers regarded as the military system most compatible with republican liberty and whose existence helped offset the menace of "standing armies" drawn from outside the community ("crimped scum") loyal only to their immediate superiors (men of "ambition" or a "court party"). The armed proprietor was the idealized republican citizen, and the Second Amendment enshrines his role in the ideological and political systems.

Some latter-day writers on republicanism have a way of overestimating the tensions within the American synthesis. But some of the alleged incompatibilities—"agrarianism" versus "commercialism," "virtue" versus "luxury"—were either handled well enough by Americans, or exist mainly in the eye of the beholder. Wendy Kaminer, for example, writes that "[a]t the heart of the gun-control debate is a fundamental tension between republicanism and individualism" (that is, liberalism).[2] A look at the Second Amendment is an opportunity to learn more about American republican ideology and to gain a better understanding of the Amendment itself.

Kaminer writes of "the challenge posed by republicanism to the individualist culture that many gun owners inhabit."[3] But when have Americans *not* inhabited an individualist culture? And when did American "individualists" *not* live in communities? (Re-read Tocqueville.)

The problem as set up by Kaminer rests on the old caricature of "atomistic liberalism." It does not follow that because John Locke started with individuals and their rights, that he or any other liberal writer overlooked the existence of families, churches, and other social institutions. It has never been strictly a matter of "the individual versus society"; rather it has been about what *kind* of society we live in, or wish to live in, and whether or not a free society is desirable and possible. If there are

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"atomistic" versions of liberalism, the French can answer for them, since the English, Scottish, and American writers did not create them. The rootless, abstract individual, who can only be made "whole" again by participating in an authoritarian-to-totalitarian form of republic, is central to Rousseau's system—not Locke's.[4]

The Second Amendment in a Distinctively American Republicanism

Anti-Second Amendment writers have great sport trying to separate the individual's right to bear arms from the same individual's role in the militia. On their reading of republicanism, the community stands opposed, somehow, to those who make it up, and the people have "the right to keep and bear arms" only in relation to their duties in the militia. We are asked to take seriously the view that these individuals only keep and bear arms at the command of the state, and really ought to store them all in a central warehouse, whence they will be issued when the state organs (of "national security"?) decide there is an emergency. The state militias, it is likewise asserted, mean nothing today, having been consumed by the National Guard, with its sort of Third World name. I shall demonstrate the leglessness of this stand directly.

As far as an individual right to self-defense goes, the law—which is very conservative—gives us examples from the earliest societies connected with the Indo-European language family. It was a settled thing in Greek, Roman, and Slavic law that a man who caught an intruder in his house by day, should seize him and hold him for the authorities; if the intruder came at night, he could kill him. I suppose he could do this barehanded, but more likely he was armed

We need not reach so far back for precedent, however. William Blackstone, whose views on English law were more or less committed to memory by the Founders, regarded self-defense as one of the three most fundamental rights embodied in that law. In the run-up to the American Revolution, colonial radicals held forth on natural rights and the Rights of Englishmen (which in their minds were much the same thing). James Otis advanced arguments from *both* directions in his speech against the Writs of Assistance, making good use of the truism that an Englishman's home is his castle.[5]

Much of that ground had been covered in the Puritan Revolution and the Glorious Revolution of 1688. The seventh item in the English Bill of Rights of 1689 stands in ancestral relation to our own and says: "That the subjects which are Protestants may have arms for their defence suitable to their conditions, and as allowed by law." This is not very "inclusive"—as we say these days—but this was the Parliament that had just deposed James II for being too absolutist and too Catholic, and we can hardly expect these lords and great landholders to have shared the right of self-defense fully with the lower orders.[6]

The immediate context of the Second Amendment is, of course, the struggle over the ratification of the second U.S. Constitution. Part of this context is the revolutionary generation's correct view that the militia had played an important role in the success of the American war of secession from the British Empire. Perhaps the only believable reason for throwing over the existing Articles of Confederation (the first constitution) was the claim that a slightly more effective federal government was needed to defend the confederacy from European powers that still held large parts of North America. This, in turn, raised many questions that went to the heart of republican theory: internal versus external taxation, standing armies versus militia, "empire" versus republican decentralization, and the like. It is not surprising, therefore, that seven state conventions ratified the second Constitution with reservations. They submitted declarations about rights to spell out their understanding of the new charter and proposed amendments to set right ambiguities they saw in it.

Some of these proposals spoke directly to the related questions of the militia and the people's right to bear arms. New Hampshire asked for amendments—among others—stating that "no standing army shall be Kept up in

time of Peace unless with the consent of three fourths of the Members of each branch of Congress" and that "Congress shall never disarm any Citizen unless such as are or have been in Actual Rebellion." Asserting the power to "resume" (take back) powers granted if they should be abused, Virginia called for a Bill of Rights to include the following: "That the people have the right to keep and bear arms; that a well-regulated Militia *composed of the body of the people* trained to arms is the proper, natural and safe defence of a free state. That standing armies in time of peace are dangerous to liberty, and therefore ought to be avoided. . . ." (My italics.) New York, also asserting the right of the people to "reassume" powers abused by the new federal government, declared that "the people have a right to keep and bear Arms; that a well-regulated Militia, including the body of the People *capable of bearing arms*, is the proper, natural and safe defence of a free State; [t]hat the militia should not be subject to Martial Law except in time of War, Rebellion or Insurrection. That standing armies in time of Peace are dangerous to liberty, and ought not to be kept up, except in Cases of necessity. . . ." (Italics in original.) North Carolina likewise: "[T]he people have a right to keep and bear arms; that a well-regulated militia *composed of the body of the people*, trained to arms, is the proper, natural and safe defence of a free state." (My italics.) Finally, Rhode Island, asserting the right of the people to "reassume" delegated powers, declared that "the people have a right to keep and bear arms," with the same language regarding militia, standing armies, etc., used by the other state conventions.[7]

It would seem that the men who demanded what became the Second Amendment expressed their views with great power and clarity. Yet it is this straightforward proposition that overmasters the reasoning power of several prominent northern congressmen and senators today.

The Hermeneutics of the Second Amendment

The wording of the actual text of the Second Amendment can be described as "sloppy draftsmanship" only in the sense that the sentence structure leaves itself open, perhaps, to deliberate and willful misreading that the amendment's framers could never have foreseen. That they and their contemporaries understood what they were about, and what the amendment means, is clear from the state proposals cited as well as from a mountain of related language in contemporary opinion and private communications. Judge Joseph Story of Massachusetts—High Federalist, U.S. Supreme Court Justice, and a founder of the Yankee theory of the union—wrote in 1840 that the right to keep and bear arms is "the palladium of the liberties of a republic; since it offers a strong moral check against the usurpations and arbitrary power of rulers; and it will generally, even if these are successful in the first instance, enable the people to resist and triumph over them."[8]

Stephen P. Halbrook quotes Thomas Jefferson's and James Madison's comments on Virginia legislation to show that there is no mystery about the meaning of "bear" (it means "carry"). This goes to the modern liberal superstition that Second Amendment advocates believe in private ownership of tanks and nuclear bombs. If the private right were not already clear from the ratifying conventions' drafts, Robert Shalhope cites Thomas Jefferson's views: "Let your gun therefore be the constant companion of your walks." A ramble through the country with your gun is manifestly not service in the militia.[9]

The meaning of the Second Amendment is also clarified by a look at comparable provisions in eighteenth-century and nineteenth-century state bills of rights. Here I will cite only the Texas Constitution of 1876: "Every citizen shall have the right to keep and bear arms in the lawful defense of himself or the State; but the Legislature shall have power, by law, to regulate the wearing of arms, with a view to prevent crime."[10] Here as elsewhere, there is no question that an individual right of self-defense exists alongside but separate from any militia issues. The point about the "wearing" of arms, and the state's right to regulate that, brings up some issues as to the scope of the Second Amendment within a federal system.

The original understanding—if we may use this phrase—was that the Bill of Rights applied against the new and feared general government and not against the several states. The language of the Second Amendment is so broad that it might be argued that the states bound themselves by it ("the right . . . shall not be infringed" versus "*Congress* shall make no law" in the First Amendment). Usage suggests, however, that protection of the right was left—at the state level—to bills of rights in the state constitutions where the actual details might vary. The Fourteenth Amendment (if actually ratified) may alter matters. The Supreme Court has proclaimed that the Fourteenth Amendment "incorporates" those rights in the first ten amendments to which the Court is partial. So far, it has not seen fit to extend this reasoning to the Second Amendment.

The Bad Faith of the Gun Grabbers

If the gun opponents were honest, they would—like George Will—concede the overwhelming case against their "interpretation" of the amendment, and then go out and work to get their own amendment. The opponents want to get by with "interpreting" the amendment away, or simply ignoring it as so much "irrelevant" eighteenth-century metaphysics, while Congress gets on with the important work of overriding, "infringing," and eliminating the right to keep and bear arms. They wish to proceed as if we were living under the Anti-Constitution composed by Rexford G. Tugwell, ex-New Deal technocrat and planner. Tugwell's version of the amendment reads, "No person shall bear arms or possess lethal weapons except police, members of the armed forces, or those licensed under law according to rules established by the Court of Rights and Duties." In 1941, Clarence G. Streit, Anglophile proponent of federation between the United States, Britain, Australia, New Zealand, and South Africa, wrote a draft "based on the U.S. Constitution" that simply left out any right to bear arms. More to the point may be the plan of government for the Philippine Islands drawn up in 1913 by the U.S. Secretary of War, which, as Philip Jessup put it, "secured to the Philippine people all the guarantees of our Bill of Rights except trial by jury and the right to bear arms"—that is, all but the two most important ones. Of course the American colonialists, having just fought a brutal counter-insurgency war to make good their claim to the islands, and which led to the death of some 200,000 Filipinos, were not in a mood to encourage unreliable Filipinos to bear arms.[11] It may be significant, however, that proponents of gun control think it appropriate to treat Americans the way an imperial power treats its far-off colonial subjects.

The gun-controllers, to put it another way, can't see why Americans are so reluctant to submit themselves unquestioningly to the benevolent rule of a social-democratic welfare-warfare state of the sort in place in the happy and peaceful nations of western Europe. In such a state things will be very orderly—and there is absolutely nothing to fear because we will all have that all-important right to trudge to the polls every so often to show (perhaps under threat of fines) our acquiescence in whatever the politicians decide to do with our lives, incomes, and property. No matter how detailed bureaucratic oversight of people's lives may become, they can always vote for a change in personnel—if not about anything substantive. This happy scenario looks to a re-creation of the Old Order in which priests and warriors rule over the economic producers who, after all, need only do what they are told.

Why Bother with Republican "Discourse"?

Law professor William Van Alstyne writes that the Second Amendment is not "mysterious, equivocal, or opaque"—"today it is simply unwelcome." As for those who dislike it, "it is for them to seek a repeal." He adds that "the essential claim" made by the NRA "is extremely strong."[12] Even so, it is likely that Congress will go on infringing the amendment and order the states to infringe it further, and that the courts will regard the right as "irrelevant" and of mere antiquarian interest. People will still believe in their right of self-defense.

So what do we gain by going over all this? We learn the truth, and that is probably a good thing in itself. We learn something about the American revolutionary synthesis and, alas, the difference between ourselves and our forefathers. And we may learn something about constitutional morality as against "stealth" amendment by Congress and the courts, which present us every few years with a brand new "constitution" they have found lurking inside the real one. □

1. For a discussion of the various themes and references, see my article "Tensions in Early American Political Thought," *The Freeman*, May 1999.

2. Wendy Kaminer, "Second Thoughts on the Second Amendment," *The Atlantic Monthly*, March 1996, p. 32.

3. Ibid., p. 43.

4. See Robert A. Nisbet, *Tradition and Revolt* (New York: Vintage Books, 1970), "Rousseau and the Political Community," pp. 15–29.

5. James Otis, "On the Writs of Assistance" in *Orations of American Orators*, I (New York: The Co-operative Publication Society, 1900), pp. 19–24.

6. English Bill of Rights, 1689, in Irwin Edman, ed., *Fountainheads of Freedom: The Growth of the Democratic Ideal* (New York: Reynal & Hitchcock, 1941), p. 338. The Whig landlords who ousted the Stuarts soon passed the draconian Black Act, which almost made it a capital crime to even think about shooting any game on their vast estates. See E.P. Thompson, *Whigs and Hunters* (New York: Pantheon Books, 1975). The connection between game laws, arbitrary search and seizure, and gun confiscation seems fairly obvious.

7. The full text of ratifications is in Charles C. Tansill, ed., *Documents Illustrative of the Formation of the Union of the American States* (Washington, D.C.: Government Printing Office, 1927), pp. 1009–1059.

8. Joseph Story, *Familiar Exposition of the Constitution of the United States* (Lake Bluff, Ill.: Regnery Gateway, 1986), p. 319.

9. Stephen P. Halbrook, "What the Framers Intended: A Linguistic Analysis of the Right to 'Bear Arms,'" *Law and Contemporary Problems*, Winter 1986, pp. 151–162, and Robert E. Shalhope, "The Armed Citizen in the Early Republic," ibid., pp. 125–141.

10. *Texas Almanac, 1980–1981* (Dallas: A.H. Belo Company, 1979), p. 482.

11. Rexford Guy Tugwell, *Model for a New Constitution* (Santa Barbara: Center for the Study of Democratic Institutions, 1970), p. 81; Clarence G. Streit, *Union Now with Britain* (New York: Harper & Brothers, 1941), pp. 215–16; and Philip C. Jessup, *Elihu Root*, vol. I (Hamden, Conn.: Archon Books, 1964 [1938]), p. 354.

12. William Van Alstyne, "The Second Amendment and the Personal Right to Arms," *Duke Law Journal*, April 1994, p. 1250.

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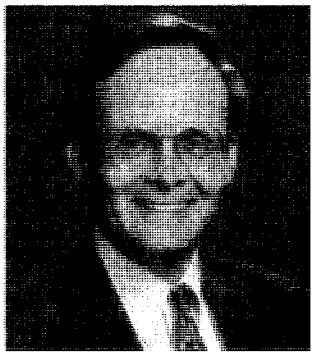


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A Tax Is Not a User Fee!

Politicians and bureaucrats are notorious for manufacturing euphemisms—clever but deceptive substitutes for what they really mean but don't want to admit. That's how the phrase "revenue enhancement" entered the vocabulary. Some of our courageous friends in government couldn't bring themselves to say "tax hike."

At all levels of government, a bipartisan effort to impose new or higher taxes and mislabel them as seemingly less onerous "user fees" provides another example. Sometimes, a user fee is indeed a user fee. Other times, it's not that at all. Instead, it's a tax hike disguised by a misnomer.

When someone chooses to use a government service and pays for it, he's paying a user fee. Furthermore, what he pays should cover the cost of the service he is receiving; if it goes for something he isn't getting or doesn't want, then he's paying a little of both—a user fee *plus* a tax. Taxes differ from user fees in that paying them isn't a matter of choice and what you pay is not tied directly to what you're using.

In principle, true user fees make a lot of sense, especially if you want people to understand that nothing from government is truly "free." Indeed, the more government finances itself through user fees instead of taxes, the less it looks like government and the more it gets out of the redistribution business and begins to resemble private firms operating in free markets.

Instinctively, most people sense a certain fairness about true user fees. You pay for what you get, and you get what you pay for. Most people understand and support user fees for such things as toll roads, harbors and waterways, and even parks and recreational facilities. If they understand that private enterprise would probably do a better job with these things, they know that at least a user fee approach for government services gives them an opportunity to make a rational economic choice: buy it if it's worth the price, patronize an alternative, or do without. All this makes for useful background to a victory that advocates of liberty and sound economics recently won in my state of Michigan.

In 1978, Michigan voters approved the Headlee Amendment to the state constitution. Among other provisions, the amendment requires voter approval before a tax can be imposed or increased. In its 1994 report, the Headlee Amendment Blue Ribbon Commission found that a growing number of Michigan townships, counties, and cities were skirting that requirement by mislabeling certain taxes "user fees." The commission recommended that the legislature clarify the difference between a tax and user fee. The Michigan Supreme Court now has done what the legislature never got around to doing. Here's how the case arose:

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In 1995, the city of Lansing adopted Ordinance 925, known by many as the "rain tax." It provided for the creation of a storm water enterprise fund "to help defray the cost of the administration, operation, maintenance, and construction" of a new storm water system that would separate sanitary and storm sewers. Heavy rains had occasionally caused the city's combined sanitary and storm sewer system to overflow, discharging untreated and partially treated sewage into the Grand and Red Cedar rivers. Fifty percent of the 30-year, $176 million cost of the system was to be financed through an annual "storm water service charge" imposed on each parcel of property in the city. The city maintained that the service charge was a user fee and therefore did not have to be put before the voters for approval. But Lansing citizen Alexander Bolt had read the constitution and knew a tax when he saw one.

Bolt challenged the Lansing "rain tax," taking the case all the way to the Michigan Supreme Court, a majority of which on December 28, 1998, declared, "We hold that the storm water service charge is a tax, for which approval is required by a vote of the people. Because Lansing did not submit Ordinance 925 to a vote of the people as required by the Headlee Amendment, the storm water service charge is unconstitutional and, therefore, null and void." The decision established an important precedent that puts municipalities on notice that the voters who approved the amendment intended for it to be enforced, not subverted.

The Court's majority opinion refreshingly argues that "a primary rule in interpreting a constitutional provision . . . is the rule of 'common understanding.'" In other words, in this case the intent of the voters should be of utmost importance, as opposed to some judicially activist fabrication. The Court affirmed that the voters intended to place limits on taxes and governmental expansion.

Just what exactly distinguishes a user fee from a tax? The Court advanced three main criteria: (1) a user fee is designed to defray the costs of a regulatory activity (or government service), while a tax is designed to raise general revenue; (2) a true user fee must be proportionate to the necessary costs of the service, whereas a tax may not be; and (3) a user fee is voluntary, whereas a tax is not.

The Lansing ordinance failed all three tests of a user fee. The Court determined that it constituted "an investment in infrastructure as opposed to a fee designed simply to defray the costs of a regulatory activity" and agreed with the dissenting opinion in a lower court ruling that the revenue from the charge was "clearly in excess of the direct and indirect costs of actually using the storm water system." The Lansing rain tax applied "to all property owners, rather than only to those who actually benefit," contrary to a genuine user fee. Moreover, the ordinance "failed to distinguish between those responsible for greater and lesser levels of runoff."

Most plainly, the rain tax was utterly involuntary. True user fees are only "compulsory" for those who choose to use a service, but Lansing property owners in this case had "no choice whether to use the service" and were "unable to control the extent to which the service" was used.

The Court's majority concluded by quoting the Headlee commission report, "This is precisely the sort of abuse from which the Headlee Amendment was intended to protect taxpayers." Amen!

The message is clear to Michigan municipalities: You now have no legitimate excuses for mislabeling taxes as "user fees." Be honest. If it's a tax, put it before the voters as the Headlee Amendment requires and make your best case. You can't junk the constitution just because you want the money. It's a refreshing message that ought to be applied everywhere. □

THE FREEMAN
Ideas On Liberty

The Reserve Requirement Debacle of 1935–1938

by Richard H. Timberlake

The principal thrust of Treasury-Federal Reserve monetary policy throughout the 1920s and 1930s was by turns restrictive, contractionary, and depressive. Even as the economy was floundering helplessly in a financial environment of monetary austerity, no one in the Treasury-Fed bureaucracy seemed to understand the ongoing disequilibrium. Most economists and bankers could not grasp it either. Federal Reserve spokesmen claimed that "low" interest rates were a sign of monetary ease and plenty of credit. Since market interest rates had almost disappeared into the woodwork, "money" was supposedly plentiful. In fact, the quantity of money—the money the central bank was supposed to provide scientifically and opportunely to the economy—was suffocatingly inadequate.[1]

Part of the problem was the flawed real bills doctrine that most commercial bankers and, subsequently, Federal Reserve officials embraced to fashion credit policy. If bankers and businessmen were not borrowing at the minuscule rates then current, the argument went, their enterprises were just not productive enough to warrant additional monetary resources. According to this view, the production of goods, services, and capital led to the production of money through the operation of banks and the gold standard. In fact, with the production of money in the province of human design, it was the other way around: Without *some* human provision on *some* basis for supplying money to the economy, the economic machine was derelict.

A related policy shortcoming that aggravated the Federal Reserve's restriction of money was the official attitude toward "the" gold standard. Since 1920, the gold standard in practice had become an unwelcome nuisance to be fit into the government's monetary-fiscal program in ways that would not interfere with the current hands-on priorities of current policy. Especially was this stance clear after 1933.

Eclectic Model

Treasury and Federal Reserve excuses for past mistakes were highly successful. Fed spokesmen then trotted out their eclectic model of the economy, which claimed that the depression was worldwide and developed from a number of independent causes. One of their favorite slogans was, "Monetary policy is like a string. You can pull with it, but you can't push on it." Those who had a collectivist bent were only too happy to hear that a market order based on individual property rights and the rule of law could not thwart a great depression.

Another factor that obscured a path out of the depressionary forest was the policy of raising the price of gold after all the gold had gone to Washington and been buried in the Treasury's dungeons. Government ownership of the gold, and the actual illegality of private

Richard Timberlake is a professor of economics retired from the University of Georgia. This is the last in a series.

ownership, left gold with no more function than ballast in the basement that would prevent the U.S. Treasury building from rocking in a windstorm.

The middle 1930s witnessed an even more astonishing event. The belated recovery, helped in part by monetary expansion from the massive gold monetization, was just beginning to show some vitality when Treasury-Fed officials decided that the continuing gold inflows were leading to the acute danger . . . *of an inflation*! Official opinion in the two agencies concluded that the proper tactic now was for the Fed to increase member-bank reserve requirements using the new power it had been granted by the Banking Act of 1935. Simultaneously, the Treasury would reinstitute the gold-sterilization procedures that the Fed had used so conspicuously in the 1920s. The Board of Governors regarded the monetary conditions of the mid-thirties as a made-to-order opportunity to experiment with its new reserve-requirement gadget.

Reserves and Reserve Ratios

Before going further, the reader might find useful an explanation of banks' reserve ratios and the central bank's authority over legal reserve requirements. A bank's reserve ratio is the fraction of the bank's effective reserves relative to its demand obligations (that is, checking deposits). It is stated either as a decimal or as a percentage. Reserves always included currencies and cash, such as gold, silver, and other legal tender. All legal tender currency is government issued or government guaranteed, and has included greenbacks, silver certificates, gold certificates, national bank notes, and Treasury notes. Since 1913, the principal currency has been Federal Reserve notes issued by the twelve Federal Reserve Banks.

Reserves also include reserve-deposits that member banks maintain in Federal Reserve Banks. These accounts are the balances that Fed Banks use to clear the demand obligations of their member banks to other banks. They are similar to the commercial bank accounts households and businesses write checks against for conventional transactions. All these reserve items are ultimate legal satisfaction for redeeming the demand deposits (and in the nineteenth century, bank notes) that the commercial banks issue(d) as a by-product of their lending and investing operations.

Before governments imposed legal reserve requirements, bankers maintained their own reserve accounts. The typical banker considered a variety of circumstances to determine the fraction of reserves he should keep against the bank's demand obligations: the volatility of his lending business, his bank's geographical location—rural or urban and its proximity to financial centers, the season of the year, and the general state of business. Especially did he consider banking laws that added institutional restrictions to his other concerns. Banking laws have been especially onerous for banks, probably because all legislators know that banks somehow create money and the legislators feel that it is their duty to protect their constituents from these "predators."

Clearly, the importance of the many factors determining the volume of reserves the banker felt he needed would vary over time. The banker would then adjust the ratio by extending or diminishing his loans and accommodations to the borrowing community. Whatever his reserve position, the banker had his reserves on hand and knew he could use them to the fullest if any panic or emergency threatened.

At first blush, specification of minimal reserve requirements seems to be a logical function of government—something akin to police protection. Indeed, that was the view when Congress first considered the idea in the mid-1830s, as the U.S. Treasury deposited the money from land sales and tariffs in private banks. Congress then deliberated a plan that called for a 20 percent legal reserve minimum for all banks holding U.S. Treasury balances. At first, the proposal had a good deal of support. On reflection and "reconsideration," however, the lawmakers of the time backed away from a specific prescription. They decided to let the secretary of the treasury stipulate the reserve qualifications for banks that held government balances.[2]

Some state governments began specifying legal reserve requirements for banks as early as the 1840s. Then the National Bank Act passed during the Civil War included reserve requirements for all national banks. It listed three classes of banks (described last month): central-reserve-city banks, reserve-city banks, and "country" (all other) banks. Only state laws governed the reserves of non-national banks, and some states had no formal reserve requirements at all.[3]

Of course, no bank, regardless of state law, can operate without a contingency or providential reserve of some amount. Competition among banks for deposits and loan-making opportunities, and clearing of banks' checks through clearinghouses, force banks to maintain some level of reserves. *Legal* minimal requirements simply mandate what solvent and responsible banks would do anyway to stay in business as cost-recovering enterprises—with this exception: legal minimums are usually a fixed percentage for a wide classification of banks, and are, therefore, somewhat greater than most banks would keep if left to themselves. They are greater because a governmental regulatory agency must cover a wide spectrum of banks that have diverse exposures to risks and other reserve maintenance requirements.

Though minimum legal reserve requirements seem sensible and have become part of the conventional wisdom, their presence has proven in practice to be destabilizing to the banking and monetary system. First, the "correct" ratio is highly variable from bank to bank, depending on all the factors listed. Since it is also highly variable from season to season for the same bank, it is not a parameter that a government agency, even with perfect wisdom, can specify for banks collectively. It is another example of the synoptic regulatory delusion.

Finally, the very nature of a *legal* reserve requirement raises this unresolvable question: if a bank must keep a minimal ratio of reserves to deposits, how can it use those reserves when redemptions of its notes or deposits would bring its reserve ratio down below the legal minimum?

This dilemma has never been satisfactorily solved. Some banking laws have allowed banks to trench on their required reserves by paying substantial penalties. Often, however, the reserve requirement was treated as an ironclad minimum, which if breached, gave banking authorities cause to shut down the offending bank. In other cases, the bad publicity banks received when their reserve ratios became deficient practically put them out of business. Under such opprobrium, the legal minimum percentage converted what would have been a cushion of usable reserves against unusual redemptions into an unusable fixture that banks only dared breach when they were at the end of their other resources.

Uncertain Effects

The potential effect on the money supply from the reserve-requirement manipulation the Banking Act of 1935 vested in the Federal Reserve Board was very uncertain. The greatly increased quantity of monetized gold had expanded bank reserves to double the dollar amounts that current requirements—7, 10, and 13 percent for the different classes of banks—specified. Banks had plenty of reserves but they were not using them to make loans and investments to households and businesses. Given that dollar reserves were double the amount legally required, the banking system, by expanding credit and deposits to the legal limit, could have doubled the quantity of demand deposits.[4] This unused potential implied two questions: First, what was the probability of such a bank credit expansion? Second, if it happened, what would be the effect on prices?

Marriner Eccles, the new chairman of the Federal Reserve Board, was one of many Treasury and Fed officials who thought that the reserve overhang was dangerous. These reserves, he observed in late 1935, "could become the basis of a potential expansion of bank credit of such proportions that the Federal Reserve could lose all control or influence over the supply and cost of money."[5] He noted, however, that the Board of Governors still saw "no evidence of overexpansion of business activity or of credit."[6]

In the next six months the continuing gold inflow raised total bank reserves to $6 billion,

and excess reserves to $3 billion. These numbers convinced Eccles, other Fed and Treasury officials, and much of the financial community that an increase in reserve requirements was advisable. What the policymakers especially disliked was the fact that the banks, with all their excess legal reserves, could operate outside the control of the Fed. Once the excess reserves became required, Fed policymakers would have a tight rein on the banks. "Even if the increase was as much as fifty per cent," Eccles concluded, "the remaining reserves would still be beyond current or prospective needs of business and would provide a more than adequate basis for legitimate credit expansion."[7]

The Fed Board, under the urging of the Fed Bank of New York, raised reserve requirements by 50 percent in August 1936. The increase, as far as the banks were concerned, made half—$1.5 billion—of their existing reserves unavailable. However, they still had excess legal reserves of $1.5 billion. So the Fed Board in early 1937 raised requirements again, effective in March and May, to "mop up" the remaining legal excess. The total volume of reserves moved from "excess" to "required" came to $3 billion.

The magnitude of this change is understood best when it is viewed in equivalent dollar value to an open-market sale of government securities. As Friedman and Schwartz point out, $3 billion "amounted to nearly one-quarter of total high-powered money." Since the total amount of government securities in the Fed Banks' portfolio at the time was only $2.4 billion, the Federal Open Market Committee could not possibly have carried out such a momentous open-market sale. Neither would it have considered the idea for an instant.[8]

Raising reserve requirements had a good deal of support outside the Fed and Treasury. Benjamin M. Anderson, a conservative critic of both New Deal policies in general and monetary policy in particular, expressed a typical view. The great increase in excess reserves, Anderson noted, had had very little effect on interest rates. Therefore, decreasing reserves by raising requirements would have very little reverse effect.[9]

Anderson's arguments reflected the conventional economic reasoning of the time. Monetary policy could only influence financial and business conditions by its limited effect on interest rates. Since rates were already at rock bottom, excess bank reserves made no difference, and their elimination would do no harm.[10]

Contradictions in Reasoning

Both Anderson's and Eccles's comments, and also those of many other observers, were clearly contradictory. On the one hand, excess reserves did not have any monetary thrust for restoring normal levels of business activity; on the other hand, they gave rise to inflationary levels of credit expansion. Now which view was correct?

No one at the time had the energy or initiative to do so, but a simple empirical analysis can estimate the price-level potential of the excess reserves then current. The questions to be answered are: (1) How much money could the banking system have generated with all the reserves it held before the policy actions that reduced excess legal reserves to virtually nothing? (2) What were the chances that this expanded money stock would produce an inflation? (3) Finally, what was the probability that commercial bankers would expand their loan and deposit accounts to this maximum?

The table on the next page includes the monetary, employment, and price-level data of the period to suggest practical answers to the first two questions. Columns (1) and (2) show member-bank deposits and reserves for the dates listed. Column (3) shows required reserves as of those dates. The difference between columns (2) and (3), excess legal reserves, is in column (4).

If the banks had used these excess reserves at the various dates to extend their loans and investments to the limits then current, bank deposits would have increased by the values shown in column (5). Column (6) is the M2 money stock—the sum of currency and demand deposits, plus time deposits in commercial banks—for the dates shown. Therefore, the maximum money stock that could have appeared because of bank-credit expansion is column (7), "maximum money

Deposits and Reserves of Member Banks, Various Money Stocks, Unemployment, and Prices, 1935–1938*

Date	Member bank deposits (1)	Member bank reserves (2)	Member bank required reserves (3)	Member bank excess reserves (2)-(3) (4)	Possible increase in member bank deposits (5)	M2 money stock (6)	Maximum M2 money stock (5)+(6) (7)	Full employment money stock (8)	Inflationary potential of (7) (9)	Unemployment as percent of labor force (10)	Prices, 1929=100 (11)
1935											
Dec. 31	28.9	6.28	3.30	2.98	26.1	40.3	66.4	59.2	+12.2	18.5	80.5
1936											
June 30	31.3	6.17	3.58	2.59	22.6	43.3	65.9	62.4	+ 5.6	16.9	80.9
Dec. 31	32.2	7.33	5.28	2.05	12.5	45.0	57.5	63.5	–9.5	15.6	82.3
1937											
June 30	37.3	7.38	6.50	0.88	4.4	45.2	49.6	61.5	–19.3	14.3	83.8
Dec. 31	31.7	7.71	6.64	1.07	5.0	44.0	49.0	61.6	–20.5	16.6	83.1
1938											
June 30	31.6	8.61	5.85	2.76	14.9	44.1	59.0	64.4	–8.4	19.0	82.3

*Monetary data in $ billions; unemployment data and prices in percentages.

Sources: Philip Cagan, *Determinants and Effects of Changes in the Stock of Money, 1875–1960,* National Bureau of Economic Research (New York: Columbia University Press, 1965), table F-8, p. 350; Board of Governors of the Federal Reserve System, Banking and Monetary Statistics (Washington, D.C., 1943), pp. 396–97; Friedman and Schwartz, *Monetary History of the United States, 1867–1960,* table A-1, pp. 714–15.

stock," the sum of columns (5) and (6).

Column (8), the "full employment money stock," is a constructive estimate of how much common money (M2) the U.S. economy would have required to achieve full employment on the dates shown. It is based on two conceptual adjustments to the existing money stocks. First, a greater quantity of money would have been necessary to transact the increased volume of goods and services that a fully employed labor force would have produced. Second, an additional quantity of money would have been necessary to get the price level back to the value it had in 1929, the last time at which the economy enjoyed substantially full employment.[11] In a market economy suffering from severe unemployment, increases in the money stock simultaneously stimulate both revived output and higher prices. (In technical terms, the aggregate supply function is neither perfectly elastic nor perfectly inelastic.)

Column (9) is the percentage excess (+) or deficiency (–) of the money stock for the date. It is a measure of potential inflation calculated by dividing (8) into (7) and subtracting 1 in order to state the excess (or deficiency) as a percentage. On these terms, column (9) estimates the inflation that the banking system *could* have generated given the institutional constants then present. Columns (10) and (11) are the data for unemployment and prices as conventionally measured by the Bureau of Labor Statistics. For simplicity, the price index value for 1929 is given as 100.

As Column (9) shows, the maximum potential inflation in the system was only 5.6 percent in June 1936, just before the first massive increase in reserve requirements of August 1936. After the increase, the inflationary potential became negative (–9.5 percent) implying that the economy could no longer reach full employment under the conditions then prevailing, no matter how prodigally commercial banks expanded their accounts.

On the basis of well-intentioned ignorance, the first increase in reserve requirements could be forgiven. It undid part of the immense increase in gold monetization that Roosevelt's inexcusable increase in the price of gold had induced. The second round of increases in March and May 1937, however,

turned what had been an ongoing recovery into another cyclical disaster. "Inflationary" potential came down to –20.5 percent, and all the leading indicators of business activity turned negative. By September the recession was unmistakable. Both the Treasury and the Fed undid some small part of their restrictive measures in mid-1938, but a state of healthy economic activity did not appear again until the wartime monetary increases of 1941–1942. So, to answer the first question posed above: No inflation of any size could have occurred between 1937 and 1941. What did appear as a result of Fed-Treasury policies was a sharp *recession* that further undermined confidence in the market system.

The third question—What was the probability that commercial bankers would expand their loan and deposit accounts to this maximum?—cannot be answered with monetary data. To answer this question, the observer must imagine the mindset of a typical banker of the time who has survived the Great Contraction, many unsavory New Deal shenanigans, and now the extraordinary reserve requirement increases.

Cautious Bankers

Bankers, to begin with, are not by occupation very radical. They operate institutions that have only fractional reserves with which to meet liquidity demands. Assume this bank has survived eight years of monetary turmoil, and now finds its legally required reserves doubled in less than a year. Four to six years earlier it had perhaps sought accommodation from its regional Fed Bank, as anxious depositors filled its lobby during one of the banking crises in the early 1930s. To extend his reserves and satisfy his clients, the banker may have taken some of his "eligible paper" to his regional Fed Bank for discount. The Fed Bank loan committee might well have replied in "shaggy dog" terms that his bank's paper "was not eligible enough," and refused the loan application.

This response surely would have conditioned the banker not to rely on the Fed Bank to save him from liquidity shortages. Milton Friedman, who reviewed this episode in minute detail, remarked: "Bitter experience during the years from 1929 to 1933 had taught banks that it was not enough to keep . . . only the minimum amount [of reserves] required by law; legally required reserves could not be drawn on to meet emergency demands without the banks being liable to closure [by order of governmental banking authorities]. . . . Little wonder that the survivors of the holocaust felt it necessary to provide their own protection against unexpected demands. [Bank] deposits in excess of required legal reserves were essentially uncovered [bank] liabilities for which only the *excess* of high-powered money over required reserves provided an effective reserve."[12]

The experience of having survived the banking crises of the times because he had been more conservative in lending operations than his fellows would have added to the banker's conservatism. Now the Federal Reserve Board suddenly *doubles* his reserve obligations before his bank has recovered any significant fraction of its pre-depression income. In addition, the Supreme Court has just upheld abrogation of the gold clauses in government contracts, labor unions are showing increased virulence, and Social Security taxes have appeared. What are his profitable lending prospects at this point? What problem can he next expect from the "lender of last resort," who is supposed to be his protector?

Required reserves are not just numerical artifacts, and paradoxically they fail in practice to protect bank obligations. However, they have very important side effects on banker behavior. Since the horrendous blunders in their implementation during the 1930s, the Federal Reserve has used them less and less for monetary control purposes. Today, the Fed relies almost exclusively on open-market operations to manage the economy's money stock. Even if not used, however, legal reserve requirements should be abolished completely so that the Federal Reserve Board could not blunder again into the monetary catastrophe it fostered in the 1930s. Banks would manage their own reserves, and reserves would once again fulfill their traditional purpose. □

1. This article draws heavily from the outstanding and exhaustive account of the Great Contraction and Great Depression carefully detailed and analyzed by Milton Friedman and Anna J. Schwartz in their monumental *A Monetary History of the United States, 1867–1960* (Princeton, N.J.: National Bureau of Economic Research and Princeton University Press, 1963). I have supplemented their account with some material from my *Monetary Policy in the United States: An Intellectual and Institutional History* (Chicago: University of Chicago Press, 1993).

2. See *Monetary Policy in the United States*, chapters 4 and 5, for an explanation of this episode.

3. The state of Illinois, for example, required no legal reserves of banks chartered by that state until the Monetary Control Act of 1980 made legal reserve requirements mandatory for all banks regardless of the states in which they were chartered. Practically no other country in the world imposes reserve requirements on its commercial banks.

4. It is important to emphasize here that the commercial banking system could not carry out such an expansion deliberately and purposively. Any expansion that banks undertook necessarily would be a result of decisions made by individual banks, and their intent would be to earn profits from successful financial operations. In short, commercial banks could not (and cannot) make monetary policy. Only the central bank can do that.

5. Marriner Eccles, *Beckoning Frontiers* (New York: Alfred Knopf, 1951), p. 287.

6. Ibid.

7. Ibid., pp. 288–89.

8. Friedman and Schwartz, *A Monetary History of the United States*, p. 532. The authors discuss the political and intra-government power factors behind the policy. The scenario they document reveals how important noneconomic causes were and are in the actions of an agency supposed to be devoted completely to the good stewardship of the monetary system and the economy.

9. Benjamin M. Anderson, *Economics and the Public Welfare: A Financial and Economic History of the United States, 1914–1946* (Indianapolis: Liberty Press, 1979 [1949]), p. 405.

10. Ibid., pp. 432–33.

11. These adjustments do not include a possible change in the velocity of money. Cyclical experiences of monetary velocity confirm that it changes only sluggishly and belatedly. For a more detailed analysis of the "full employment money stock," see *Monetary Policy in the United States*, pp. 292–94. *If* the dollar price structure were perfectly flexible downward, "full employment" could result at any level of prices. In the real world of the 1930s, however, prices were no longer flexible downward as they had already gone through the floor. More to the point, government programs had actively worked against money price declines for almost ten years.

12. Milton Friedman, *A Program for Monetary Stability* (New York: Fordham University Press, 1960), p. 46; emphasis added. In their *Monetary History*, Friedman and Schwartz comment similarly on page 348. Every bank panic that occurred in the presence of governmentally mandated reserve requirements bore witness to this paradox: Set up a system of legally required reserves for banks, and the reserves will not be used for their intended function.

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The Great Gold Robbery

by James Bovard

The New Deal established much of the moral framework of contemporary political life. Though some of the programs and policies of that era have been terminated, the moral heritage of the New Deal continues to permeate American government and political thinking.

In 1936 Franklin Roosevelt declared, "I should like to have it said of my first Administration that in it the forces of selfishness and of lust for power met their match. . . . I should like to have it said of my second Administration that in it these forces met their master."[1] No American president has rivaled Roosevelt in his denunciation of what he called "economic royalists." He sought to "master" the "forces of selfishness" by making government master of every person's private financial destiny. Like today, the citizen who wanted to retain control over his own life was selfish, while the bureaucrat who wanted to seize power over the citizen was automatically presumed benevolent.

One of the most controversial New Deal policies was the seizure of citizens' gold.[2] During the Great Depression, several foreign nations repudiated their promises to redeem their currencies for gold. In 1933, when Roosevelt became president, the United States had the largest gold reserves of any nation in the world. He announced on March 8, 1933, a few days after taking office, that the gold standard was safe. But three days later, he issued an executive order forbidding gold payments by banks; Treasury Secretary Henry Morgenthau, Jr., announced on March 11 that "the provision is aimed at those who continue to retain quantities of gold and thereby hinder the Government's plans for a restoration of public confidence."[3] Thus, according to Morgenthau, any limit on government power was bad for public confidence. And whatever confidence people might seek to achieve must be left in abject dependence on politicians' latest salvation scheme.

The ban on bank gold payments created widespread doubts about the Roosevelt administration's intentions. Ogden Mills, who had served as President Herbert Hoover's treasury secretary, observed that "it was not the maintenance of the gold standard that caused the banking panic of 1933 and the outflow of gold. . . . [I]t was the definite and growing fear that the new administration meant to do what they ultimately did—that is, abandon the gold standard."[4] People naturally sought to get rid of their paper currency and to put their savings into something with more secure value—gold.

Gold as Contraband

Fear of devaluation spurred a panic, which Roosevelt invoked to justify seizing people's gold. On April 5, 1933, Roosevelt commanded all citizens to surrender their gold to the

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government. No citizen was permitted to own more than $100 in gold coins, except for rare coins with special value for collectors. Morgenthau announced on the same day that "gold held in private hoards serves no useful purpose under present circumstances."[5] Gold was thus turned into the same type of contraband as Prohibition-banned rum. Roosevelt announced, "Many persons throughout the U.S. have hastened to turn in gold in their possession as an expression of their faith in the Government and as a result of their desire to be helpful in the emergency.

There are others, however, who have waited for the Government to issue a formal order for the return of gold in their possession."[6] To speak of the "return of gold" implied that government was the rightful owner of all the gold in the nation, and thus that no citizen had a right to possess the most respected store of value in history. Roosevelt assured the country: "The order is limited to the period of the emergency." But the order stayed on the books until 1974.

Roosevelt labeled anyone who did not surrender his gold a "hoarder." His executive order defined "hoarding" as "the withdrawal and withholding of gold coin, gold bullion or gold certificates from the recognized and customary channels of trade."[7] Actually, Roosevelt was not concerned with the gold being in the "customary channels of trade"; instead, he wanted government to possess all the gold. And the notion that people were "withholding" their gold merely because they did not rush to the nearest Federal Reserve bank to surrender it was political logic at its best.

Roosevelt, in a later note to his *Public Papers*, justified the order because it "served to prevent the accumulation of private gold hoards in the U.S."[8] Roosevelt used the same "hoarding" rhetoric against anyone who owned gold that Stalin used against Ukrainian peasants who sought to retain part of their wheat harvest to feed their families. But while Stalin sent execution squads to kill peasants who had a few bushels of grain hidden in their hovels, Roosevelt was kinder and gentler, seeking only ten-year prison sentences and $250,000 fines for any citizen who defied his edict and possessed more than five Double Eagle gold coins.

Roosevelt was hailed as a visionary and a savior for his repudiation of the government's gold commitment. Citizens who distrusted the government's currency management or integrity were branded as social enemies, and their gold was seized. And for what? So that the government could betray its promises and capture all the profit itself from the devaluation it planned. Shortly after Roosevelt banned private ownership of gold, he announced a devaluation of 59 percent in the gold value of the dollar. In other words, after Roosevelt seized the citizenry's gold, he proclaimed that the gold would henceforth be of much greater value in dollar terms.

Citizens who had desired to hold gold as a hedge against government inflation policies were completely vindicated. FDR's administration subsequently did everything possible to inflate prices, foolishly confident that a mere change in numerical prices would produce prosperity. Citizens had accepted a paper currency based on the government's pledge to redeem it in gold at $20 per ounce; then, when Roosevelt decided to default on that pledge, he also felt obliged to turn all citizens holding gold into criminals. Roosevelt stated that the ban on private ownership "was the first step also to that complete control of all monetary gold in the United States, which was essential in order to give the Government that element of freedom of action which was necessary as the very basis of its monetary goal and objective."[9] But the primary "freedom" government acquired was the freedom to default on its promises and to manipulate the lives of everyone depending on U.S. dollars in their daily transactions.

Curiously, FDR retained his denigrating tone toward so-called gold-hoarders even after he defaulted on the federal government's gold redemption promise. Even though people who distrusted politicians' promises were vindicated, they were still evil people because they had not obeyed FDR's demand to surrender their gold. In the moral world of the New Deal, justice consisted solely of blind obedience to political commands. FDR had absolutely no sense of embarrassment or

shame after he defaulted on the federal government's gold promises—it was simply political business as usual.

Senator Carter Glass of Virginia, chairman of the Senate Finance Committee, denounced the gold seizure: "It's dishonor. This great government, strong in gold, is breaking its promises to pay gold to widows and orphans to whom it has sold government bonds. . . ."[10]

Free to Inflate

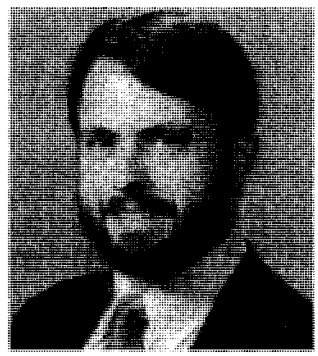
The refusal to convert paper dollars into gold meant that the government was "free" to flood the country with paper money and sabotage the currency's value. The stability of the value of currency is one of the clearest measures of a government's trustworthiness. Before Roosevelt took office, Americans clearly recognized the moral implications of inflation. Vice President Calvin Coolidge had bluntly declared in 1922: "Inflation is repudiation." Inflation is a tax whereby government prints extra money to finance its deficit spending. The value of money is largely determined by the ratio of money to goods; if the quantity of money increases faster than the increase in the amount of goods, the result is an increase in the ratio of money to goods and an increase in prices. Thus, the government's printing presses devalue people's paychecks and effectively allow government to default on the value of its debt.

The threat of inflation was invoked in the early 1940s to justify imposing payroll tax withholding[11] (protecting people from their own paychecks) and in the 1970s to impose price controls over the entire economy. Apparently, politicians who decide to flood the money supply automatically become entitled to increase their coercion of their victims who hold increasingly worthless currency.

Since Roosevelt banned citizens from owning gold in 1933 and forced people to rely on the unbacked promises of politicians for the value of their currency, the dollar has lost about 93 percent of its purchasing power.[12] The collapse in the dollar's purchasing power severely disrupted the ability of scores of millions of Americans to plan their own lives and save for retirement. If someone proposed a law to give government the right to explicitly default by 2 to 3 percent a year on all its debts, the proposal would be widely denounced. Yet, this is what the government has been doing for decades. Though inflation has slowed since 1980, the purchasing power of the dollar has fallen by over 50 percent in subsequent years according to the government's own numbers (which slightly exaggerate the damage to the dollar), making a mockery of people's attempts to calculate and save for the future. A 1997 study by Congress's Joint Committee on Taxation found that because of how capital gains taxes are calculated, many citizens are forced to pay taxes on investment "gains" when in reality they have suffered losses due to the deterioration of purchasing power.[13]

Roosevelt's gold seizure was based on the doctrine that in order for government to save the people, it must be permitted to breach all the promises it made to the people. According to modern conventional wisdom, government has no obligation to do justice or treat any specific individual citizen fairly—instead, government's only duty is to achieve "social justice" or some other abstraction perfectly suited for evasion. □

1. *The Public Papers and Addresses of Franklin Roosevelt, 1936* (New York: Random House, 1938), pp. 232–33.
2. Editor's note: See Richard Timberlake's article "Gold Policy in the 1930s," *The Freeman*, May 1999.
3. Gustav Cassell, *The Downfall of the Gold Standard* (New York: Augustus Kelley, 1966 [1936]), pp. 118–19.
4. Barry J. Eichengreen, *Golden Fetters: The Gold Standard and the Great Depression* (New York: Oxford University Press, 1992), p. 321.
5. Cassell, p. 124.
6. *The Public Papers and Addresses of Franklin D. Roosevelt, The Year of Crisis, 1933* (New York: Random House, 1938), pp. 110–11.
7. Ibid., p. 112.
8. Ibid., p. 114.
9. Ibid., p. 115.
10. Benjamin Anderson, *Economics and the Public Welfare* (Indianapolis: Liberty Fund Press, 1979 [1949]), p. 314.
11. Charlotte Twight, "Evolution of Federal Income Tax Withholding," *Cato Journal*, Winter 1995. See http://www.cato.org/pubs/journal/cj14n3-1.html.
12. For information on the deterioration of the dollar's purchasing power, see the Web site of the U.S. Bureau of Labor Statistics at http://www.bls.gov/cpihome.htm.
13. Bruce Bartlett, "How Inflation Hikes the Capital Gains Bite," *Washington Times*, March 31, 1997.



Balkans Bungling: Why Only Congress Can Declare War

When the U.S. attacked Yugoslavia earlier this year, it inaugurated war against another sovereign state that had not attacked or threatened America or an American ally. The President, and the President alone, made the decision. The constitutional requirement that only Congress shall declare war is obviously a dead letter. Yet the administration's embarrassing bungling in Kosovo illustrates just why the Framers intended that the decision to go to war be vested in the legislature.

Presidential war-making has become a constant. Ronald Reagan invaded Grenada; George Bush attacked Panama. Neither bothered to consult Congress. Bush planned to attack Iraq irrespective of Congress, explaining that "I don't think I need it" when asked if congressional approval was necessary. Why? "Many attorneys," he said, had "so advised me." He apparently didn't bother to read the Constitution himself.

President Clinton ended up only a Carter-brokered agreement away from invading Haiti and has promiscuously attacked other nations or groups within nations—Afghanistan, Bosnia, Iraq, Somalia, Sudan, Yugoslavia—without appropriate legislative authorization. Like his predecessor, Bill Clinton has resisted any attempt to restrict his war powers. In late 1993 the one-time law professor and state attorney general claimed that "the Constitution leaves the President, for good and sufficient reasons, the ultimate decisionmaking authority." He opposed congressional attempts to restrict his plans in both Bosnia and Haiti and more recently pressured Congress not to vote on his plan to launch air strikes on Yugoslavia and place 4,000 peacekeeping soldiers in Kosovo.

Alas, this executive presumption goes back to Richard Nixon, Harry Truman, and, indeed, much further. It was also shared by the various potentates who once ruled Europe. Observed President Abraham Lincoln: "Kings had always been involving and impoverishing their people in wars, pretending generally, if not always, that the good of the people was the object." America's founders intended to take a different path.

Article 1, Sec. 8 (11) states that "Congress shall have the power . . . to declare war." As Lincoln explained: "This, our Convention, understood to be the most oppressive of all Kingly oppressions; and they naturally resolved to so frame the Constitution that no one man should hold the power of bringing this oppression upon us."

Of this there is no doubt. James Madison wrote in 1793 that it is necessary to adhere to the "fundamental doctrine of the Constitution that the power to declare war is fully and exclusively vested in the legislature." Pierce Butler of South Carolina proposed giving the president the power to start war, causing Elbridge Gerry of Massachusetts to exclaim that he "never expected to hear in a

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republic a motion to empower the executive to declare war." The convention rejected Butler's motion.

Why? The founders wanted to make it more difficult to go to war. Thomas Jefferson wrote that "We have already given . . . one effectual check to the dog of war by transferring the power of letting him loose." The nationalist Alexander Hamilton reassured early Americans who feared that the proposed Constitution granted the president powers too similar to those of Britain's king. The president's authority, he said, was "in substance much inferior to it. It would amount to nothing more than the supreme command and direction of the land and naval forces . . . while that of the British King extends to the declaring of war and to the raising and regulating of fleets and armies; all of which by the Constitution would appertain of the legislature."

Virginia's George Mason, who favored "clogging rather than facilitating war," was blunt: the president "is not safely to be entrusted with" the power to make war. This view has certainly been validated by history. President Franklin Delano Roosevelt schemed to get America into war; both George Bush and Bill Clinton conducted dubious propaganda campaigns to build public support for their executive war-making. The pervasive dishonesty of and abuses perpetrated by executive leaders in the United States and elsewhere demonstrate the importance of circumscribing their power.

The requirement of a declaration of war obviously offers no guarantee against ensnaring the nation in costly and unnecessary overseas conflicts. But the need to win legislative assent still limits presidential discretion, while a debate puts the issue before voters and allows them to hold Congress responsible for government policy.

In a complex world filled with a variety of potential threats, there will always be unclear instances, perhaps retaliation against a terrorist group, where a president might claim colorable constitutional authority for unilateral military action. But the number of hard cases are few. There is no doubt that congressional approval is required to launch an aggressive war against Yugoslavia.

Presidents have been able to ignore the Constitution's clear strictures only because successive Congresses have allowed them to do so. The partisan flip-flops have been dazzling: Republicans raged against Truman's actions but defended Nixon; Democrats demanded that Bush go to Congress but encouraged executive war-making by Clinton. Many legislators care less about dead soldiers than dead careers. Avoiding a vote allows them to avoid taking any responsibility on the most serious of issues, war and peace.

It is time for all sides to re-examine their commitment to the Constitution. Presidents take an oath to support the Constitution; that means going to Congress for a declaration of war. Legislators, who make the same pledge, should want to protect not only the Constitution, but also their institutional authority. Yet the issue is far more fundamental than just a political struggle between the executive and legislative. The nation's security is at stake.

As a result of presidents' routinely plunging America into overseas conflicts that are at best tangentially related to U.S. security, hundreds of thousands of soldiers have been killed, hundreds of billions of dollars squandered, numerous civil liberties lost, and a host of government bureaucracies spawned. The issue of war and peace is simply too important to leave to the president.

Perhaps this never has been more obvious than after watching this administration turn a minor tragedy into a monumental crisis in Europe's tar baby, the Balkans. The President and his advisers were surprised when the Albanian Kosovars first rejected the Rambouillet diktat, surprised when bombs did not compel Belgrade's acquiescence, surprised when the Serbs struck back at the Kosovo Liberation Army and the Albanian Kosovars, surprised when refugees overwhelmed neighboring countries, surprised at the capture of U.S. soldiers stationed in Macedonia, and surprised that the conflict continued, week after week. A full and unfettered congressional debate could have prevented the looming debacle. □

Market-Share Sophisms

by Christopher Mayer

There are few more widely held fallacies than equating market share to power over consumers and competitors. That great companies maintain dominant positions in their markets is a red flag for regulators and anti-capitalist moralists, rather than a sign of hard-won success and ingenuity worthy of admiration and study. Weaker competitors use the market share of others as an excuse for their own failures when they turn to the government for assistance. Witness the pursuit of such great companies as Microsoft and Intel.

Market share is a reward for serving consumers better than competitors do. It does not confer special privileges or powers to a producer, which is subject to the same economic laws and will of the consumer as any other company. Market share can be easily lost by poor decisions and inefficiency.

These conditions hold true on a free market. But there are many influences in the real world that are not consistent with a free market. Minimum-wage laws, the plethora of entitlements, union privileges, government grants, state-managed money, regulations, and a host of interventions change the pattern of production in unknowable ways from what might have been in the absence of these things. We can only imagine where some of the capital deployed in the steel industry would have gone had the U.S. government not protected it from foreign competition.

Christopher Mayer is a loan officer at a bank in Maryland and an MBA student at the University of Maryland.

What's the Market?

Another complication is how a given market is defined. Do manufacturers of corn flakes compete only against one another? Or do they also compete against makers of other ready-to-eat cereals? What about hot cereals? What about bacon and eggs? The answers to those questions make a big difference for the market shares of companies. Regulators base their claims on arbitrary assumptions. What counts is how consumers see things.

One final element that's often neglected in the analysis of market-share data: time. Market positions are snapshots. They change. The market leaders of ten years ago are different from today's. They'll be different years from now. In a free market, the continued long-term dominance of a firm reflects its superior ability to satisfy consumers.

Size doesn't determine a firm's degree of control over prices and production. Large and small companies may produce in whatever quantity they wish and attempt to charge whatever price they wish. Ludwig von Mises got to the heart of the matter when he wrote that "What those who blame the economies of big-scale production for the spread of monopoly prices are trying to say is that the higher efficiency of big-scale production makes it difficult or even impossible for small-scale plants to compete effectively."

That inefficient firms are kept from the market is no vice. In fact, this is one of the market's virtues. But that doesn't mean small

companies have no chance. Large firms are not always best at providing value to customers. There may be diseconomies of scale that make it increasingly difficult to compete effectively beyond a certain size.

This is not to deny certain advantages that large dominant firms enjoy. Large firms with deep pockets have the financial wherewithal to respond to opportunities and weather storms better than smaller, less well-capitalized rivals. A bountiful corporate treasury provides a margin for error that smaller firms may not have. This is not a market failure, but the reward for past successes.

Calculation Problem

There is something that limits the size of firms in the free market: the need for economic calculation. The application of the calculation problem to private firms, an extension of Mises's refutation of socialism, was an important insight of Murray Rothbard in *Man, Economy and State*. Ronald Coase's analysis of the firm concluded that the free market would establish a size that tended to optimize transaction costs. (See Max More, "Small is Awesome," in the February 1999 issue of *The Freeman*.) But the problem of economic calculation is more fundamental.

While the economist can say little about the optimal size of a specific firm, he can say the market will tend to establish the best possible arrangement thanks to the calculation that market prices make possible. Imagine a firm that grew so big that it swallowed up the external markets for its inputs. In the absence of market prices for those inputs, the firm could not engage in economic calculation and thus could not know if it was deploying its capital in the most efficient manner. As Rothbard wrote, "When any of these external markets [for inputs] disappears, because all are absorbed in the province of a single firm, calculability disappears, there is no way for the firm rationally to allocate factors to that specific area. The more these limits are encroached upon, the greater and greater will be the sphere of irrationality, and the more difficult it will be to avoid losses"(p. 585).

The upshot is we can let the free market take its course. Let us not worry about the alleged power of dominant firms and instead focus on creating an environment in which the free market is free to function. □

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The Permanent War

Some years ago Stanley McGill, 93, mailed a check for $7,000 to the Internal Revenue Service. When he died, his daughter discovered that Mr. McGill had made a mistake. The money should not have been sent. Marian Brockamp explained to the IRS that her father was senile and asked for a refund.

The IRS said no. Requests for refunds must be made within three years.

Mrs. Brockamp took the case to court—all the way to the U.S. Supreme Court.

She lost.

In the grand scheme of things, that was a small event. The Internal Revenue Service has done far worse in its time. It has harassed and tormented people. It has seized property and frozen bank accounts. It has ruined credit records. It has driven people to suicide. Nevertheless, the Stanley McGill story sums up a great deal about the IRS and the American tax system. The IRS concedes that the $7,000 should not have been sent. Mr. McGill made a mistake. His daughter informed the IRS as soon as she discovered the error. No one questions the facts. But the IRS won't surrender the money. And the U.S. Supreme Court said the IRS doesn't have to.

Speaking for a unanimous court, Justice Stephen G. Breyer wrote:

> The nature and potential magnitude of the administrative problem suggest that Congress decided to pay the price of occasional unfairness in individual cases . . . to maintain a more workable tax enforcement system.

Congress decided to pay the price? How noble. Except that in this case it appears Congress has forced Mr. McGill's heirs to pay the price. Why? Because the rights of the individual must not be permitted to create administrative problems for the IRS or to interfere with the maintenance of a workable tax enforcement system.

Yes, that incident occurred in the United States of America.

Imagine if the tables were turned and after Mr. McGill's death the IRS discovered that he "owed" the government $7,000. Imagine further that Mrs. Brockamp politely replied that the IRS was too late in its request. What would have happened? The IRS would have seized the money and perhaps have made hell out of Mrs. Brockamp's life. And the Supreme Court would have sided with the IRS.

The IRS—tax historian Charles Adams equates it with "a miniature Soviet state"—is something we have unfortunately grown accustomed to. It is time to put the income tax, and the Sixteenth Amendment that permits it, into historical context and show its implications for morality, the relationship between citizen and state, and the quest for prosperity. The verdict on the tax is not favorable: ratification of the amendment and passage of the tax was a major turning point in

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the transmogrification of America from republic to democratic despotism. More than anything else, it converted Americans from citizens to subjects.

In carrying out its mission, the IRS is only serving a higher power: the legislators who need a never-ending flow of cash to the federal treasury. They wrote the laws that loosed the IRS on the American people. They can repeal them. Why don't they? They want the money, pure and simple.

As bad as any taxation is, the income tax is worse. It is aggravated theft, robbery with malice aforethought. Theoretically, all forms of taxation could be draconian. But in practice, the income tax has been more abusive of the people's rights than other taxes. It lends itself more readily to draconian enforcement. That justifies singling it out for special condemnation. But merely replacing the income tax with another tax designed to raise more than a trillion dollars would be a shallow victory.

The moment the principle of income taxation is granted, the ground is prepared for myriad abuses of the people. If the government is permitted to tax incomes, it will demand reams of personal information about each citizen's financial endeavors. It will compel people to report on the peaceful financial activities of others. But more than that, it must have the muscle to check that information, to spy on people, to conduct inquisitions, and to punish—hard. Why? Because there is nothing more natural than people's trying to keep what they worked to acquire. Regardless of their explicit political philosophy, most people are implicit advocates of property rights. They don't like being dispossessed of their belongings. Even thieves don't like to be robbed.

Man versus State

Income taxation inaugurates a permanent war between the people, who want to keep what they earn, and the government, which wants as much of it as it can get. The government tries to make the war less obvious by deadening the pain when possible. The withholding tax makes it unnecessary for most Americans to write checks to the IRS; indeed, they eagerly await their refunds. But the war is part of the American psyche nonetheless. All Americans sense that an awesome power lurks, ready to grab an increasing portion of anything they earn. That adversary relationship has far-reaching consequences for a society founded on the principles of the Declaration of Independence, according to which government was the rights-guarding servant and the people the master. But the income tax turns that relationship on its head.

Americans lived without the fears and burdens imposed by the income tax for over 100 years (except in the Civil War era). They built a decent and prosperous society.

The income tax has been a key factor in the growth of government. When enacted, only the few richest people in America paid the tax. It became a tax for the masses during World War II, under that reputed champion of the masses, Franklin Delano Roosevelt. Today, it accounts for over 43 percent of the revenue raised. Payroll taxes for Social Security and Medicare account for about 35 percent. Americans' incomes have provided a rich vein for the government to mine.

Thus we can see that the income tax has:

- Given the government unprecedented access to the American people's wealth;
- Provided the rationale for the government to intrude into our personal affairs;
- Reversed the traditional rule-of-law relationship between government and those suspected of lawbreaking;
- Confused "cheating" the government in order to keep one's own property with cheating one's fellow citizens;
- Bewildered the American people with constantly changing technical rules that no one can possibly comply with perfectly; and
- Permitted lawmakers to influence our conduct through selective tax deductions and exemptions.

All this has come from the principle that government may tax incomes. That is why repealing the tax, along with the Sixteenth Amendment, is an essential blow in the struggle against power and for liberty. □

THE FREEMAN
Ideas On Liberty

The Market and Political Freedom

by John Marangos

The history of civilized societies is a timeless effort to enhance freedom. Freedom must be viewed as a whole, and anything that reduces it in one aspect of life is likely to reduce it in others as well.

Free people make decisions through their independent minds and have the courage to pursue their own convictions through exchange relations in the market. Thus a free person rejects attempts by others to exercise power over his own choices. He treats other people as equals, thus limiting interaction to voluntary transactions. The market is the expression of economic freedom. In the absence of any form of discretionary power, it is an institutional process in which individuals interact with each other in pursuit of their economic objectives.

The economic and political processes are linked: one generates and sustains the other. Thus a society's economic process would have ultimate consequences for the kind of political process it ends up with. This is because the state, as a monopoly of legitimate force, is in the position to impose restrictions on the individual's action. A free person realizes the benefits derived from free-market relations, that is, the absence of discretionary power, and seeks a compatible political process. Political freedom means freedom from coercion in the sense of arbitrary power—freedom even from the coercion exercised by the government.

In a historical context, politically free societies and the market have a common origin. In *Capitalism and Freedom*, Milton Friedman states: "I know no example in time or place of a society that has been marked by a large measure of political freedom and that has not used something comparable to a free market to organize the bulk of economic activity."[1] The rise of the market is associated with the rise of political freedom and the gradual removal of governmental and religious constraints on the individual.

However, it appears that while a market system is necessary for political freedom, it is not sufficient.[2] R.E. Lane agrees that "historically, a free market has seemed to be a condition of political freedom, as exemplified in the bill of rights and free elections, but it has not been a sufficient condition."[3]

I am skeptical about this argument. I believe it was developed because in the 1960s and 1970s the political situation of the world was bleak with respect to political freedom. Suppression of political freedom was widespread in the form of authoritarian political structures, especially military dictatorships, where tenure was based on power instead of reason and irresponsible political power functioned outside the discipline of law. The argument raised by Friedman and Lane is an

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unfortunate simplification that does not correspond to reality anymore; in fact, while in the short run within a market system political freedom may be restricted, in the long run authoritarian political processes cannot survive alongside markets. This is demonstrated by the fall of military dictatorships in the end of the 1970s and in the 1980s and the collapse of authoritarian socialism that stimulated the re-establishment of political freedom.

In essence, people enjoying the benefits of the market process will question and undermine the power of authoritarian governments. Individuals who experience the benefits of freedom through market relations are likely to require freedom in the political process. The market and political freedom are internally linked: one generates and sustains the other.

Markets and Authoritarianism

The point is not obvious. Some countries have developed political systems featuring a hierarchically structured bureaucratic organization that gives privileges to an elite class. While the market is the main process for decision-making, political freedom is restricted in order to serve the purposes of this elite minority. In these instances the political process results in a loss of personal control and encourages dependency. It rewards conformity, obedience, and affiliation instead of innovation, enterprise, and autonomy. Individuals feel powerless and helpless. Such people perform less efficiently in a market system than do self-interested, competitive individuals. In addition, political authorities distort the market by allocating resources by coercion. They control a large part of the resources, and the influence of their decisions on the remainder is substantial; that results in effective control of the entire spectrum of economic decisions.[4]

Market-Produced Opposition

But the market plays an important role in providing the mechanisms of opposition to the suppression of political freedom. The market should be evaluated not only as a process for achieving the optimal allocation of resources but also as one of learning and personality development. In the market, individuals learn to be free and independent and to follow their own convictions. Freedom is a skill that is generated and sustained by the market.[5] People preserve these values throughout their adult life once they have been developed in their formative years.[6] If the market encourages self-direction, how can that behavior be restricted only to economic relations and not extended to the political process in the form of political freedom?

Despite differences among markets, they have essential features that tend to promote the acquisition of qualities important for personality development. Lane identified the qualities necessary for maximizing the development of personality: [7]

Cognitive complexity. This involves the capacity to understand abstractions, to hold preferences, to be able to judge others and oneself, to change concepts to fit reality rather than fitting reality to fixed conceptions, and finally to hold several ideas in order to arrive at original solutions.

Autonomy. This is the desire and ability to remain independent, which encourages free initiative and free expression in all areas of life. Through this quality an individual is at liberty to conform to tradition and authority—or not. Each authority is treated as a source of information rather than of command.

Sociocentricity. The thoughts and claims of others are understood and given recognition. Sociocentricity comprises socialization, experience, understanding, and reasoning. Individuals learn the rules of the game and conform to them. It is a guide to social reality and a necessary ingredient in good interpersonal relations.

Attitudes towards self. A combination of self-knowledge, self-acceptance, and self-respect are necessary for the establishment of an identity. With these qualities people avoid internal conflict and uncertainty about values.

Identification with moral values. This is necessary to secure moral reasoning and moral behavior without taking refuge in tradition and authority.

Lane aimed to identify the effects of markets and politics on personality development.[8]

Unfortunately, in his analysis the influence is one way: markets and politics influence development of personality, but individuals are unable to influence markets and politics.

But contrary to Lane, social processes are reflexive. Individuals in the market acquire qualities for personality development that will influence the political system. A market participant will require a politics based on freedom.

In the market people develop through trial and error the skills, qualities, and behavior necessary to participate effectively. They need to think for themselves. They slowly reject intellectual dependence on others. They dismiss dependency on family, village, community, ethic group, or social class. They need to make difficult complex decisions with respect to education and careers. As the market becomes increasingly complicated, with more sophisticated products, proliferating brands, and aggressive advertising, people need to search, examine, and analyze what is offered. Thus they are faced with difficult, complex choices that require complex cognition.

A sense of autonomy is achieved through the market, since the participants learn that the environment around them is responsive to their actions. Individuals work, get paid, and buy goods through the market process; this enables them to control their own destinies. Within the market individuals can afford to be self-dependent, since they have alternatives. They can follow their own convictions. Rewards are individual instead of collective. So the market participant learns that effort will be rewarded and wrong decisions penalized; he will need to bear the burden of his mistakes, but also enjoy the outcome of correct decisions. The market thus contributes to the desire for, value of, and belief in one's own competence to control one's own destiny and to develop along a unique path. It instills an appreciation for the same in others.

Economic transactions bring people together under the rule that any exchange must be voluntary and thus mutually beneficial. Participants thus need to understand one another's point of view. Agreement will only be reached when market participants realize they need to work together, communicate, bargain, and compromise. In this way, individuals become sociocentric, since success in the market requires good interpersonal skills.

Participation in the market process encourages self-knowledge, self-acceptance, and self-respect. Through successes and failures, participants realize their potentialities. They learn through their mistakes rather than through tutelage, and they succeed through their own analytical and planning strategies. The market increases awareness of the participants' potential in solving problems and realizing goals. The sense of accomplishment contributes to one's satisfaction with life.

Lastly, the market encourages fair dealing since exchange is voluntary. Capitalism contributes to identification with moral values.

Transference of Virtue

Behavior learned in one aspect of life may be applied in others. The qualities gained through the market process can be used in politics, for example, because those qualities become part of the personality. The political structure does not exist in a vacuum. Moreover, market participants equipped with the five qualities discussed will require a political process that protects their personality, that is, political freedom.

Thus economic freedom and political freedom are internally linked. One generates and sustains the other. While in the short run political freedom may be restricted in a market-oriented society, individuals enjoying the fruits of economic freedom will eventually question and undermine an authoritarian political process. Because the value of self-control is taught, exercised, and mobilized by the market, in the long run, authoritarianism cannot exist alongside free markets. □

1. Milton Friedman, *Capitalism and Freedom* (Chicago: University of Chicago Press, 1962), p. 9.
2. Ibid., p. 10.
3. R.E. Lane, "The Dialectics of Freedom in a Market Society," The Edmond James Lecture, April 16, 1979, University of Illinois, Urbana-Champaign.
4. F.A. Hayek, *The Road to Serfdom* (London: Ark Edition, 1986 [1944]), p. 45.
5. K.R. Minogue, "Freedom as a Skill," in A.P. Griffiths, ed., *Of Liberty* (Cambridge: Cambridge University Press, 1983), p. 21.
6. R. Inglehart, *The Silent Revolution* (Princeton: Princeton University Press, 1977).
7. R.E. Lane, "Markets and Politics: The Human Product," *British Journal of Political Science*, 1981, p. 5.
8. Ibid., p. 7.

THE FREEMAN
Ideas On Liberty

Against the Tide: The Life of Francis W. Hirst

by Mark Brady

Sadly, it is only an exceptionally well-informed reader who will recognize the name of Francis W. Hirst, whose stalwart advocacy of personal freedom, free trade, and peace during the first half of the twentieth century, and especially during the First World War and its aftermath, surely earns him an honored place in the pantheon of individual liberty.

Francis Wrigley Hirst ("Frank" to his family) was born on June 10, 1873, at Dalton Lodge, two miles east of Huddersfield in the West Riding of Yorkshire. He was the third of five children (two sons, three daughters) of a prosperous wool-stapler, Alfred Hirst, who went blind at 27, and his wife, Mary Wrigley.

On both sides of his family Frank Hirst had nonconformist ancestors who had worked and voted for the Great Reform Bill and the repeal of the Corn Laws. His maternal grandfather, Joseph Woodhead of Huddersfield, had supported Richard Cobden and John Bright in their opposition to the Crimean War and had voted for Cobden at Huddersfield in 1857. His paternal grandfather, Charles Hirst, had enjoined his son, Alfred, "always be against war; nine times out of ten you will be right, and the other time it will not matter."

As a young boy in the early 1880s, Frank Hirst met a few of the old handloom weavers who spoke of the hungry years during and after the French wars, when work failed and the taxed grain rose to impossible prices. Thus during his childhood, which seems to have been a happy one, he imbibed the great Liberal tradition of peace, retrenchment, and reform, causes that he held dear throughout his long life.

In 1891 Hirst won an open scholarship in classics to Wadham College, Oxford, where he had a distinguished university career. He was elected successively librarian and president of the Oxford Union, the renowned debating society, where he was a contemporary of Hilaire Belloc and F. E. Smith, later Earl of Birkenhead. In 1899 he won the Cobden Prize and was called to the bar by the Inner Temple. Although for some years he had entertained hopes of making an income as an attorney, these hopes faded away as few clients sought him out and he found he had no natural talent for court work. So Hirst practically abandoned the law for journalism and book writing.

In 1903 he married Helena Cobden, a great-niece of Cobden, at Heyshott and eventually they were to live in Cobden's old home, Dunford House, in Sussex, where he was chairman of the Dunford House Association. They had no children.

Liberal Author

As early as 1897 Hirst had co-edited and contributed to *Essays in Liberalism* by "Six Oxford Men," who included Belloc and J. L. Hammond, later to become famous as one half

Mark Brady, who was born and grew up in England but now lives in America, has been a libertarian for almost 30 years.

of the Hammonds, the labor historians. Hirst's own contribution was a stalwart defense of "Liberalism and Wealth." The book was dedicated to John Morley, the writer and Liberal statesman, with whom Hirst was to have a close relationship until Morley's death in 1923.

On February 14, 1900, with the Boer War under way, Hirst was a founding member of the League of Liberals against Aggression and Militarism. The following month Hirst and Hammond decided to collaborate on a volume of essays expressly devoted, as the eventual title said, to *Liberalism and the Empire*. It proudly appealed to the memory of "the older school of English liberals."

One unspoken target was George Bernard Shaw's celebrated pamphlet of May 1900, *Fabianism and the Empire*, which argued for what historians now call Fabian social imperialism. Hirst's essay on "Imperialism and Finance" showed how militarism and excessive expenditure on armaments both feed and are fed by calculated panics and "inevitable war," which also prevent reforms at home. It should be added that Hirst was never a pacifist. He wrote in his memoirs, *In The Golden Days* (1947), that "a clearly aggressive attack on one nation by another—e.g. that of Soviet Russia on Finland or of Germany on Holland—should be resisted until resistance is hopeless. But in nearly all the wars recorded in history it may be said that there were two sides to the quarrel; and nearly all wars have been initiated by rulers who have forced their peoples to fight, relying upon conscription or the pugnacity of the human species, especially when patriotism and the cry of 'my country right or wrong' can be evoked."

His work for *Essays in Liberalism* and his contribution to a popular life of W. E. Gladstone, the Liberal prime minister, brought him to the attention of Morley, who engaged him to help go through Gladstone's papers and later read the proofs of Morley's monumental *Life of Gladstone*, which finally appeared in November 1903. Hirst wrote *Adam Smith* (1904) for Morley's *English Men of Letters* series; he edited a useful anthology of speeches and writings under the title *Free Trade and Other Fundamental Doctrines of the Manchester School*; and he also translated and edited Josef Redlich's *Local Government in England*, a much-acclaimed work. It was also at this time that he threw himself into the fight for free trade and helped revive the Cobden Club, which published *Fact versus Fiction* (1904), a reply to Joseph Chamberlain's tariff reform speeches, and *The Burden of Armaments* (1905), a plea for the reduction of military and naval expenditures, both of which Hirst helped write. He was therefore overjoyed when in 1906 the Liberal Party swept into power under the banner of free trade.

In 1906, Hirst's *The Arbiter in Council* was published anonymously, financed by J. P. Thomasson, a Cobdenite from Bolton. Written as a series of imaginary conversations between a former associate of Cobden and others, Hirst sought to analyze the follies of war principally on economic grounds. In *Monopolies, Trusts and Kartells* (1906) he explored another timely question in some depth. Subsequently he wrote several books on money, investment, public finance, international trade, the law of the sea, and a book on the stock exchange for the Home University Library in 1911.

Years at *The Economist*

In 1907 Hirst was appointed editor of *The Economist* and proceeded to make important innovations in the publication and to extend its appeal beyond the business community. He wrote his own policy editorials and recruited a competent staff to assist him. He also printed contributions from such distinguished foreign scholars as Josef Redlich and Luigi Einaudi. Hirst remained editor until he was forced to resign in 1916 owing to his opposition to World War I. Like his friend John Morley, who resigned from the cabinet in protest at the decision to declare war in August 1914, he viewed the Great War as a tragedy from the start.

His valedictory leading article said: "Since the war began, the function of an editor who believes that truth and patriotism ought to be reconciled has been difficult and even hazardous." To his great credit he never displayed the bitterness that one might expect of someone who had been forced to give up such a prestigious position.

Hirst's *The Political Economy of War* was published in 1915. He was a zealous supporter of (the Conservative) Lord Lansdowne's Letter in 1917, which rejected a policy of unconditional surrender and sought a negotiated peace. He also helped Earl Loreburn, the former Liberal Lord Chancellor, on his book *How the War Came* (1919). He was opposed to aspects of the punitive anti-German peace treaty that came out of Versailles.

From 1916 until 1921 he edited *Common Sense*, a weekly journal of commerce that later merged with the Manchester *Guardian Commercial*, and thereafter devoted his life to writing and travel.

Collectivism on the Rise

Hirst had come of age at a time when the New Liberalism that advocated an expansive role for the State was in the ascendant, although his own sympathies lay with an older, more individualist liberalism. And he attained middle age just as the Great War began. Thereafter he observed and wrote about Britain and the world in an era when collectivist ideologies of various stripes dominated intellectual debate, and increasingly interventionist and sometimes tyrannical governments disrupted and on occasion destroyed the market order and civil society.

A notable moment in Hirst's life was his speech before the Lords of Appeal on behalf of Arthur Zadig, a naturalized British citizen of German parents, who had been interned under the Defence of the Realm Act in 1915. Although Zadig lost, Lord Shaw of Dunfermline gave a dissenting judgment that recognized Hirst's arguments grounded in English legal history, and Zadig was released two weeks later. Nearly 20 years later Hirst reprinted Lord Shaw's judgment in full in his account of *The Consequences of the War to Great Britain* (1934). He also traced the history of English liberty in one of his best books, *Liberty and Tyranny* (1935), which he wrote as "a reasoned defence of political and civil liberty." Describing the dark age for individual liberty worldwide that had been inaugurated by the Great War, he wrote: "Two centuries of emancipation have been followed by two decades of reaction." That same year also saw the publication of his *Economic Freedom and Private Property*, a defense of economic liberty.

After the war Hirst continued to write on behalf of the cause of free trade. His *From Adam Smith to Philip Snowden: A History of Free Trade* (1925) was a short political history of free trade in Britain. In *Safeguarding and Protection*, first published in 1926 as a Cobden Club pamphlet and expanded into a book the following year, he explained how the Conservative government, despite Prime Minister Stanley Baldwin's pledge against protection, had extended customs duties under the guise of "safeguarding" (a euphemism for protectionism). This had reassured voters and enabled the Tories to exploit fears of Bolshevism and defeat the pro-free trade Labour and Liberals in the 1924 general election. Hirst criticized the "American customs union," contrasted the free-trade Democrats with the protectionist Republicans, and explained how high American tariffs made it difficult for European nations to pay off their war debts to the United States. He also described how the "tariff walls of Europe" prevented economic recovery.

Hirst also wrote *Life and Letters of Thomas Jefferson* (1926), *Early Life and Letters of John Morley* (1927), and the introduction to Morley's *Memorandum on Resignation, August 1914* (1928), which Morley had written immediately after his resignation from the cabinet. In his entry on Morley in the *Dictionary of National Biography*, Hirst wrote that Morley's "loyalty indeed was to the faith rather than to the party," a statement that applied as much to Hirst himself. (Hirst stood unsuccessfully as a Liberal candidate in the general elections of 1910 and 1929, but subsequently moved away from the official leadership of the party, even supporting the Munich agreement.)

Pure Individualism

During the Second World War, Hirst was involved in the foundation of Sir Ernest Benn's Society of Individualists in 1942 and wrote some pamphlets for it. But he found

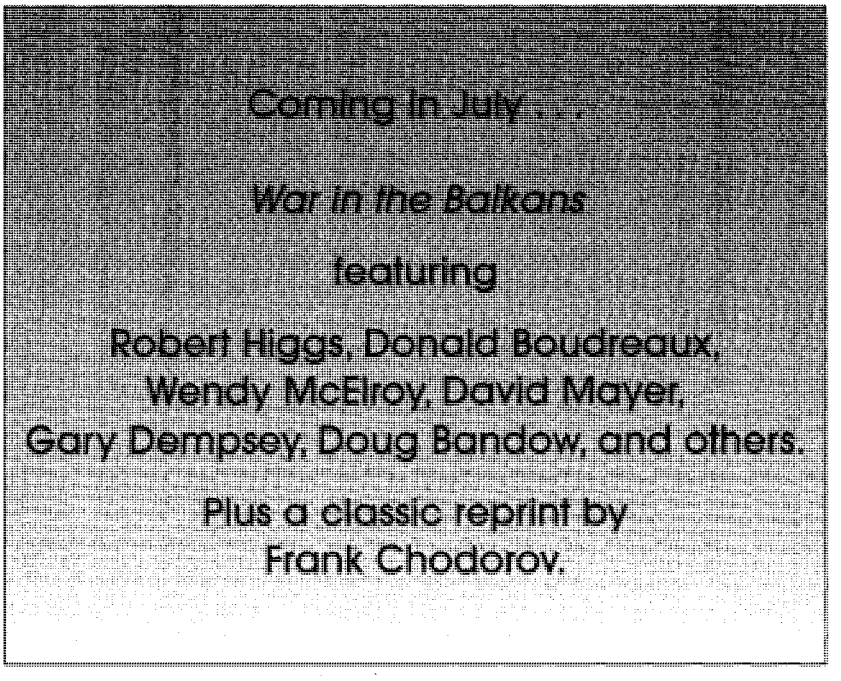
this body more conservative than he had supposed and withdrew his support. In *Free Markets or Monopoly* (1941, revised 1944) he wrote: "When I was an Oxford undergraduate, I met pure individualism in the person of Auberon Herbert, and in later life I have become acquainted with disciples of Karl Marx. I call myself an Individualist, not because I object to State activity, either central or local—such as existed in England before 1914—but because I hold that the State exists for the individual citizens who compose it and ought to control it." He also wrote: "Private Property, Free Competition, the right to make profits, the right to save and to employ your savings (the reward of skill or thrift) as you like are all the rights of a free citizen in a free State. They are the precious inheritance of Englishmen." It greatly pleased him that the Cobden Club was on the Gestapo's infamous Black List of people and organizations to be suppressed were the Nazis to conquer Great Britain.

Hirst denounced the welfare state as the "Beveridge hoax," after the Liberal Sir William Beveridge, author of the report that bore his name and was accepted by the Labour, Liberal, and Conservative parties as the basis for the postwar welfare state. He also disapproved of redistributive taxation and was critical of Keynesian economics. Regarding Marxism, he wrote: "Those who favour class war, while denouncing capitalist war, cannot be counted among the forces favourable to peace."

A volume of Hirst's memoirs, going only to 1906, was published in 1947 and he died at Singleton in Sussex on February 22, 1953, after an attack of influenza.

Truth described him as "one of the greatest libertarians of all time" for his work as an apostle of civil liberty and personal freedom. A book of reminiscences by his family and friends appeared in 1958, in which his lifelong friend and brother-in-law, J. E. Allen, wrote that he had a "genius for friendship" and the historian G. P. Gooch declared, "I have never known a man whose character and convictions underwent less change with advancing years."

Hirst was a prolific writer, skillful biographer, and scholarly exponent of basic principles, who devoted his life to the cause of individual liberty when at times it must have seemed that collectivism had triumphed. It is therefore appropriate that we salute Francis W. Hirst as a valiant defender of the Cobdenite tradition of peace and free trade. □



Economics



Private Property and Opportunity Costs

In three previous columns I discussed opportunity cost and the importance of this concept to understanding economics. We have considered the advantage the market has over government at incorporating opportunity costs into the calculus of decision-makers. Markets promote the general interest by revealing costs while governments commonly favor special interest by concealing those costs. In this column I shall extend the discussion of opportunity costs by introducing the critical role of private property. Private property lies at the foundation of market economies because without private property, and the exchange it fosters, people would be unable to consider the full costs of their decisions.

Too Costly to Drive

Assume you win a Rolls Royce Silver Shadow, with insurance, maintenance, gas, and taxes paid. While this isn't quite as nice as winning the state lottery, the going price for a Silver Shadow is around $250,000. That's the good news. The bad news is that you're probably not wealthy enough to drive this car. Your first reaction is likely: What do you mean I can't afford to drive it? Everything is paid for by someone else.

True, but I still predict that you will find the car too costly to drive. Regardless of how you got the Rolls Royce, the cost of driving it is the price someone else is willing to pay for it. And because the car is your private property, you can't ignore that cost. As the owner you can sell it at a price that reflects the highest value someone else places on it. So you will continue driving your Rolls only if you value it by at least as much as, or more than, what you could buy with the approximately $250,000 that some Rolls Royce aficionado is willing to pay you for it. Most likely you will sell the Rolls, buy a perfectly nice and serviceable car for $20,000, and have $230,000 left over to save or spend on other things.

This story is fanciful, or course, since you are not likely to win a Rolls Royce. But it illustrates a real and important point—private property prompts people to consider the opportunity cost (the value forgone) of their decisions. Because of private property, this consideration is the hallmark of market action and explains the market cooperation that directs resources and products into the hands of those who value them most.

Cooperation Between Bird Watchers and Hot Rodders

Members of the Audubon Society are interested in protecting fragile habitat for birds and other animals. It is easy to predict how it would come down on a choice between protecting wildlife habitat and increasing the availability of gasoline for high-powered cars, or any other cars for that matter. For example,

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the Audubon Society strongly opposes offshore drilling for oil. Oil companies promise to, and in fact do, take extraordinary precautions to prevent oil spills, but the Audubon Society is not convinced. Regardless of precautions, its position is: No offshore drilling—*none!*

How can hot rodders possibly communicate their desire for cheaper gas to the Audubon Society so as to convince it to accommodate them by risking wildlife habitat? In fact, they have succeeded at doing just that. Hot rodders, along with all other gasoline consumers, have convinced the Audubon Society that the value they place on gas is an opportunity cost of protecting habitat that the Society shouldn't ignore. They have done so through market communication based on private property.

The Audubon Society owns a wilderness area in Louisiana known as the Rainey Preserve. It is an ideal habitat for birds and other wildlife, but it also contains commercial quantities of petroleum and natural gas that oil companies are eager to recover. One might conclude that since the Audubon Society owns the land and can easily prevent oil companies from drilling on it, they would do so. Wrong! The Audubon Society allows oil companies to drill there.

Of course, it requires the companies to take strong precautions against oil leaks, but not as strong as it claims to be necessary with offshore drilling. Why the difference? Because the Audubon Society owns the Rainey Preserve, the money others are willing to pay for the oil represents an opportunity that would be sacrificed if it refused to allow drilling. But the Society doesn't face an opportunity cost on offshore sites because it doesn't own them. It thus has no motivation to take the interest of others in offshore oil into consideration.

Private property not only motivates the Audubon Society to cooperate with hot rodders, it also motivates hot rodders to cooperate with the Audubon Society. Their purchase of gas allows the Audubon Society to obtain and protect wildlife habitat that it believes is more valuable than what it sacrifices in the Rainey Preserve because of oil drilling. Members of the Audubon Society may despise hot rodders and hot rodders may laugh at bird watchers, but because of private property, each takes the concerns (and opportunity costs) of the other into consideration and acts to promote the other's interests.

The Opportunity Cost of Prisoners of War

European wars during the Middle Ages were often rather peaceful affairs, with prisoners typically well treated. It was not uncommon for opposing armies to count the number of soldiers on each side, before the smaller army surrendered. Such nonviolent "combat" occurred because at that time soldiers had a property right in the prisoners they captured. That legal right included the power to sell prisoners back to their families, creating an opportunity cost for the victors if they killed their prisoners. Private organizations, some of them religious orders, began specializing as middlemen between those who had prisoners to sell and those who wanted to purchase them.

Unfortunately for prisoners of war, when long-range weapons became available and hand-to-hand combat became uncommon, it was less likely that individual soldiers would capture prisoners. Wars then became more brutal, not only because the technology of slaughter improved, but also because the ownership of prisoners shifted to the state. Because opportunity costs to individuals diminish when property belongs to the state, it became far more common to kill or mutilate prisoners. Human beings obviously should not be treated as private property. But because of the phenomenon of opportunity cost, captured soldiers are far better off as "private property" than "public property."

Private property is essential to the cooperation that emerges from market interaction, because it ensures that people consider the opportunity cost of their actions. It is both sad and ironic that so many people blame private property for problems that exist because of the lack of private property. This will be the topic of my next column. □

THE FREEMAN
Ideas On Liberty

Educational Savior?

by Daniel Hager

George S. Counts is not a widely recognized figure in twentieth-century American education, but he was extremely influential. Twenty-five years after his death, the damage caused by this one-time president of the American Federation of Teachers lives on.

The first step in counteracting his effects is to challenge the premise on which he operated and which remains entrenched in public thinking—that governments should be involved in elementary and secondary schooling.

Counts carried the premise beyond simple involvement. Tax-funded teachers, he maintained, must enlarge their task past mere classroom instruction and become primary forces in fundamentally restructuring the nation socially and economically. From the eminence of Columbia University's Teachers College, where he was a faculty member from 1927 to 1955, he was in demand as a speaker to professional educators, and in 1932 he delivered three speeches that he combined into a book titled *Dare the School Build a New Social Order?* Although he muted the radicalism of his thesis by phrasing it interrogatively, he clearly answered the question in the affirmative. Powerfully organized teachers using the medium of the classroom should steer the young away from the bankrupt American individualism of the past toward a future in which all would work for the common good. Strong social and economic planning, according to his vision, would deliver bounty and the good life for all.

In Counts's view, the masses were helpless victims of twentieth-century industrialism. Their rescue would have to be effected by persons anointed to that noble calling, messianocrats who knew better than the people themselves what the people needed. Teachers should become part of the self-appointed elites that must carry out that mission.

Uncommonly Common

The ironies endemic to messianocracy abounded in Counts's life. For instance, he fancied himself a champion of the common man but lived uncommonly well. He purchased a Pennsylvania farm to which he repaired often from his New York City home. In 1931, when the unemployment rate was 15.9 percent, he had a salary of $15,000, the equivalent of a six-figure income today. During the same period he was referring to "the most terrible form of human madness—the struggle for private gain."[1]

Counts believed that because "the urge for private gain tends to debase everything that it touches,"[2] capitalism had to go. "With its deification of the principle of selfishness, its exaltation of the profit motive, its reliance upon the forces of competition, and its placing of property above human rights, it will either have to be displaced altogether or changed so radically in form and spirit that its identity will be completely lost."[3]

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He grew up on a northeastern Kansas farm in the waning days of the agrarian order, which fostered self-reliance. But industrialization had raised "the most profound issue" of the day—"the issue of the control of the machine. In whose interests and for what purposes are the vast material riches, the unrivaled industrial equipment, and the science and technology of the nation to be used? . . . [A]ll of these resources must be dedicated to the promotion of the welfare of the great masses of the people."[4] He stated, "If property rights are to be diffused in industrial society, natural resources and all important forms of capital will have to be collectively owned."[5] He concluded that "the growth of science and technology has carried us into a new age where ignorance must be replaced by knowledge, competition by cooperation, trust in providence by careful planning, and private capitalism by some form of socialized economy."[6]

Counts was enamored of the Bolshevik experiment then under way in the Soviet Union and in 1929 made a 6,000-mile automobile journey through the nation. In an irony that apparently escaped him, he did not secure a vehicle in that collectivized economy, where automobiles were scarce and ownership tightly controlled by the government. Instead, he bought a new Ford, the product of the capitalist system he scorned, and paid only $661.42 for it, delivered in Leningrad, including $23.57 in spare parts.

He traveled through the Soviet Union like a wide-eyed farm boy just arrived in the big city. Although he acknowledged the stifling inefficiency of the bureaucracies he encountered, he stated that "as an intellectual achievement the revolution has been an astounding success."[7] The vast 1928 Five-Year Plan for industrialization and agricultural collectivization was being implemented, and he admired its visible results. Already in 1929, however, as Vladimir V. Tchernavin documented in *I Speak for the Silent: Prisoners of the Soviets*, the Five-Year Plan was in a shambles, and the nation was being kept afloat by the GPU, the secret police that operated an economy within an economy through wealth produced by expendable slave labor.[8]

But Counts glowed "that a new morality is emerging. . . . The welfare of society as a whole is being placed above the narrow self-interest of the individual."[9] When he looked at the children, "I thought of the latent powers which a rational system of nurture and education would bring to full fruition."[10] As he traveled the "workers' republic," he found that "the workmen know that they rule the country and take great pride in the belief that theirs is the first society in history to be so governed."[11] Against the backdrop of "centuries of poverty" under the czars, now "both pessimists and optimists . . . dream of an era of material plenty" because "the new order will be realized through the introduction of machines and the careful ordering of the processes of production."[12]

Back home a year later Counts read a copy of a Russian schoolbook on the Five-Year Plan and responded that "practically every page carries the mark of genius."[13] He translated it into English, including a chapter that caricatured capitalism and claimed the system inevitably collapses because "they work without a plan." In his preface Counts wrote, "Perhaps the most challenging feature of the little book . . . has to do with the relation of education to social planning. . . . The American teacher will be forced to put to himself the question: Can we not in some way harness the school to the task of building a better, a more just, a more beautiful society?"[14]

Retreat from Bolshevism

By the mid-1930s Counts had to retreat from his ardor for the Soviets as their internal repression became widely known. He was active by then in advancing organized teachers as a political force. In 1939 he was elected to the first of his three terms as national president of the American Federation of Teachers (AFT). He had recently discovered that international communists had been infiltrating the organization, and during his tenure three large AFT locals were purged for being under communist control. He affirmed his anti-communism in 1949 by co-writing, with his administrative assistant, Nucia Lodge, *The*

Country of the Blind: The Soviet System of Mind Control.[15]

But Counts remained throughout an adherent of collectivism, committed to the principles of benevolent messianocracy. In 1941 he began a political career on a local level with the American Labor Party. That career included an unsuccessful run for the U.S. Senate from New York in 1952 for the American Liberal Party. Following his compulsory retirement from Columbia University at 65 in 1955, he took several short-term positions with education schools. He then spent nine years, until 1971, at Southern Illinois University, where he was so admired and influential that in 1980, six years after his death, the university press published a tribute, *George S. Counts: Educator for a New Age.* The new age in education had turned increasingly collectivist as the National Education Association (NEA) became in the 1960s and 1970s as militant as its smaller rival, the AFT.

In a free society, collectivists have a right to their beliefs but not a right to other people's money to propagate their beliefs. The legacy of George S. Counts is that successive generations of protégés have leveraged public money to their own advantage and the advancement of their agendas.

Counts complained in 1932 that "almost everywhere it [the existing school] is in the grip of conservative forces and is serving the cause of perpetuating ideas and institutions suited to an age that is gone."[16] His final irony is that his intellectual descendants are now the conservative forces seeking to preserve a status quo unsuited to the present age. He was considered a progressive, but now the progressives are those who want to detach all schooling from state control.

Today's reactionaries balk at even a hint of competition, such as charter schools and tuition vouchers. Such devices give only an illusion of competition, however, because they still depend on coercively obtained funds. As long as this "free" money funneled through the public treasury exists, it distorts the market and the seller-buyer relationship.

The genuine new age in schooling will be one that rids itself of messianocracy, which is no more appropriate in that field than in any other. A freed schooling market stripped of public funding will determine which suppliers offer customers the best value according to the customers' own interests, irrespective of the windy aspirations of the contemporary Countses.

But what about those who can't afford to pay for schooling? The marketplace will drive prices down. Entrepreneurs will see to that, just as Henry Ford brought a road tour of Russia within the grasp of George S. Counts.

But if the price is still too high? As Leonard Read is said to have responded, "If you had to pay the entire costs of your child's schooling yourself, wouldn't you do it?" □

1. George S. Counts, *Dare the School Build a New Social Order?* (New York: The John Day Company, 1932), p. 17.
2. Ibid., p. 47.
3. Ibid.
4. Ibid., p. 43.
5. Ibid., pp. 45–6.
6. Ibid., p. 48.
7. George S. Counts, *A Ford Crosses Soviet Russia* (Boston: The Stratford Company, 1930), p. 186.
8. London: Hamish Hamilton, 1935.
9. *A Ford Crosses Soviet Russia*, p. 181.
10. Ibid., p. 145.
11. Ibid., p. 172.
12. Ibid., p. 191.
13. M. Ilin, *New Russia's Primer: The Story of the Five-Year Plan* (Boston and New York: Houghton Mifflin Company, 1931), p. v.
14. Ibid., pp. viii–ix.
15. Boston: Houghton Mifflin Company, 1949.
16. *Dare the School Build a New Social Order?*, p. 5.



CAPITAL LETTERS:



Does Survival Trump Morality?

To the Editor:

I welcomed the article "Philosophy 1 On 1" (*The Freeman*, March 1999), because James Otteson makes the moral case for a free society. Usually, libertarians focus upon utilitarian issues, seemingly unaware that we often lose on this basis because our adversaries have taken the moral high ground. Moreover, frequently the very cause of economic and material loss is an outgrowth of the violation of moral principles, as when incentives are given for destructive behavior while penalties are given for responsible behavior. Consequently, the author is right to raise the fundamental question as to whether slavery and theft are wrong.

However, there is a stumbling block to the suggestion that we adhere to moral principles. People respond that although they find murder and theft abhorrent, there are times when they are called for. Here it does not suffice to simply repeat that what is wrong is wrong. Rather, one needs to acknowledge the conditions under which morality must be violated (as when a soldier kills, or an escapee from a concentration camp steals). The guide is simple: survival trumps morality. It is this requirement that necessitates government, and which should provide its limits. Consequently, theft and taxation can be justified, even as they violate morality—provided there is no realistic alternative, and they are limited to their minimum extent. By this criterion, almost all intervention is precluded. However, it remains for libertarians to acknowledge that liberty is not indivisible, but on rare occasion must be compromised for survival (as when the Continental army fought the British). With that modification, the position of Dr. Otteson can establish "the philosophical underpinnings of the free society."

—ALLEN WEINGARTEN
Morristown, New Jersey

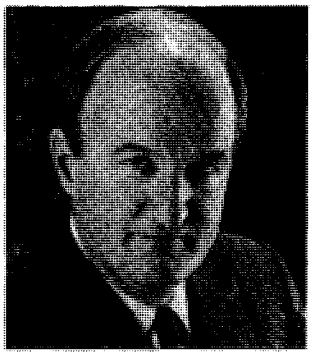
James Otteson responds:

I thank Dr. Weingarten for his letter, but I am not sure what his disagreement with my position is. The two exceptions he offers to the moral principles I discuss in my essay both presuppose prior violations of those same principles: if a soldier is justified in killing someone, presumably this is because some violation of life, liberty, or property has already taken place; similarly, if an escapee is justified in stealing from (perhaps even killing) his captors, it must be only because a similar violation has already taken place.

I assume Dr. Weingarten agrees with me that if there had been no such violations, then the killing and stealing would not in fact be justified. If so, his examples actually underscore, not undermine, the importance of respecting others' life, liberty, and property.

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THE FREEMAN
Ideas On Liberty
JUNE 1999



New Possibilities for Our Grandchildren

"It would not be foolish to contemplate the possibility of a far greater progress still."
—JOHN MAYNARD KEYNES[1]

In 1930, after the Roaring Twenties, John Maynard Keynes wrote an optimistic essay titled "Economic Possibilities for our Grandchildren." After lambasting his disciples who predicted never-ending depression and permanent stagnation, Keynes foresaw a bright future. Through technological improvements and capital accumulation, mankind could virtually solve its economic problem within the next hundred years, he said. Goods and services would become so abundant and cheap that leisure would be the biggest challenge. According to Keynes, capital could become so inexpensive that interest rates might fall to zero.

Interest rates have not fallen to zero, but our standard of living has advanced remarkably since the Great Depression. In fact, we have probably already fulfilled Keynes's prediction that "the standard of living in progressive countries one hundred years hence will be between four and eight times as high as to-day."[2]

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Can We Grow Faster?

Today's economists don't appear to be as optimistic as Keynes, even as we enter another year of a dynamic, full-employment economy. I asked several well-known economists for recommendations that would give us sustained (long-term, not short-term) economic growth rates of 6, 7, or maybe even 10 percent a year, eventually fulfilling Keynes's economic nirvana.

"Not possible!" most of them exclaimed. "I think it's impossible to double the long-term growth rate in the U.S.," answered Harvard economist Robert Barro. David Colander of Middlebury College agreed. "The idea of doubling economic growth in ten years sounds very much like a central planning goal of the former Soviet system." He quoted Herbert Stein: "Economic policy is random with respect to the performance of the American economy, but thank God there isn't much of it."

Recently a whole book of essays was devoted to charting a course toward higher growth rates. In the foreword to *The Rising Tide*, Dana Mead, CEO of Tenneco and former chairman of the National Association of Manufacturers, rejects the notion that the U.S. economy can't exceed its secular long-term growth pattern of around 3 percent a year. He

argues that faster economic growth is achievable without creating shortages, rising labor costs, and higher interest rates. As Jack Kemp states, "We can raise the ceiling on growth by judicious changes in policy."[3]

Of course, not all the economists in the book agree with Mead and Kemp. James Tobin, Yale professor and Nobel laureate, declares, "Although politicians freely promise faster growth, governments have no handy set of tools for effecting it."[4] Apparently he hasn't found the formula to fulfill his mentor Keynes's dream of universal opulence.

Despite their skepticism of substantially higher growth rates, major economists do offer several ways to improve long-term prospects. Rudi Dornbusch of MIT recommends privatizing Social Security and education. Robert Barro urges a flat-rate consumption tax, exemption of savings from taxation, deregulation of labor and business, and a 10 percent cut in the size of government. Robert Mundell warns against inflating the money supply as a growth tool and instead favors slashing capital gains and income tax rates to encourage entrepreneurship and investing. "A lower level of government spending would make more of the surplus of society available for capital formation and growth. A shift in government priorities from consumption and redistribution to social overhead capital, improved education, and investment in scientific and medical research would go far in raising the productivity of capital with a permanent effect on growth."[5]

The Future Is Boundless

My own view is that we are selling our country short by thinking that super-growth cannot be sustained over the long run. Imagine how much advanced our standards of living could become if we

- slashed government spending to its legitimate functions, which undoubtedly means less than 10 percent of GDP;
- replaced the current tax code with a simplified 10 percent flat tax;
- privatized Social Security, or better yet, let Americans make their own plans for retirement;
- established a sound money standard that discouraged malinvestment and the boom-bust business cycle;
- established a fair system of justice that freed 90 percent of the lawyers in this country to become productive citizens; and
- stopped interfering in foreign military affairs.

Imagine the breakthroughs in medicine, transportation, housing, telecommunications, and science that could take place by adopting this laissez-faire program. It boggles the mind to think that we could double or triple our living standards in a short time. To quote Keynes: "Thus for the first time since his creation man will be faced with . . . how to use his freedom from pressing economic cares, how to occupy his leisure, which science and compound interest will have won for him, to live wisely and agreeably and well."[6] □

1. John Maynard Keynes, "Economic Possibilities for Our Grandchildren," *Essays in Persuasion* (New York: Norton, 1963), p. 365.
2. Ibid.
3. Quoted in Jerry J. Jasinowski, ed., *The Rising Tide* (New York: John Wiley & Sons, 1998), p. xxi.
4. James Tobin, "Can We Grow Faster?," in ibid., p. 44.
5. Robert A. Mundell, "A Progrowth Fiscal System," in ibid., pp. 203–04.
6. *Essays in Persuasion*, p. 367.

Professor Skousen's *Economic Logic* Now Available

"*Economic Logic* is a first-rate and exciting introduction to economics. It's clear and accessible, uncommon among today's textbooks."

—Don Boudreaux

The first volume of Mark Skousen's breakthrough college textbook, *Economic Logic*, has just been published. This "micro" text covers supply and demand, monopoly vs. competition, entrepreneurship, wages, capital and interest, and the financial markets. *Economic Logic* is a no-compromise free-market college textbook, with a hands-on approach (it begins with a profit-and-loss income statement). Price is $29.95 each. Send your order to: Skousen Publishing Co., P. O. Box 2488, Winter Park, FL 32790, or e-mail Mskousen@aol.com. Instructors should e-mail requests for a review copy.

BOOKS

A Life of One's Own: Individual Rights and the Welfare State

by David Kelley

Cato Institute • 1998 • 174 pages • $18.95 cloth; $9.95 paperback

Reviewed by Ellen Frankel Paul

David Kelley, erstwhile professor of philosophy, social commentator, and executive director of the Institute for Objectivist Studies, has written a marvelous yet slim volume exposing virtually everything that is wrong with the welfare state. Kelley's writing is always pellucid—an academic's word for clear—and utterly comprehensible, which no doubt explains why he left college teaching. This book is simply outstanding.

Kelley is a superb synthesist, and one could hardly do better than to purchase a copy of *A Life of One's Own* to acquire an understanding of the defects of the welfare state. Here one finds elegant refutations of the key arguments that opponents of America's tradition of individual liberty have employed to undermine our freedom. Primary among these is the notion of "welfare rights," which he argues are spurious because they are parasitic on the efforts of other people: one person's right to welfare payments as an unwed mother, for example, is dependent on the coerced transfer of money from its rightful owners, the taxpayers who actually earned it. In contrast, the natural rights of life, liberty, and property are not parasitic on the efforts of others, and ask of others only that they not interfere with what is mine and thine. What is fundamentally wrong with "welfare rights" is that they cannot be implemented without violating liberty rights.

Kelley is at his most instructive when he analyzes why the welfare state developed out of the Industrial Revolution. Defenders of individual liberty, free markets, and limited government often are weak on the question of why such appealing doctrines have fared so poorly in the twentieth century. Kelley provides some interesting answers. Tracing the origins of the welfare state back to Bismarck's Germany of the 1880s—with its payroll taxes to fund unemployment, accident, health, and old-age insurance—Kelley shows how American resistance to this Prussian model broke down under the pressure of the Great Depression and the exhortations of prominent social activists and academics.

Fundamentally, these welfare state initiatives were a response to changes in the way people led their lives during the Industrial Revolution. In the new economy based on employment for a wage, the vagaries of economic cycles, chance, and bad luck played a much more significant role in people's lives, and they desired protection against those risks. Disabling accidents in the factory, sickness of the breadwinner, old age, and unemployment were potential calamities that wage earners and their families faced. This broadened the constituency for governmental remedies beyond the narrower band of the chronically poor.

While conceding that these risks were real, Kelley shows how they were being addressed by insurance, friendly societies, and other voluntary charitable associations. In other words, he sees nothing inevitable about the development of the welfare state. For such voluntary remedies to have been usurped by state programs, a "sea change in thinking about the problems of poverty and economic risk" had to have transpired. The transformation from private to public provision of assistance could not have happened from economic causes alone, Kelley contends, but rather, resulted from a revolution in "ideas, values and philosophical outlook."

Virulent critics of individualism set the moral stage for the welfare state's assault on liberty. Ideas essential to liberty—such as the morality of self-interest and the efficacy of reason—were ridiculed and repudiated. The "new liberals" paved the way for the welfare state in five key ways, Kelley argues: (1) by redefining freedom into a spurious "positive freedom" to be taken care of by the state, (2) by redefining "coercion" to mean what employers do to their employees by offering

them a wage, rather than the threatening of people with harm if they don't obey, (3) by undermining individualism with the claim that we are all helpless creatures of social forces, (4) by advocating a secular variant of altruism that replaced service to God with service to society, and (5) by undermining the distinction between society and the state, and deifying the latter.

Kelley concludes his demolition of the welfare state on an optimistic note. Just as communism imploded when its myth of a workers' paradise wrought by central planning lost its credibility, so might the welfare state collapse under the weight of its myths and nearly bankrupt programs.

Not as sanguine by nature as Kelley, I do hope that his powers of prognostication are keen. I wonder, though, whether a system based on pure evil, like communism, is more vulnerable to collapse than one grounded on smaller, subtler evils, like the welfare state. We shall see. □

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Mugwumps: Public Moralists of the Gilded Age

by David M. Tucker

University of Missouri Press • 1998 • 160 pages • $27.50

Reviewed by Burton Folsom

At last, the Mugwumps have their modern-day champion: Professor David Tucker, a historian at the University of Memphis. The Mugwumps are best known as civil service reformers who worked within the Republican party to quash the spoils system with the Pendleton Act of 1883. As Tucker shows, however, the Mugwumps were much more than mere moral reformers. They were eloquent and persuasive spokesmen for free markets and free trade throughout the late 1800s.

The Mugwump name came from the Algonquian word for "chief." Tucker looks at, among others, the careers of Mugwump "chiefs" William Graham Sumner, professor at Yale University; E. L. Godkin, editor of *The Nation*; Carl Schurz, senator from Missouri; David Wells, a government statistician; and Henry Adams, popular writer descended from two presidents.

The Mugwumps greatly admired the writings of British thinkers Adam Smith, Richard Cobden, and John Stuart Mill. The ideas of free markets, strong property rights, sound currency, and limited government were hallmarks of Mugwump thinking. As Tucker notes, "They mastered historical and statistical material that demonstrated that steam and electricity had multiplied the productivity of workers and would create an abundance if only individuals learned personal virtue and if governments withdrew their market interferences."

Not only would society function more smoothly if entrepreneurs were unleashed and government restrained, but poor people and immigrants would have greater chances for success. Protective tariffs, according to Mugwump research, helped fewer than 10 percent of American workers and pushed prices upward for the rest. Tariffs further created lobbies of special interests who corrupted government by pressuring politicians to vote special favors for them.

The Mugwumps deplored the political arena and preferred to write rather than run for office. Their big political success was when they bolted the Republican party in 1884 and helped Grover Cleveland win the presidency. Cleveland proved to be a strong free-market thinker and his two terms were the high point of Mugwump influence.

In the late 1800s, the Mugwumps were challenged by the Populists, who wanted government aid for farmers; silver miners, who wanted the government to buy large amounts of silver at high prices; and some intellectuals, who saw government as a useful tool to create a more perfect society. Tucker describes these challenges to free-market ideas and observes that Mugwumps opposed federal tinkering because "government policies violated liberal beliefs in absolute individual rights of life, liberty, and property."

Tucker does an excellent job of presenting the Mugwumps and their ideas, which he says were compelling and logical. They won some battles, lost others, and, by the early 1900s, were overshadowed by the Progressives. "Politicians," Tucker says, "always needed encouragement to do the right thing, and even if the advice was rarely followed, critics were not necessarily failures."

In the past, historians have ridiculed Mugwumps as priggish, selfish, and suffering from declining status in society. Tucker argues that this view says more about the historians than it does about the Mugwumps. "Mugwumps were given their reputation for failure by later cheerleaders for the welfare state," he observes. "[A]fter the Great Depression of the 1930s turned educated opinion to Keynesian economics, nineteenth-century liberals who feared government as the enemy of freedom and progress were recast as selfish, wrongheaded agents for the middle class."

Tucker's research is solid and he explores a wealth of primary and secondary sources. His writing is clear and crisp and his chapters are well organized. Most historians assume that free-market ideas lost because they were not sound; Tucker, by contrast, assumes that the Mugwumps held ideas that were solid and enduring. To explain their ultimate defeat, he explores how the German ideas of statism and empire-building began to permeate American society in the late 1800s.

Tucker's book is an excellent addition to the literature on the Gilded Age and a valuable correction to the standard books by historians Richard Hofstadter, Ari Hoogenboom, and John Sproat. □

Burton Folsom is senior fellow with the Mackinac Center for Public Policy in Midland, Michigan. His book The Myth of the Robber Barons *is in its third edition.*



Who Killed Homer? The Demise of Classical Education and the Recovery of Greek Wisdom

by Victor Davis Hanson and John Heath

Free Press • 1998 • 288 pages • $25.00

Reviewed by Fred D. Miller, Jr.

Over a decade ago, Allan Bloom's explosive book, *The Closing of the American Mind*, opened the floodgates of criticism of American higher education for perverting its ostensible mission and values. Professors of the humanities, in particular, have been excoriated for behaving like politically correct ideologues and overspecialized self-promoters and careerists rather than teachers and scholars in the traditional sense. *Who Killed Homer?* presses the attack into that most venerable citadel of the academy: the discipline of classics, which studies the languages and literature of the ancient Greeks and their intellectual heirs, the Romans.

Authors Hanson (professor of Greek at California State University-Fresno) and Heath (professor of classics at Santa Clara University) start with a paradox: In 1992 classicists published over 16,000 books, articles, and reviews, double the output of 1962. Yet during this time, enrollments in Latin have plummeted and Greek has all but disappeared. As a result, "there are now five or six Classics professors in the country for every senior Classics major, and over thirty articles and books each year for every graduating student." This is having dire effects: retiring classicists are not replaced, and ever fewer courses in classics are being taught. How did this happen? Or, as the authors ask, who killed Homer?

There has been a drastic decline in the quality of American public education (partially concealed by grade inflation and the "dumbing down" of standardized tests), and the elimination of foreign language requirements has had a disproportionate effect on Latin and Greek. But the authors place much of the blame on classicists themselves who are unimpressed with or unaware of the values of Greek and Roman civilization and have little interest in explaining them to the general public. This is

in part the result of the hyperreaction against Western civilization that has seeped into the university professoriate along with postmodernism and multiculturalism. The Greeks, especially, have been ignored, debunked, or denigrated, although they bequeathed to us enduring ideals such as rationality, scientific inquiry, and freedom of speech.

Classical scholarship has unfortunately followed the lead of literary criticism, "adding a vacuous jargon and sophistic superstructure on top of the multiculturalist perspective." Books in classics are routinely praised by reviewers for being "densely argued" or "challenging," rather than panned for their turgid, unintelligible verbosity. The authors document this with a series of outrageous and sometimes hilarious examples of pretentious verbiage, which receive adulation from other academic reviewers. For example, one book review in the esteemed *Journal of Hellenic Studies* concludes:

> In sum, this book might be refigured as revealing the contradictions between a mainly "pessimistic" post-structuralist/deconstructive discourse and a more "optimistic" Marxizing discourse, contradictions through which—could one say?—glimmer sights of the Althusserian "real conditions of existence." Or not.

Why do academics publish such stuff? Because they learn that the key to success is recognition within their academic guild. So they strive to earn Ph.D.'s from illustrious universities, find jobs at similarly illustrious universities, secure tenure, and ultimately ascend to stardom, which is measured in terms of grants, endowed chairs, appointments to editorial boards, professional recognition, reduced teaching loads, extended leaves, and prestigious fellowships. In pursuing these goals, however, scholars are making themselves collectively irrelevant.

The authors show from experience that teaching Greek and Latin is not easy. In order to motivate students, teachers must be highly dedicated and view the task of teaching as their primary responsibility. They must communicate to students the light at the end of the tunnel: the power and beauty of classical literature and the values it contains.

An effective jeremiad must exaggerate somewhat, and this book is no exception. The profession of classics includes many dedicated teachers who devote long hours to their students and many scholars who conscientiously search for the truth. But the book's thesis is correct that the discipline of classics as a whole is "in crisis."

The solution proposed in this book is a fundamental change in how universities do business: professors should be expected to teach a lot more, they should be expected to motivate their students to learn, and they should be hired, promoted, and rewarded on the basis of their teaching to a much greater extent than they are now.

The prospects for such reforms seem dim. Academics generally, and classicists in particular, have little incentive to alter their behavior. Until and unless there are fundamental changes in how higher education is offered to students, it is unlikely that Homer will rise again from the dead. □

Fred Miller teaches the classical Greek language and is professor of philosophy and executive director of the Social Philosophy and Policy Center at Bowling Green State University.

Secession, State & Liberty
edited by David Gordon
Transaction Publishers • 1998 • 344 pages • $44.95

Reviewed by George C. Leef

Herbert Spencer argued in a famous essay that individuals have a right to ignore the state. If so, it follows that a group of individuals also has the right to ignore the state, and enter into some new political arrangement if they choose. That is, they may secede. Although secession has had a bad press in the United States since the Civil War, with the secessionist cause and slavery almost invariably linked, this book brings together 11 essays which collectively make the case that it merits serious consideration.

The essays fall into three categories—those

examining American history for fresh insights on the legality and morality of secession, those taking a theoretical look at secession generally, and those applying secession theory to the contemporary world.

In the first category are Donald Livingston's "The Secessionist Tradition in America," Joseph Stromberg's "Republicanism, Federalism and Secession in the South, 1790 to 1865," Thomas DiLorenzo's "Yankee Confederates: New England Secession Movements Prior to the War Between the States," and James Ostrowski's "Was the Union Army's Invasion of the Confederate States a Lawful Act?" If you enjoy challenges to conventional wisdom, these essays are a feast.

Livingston takes great pains to attack "the absurd nationalist theory of the Constitution propounded by Story and Webster," maintaining that the prevailing philosophy of the Founders was that the country was a voluntary union of sovereign states, each possessing as much right to depart as they had to depart—secede—from the British Empire. Stromberg, traversing much of the same ground, quotes Madison that ratification of the Constitution was "the act of the people, as forming so many independent states, not as forming one aggregate nation." DiLorenzo makes the historically deft point that talk of secession did not originate in the South, but rather in New England in the years before and during the War of 1812. Hostility to Jefferson's trade embargo and the war caused leaders in New England to convene in Hartford to discuss secession. The movement fizzled, of course, but DiLorenzo concludes that "there was virtually universal support—from Republicans and Federalists alike—for the right of secession."

Arguably the most affecting in this group is Ostrowski's essay, an extended analysis of the arguments advanced by President Lincoln for the legality of sending troops into Confederate territory. Ostrowski finds no constitutional support for any of those arguments. Instead, he marshals considerable support for the opposite proposition, that the war was conducted in violation of the Constitution, concluding that "the purposes of the Constitution do not envision the use of armed force against a state that has concluded it is no longer benefiting from the union." Ostrowski ends his piece with his thoughts on the present-day legality of secession, holding that the Civil War and subsequent constitutional amendments did not change underlying legalities: the Ninth and Tenth Amendments still protect the right to secede.

In the second group of essays, Steven Yates asks, "When is Political Divorce Justified?" and answers that because the federal government has ignored its legitimate functions and has undertaken many illegitimate ones, "Americans are morally justified in taking action to restore limited government, including, as a last resort, secession." Scott Boykin explores "The Ethics of Secession" and, among other things, refutes arguments that have been made purporting to limit the right to secede. The late Murray Rothbard's "Nations by Consent: Decomposing the Nation-State" is classic Rothbard. He writes, "One goal for libertarians should be to transform existing nation-states into national entities whose boundaries could be called just . . . that is, to decompose existing coercive nation-states into genuine nations, or nations by consent." As Clyde Wilson's "Secession: The Last, Best Bulwark of Our Liberties" argues, "The right of self-government rests on the right to withdraw consent from an oppressive government. That is the only really effective restriction on power, in the last analysis."

In the third category of essays, Hans-Hermann Hoppe contends that secession is a healthy trend in "The Rationale for European Secession." Pierre Desrochers and Eric Duhaime examine the case of Quebec. Lastly, Bruce Benson contributes "How to Secede in Business Without Really Leaving," an essay exploring arbitration as a means of "seceding" from the government's system of law and courts. Of particular interest here is the battle that the "anti-secession" forces (mainly lawyers who fear the loss of business if arbitration provides an attractive alternative method of dispute resolution) have waged with considerable success to undermine the advantages of arbitration.

A most intriguing book! □

George Leef is book review editor of The Freeman.

Money and the Nation State: The Financial Revolution, Government and the World Monetary System

Edited by Kevin Dowd and Richard H. Timberlake

Transaction Publishers • 1998 • 453 pages • $34.95 cloth; $19.95 paperback

Reviewed by Bert Ely

This is a book on a vital—and much misunderstood—topic. It is sometimes excellent, but largely disappointing.

The book consists of 13 chapters divided into three sections: The History of the Modern International Monetary System, Modern Money and Central Banking, and Foundations for Monetary and Banking Reform. The editors' introduction provides a good summary of each chapter. As Merton Miller notes in the foreword, the authors felt free to "disagree among themselves in their interpretations of key events, empirical evidence on devaluations, and a variety of other monetary issues."

The book's first section is its strongest. The late Murray Rothbard's contribution, "The Gold-Exchange Standard in the Interwar Years," alone is worth the price. Rothbard is especially effective in differentiating the "gold-exchange" standard, which Britain adopted in 1925, from pre-World War I monetary arrangements when gold coins circulated freely. Another noteworthy chapter is Frank van Dun's "National Sovereignty and International Monetary Regimes," in which the author draws on the work of political philosophers to explain why governments seek to dominate monetary systems at the expense of market efficiency.

The latter two sections generally reflect a weakness characterized by the first word in the book's title—an excessive emphasis on *money* that disregards how electronic technology has altered the financial marketplace in recent years. By failing to describe how this marketplace actually works today, particularly in the industrialized nations, the authors misinterpret recent monetary events, which leads to policy prescriptions based on outdated understandings of that marketplace.

Today, all forms of money are merely credit instruments that also readily serve as media of exchange. That is, coins, currency, and checkable bank deposits represent credit extended to the issuers of media of exchange.

The authors seem not to understand that inflation is caused by excessively rapid credit expansion, because it is *credit*, not media of exchange per se, that gives individuals, businesses, and governments the ability to own assets or mortgage future income and tax collections. Media of exchange merely represent one way to facilitate a purchase; using a credit card or a check drawn against a pre-established line of credit represents an increasingly common way of buying something without any "money" changing hands.

Such transactions create credit; credit growth in turn is controlled by interest rates. If rates are too low, in real or inflation-adjusted terms, credit will grow too rapidly, causing inflation, *regardless of what happens to the money supply*. If rates are too high, credit demand will contract, eventually causing a recession, again regardless of changes in the money supply.

Interest, of course, is a price. Therefore, price stability depends on how accurately the credit markets price interest. Inflation's decline in recent years reflects the improved functioning of the increasingly globalized financial marketplace in which debtors and creditors, acting out of self-interest, negotiate interest rates whose cumulative effect is to foster non-inflationary credit growth.

Unfortunately, the essays provide no sense of how the credit markets work and the overriding importance of properly priced interest even as they acknowledge the importance of the pricing mechanism generally. Consequently, they present worn-out, statist solutions, usually involving central banks, for ensuring price stability. For example, Steve Hanke and Kurt Schuler advocate currency boards (backing the local currency with the currency of another country). However, currency boards are unnecessary: merely guaranteeing the convertibility of government-issued

currency into debt carrying a market rate of interest will protect any economy from a currency-driven inflation.

Lawrence White, Richard Timberlake, and others write fondly of a gold-based monetary standard. Gold and other specie standards, however, have never provided price stability, except over the very long term, nor have they been sustainable.

Several authors advocate fixed exchange rates, but they are unsustainable and wreak economic havoc when the inevitable devaluation occurs—witness today's Asian crisis. Robert Keleher, for example, argues in "Global Economic Integration: Trends and Alternative Policy Responses" that fixed exchange rates "minimize the variability and dispersion of many other prices, and so further improve the workings of the price system." Such price smoothing, though, distorts important price signals coming from the rest of the world. What advocates of fixed exchange rates ignore is that an exchange rate is a price, and therefore should no more be manipulated than the price of crude oil or toothpaste. Instead of distorting the pricing mechanism, public policy should ensure price stability by relying on market-determined prices, especially the price of credit and prices expressed in other currencies.

The subject of this book—ideal modern monetary and credit policies and institutions—desperately needs a penetrating analysis. Sadly, this book fails to deliver it. I hope that the next book to address this subject will. □

Bert Ely is a financial institutions and monetary policy consultant in Alexandria, Virginia.

Policy Analysis and Public Choice: Selected Papers

by William A. Niskanen

Edward Elgar • 1998 • 448 pages • $95.00

Reviewed by Bruce Yandle

This volume has much to recommend it. First off, William Niskanen, chairman of the Cato Institute, presents an organized collection of 34 papers that span his interesting and productive 40-year career as a professional economist. Never so technical as to restrict access to readers of policy analysis, the papers cover issues as diverse as school choice, drug policy, Reaganomics, trade policy, voting rules, and the prospects for a liberal economic order. In short, the papers represent a delightful smorgasbord of policy analysis by one who is at once a respected scholar and a friend of liberty.

But the range and quality of the papers is just one gainful reason for reading the book. The second reason, and perhaps the more interesting one, is that the collection reveals the author's preferences regarding the work of his long and impressive career. In that regard, Niskanen shows that he is as much concerned about rules of just conduct and constitutional constraints that assure a liberal order as he is about good economic analysis and the powerful insights offered by Public Choice. The papers demonstrate thoughtful appreciation of both the normative and positive aspects of public policy.

To Public Choice scholars, the name Niskanen brings an immediate association with his seminal work on bureaucratic tendencies to increase budgets and bargain with politicians in all-or-nothing deals to expand activities beyond efficient margins. To industry economists, the name generates memories of Ford Motor Company's chief economist who resigned after attempting to counter the firm's protectionist stance. To defense and government economists, Niskanen is known for his work at the Pentagon and as acting chairman of President Reagan's Council of Economic Advisers. And to those who know none of this, the collection demonstrates the power of careful analysis to offer useful and sometimes unexpected insights.

Niskanen's 1994 paper on crime and police offers an example of the power of his thinking. After his analysis of the data, one begins to doubt the generally held idea that crime rates rose; for one thing, crime reporting has improved considerably. Moreover, what can be done to counter any possible crime increase? The author's conclusion: not much. To a large degree criminal activity represents tolerance for crime, the demise of rules of just conduct. The best thing the federal govern-

ment could do would be simply to get out of the way by repealing its own crime legislation and encouraging state and local experiments.

A strong believer in looking at the data, Niskanen does this in spades when he deals with drug policy. After modeling the problem, he concludes that legalization would reduce drug-control expenditures by as much as $10 billion annually, reduce violent crime and AIDS transmission, and generate substantial tax revenues from an excise tax on drugs. But Niskanen has a habit of recognizing all sides; so he describes the fallout that might be generated by a more open market for drugs: cocaine babies, increased health-care costs borne by taxpayers, and additional welfare dependency. Weighing the evidence, he concludes that legalization could generate net benefits, but that some new costs would be produced along the way.

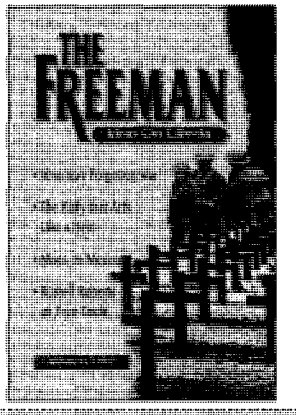
Niskanen's paper on economists and politicians overflows with insights into the activities in the higher reaches of government. He begins with a question: Why do politicians hire economists? He stakes out his answer by describing canons of good policy analysis, which are worth studying. Niskanen then describes the rising status of economic advisers in government, noting the arrogance that developed among those who thought Keynesian economics would solve the nation's unemployment problems. Finally, Niskanen returns to his Public Choice roots by observing that politicians hire economists to serve political interests. On the whole, the record of economists as policy advisers has been more congenial to the growth of government power than to liberty.

Of all the papers in this stimulating book, my favorite is a graduation address given at Suomi College in Michigan in 1983. Here Niskanen lays out some simple but profound rules for living: recognize and reinforce your natural abilities, be willing to take risks, learn from the errors risk-taking generates, be humble, keep a sense of humor, and develop respect, but not fear, for the many mysteries of life.

Public Choice scholars, anyone who appreciates strong policy analysis, and readers interested in political economy should put this book on their reading list. □

Bruce Yandle is Alumni Professor of Economic and Legal Studies at Clemson University.

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Nothing's Free

My brother and I have a game we play from time to time. He calls me with a can't-miss investment opportunity, and my job is to figure out what's wrong with it. There is always something wrong with it. In fact, the better it looks on the outside, the worse it looks on the inside when you take a closer look. That doesn't necessarily make it a bad investment. But it's never the bargain it appears to be at first.

Such is the economist's burden and blessing. There is no free lunch. The bigger the bargain, the more likely it is that something worrisome lurks beneath the surface that needs to be examined. There's always a catch. Usually it's easy to discover: the bargain is of questionable quality; the bargain has a hidden payment that comes later; the bargain involves an unforeseen risk. But every once in a while a bargain comes along that looks so good, you wonder if it might actually be a genuine bargain. This should make you especially nervous. For that means the catch is especially hard to see. So look carefully before you leap, then look some more.

State Lotteries

So it is with the "free" education that is being offered in some states with lotteries. In Georgia, for example, any student with a sufficiently high grade point average gets "free" education at any public Georgia college. The funds come from sales of lottery tickets. It sounds like the ultimate bargain. Who can quarrel with free education?

Let's take a closer look. There are many senses in which a University of Georgia education is not free. Resources get used up to provide it. Those resources could have provided something else of value.

But who provides those resources? If the education is not really free, someone must be paying. It would seem to be the losers in the lottery. And that's why the education seems free. We know there have to be losers in the lottery. They help pay for education. Sounds great. And besides, no one forces anyone to play the lottery, so the whole thing is more like a voluntary contribution than a tax.

To see the flaw, suppose the government decided to fund free education by opening a chain of dry-cleaning stores. Profits from the store are used to pay for "free" education. To make sure the stores are sufficiently profitable, the government decides to charge a dollar more per shirt than dry cleaners currently in operation. And to keep those privately run stores from attracting customers at lower prices, the government decides to ban all private competition and enjoy a monopoly.

We would all understand that in this world the "free" education is being paid for by people who enjoy pressed and clean clothes. Such people would be paying in two senses. The first sense is literal: they fund the education with their excess payments above the compet-

Russell Roberts (roberts@mail.olin.wustl.edu) *is director of the Management Center at the John M. Olin School of Business at Washington University in St. Louis. He is the author of* The Choice: A Fable of Free Trade and Protectionism *(Prentice Hall).*

itive prices that would prevail without a government monopoly. They also pay in the sense of having their clothes cleaned less often than they would under a private system. Given the higher prices, some people are going to do less dry cleaning and some are going to do none at all. Under such a system, it would be ludicrous to claim that the education is free. It's clearly being paid for by the users of dry-cleaning services. Funding education from the pockets of dry-cleaning customers also raises a question of morality. Why should the burden of funding education fall arbitrarily on those who like clean clothes?

Government Monopoly

Now, let's return to the state lotteries. About 55 percent of the receipts go to prizes, 10 percent to expenses, and 35 percent to education or some similar unimpeachable cause. Because 35 percent goes to neither winners nor losers, the real cost of the lottery is that you win less often and the prizes are smaller than would be the case without a government monopoly. If government allowed competition or made gambling legal, people who like to gamble would have a higher chance of winning and there would be more money distributed to winners.

So lottery-funded education is not free after all. Subsidizing education out of lottery proceeds punishes people who like to gamble. Those turn out on average to be people who are relatively poor with less education. Can you think of a more immoral solution for funding education than to take the money from those with the least education?

People like to defend the lottery by saying it's voluntary. After all, you don't have to play. It's also true you can avoid the income tax by not working. So I guess that's voluntary, too. But it's hard to argue that the lottery is a voluntary tax when the government has a monopoly. Can you imagine how many people would play state lotteries if there were competing private lotteries that paid 90 percent of the proceeds in prizes instead of the typical 55 percent?

Under a private, competitive lottery system, the prizes would be bigger and the odds of winning would be higher. It would be a better world than the one we now live in, where people in search of hope are forced to pay a 35 percent tax to finance the college education of mostly upper-class children. That's why I like my dry-cleaning proposal. Sure it's unfair. But it's better than using the money from a government lottery. □

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Cover: Bombing damage in Kosovo. (AP/WIDE WORLD PHOTOS).

PERSPECTIVE

Operation Legacy

The Clinton policy in the Balkans can be criticized at many levels: the apparent lack of forethought, the misapprehension of the conflict and the region's history, the likely dishonesty about the intention to use ground troops, the law of unintended consequences (the boost to Greater Albania, for example), and so on. That all has been much commented on. What's most neglected is the domestic reason for forswearing such foreign adventurism, no matter how heart-wrenching the CNN coverage.

I can do no better than to quote James Madison on this subject.

"Of all the enemies to public liberty," he said, "war is, perhaps, the most to be dreaded, because it comprises and develops the germ of every other. War is the parent of armies; from these proceed debts and taxes; and armies, and debts, and taxes are the known instruments for bringing the many under the domination of the few. . . . No nation could preserve its freedom in the midst of continual warfare."

The reader is referred to Robert Higgs's *Crisis and Leviathan* for documentation of the Madisonian principle.

Mr. Madison proceeded to describe the bloated executive that war produces. Could he have foreseen the day when a president makes war without a congressional declaration? (These days we have "consultation" or, at best, debate *after* the president has committed the country to war.)

"War," Madison continued, "is in fact the true nurse of executive aggrandizement. In war, a physical force is to be created; and it is the executive will, which is to direct it. In war, the public treasuries are to be unlocked; and it is the executive hand which is to dispense them. In war, the honors and emoluments of office are to be multiplied; and it is the executive patronage under which they are to be enjoyed; and it is the executive brow they are to encircle. The strongest passions and most dangerous weaknesses of the human breast; ambition, avarice, vanity, the

honorable or venal love of fame, are all in conspiracy against the desire and duty of peace."

Milosevic takes his place beside a long list of state-wielding butchers. He's caused the burial of thousands of ethnic Albanians. The president of the United States didn't have to let that tragedy dump more dirt on the gravesite of limited government here.

* * *

We devote a major portion of this issue of *The Freeman: Ideas on Liberty* to the U.S.-led war against Yugoslavia. David Mayer argues that the war is an act of aggression that violates the U.S. Constitution, not to mention the charters of the United Nations and NATO. He also points out that events in Serbia and Kosovo bear no relation to any vital interest of the American people.

Gary Dempsey outlines the history of Kosovo, beginning about 2000 B.C., and its importance to both the Serbs and Albanians, showing that brutality is not unknown to either side.

Peter Mentzel adds to the historical analysis, emphasizing the modern roots of the conflict.

Next we reprint a classic from the autobiography of Frank Chodorov in which he defends isolationism as a sensible human impulse to mind one's own business and to avoid far-off conflicts that one likely doesn't understand.

Robert Higgs summarizes America's involvement in two world wars and the cold war to illustrate how foreign adventurism bolsters the power of government and shrinks the sphere of liberty.

Michael Palmer finds himself thinking back to 1969, when he was dispatched to the barren and perilous Ashau Valley in South Vietnam, and fears for the young Americans facing combat in the Balkans today.

Wendy McElroy takes a close look at Randolph Bourne's famous sentence—"War is the health of the State"—and shows that he had more in mind than taxes and spending.

Two of our columnists also focus on the war. Donald Boudreaux explains that government doesn't have the competence to impose itself on other people's conflicts. And Doug Bandow tries heroically to make sense of a foreign policy that defies explanation.

No idea is more important to the freedom philosophy than that of unplanned, or spontaneous, order. Yet it is counterintuitive and therefore hard for many people to accept. Nigel Ashford explores the products of human action but not human design.

When the government sets out to create equality in any sense other than equality before the law, all manner of mischief is possible. James Bovard reports that "tyranny" is not too strong a word for what egalitarian officials are capable of inflicting.

Why are frog populations declining and deformities increasing? Does it portend an environmental cataclysm? Some officials would have us believe so. Brian Doherty says the real meaning may be less worthy of headlines.

Americans of the nineteenth century knew something about the nature of money that has long since escaped citizens of today. Joseph Stromberg demonstrates this through the memoirs of an obscure but classic pioneer and jack-of-all-trades.

Lawrence Reed's column points out that Bill Clinton could have learned a thing or two about taxes from Grover Cleveland and Calvin Coolidge. Dwight Lee finds it ironic that property rights are blamed for problems caused by the lack of defined property. Thomas Szasz says suicide is a moral, not a medical, issue. Mark Skousen explains "economic value added." Walter Williams wonders when people will stop blaming others. And David Kelley examines the claim that tax policy should make "winners" compensate "losers," concluding, It Just Ain't So!

In the book review section, volumes on welfare, Calvin Coolidge, H.L. Mencken, the rich, and freedom of speech on the Net get a going over.

—SHELDON RICHMAN

THE FREEMAN
Ideas On Liberty

Tax Cuts Are Unfair?

It Just Ain't So!

Federal tax revenues last year were nearly 22 percent of GDP—the highest level in American history. With federal coffers swollen, the government is enjoying a surplus that, until recently, no one would have expected. It is obviously time for a tax cut to return some of this largess to its rightful owners, the taxpayers.

Republicans have been pushing for a 10 percent cut in income-tax rates. This proposal has encountered the usual protests that it would favor the rich. A typical comment appeared in a *New York Times* op-ed, "The Trouble with Tax Cuts" (February 24, 1999) by Frank Levy, an economist at MIT, and Iris J. Lav, deputy director of the Center on Budget and Policy Priorities.

Levy and Lav argue that "the economy heavily favors the better educated" at the expense of less-educated and semi-skilled workers. "Since good times don't automatically benefit everyone," they claim, "winners need to use some of their extra income to compensate losers." A rate cut of 10 percent, they assert, would "work in the opposite direction: it would increase income inequality." The upper tenth of the income distribution, with earnings above $90,000, would receive 55 percent of the tax cut. The bottom 60 percent would receive only 10 percent. And the 35 million households that pay no income taxes would receive no benefits at all! In their view it's just not fair.

Or is it? The case that Levy and Lav make against the tax cut is not a matter of economics but of morality, and their standard of justice is warped.

Let's begin with two obvious points. First, a tax cut does not confer a "benefit" on taxpayers, as if the money belonged to the government, which was generously conferring gifts on its citizens. If you follow that conception to its logical conclusion, all income belongs to the state, and any tax rate below 100 percent constitutes a gift. But that conception is wrong. It is the taxpayers who earn the income by producing it; it belongs to them. A portion is taken in taxes, and when government lowers the tax rate it is simply refraining from taking as much as it used to.

The second point is that the wealthy save the most from a lower tax rate because they pay the most in taxes. Levy and Lav complain that with a 10 percent rate cut, the upper tenth would receive 55 percent of the tax-cut total. But those people are currently paying 62.4 percent of all income taxes. The bottom three-quarters of all earners pay less than a fifth of all income taxes, while the upper tiers pay a vastly disproportionate share. So *of course* the wealthy would save the most from a rate cut—and they should.

Deeper Flaws

Beyond these obvious points, the argument is flawed at a deeper level. It rests on a false conception of how an economy works and of how people earn their incomes.

The implicit premise of Levy and Lav's argument is that the U.S. economy is a collective enterprise in which income is distributed to individuals who are more or less passive recipients of what they get. The distribution is determined by various factors: the level of skill and training an individual gets from the educational system, the level of technology, market forces (including foreign competition), and government tax and spending policies, among others. The government, on this conception, has the responsibility of counter-

ing the effect of the nongovernmental factors so as to produce a fairer overall distribution than a free market would achieve. Levy and Lav assume that greater equality is good, less equality is bad.

But this whole outlook is misconceived. People are not passive recipients of an income "distribution." They acquire money by trading with others, earning income in diverse ways. Some people form long-term relationships with employers, trading their time, effort, and skill for a salary; others operate solo, selling goods or services directly to customers. Some trade the use of their property for a rent payment, or the use of their savings for interest.

What determine a person's income are his own choices and the choices of individuals who trade with him. People differ in their desire for money, as opposed to leisure, time with the family, or other goods. They differ in the kind of work they find meaningful, and the kinds of working conditions they prefer. The market—which is just a sum of individuals who produce and trade—values some work more highly than others and pays more for it. And of course people differ in ability, knowledge, and skill—sometimes because of innate capacity or the environment in which they grew up, sometimes because of previous choices they have made in their lives.

Each of us is an entrepreneur in his own life, with the capacity—and the responsibility—to find ways of acquiring money through trade, each in accordance with his talents and preferences. Each of us is an active agent, constantly making choices about how to exploit the opportunities we have—and how to create new opportunities for ourselves. And over time, virtually everyone increases the income he can earn as he acquires experience, training, knowledge, contacts, savings, and other productive assets.

Winners and Losers?

The most offensive aspect of Levy and Lav's argument, morally speaking, is the notion that people with lower incomes are "losers" who must be compensated by the "winners." An economy is not a competitive scramble for shares of a fixed pool of wealth, but a process of cooperation in producing wealth on an ever-increasing scale. And those at the bottom benefit the *most*, not the least. They are able to enjoy a standard of living made possible by those who created the industries they work in and the products they buy. As Ayn Rand observed, there's a pyramid of ability in which benefits flow downward, from the most to the least able. "When you work in a modern factory, you are paid, not only for your labor, but for all the productive genius which has made that factory possible," the industrialists, financiers, engineers, scientists, and other creators without whom the unskilled worker would not have a job in the first place.

Bill Gates's billions are but a fraction of the value he has showered on the office workers who use his software and earn higher wages because they can produce more efficiently; the home users who can track their finances and surf the Net; the retailers who sell the software or the computers that use it; the programmers whose software runs under Windows; and on and on.

Are the "winners" in economic growth morally obliged to pay compensation to the "losers"? It just ain't so. There are no real losers—and that's because the "winners" have already spread the prodigious benefits of their productive ability to everyone with whom they trade. Let's cut taxes, and allow everyone to reap more of the benefits of their place in the pyramid of ability.

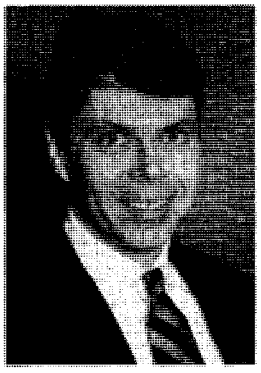
—DAVID KELLEY
Institute for Objectivist Studies

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Thoughts on Freedom

by Donald J. Boudreaux



Outside the Limits

"Slobodan Milosevic is hideous. If tomorrow he is run over by a beer truck the world will be a better place."

That was my response to the bright woman who was simultaneously cutting my hair and seeking my opinion of U.S. military involvement in Kosovo.

"So you agree that NATO's bombing mission is justified?" she asked.

"Well, no. I think it's atrocious. Milosevic is no threat to the United States. As I see it, if the U.S. military has a legitimate role it is to protect Americans from foreign coercion. That should be its only function."

"How can you say that?! The Serbs are slaughtering the Kosovars and driving them from their homes by the hundreds of thousands! We have a moral obligation to help those poor people."

"Who's the 'we'?" I asked. "You and I aren't in Kosovo, and I have no plans to go there; I bet that you don't either. You must mean that this obligation is owed by the U.S. government—not by 'we'."

"But our government IS us. Because it represents us, it is our tool for doing what we Americans feel is just and necessary."

"I couldn't disagree more. Despite elections to decide which particular people occupy various government offices, the government is not us. Don't be deceived by the high-school-civics fantasy that a wide franchise and regular elections ensure that government does only what is willed by The People. In fact, even democratic governments are driven overwhelmingly by pressures from special-interest groups. These groups routinely get government to do their bidding at the expense of innocent citizens whose only political access is an occasional trip to the voting booth. And don't forget that government itself is a special-interest group. Politicians and bureaucrats have potent incentives to stay in power even if this means doing things that aren't in the best interest of the country as a whole. It happens all the time. The government isn't us."

"I really, really disagree with your cynical view of our political system. NATO's current air strikes against Milosevic prove you wrong. America has nothing to gain by interfering in Kosovo. We're there to right a wrong, not to help some special-interest group."

I could tell she was worked up.

"And further, even if your cynical view is correct, what can be wrong with helping the Kosovars escape ethnic cleansing?"

"Look, it's naïve to suppose that bureaucrats in the Department of Agriculture, H.U.D., the F.T.C., and other domestic agencies are pawns of interest groups while bureaucrats in the military and diplomatic corps are saintly patrons of the public interest. But even if I concede that government officials are forever selfless when it comes to diplomatic and military relations with foreign countries I would still oppose U.S. military involvement in Kosovo."

"On what basis?"

"Institutional competence. The fact that the

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American military possesses vast firepower doesn't mean that those in charge possess vast wisdom. Even if such people are immune to interest-group pressures, they can never be immune to vanity, ignorance, and error. They're human. Given this fact, it's unwise in the extreme to entrust military power to anyone for any purpose other than national defense."

"Why just national defense?"

"Because it's a relatively easy goal to define and one that enjoys nearly universal approval. It's within the confines of what a government is institutionally able to do—protect its citizens from foreign military invasion.

"But Americans today suffer the dreadful misconception that because our country is wealthy and our government powerful, our government can right *all* wrongs—that our government can create an earthly paradise; that our government is superhuman; that our government should address every evil, big and small. Did the Mississippi River flood into your home? No problem. Uncle Sam will cover your losses and fix the river. Did crazed teenagers shoot and kill innocent children in a school library? Don't worry. More gun-control legislation will ensure that such massacres never happen again. Did you get sick on some tainted turkey? Can your children access porn sites on the Internet? Did a waiter in some restaurant take too long to serve a Latino family? Is there a nasty ethnic conflict in the Balkans? Not to worry. Uncle Sam and his minions will solve all problems."

I looked up to chart the progress of my cut, then continued: "But social engineering is impossible, no less so on the international than on the domestic front. Many of my conservative friends don't grasp this fact. They generally agree that government isn't to be trusted to interfere in economic matters because they recognize rightly that government is institutionally incapable of making things better. Politicians and government regulators are too ham-fisted and detached from the countless details and nuances of the markets to do anything but make matters worse.

"But this good judgment about the institutional limitations of government disappears when it comes to military adventures. These same conservative friends innocently trust not only the motives of politicians who get us involved in foreign military campaigns, but also their abilities.

"I ask why? If we can't trust Bill Clinton and his appointees to craft a worthwhile statute to restrict access to guns or to reduce greenhouse gases, why can we trust him to deploy in another region of the world the most powerful military machine humankind has ever known? Why should such government actions be trusted not to breed larger problems than those that they are meant to solve? Are politicians wiser on the foreign front than on the domestic front? Hardly."

My hairdresser thought for a moment. "*But if you're right, we shouldn't trust government to use the military to defend even our own shores against aggressors.*"

"Entrusting anyone, for any reason, with the power to coerce others is inherently dangerous. But, again, if our armed forces are charged only with defending Americans from foreign aggression, it's far easier for citizens to tell if the military is being used appropriately. All we need to ask is 'Have we been attacked or are we on the verge of being attacked?' If the answer is 'yes,' then—and only then—should our military swing into action. Of course, reasonable people can disagree about whether or not, in some instances, we are on the verge of being attacked. But at least the goal is clear and unambiguously just. That goal is national defense. By sticking to this goal, we mind our business, make far fewer enemies, and avoid unexpectedly opening cans of worms. Also, we citizens can better monitor the appropriateness of our government's use of its most potent weapon, the military. In an imperfect world, these are stellar achievements."

I don't know if I persuaded my hairdresser. But I do know that NATO bombs and ground troops will not create a civil and peaceful society in Kosovo. □

Immoral, Unconstitutional War

by David N. Mayer

The United States has no vital interests at stake in Yugoslavia; the conflict there is the kind of European war that Americans should avoid if we follow the advice of the early American presidents, beginning with George Washington in his famous Farewell Address. The situation in Yugoslavia has been ably summarized by journalist Philip Terzian: "We are bombing a sovereign nation, not a member of NATO, which is not disturbing its neighbors but seeking, instead, to prevent one of its provinces from seceding. Bear in mind that the United States fought a bloody, four-year civil war, on the issue of secession (we're against it) and that NATO, in its action against the Serbs, now proposes to invade a European state—in the Balkans, no less—to resolve an internal ethnic dispute. For the first time since 1945, the German air force is in action against another European country. And everyone agrees that air assaults are not conclusive. In order to achieve what we want, it might well be necessary to introduce ground troops."

The Clinton administration's decision to bomb Yugoslavia, under the rubric of NATO, is an incredible foreign policy blunder. Not only is the situation there none of the United States' business, but our participation in the NATO bombings also threatens to destabilize eastern Europe far more than anything done by Slobodan Milosevic's government. (Indeed, it can be argued that the bombing of Kosovo worsened the so-called "ethnic cleansing" and other atrocities being committed by Serbian or Yugoslav forces in that province.) Critics of the United States and of the West generally can point to the bombings as clear evidence of Western "imperialism." Undoubtedly, many communists and other leftists in the new NATO member nations of Poland, Hungary, and the Czech Republic are doing just that—possibly setting back for decades whatever progress in foreign relations the United States has made in eastern Europe since the fall of the Soviet Union.

Regardless of the outcome of the war itself politically—whether it will bring about the demise of Slobodan Milosevic, and at what price—the lasting importance of the war to Americans will be its significance constitutionally. What it reveals is that the actual balance of power in matters of foreign policy has shifted decisively toward the President, and that Congress has failed utterly to function as the institution the Framers of the Constitution intended it to be. What that signifies, in terms of the concentration of unchecked power in the White House, should be a matter of profound concern to all Americans.

The Wisdom of the Framers

The Framers of the Constitution gave the power to declare war to Congress, and not to the President, because they recognized that the people have a vital stake in war: it

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involves the expenditure of American tax dollars as well as the loss of American lives. For that reason, Congress must be involved in making the initial decision to commit American forces abroad. As James Madison explained in 1793, the momentous questions of war and peace properly belong to the legislature, where they can be publicly debated by the people's representatives.

The decision to declare war—that is to say, the decision to initiate the use of force aggressively and not in self-defense—is a decision that only the Congress can make. The debate over war—indeed, the debate not only over strategy (war versus economic sanctions) but also whether any American intervention is justified, as a matter of policy—should have taken place publicly in both houses of Congress, not in the Oval Office among a clique of presidential advisers. By committing the United States to a course that led inevitably to war without the explicit authorization of Congress, President Clinton committed an act that violates the Constitution.

Congress's exclusive power to declare war under Article I, Section 8, is not the only provision of the Constitution violated by Bill Clinton's war in Yugoslavia. Arguably, the Yugoslav war also violates the first clause of Article I, Section 8, which limits Congress's taxing power—and hence, the U.S. government's spending power—to matters that concern "the common Defence and general Welfare of the United States." Nothing in the Constitution authorizes the President, even with Congress's consent, to use the military forces of the United States not for national defense, but for offensive military actions in Europe—in effect to transform the U.S. military into a kind of Peace Corps with guns. Moreover, Article II, Section 2, provides, "The President shall be Commander in Chief of the Army and Navy of the United States." By committing U.S. troops to a NATO operation, under NATO command (whether or not the NATO commander is an American), Clinton has abdicated his legitimate power as commander-in-chief (the power to actually wage war) in the name of asserting a fictitious power as commander-in-chief (the power to enter into war) that in fact usurps Congress's legitimate authority.

Some legal scholars have advanced the extraordinary argument that Congress has neither a constitutional obligation nor a right to declare war before the United States joins in a "police action" sanctioned by either the United Nations or NATO. They argue that U.S. ratification of the U.N. Charter and of the North Atlantic Treaty after World War II made us part of a "new world order" in which member nations can no longer "make war," in the classic sense. The implication of this argument is that the Article I, Section 8, grant of the war-making power to Congress has been rendered obsolete since 1945. Even with concurrence of the Senate, however, the President cannot amend the Constitution; only the people can do that, according to the amendment procedures prescribed by the Constitution itself. Until that happens, the Constitution binds all the branches of government, especially the President, who has no higher obligation than his duty to adhere to the oath he swore, to "preserve, protect, and defend" the Constitution.

Charter Violations

NATO's attack on Yugoslavia, moreover, violates both the United Nations Charter and NATO's basic charter, the North Atlantic Treaty. Article 2(4) of the U.N. Charter requires that members "refrain in their international relations from the threat or use of force against the territorial integrity or political independence of any state." Similarly, Article 2(3) states, "Members shall settle their international disputes by peaceful means." No matter how great a thug Slobodan Milosevic may be—no matter what atrocities the Serbians commit in Kosovo—no member of the United Nations has a right, under the U.N. Charter, to initiate the use of force against Yugoslavia. Article 51 of the Charter does recognize the "inherent right of individual or collective self-defense" for all members, but the bombing of Belgrade is not self-defense; it is an act of aggression. Similarly, Article 5 of the North Atlantic Treaty contemplates use

of military power only defensively, not offensively; it provides, "an armed attack on one or more [members] . . . shall be considered an attack against them all," clearly a defensive provision. Needless to say, Yugoslavia has not attacked any NATO member.

NATO was created for the purposes of mutual defense (by the United States and western European nations) against a hostile Soviet Union. With the Soviet Union no longer existing, one might ask whether NATO itself is today obsolete. Even if we assume that Russia poses a great threat, NATO's legitimacy still rests on its fundamental purpose as a defensive alliance. Nothing in NATO's charter allows it to become a general European police force, which is what it has now become.

Advocates of presidential war power (whether defending George Bush's war in the Persian Gulf or the various actions in which Bill Clinton has committed U.S. military forces in such places as Haiti, Bosnia, and now Kosovo) also have asserted that the need for an international consensus prior to a NATO- or U.N.-sanctioned "police action" provides a sufficient check on presidential power. The validity of that argument, however, is belied by these presidential military actions themselves. It is not surprising that both Presidents Bush and Clinton bypassed Congress and the American people, choosing instead to first assemble international support. Of course other nations will approve "police actions" staffed almost entirely by U.S. troops and funded almost entirely by U.S. taxpayers. To be effective, the check on presidential powers must be given to Congress because Congress is directly representative of the American people, who must pay for these "police actions" with their taxes and their blood. International politics cannot adequately substitute for the checks and balances of the Constitution.

The Framers of the Constitution carefully devised a scheme of separation of powers and checks and balances to minimize the dangers of concentrating too much power in the hands of any one person, or group of persons. They would be appalled at the resolutions in Congress expressing unqualified support of the president in whatever actions he should decide to take—resolutions that reveal the degree to which Congress has failed to fulfill its constitutional obligation to act as a check on presidential power. Nothing could be farther from the intent of the Framers. As Thomas Jefferson explained it in 1798, "Free government is founded in jealousy, and not in confidence; it is jealousy and not confidence which prescribes limited constitutions, to bind down those whom we are obliged to trust with power. . . . In questions of power, then, let no more be heard of confidence in man, but bind him down from mischief by the chains of the Constitution."

The Other Costs of War

American involvement in war is too important a matter to be left to the private deliberations of the president and a small group of advisers. Surely the lives of tens of thousands of Americans lost in Korea and Vietnam—wars in which other presidents unilaterally embroiled the country—bear eloquent witness to the other, noneconomic costs of war. Just as surely, the domestic turmoil that resulted from those conflicts, particularly Vietnam, illustrates the danger of presidents' making commitments that the American people do not wholeheartedly support.

Bill Clinton and his apologists (who include many conservatives as well as so-called "liberals") defend U.S. involvement in Yugoslavia with the argument that the United States, as the world's only superpower, has a duty to use its military force for "humanitarian" purposes. The argument assumes that Americans should take the responsibility for the world's troubles simply because their country is a superpower. But the United States is a superpower—and, indeed, also is the world's richest nation—because its legal and constitutional system more fully protects free-market capitalism and the rights of the individual than any other system anywhere in the world. Americans should not feel guilty about their wealth or power; they've earned it. And simply being successful does not make a nation responsible for the problems of other

nations, just as being successful as an individual does not make one responsible for the problems of other individuals. The fundamental rules of morality apply equally to nation-states as to individuals; and the basic rule of morality—the only rule of morality based on reason rather than emotion or mysticism—is the precept "do no harm to others." Rather than following that basic rule of good behavior (for nation-states as well as for individuals), Bill Clinton has led the United States into acts of aggression that violate the principle. And our so-called "humanitarian" effort—like similar assumed "humanitarian" policies domestically—is in fact exacerbating the problem, for the NATO bombing compounds the atrocities being committed on the people of Kosovo.

Altruism Makes Bad Policy

Morally, the essential flaw in Clinton's war on Yugoslavia is the principle of altruism that underlies it. By "altruism," I mean the moral code that asserts that people should sacrifice their own happiness or well-being to the happiness or well-being of others; the moral code that preaches that self-interest is bad but that self-sacrifice is noble, that the proper ethical posture of human beings is that of sacrificial animals to the supposed "good" of society, or some other collective. This moral code of altruism is a very old, traditional moral code that has been responsible for virtually all the evil, all the suffering, that has occurred throughout human history. It is the same moral code that underlies the atrocities being committed in Kosovo itself, where people on both sides of the ethnic conflict (Serbian and Albanian alike) ignore the rights of individuals and instead regard people as significant only as members of a collective (in this case, an ethnic group).

Tyrants throughout human history have justified their tyranny by appealing to some form of collectivism. The pharaohs of ancient Egypt, the emperors of Imperial Rome, and the kings of medieval Europe all called upon their people to sacrifice their individual well-being to that of the collective; and their accomplices were the priests, who appealed to superstition and mysticism—the supposed will of the one or more gods—to convince the people that it was a "sin" not to sacrifice their well-being to the thugs who ran the government.

In more recent times, totalitarian dictators on both the "left" and "right"—Lenin, Stalin, and Mao, as well as Hitler, Mussolini, and Perón—similarly have preached that the individual is nothing, that the collective is everything. They too have been supported by priests of sorts, namely, so-called "intellectuals" who preach either a sectarian or secular form of civic religion that also condemns as sinful the individual's pursuit of his own happiness or self-interest and extol a "duty" to serve the state. As F. A. Hayek has shown, "the road to serfdom" has taken many paths in the twentieth century. The call for "national service" that Bill Clinton and like-minded collectivists (again, both on the left and the right) made at the President's Conference on America's Future in April 1997 differs from the philosophy of other twentieth-century totalitarians only in degree, not in kind.

The principle of altruism makes bad policy, whether in domestic law or in foreign relations. In domestic law, it has made possible the welfare state and all the problems associated with it—not only economically but socially and morally—as David Kelley ably shows in his excellent new book, *A Life of One's Own*. In foreign relations, it has made possible a series of wars in the twentieth century, beginning with World War I (and Woodrow Wilson's campaign to "make the world safe for democracy"), in which young Americans were told it was their duty to sacrifice their lives not for their own country's freedom or security, but for some fancy of the foreign-policy wonks who advise the President. It's time that those of us who truly "support our troops"—those of us who believe that the lives of young Americans are too precious to waste on the follies of presidential advisers—show our support for them by calling for the immediate end of this immoral and unconstitutional war. □

The Kosovo Tangle

by Gary Dempsey

Bordering Albania and Macedonia, Kosovo is the southernmost province of present-day Serbia, which, together with Montenegro, makes up what remains of the Socialist Federal Republic of Yugoslavia. Kosovo was originally populated by the Illyrians, an ancient people who inhabited the western part of the Balkans from about 2000 B.C. The earliest known Illyrian king was Hyllus, who died in 1225 B.C., and the last was Gentius, who was defeated by the Romans in 165 B.C.[1] Although it is a point of anthropological debate, many modern Albanians contend that they are the direct descendants of the ancient Illyrians and thus the original inhabitants of Kosovo.

The first Slavs appeared around Kosovo in the late fourth century A.D. as marauders who raided Roman settlements. By the end of the eighth century, the Slavs had colonized most of the area of modern Yugoslavia, including Kosovo. Serbs are not identified until the tenth-century writings of Byzantine emperor Constantine VII. There they are described as Slavs residing in the area of present-day Kosovo, Montenegro, and Bosnia, who converted to Eastern Christianity in the ninth century. In the twelfth century, Serbs successfully fought against the Byzantine Empire to establish an independent Serbian kingdom. Kosovo was crucial to that kingdom and to the Serbian Orthodox Church for the next two centuries. In fact, virtually all of the oldest monuments in Kosovo are Serbian and most names of places have a Serbian-language root. But in 1389 the Serb dynasty fell to the Ottoman Empire at the battle of Kosovo Polje. Although they fought alongside Serbs during the battle, the vast majority of ethnic Albanians in the area converted to Islam in the fifteenth and sixteenth centuries and participated in the Ottoman administration of Kosovo.

As the Ottoman Empire declined in the eighteenth and nineteenth centuries, Kosovo became the focus of competing Serbian and Albanian independence movements. In 1878, the League of Prizren, which sought to create an independent Albanian state, was founded in Kosovo. But when the Ottoman Empire finally buckled under the weight of the First Balkan War in 1912, Kosovo was granted to Serbia pursuant to the Conference of Ambassadors held in London. By that time, however, Serbs comprised only about 20 to 25 percent of Kosovo's population.[2]

Kosovo After World War I

At the end of World War I, Croatia and Slovenia joined with Serbia to form the Kingdom of Serbs, Croats, and Slovenes, with Kosovo remaining a constituent part of Serbia. During the 1920s, Serbian authorities attempted to repopulate Kosovo with Serbs. By 1928, the Serb population in Kosovo was increased to about 38 percent, mainly because of state-organized immigration from

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inner Serbia.[3] In 1929, the Kingdom of Serbs, Croats, and Slovenes was renamed Yugoslavia.

During World War II, following Yugoslavia's defeat by the Axis Powers in April 1941, the population trend lines in Kosovo were reversed. Fascist Italy ceded the province to neighboring Albania, which had been under Axis occupation since 1939, and Kosovo was ruled as part of Italian-occupied Albania for the remainder of the war. Between 1941 and 1945, more than 70,000 Serbs fled Kosovo while 75,000 Albanians migrated there.[4]

After World War II, Kosovo was returned to Serbia. But, wanting to forge a Balkan communist federation with Albania and Bulgaria, the new Yugoslav government under Josip Broz Tito hoped that the prospect of reacquiring Kosovo would draw Albania into the pact. Tito, therefore, wanted Kosovo to remain predominantly Albanian. On March 6, 1945, he issued a decree forbidding Serbs displaced by the war from returning to their homes in Kosovo.[5] The following year, Kosovo was made an "autonomous region" within Serbia. Tito's plan to create a Balkan communist federation, however, collapsed in 1948 when Yugoslavia broke with the Soviet-led Cominform.

Nevertheless, the ethnic Albanian population in Kosovo continued to grow and to push for greater autonomy. In 1963, Kosovo was made an "autonomous province," and under Yugoslavia's 1974 constitution it was granted separate federal representation and was only formally linked with Serbia. During that period of enhanced autonomy, ethnic Albanians exercised almost complete control over Kosovo's provincial administration, but many Serbs complained of pervasive discrimination in employment and housing, and of the authorities' unwillingness to protect them from anti-Serb violence.

Kosovo After Tito

By 1981, official census data pegged Kosovo's ethnic Albanian population at 77.5 percent.[6] The same year, in the wake of Tito's death, riots broke out in Kosovo as ethnic Albanians demanded full republic status within the Yugoslav federation. In the course of the violence, Serbs and Montenegrins in Kosovo were beaten, their homes and businesses burned, and their shops looted.[7] Also, a mysterious fire was set at one of Serbia's most cherished religious shrines, the Pec Patriarchate in Kosovo, a complex of medieval churches and the historical seat of the patriarch of the Serbian Orthodox Church.[8] The civil unrest was eventually quashed by the communist authorities, but thousands of Serbs fled Kosovo following the violence.

Throughout the rest of the 1980s the Serbian Orthodox Church in Kosovo and Serbian civic groups documented numerous cases of harassment, intimidation, vandalism, destruction of Serbian monuments and churches, and attacks on Serbian priests, nuns, and civilians by ethnic Albanians. As historian Noel Malcolm reports,

> In the mid-1980s the Serbian Academy of Sciences commissioned a survey of 500 households of Serbs who had migrated to inner Serbia from Kosovo. Many of the people interviewed thought that there was a political dimension to the deterioration of conditions for the Slavs in Kosovo. . . . When giving the reasons for their migration, 41 percent mentioned "indirect pressure" from the Albanians, and 21 percent referred to direct pressure: that last category was composed of verbal abuse (8.5 percent), material damage (7.5 percent) and personal injury (5 percent).[9]

While the number of cases of abuse against Serbs varies by source, historian Miranda Vickers has concluded that "many Serbs and Montenegrins who decided to leave Kosovo [in the 1980s] had experienced intimidation, pressure, violence, and other severe abuses of their human rights because of their ethnicity."[10] Similarly, historian Richard West notes that while ethnic Albanians from Kosovo were "always ready to tell sympathetic journalists an account of their suffering under the Serbian regime . . . foreign observers failed to notice that, although the Serbs were supposed

to be the oppressors, they themselves were departing from Kosovo, complaining about the destruction of property, the desecration of graves, and many assaults and rapes."[11]

Enter Slobodan Milosevic

In April 1987, over 60,000 Serbs from Kosovo signed a petition calling on the government in Belgrade to stop the ethnic violence and intimidation aimed at them.[12] In an opportunistic attempt to raise his political profile, then Serbian Communist Party president Slobodan Milosevic traveled to Kosovo and played the nationalist card, proclaiming to Serbs everywhere, "No one should dare beat you again."[13] By October 1987, federal riot police and army troops were deployed in Kosovo following demonstrations by thousands of Serbs protesting an alleged comment by a Kosovar Albanian leader that "the incidents of [ethnic] Albanians raping Serbian women could be reduced if more Serbian women worked as prostitutes."[14] In 1989, Belgrade downgraded Kosovo's autonomy to its pre-1974 level, and Milosevic was elected president of Serbia with 65 percent of the vote. As Aleksa Djilas later noted in *Foreign Affairs*, Milosevic "succeeded because he understood the power of fear and knew how to use it for his own purposes."[15]

Following the reduction of Kosovo's autonomy, Belgrade imposed "emergency measures" in Kosovo, summarily dismissing thousands of ethnic Albanians from state-sector jobs. No part of Kosovo's society was left untouched. Even the provincial theater in Pristina was placed under "emergency management" and the theater manager removed by police officers and replaced by a Serb. The greatest changes, however, occurred in education. The teaching of Albanian history, literature, and language was reduced to a minimum. Also, ethnic Albanian students were forbidden from enrolling in secondary school unless they could pass Serbian literature and language examinations, which few could do.[16]

In 1991, ethnic Albanians responded to their diminished autonomy by forming a shadow government, complete with a president, a parliament, a tax system, and schools. Shadow president Ibrahim Rugova thereafter worked for Kosovo's independence through peaceful means, but a more militant group soon emerged.

The Kosovo Liberation Army

By the mid-1990s, the ethnic Albanian population in Kosovo had grown to between 85 and 90 percent, and the human rights conditions in the province continued to deteriorate.[17] As Human Rights Watch, a New York-based rights organization, reported,

> Since the revocation of Kosovo's autonomy, the human rights abuses against ethnic Albanians by the Serbian and Yugoslav governments have been constant. The names of the victims change, but the frequency and the manner of beatings, harassment, and political trials remain the same. It is a status quo of repression. . . . The brutality of the police continues against the population. Random harassment and beatings are a daily reality for ethnic Albanians in Kosovo, especially those in villages and smaller towns.[18]

In 1996, a shadowy separatist organization called the Kosovo Liberation Army (KLA) surfaced for the first time, claiming responsibility for a series of bombings in Kosovo. By its own admission, the KLA killed more than 50 government officials and ethnic Albanian "collaborators" over the next two years. The KLA's intention: to trigger the secession of Kosovo from the Yugoslav state. Pursuing a textbook strategy, the KLA carried out attacks on police and civilians aimed at provoking a government crackdown that would radicalize the ethnic Albanian population in Kosovo. In February 1998, the KLA intensified its attacks against Yugoslav authorities and Serb civilians. Armed KLA guerrillas attacked Serb houses in the villages of Klina, Decani, and Djakovica, and a Serb refugee camp in Babaloc. KLA guerrillas also ambushed and killed two Serb policemen patrolling on the road between Glogovac and Srbica.

A government crackdown on the KLA immediately followed, and the world soon learned that nearly 80 Kosovar Albanians, including many women and children, were killed by Serbian internal security forces in Kosovo's central Drenica region. The Yugoslav Interior Ministry claimed that the action was directed against Adem Jashari, whose family clan allegedly constituted the core of the KLA organization. On a closely supervised trip to the village of Prekaz, foreign reporters were told that government security forces had killed Jashari and destroyed the power base of the KLA organization. "We have struck at their heart and we have dealt terrorists a lethal blow," a police spokesman said.[19] The spokesman was wrong. Government-versus-guerrilla clashes continued in Kosovo, leaving more than 2,000 dead over the ensuing 14 months.

Tying the Balkan Knot

For Serbs, Kosovo is widely considered the cradle of their culture, history, and religion. In fact, over 75 percent of all Serbian cultural and national monuments are located in Kosovo, including the historic fourteenth-century monastery of Samodrezi, where the Serbian king blessed his army just before their defeat at the hands of the Ottoman Turks in 1389 and the famous Kosovo Polje battlefield—the Serbian equivalent of the Alamo. Accordingly, Yugoslav Army General Dusan Samardzic recently told a group of new officers,

> This is a turning point for Yugoslavia, when we need to show the world our military ability and might. Kosovo's integrity has been threatened by [ethnic] Albanian secessionists, with assistance from abroad. Our ancestry and posterity would never forgive us if we surrendered the cradle of Serb culture to someone else.[20]

On the other side of the dispute, ethnic Albanians outnumbered Serbs in Kosovo nearly 9 to 1 before NATO's air strikes began on March 24, 1999, and representatives of the KLA have sworn that they will not stop fighting the Serbian government until they achieved the "total liberation" of the province.[21]

The conflict in Kosovo is thus not simply a matter of Kosovar Albanians suffering under a brutal and repressive regime—which they were and are—but a complex clash of mutually exclusive political claims that are aggravated by conflicting historical grievances. As former U.S. ambassador to Yugoslavia Warren Zimmerman correctly observes,

> The competing claims of Serbs and Albanians have been hopelessly tangled in the webs of history and myth. In its essence, however, the main issue is as simple as it is intractable. The Serbian claim . . . is based primarily on the historical-cultural principle—the Jerusalem argument. The Albanian claim to independence is based largely on the demographic principle—the majority argument. Since these claims are mutually incompatible, there is little reason to believe that Kosovo will be easy to solve.[22] □

1. See John Wilkes, *The Illyrians* (Oxford: Blackwell, 1992).
2. Noel Malcolm, "The Violent History of Kosovo Doesn't Justify 'Ethnic Cleansing,'" *Washington Times*, April 14, 1998, p. A16.
3. Noel Malcolm, *Kosovo: A Short History* (New York: New York University Press, 1998), p. 282.
4. Alex Dragnich and Slavko Todorovich, *The Saga of Kosovo: Focus on Serbian-Albanian Relations* (Boulder, Colo.: East European Monographs, 1984), p. 138; and Dusan Batakovic, *The Kosovo Chronicles* (Belgrade: Plato Publishers, 1992), p. 14.
5. Branko Mikasinovich, *Yugoslavia: Crisis and Disintegration* (Milwaukee: Plyroma Publishing, 1994), p. 63.
6. Miranda Vickers, *Between Serb and Albanian: A History of Kosovo* (New York: Columbia University Press, 1998), p. 318.
7. Vickers, p. 197.
8. Ibid.
9. Malcolm, *Kosovo: A Short History*, p. 331.
10. Vickers, p. 220.
11. Richard West, *Tito and the Rise and Fall of Yugoslavia* (New York: Carroll & Graf, 1994), p. 223.
12. Ibid., p. 343.
13. Laura Silber and Allan Little, *The Death of Yugoslavia* (London: Penguin Books, 1995), p. 37.
14. Vickers, p. 226.
15. Aleksa Djilas, "Profile of Slobodan Milosevic," *Foreign Affairs*, Summer 1993, p. 84.
16. Vickers, pp. 246–48.
17. Ibid., p. 320; and International Crisis Group, *Kosovo Spring: The International Crisis Group Guide to Kosovo* (Brussels: International Crisis Group, 1998), pp. 13–14.
18. International Crisis Group, p. 13.
19. "Only One Option: A War for National Liberation, UÇK," RFE/RL Newsline, March 9, 1998.
20. Quoted in Vickers, p. 300.
21. Quoted in International Crisis Group, p. 72.
22. Warren Zimmerman, "The Demons of Kosovo," *The National Interest*, Summer 1998, p 10.

Remembering and Inventing: A Short History of the Balkans

by Peter Mentzel

Since the Federal Republic of Yugoslavia descended into bloodshed and mayhem during the summer of 1991 a number of different historical explanations for the conflict's origins and ferocity have been written. While these accounts differ in their details, in general they paint two different pictures of Balkan history. One argues that the wars of the Yugoslav succession are the result of "ancient tribal hatreds." That is, the violence in the modern Balkans is the result of hatreds dating back hundreds, if not thousands, of years. The second picture of Balkan history takes issue with this argument and offers instead a story of tolerance where each community coexisted in peace, if not harmony. This entire conversation is closely tied to the history of the development of Balkan nation-states.

Nations and States

In an attempt to address these historiographical points, this article will take one simple starting point: the Balkan nations and Balkan nation-states are all very young. None is more than 200 years old. Thus the hatreds there cannot be "ancient." In fact, the current ethnic hatreds in the Balkans, while unfortunately very real indeed, all have their roots in the statist nationalism of the nineteenth and twentieth centuries.

Balkan national ideologies were based primarily on interpretations of imported Franco-German notions of nationalism. In their most basic articulations, these theories had two aspects in common. First were the quasi-mystical organic roots of nations. They were deemed to have been always-existing, at least very ancient, entities with their own distinct characteristics. The second common aspect of this kind of nationalism was its emphasis on the state as the embodiment, or at least expression, of the nation's will.

As a result of these principles, the new states of the Balkans devoted considerable energy to the creation and/or inculcation of a nationalist history. These histories varied from place to place but were remarkably similar in their outlines. They all resembled the following model: in the Middle Ages our nations had strong and wealthy states (often empires). Then the Turk destroyed our states and subjected our nations to centuries of slavery and oppression. Finally, our national heroes rose and reclaimed our states. This outline is very basic and most serious historians, even those of Balkan origin, qualify these points with numerous caveats. However, the official "schoolbook" national histories taught in the educational systems of these states followed, and for the most part still follow, these basic points.[1]

There are two serious problems with these official nationalist histories. First, they are anachronistic, and second, their implications are extremely destabilizing.

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Origin Myths

Most of the work on nationalism and national identity over the past three or four decades has argued for their constructed, subjective nature. That is, in contrast to older concepts, nations are not organic, objectively existing entities, but have a highly subjective nature. They exist insofar as a sufficient number of people believe they exist. Also widely argued in the current literature is the modernity of nations and (the more controversial contention) that nations are the creation of states, not the other way around. In other words, the modern state created nations, or at least nationalism, as a means of raising and maintaining large conscript armies and, especially, of legitimizing itself.

If these arguments are valid, then it is clear that the medieval Balkan kingdoms (or any medieval kingdoms for that matter) were not "nation-states" and that the people who lived in them did not constitute "nations" in the post-nineteenth-century sense of that word. An important example of Balkan national origin stories is the Battle of Kosovo. Serb nationalist history uses this event as the defining moment in the history of the Serbian nation. But it is clear that although a feudal state known as the Kingdom of Serbia was defeated there, it is anachronistic to say that this kingdom was a Serbian nation-state. Indeed, only a few years after the battle, Serbian knights fought (by most accounts valiantly) as vassals of their new imperial overlord, the Ottoman Sultan, against Timur Lenk (a.k.a. Tamerlane) in central Anatolia. Likewise, it is a back-projection of modern national ideas to argue (as Serb nationalist histories do) that the Ottoman armies at the Battle of Kosovo were "Turks." They were, like their enemies at that battle, soldiers in the army of a dynastic state. There were, in fact, Christian vassals of the Sultan fighting on the Ottoman side.[2] The Balkan nationalist histories, however, portray the Balkan dynastic medieval kingdoms as nation-states and as the direct antecedents of the modern Balkan states.

Small-Power Imperialism

The other effect of these Balkan nationalist histories was to foster, perhaps unavoidably, an irredentist and militaristic foreign policy that some historians have called "small-power imperialism." Since all the modern Balkan national states self-consciously base their existence on medieval dynastic ones, the borders of those medieval states have become, quite consistently, the borders desired by the nationalist leadership of the new states. The problem is that the borders of all of the medieval states fluctuated widely over the years and always overlapped each other. The best example of this problem is Macedonia. Historically, Macedonia was a geographical term that described the area encompassed by the modern Republic of Macedonia, southwestern Bulgaria, and most of northern Greece (the Greek province of Macedonia). At one time or another, this area, or at least substantial parts of it, was ruled by the Kingdom of Serbia, the Bulgarian Empire, or the Byzantine Empire (taken by Greek nationalists as the antecedent of the Greek nation-state). Thus, during the late nineteenth century, the newly formed Serb, Bulgar, and Greek nation-states claimed the area on historical grounds.

As if the problem of overlapping "historical" claims were not daunting enough, each of the new national states also claimed territory on the basis of national identity. Again, the example of Macedonia is illustrative of the broader phenomenon. The small Serb, Bulgar, and Greek national states wanted to incorporate Macedonia (still part of the Ottoman Empire until 1912) into their own realms. In addition to their supposed historical titles to the territory, agents of these states also attempted to foster in the population of the region a sense of nationalism friendly to their own states. So Serb, Bulgar, and Greek nationalists, usually working with at least the tacit approval of their governments, tried to set up schools, clubs, and associations in Macedonia in an effort to convince the members of these institutions of their Serb, Bulgar, or Greek identity. A more pernicious side of

this process was the use of terror by armed bands of each of these nationalities when education and argument did not succeed.[3]

The objective of these activities in Macedonia (and in other highly contested regions such as the Dobruja, Thrace, and the Vojvodina) was to convince the local population to declare themselves members of one of the nations on offer. Occasionally, as in the case of Macedonia, or in the region that eventually was to become Albania, some of the locals responded by developing their own national identities (in this case Macedonian or Albanian) and, subsequently, nationalist movements.

Great-Power Imperialism

Besides nationalism, another major factor in the establishment of the Balkan national states was the influence of the Great Powers. From the late eighteenth century until the end of World War I, much of European diplomatic thinking was dominated by the so-called "Eastern Question." In its most basic form, this term referred to the set of problems surrounding the apparent weakness of the Ottoman Empire and the centripetal tendencies of many of its parts, especially those coming under the influence of nationalist intellectuals.

Of the European Great Powers, the British were, until the end of the nineteenth century, the strongest supporters of the continued maintenance of the Ottoman Empire, while the Russian government was probably the biggest external threat to the Empire. The British government wanted to maintain the Ottoman Empire as a buffer against Russian expansion in the Near East, which British diplomats and military men saw as a threat against British India. Russian imperialists, in turn, were animated by the ideas of Pan-Slavism or the ability to break out of the Black Sea basin.

During the nineteenth century, however, most of the diplomacy surrounding the Eastern Question focused on how the Ottoman Empire could be maintained, or at least divided up in as peaceful a way as possible. The Powers were very worried, correctly as it turned out, that the disintegration of the Ottoman Empire could provoke a crisis that would lead to a general European war. Such a war indeed almost broke out in 1878, averted only by Prince Otto von Bismarck's cynical, yet effective, diplomacy. Unfortunately, another Balkan crisis in the summer of 1914 spun rapidly out of control with results familiar to all of us.

Nationalism, Genocide, and "Brotherhood and Unity"

With the end of the Ottoman and Habsburg Empires in the last days of World War I, the Eastern Question effectively ended. The political map of the Balkans took on the shape it was to hold, except for a few years during World War II, until the disintegration of the Socialist Federal Republic of Yugoslavia beginning in 1991.

The map of the Balkans in 1918 represented the triumph of nationalism. The consolidation of the nation-state system, however, far from ushering in a period of peace and cooperation among the Balkan states, only created renewed tensions. The problems were caused by exactly the same factors that had led to violence during the prewar period. That is, none of the nationalists in the new Balkan states (with the important exception of the Republic of Turkey) accepted the political borders as final. Quite the contrary, the Balkan nationalists saw on the maps of the Balkans drawn up at Ste. Germaine, Trianon, and Neuilly *terrae irredenta*, territories and populations of their co-nationals crying for freedom and union with the "Motherland." In particular, Bulgarian and Greek nationalists felt that their states had been cheated out of Macedonia. Bulgaria also had lost territory to Romania (the southern Dobruja) and to Greece (Western Thrace). Albanian nationalists wanted a Greater Albania that included the province of Kosovo and swaths of Macedonia (both Serbian after 1912 and part of Yugoslavia after 1918). The Vojvodina was disputed among Hungary, Yugoslavia, and Romania.

The territorial claims of the Balkan states against each other were paralleled by the internal problems caused by the presence of sizable minority populations. Nowhere was this problem more acute than in the Kingdom of the Serbs, Croats, and Slovenes, renamed the Kingdom of Yugoslavia in 1929. While ostensibly the national state of the Yugoslavs, many of its citizens, perhaps the majority even in 1918, did not have a "Yugoslav" national identity at all, but thought of themselves as members of different nations, for example, Serbs, Croats, Slovenes, Macedonians, and so on.

Yugoslavism, the idea that all of the South Slavs constituted one nation, was popular mainly among Slovene and Croat intellectuals. There were also, however, Croat (and a much smaller number of Slovene) nationalists who thought in terms of independent or autonomous Croat or Slovene nation-states. Very few Serbs or Muslim Slavs showed much interest in Yugoslavism. Most Serbs preferred to think in terms of the creation of a Greater Serbia, while the Muslims were mostly concerned with maintaining good relations with their rulers (whoever they might be) so as to secure the free practice of their religion and the maintenance of their religious schools and socio-economic institutions.

The story of the formation of the Yugoslav state and its constitutional and national crises are beyond the scope of this short essay.[4] A generalization about this period is that the tensions between the different nationalities of Yugoslavia, and especially between the Croats and Serbs, intensified steadily during the 1920s and 1930s. The Croat fascist Ustasha organization, aided by Italy, emerged and pursued a campaign of terror against the Yugoslav state. Following the Nazi invasion of Yugoslavia in 1941 (preceded by an air attack on Belgrade by the Luftwaffe), the Ustasha leader, Ante Pavelic (1889–1959), became the ruler of the "Independent State of Croatia" (often referred to by its Croatian initials NDH). The Nazis granted their puppet state generous borders, including most of Bosnia-Herzegovina. The Ustashas actively courted the Bosnian Muslims, while at the same time considering them to be "Croats of the Muslim religion." Pavelic even ordered the construction of a mosque in Zagreb (called the Poglavnik's Mosque after his official title) in his efforts to secure the loyalty of the Muslim Slavs. Many, but certainly by no means all, of the Muslims of Bosnia-Herzegovina responded to the fascist Croat authorities, as they had responded to all outside occupiers since 1878, with cautious cooperation or at least passivity. Some of the Muslim population actively supported the Ustasha regime. There were 11 Muslim deputies in the NDH's parliament (the Sabor) and there was even a Bosnian Muslim division (called "Handzar" or scimitar) within the Waffen SS.[5] Under the leadership of the Ustashas, hundreds of thousands of Serbs, Gypsies, Jews, and "enemies of the state" were murdered. The Ustashas even had their own concentration camp at Jasenovac in northern Bosnia.

Most of the rest of Yugoslavia was partitioned among the Axis powers and their allies. Most of Slovenia was incorporated into the Third Reich. Much of the Vojvodina went to Hungary. Macedonia was occupied by Bulgaria, and most of Kosovo was joined to Italian-occupied Albania.

The Ustasha and the Axis occupation armies were opposed by two main armed guerrilla groups, commonly called the Partisans and the Chetniks. The former group was ostensibly a broad coalition of individuals and parties from all the nationalities of Yugoslavia that were united against the NDH and the foreign occupiers of the country. In practice the organization became dominated by the Communist Party of Yugoslavia led by Josip Broz, better known by the nom de guerre "Tito." The Chetniks were originally made up of mostly Serb units of the Royal Yugoslavian Army that had avoided destruction or capture by the invading Axis powers and had re-established themselves as guerrillas. Their leader, Colonel Draza Mihailovic, was a supporter of King Peter and the Yugoslav government in exile in London.

During the course of the war, the Partisans and the Chetniks began to regard each other as enemies and in fact spent much of their

time fighting each other. The Chetniks eventually became de facto collaborators with the Nazis and Ustashas against the Partisans. Partially because of this development, the Allies eventually decided to back the Partisans and Tito instead of King Peter and the Chetniks.

With the end of the war, the Partisans took control of the entire country and exacted swift revenge against collaborators, suspects of collaboration, and all enemies of the Communist Party of Yugoslavia. Mihailovic was captured and hanged. Pavelic managed to escape to Argentina, but most of his followers and their sympathizers were not so lucky: they were executed.

One of the most notorious events of this period occurred at the Austrian-Yugoslav border near the village of Bleiburg. A group of over 100,000 Croat men, women, and children fled before the advancing Partisans into southern Austria, at the time under the occupation of the British Army. Some of these refugees were indeed former Ustasha members, but many certainly were not. The Partisans demanded that they be sent back to Yugoslavia. The British commander on the scene was bound by agreements and treaties to comply, and they were sent back into Yugoslav territory into the custody of the Partisan forces. Over the next weeks between 40,000 and 100,000 of them died.[6] Overall, the war and its immediate aftermath were tremendously destructive. Some 1,014,000 people, almost six percent of the population of Yugoslavia, perished, many of them at the hands of their fellow Yugoslavs.[7]

After the Partisans had secured their victory, Yugoslavia was reorganized as a federal "peoples' republic." The Communist Party, renamed the League of Communists of Yugoslavia (LCY), at first tried to foster an interpretation of Yugoslavism that would subsume the country's different nationalities. But by the early 1960s the LCY had abandoned this policy in favor of an increasingly decentralized federal structure based on the different republics, each of which (with the important exception of Bosnia-Herzegovina) corresponded to a particular constituent nationality. These different nationally based republics were bound together by the monolithic control of the LCY (the only legal political party) and its slogan of "Brotherhood and Unity."

Not So Ancient

With this very brief history in mind, the events in the Balkans, and especially in the former Yugoslavia, since 1991 acquire a rather different complexion from "ancient tribal hatreds." It is certainly no accident that Croats and Serbs routinely call each other "Ustashas" and "Chetniks," respectively. Likewise, the Serb opposition to the independence of the Republic of Bosnia-Herzegovina must have been tinged with memories of the links between Croat and Bosnian Muslim fascists during World War II.

The extraordinary violence that has accompanied the disintegration of the Socialist Federal Republic of Yugoslavia is therefore based on the very real recollections, just within living memory, of the horrors of World War II. Those actions themselves, however, grew out of the invention and perpetuation of chauvinistic and expansionist national ideologies of the nationalists and especially the national *states* of the late nineteenth century. □

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2. Peter Sugar, *Southeastern Europe under Ottoman Rule* (Seattle: University of Washington Press, 1977), p. 21.

3. Charles and Barbara Jelavich, *The Establishment of the Balkan National States, 1804–1920* (Seattle: University of Washington Press, 1977), p. 211.

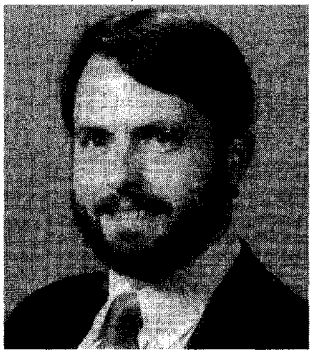
4. For a more detailed discussion of this period see Ivo Banac, *The National Question in Yugoslavia* (Ithaca, N.Y.: Cornell University Press, 1984).

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6. Jelavich, *History of the Balkans*, p. 272.

7. Ivo Banac, "Nationalism in Serbia," in Ozdogan and Saybasili, p. 143.

WAR IN THE BALKANS



Warmongering for Peace

The United States bestrides the world as a military colossus. By far the dominant global power, it is allied with every other major advanced industrialized state. America's adversaries are poor, isolated, and pitiable: Cuba, Iraq, North Korea, and Yugoslavia.

But apparently Washington policymakers can't stand the thought of living in peace. Traditionally, war has been considered a last resort. Yet this administration is implementing the most militaristic program in at least two decades. The President used U.S. troops to try to rebuild Somali society, bombed Serbian insurgents in Bosnia, warned of possible military action against North Korea, occupied Haiti, sent troops to Macedonia and Bosnia, has undertaken military exercises around the world, is conducting regular attacks on Iraq, and inaugurated aggressive war against Yugoslavia.

Obviously the administration, filled with high hubris, believed Belgrade to be an easy target. Washington was apparently convinced that it could impose an outside solution on an ancient ethnic conflict, micromanage a guerrilla insurgency, and unleash the dogs of war without their running wild.

The result was a disastrous miscalculation: the administration simultaneously magnified violence against ethnic Albanians and destabilized neighboring states. Yet U.S. officials responded to the charge that they failed to foresee the risks of their strategy by saying, essentially, yes we did. If true, the President was criminally negligent: he expected further attacks on Kosovars, massive refugee flows, and Serb intransigence, but did nothing to prepare for those consequences. Even he, one would hope, could not be so irresponsible.

It has oft been said that the world is a dangerous place, and it certainly is. But not particularly to the United States. Unfortunately, however, conflict does wrack many other countries around the world. There have been mass murders in Burundi, Cambodia, Rwanda, Sudan, and Uganda; brutal insurgencies in Angola, Congo, Ethiopia, Liberia, Mozambique, Sierra Leone, and Sri Lanka; bloody wars between Armenia and Azerbaijan, Ethiopia and Eritrea, Ethiopia and Somalia, India and Pakistan; endless civil war in Afghanistan; violent separatist campaigns in Iraq (Kurds), Mexico (Chiapans), Northern Ireland (Catholics), Russia (Chechens), Spain (Basques), and Turkey (Kurds); and varying strife in Burma, Georgia, India, Indonesia, Tajikistan, and elsewhere.

Then there is Kosovo. Without doubt, the situation is tragic. Yet the one constant of guerrilla insurgencies and civil wars is their brutality—by both sides. The Serbian government has caused many civilian casualties in Kosovo, but its conduct does not exist in a vacuum. Last June a U.S. diplomat in Belgrade told me: "If you're a Serb, hell yes, the KLA [Kosova Liberation Army] is a terrorist organization." Even ethnic Albanians admit

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that the KLA had targeted Serb policemen and other government employees, Serbs viewed as abusing Kosovars, as well as Albanian "collaborators." Each cycle of violence spawned another.

The resulting suffering of Kosovars was obvious. Yet at least until NATO intervened, the fighting in Kosovo barely rose to the status of atrocity in today's world. It certainly did not constitute genocide, a term now tossed around with wild abandon. At least three times as many people died in January alone in Sierra Leone as in Kosovo last year. Nearly as many people died in one three-day battle between Tamil guerrillas and the Sri Lankan government last fall as in Kosovo in all of 1998. By any normal standard, events in Kosovo are less important than those in many other nations around the world, where tens of thousands, hundreds of thousands, and even millions have died.

In 1991 the West encouraged the breakup of Yugoslavia. Then the United States and Europeans decided that Serbs were not entitled likewise to secede from Croatia and Bosnia, the latter of which burgeoned into a particularly bloody conflict. NATO eventually lent its air force to Muslims in Bosnia and helped impose the bizarre Dayton accord, under which three antagonistic groups are supposed to live together in an artificial state ruled by international bureaucrats. The same hypocrisy is being played out in Kosovo—Washington unreservedly supports Britain, Spain, and Turkey, for instance, in combating violent separatists, has placed no pressure on Macedonia to offer autonomy to its ethnic Albanians, and ignored massive ethnic cleansing of Serbs by Croats in 1995.

Indeed, contrast U.S. policy toward Turkey. Slobodan Milosevic is a demagogic thug. But the behavior of his government toward Albanians looks a lot like that of Turkey, a NATO member and U.S. ally participating in the assault on Yugoslavia, toward the Kurds. An oppressed people, the Kurds are seeking the right of self-determination. In response, Ankara destroys Kurdish villages and ruthlessly restricts civil liberties and political freedoms of Kurdish sympathizers. Some 37,000 Kurds have died over the last decade.

But the administration has voiced no outrage, proposed no bombing, demanded no occupation. To the contrary, Washington supplies the weapons Turkey uses to repress Kurdish separatists and apparently helped Ankara capture rebel head Abdullah Ocalan. There is much to criticize about Ocalan's Kurdistan Workers' Party, of course, but one could make similar judgments regarding the KLA. Hypocritical is perhaps the most charitable characterization of the administration's policy. Although Washington need not act everywhere if it desires to implement a policy of humanitarian intervention, surely some objective standards are necessary. The administration has articulated none. In practice, Washington seems prepared to use military force under three conditions:

- those being killed are white Europeans;
- the perceived aggressor is not a U.S. ally; and
- there is saturation media coverage of the conflict.

This makes a mockery of the humanitarian pretensions advanced by Western leaders. Nor is there anything compassionate about sending others off to fight. It's one thing to ask young men (and now young women) to risk their lives for their own political community. It is quite different for armchair warriors to treat them like gambit pawns to be sacrificed in some international chess game.

The administration's faux humanitarianism creates severe practical problems as well. In particular, it encourages intensification of local conflict. Guerrillas like the KLA often undertake strikes in order to spark retaliatory atrocities that might bring outside intervention. Kosovar leaders long sought to influence media coverage. One activist admitted to me last summer that the prospect of NATO intervention "depends on how we look on CNN."

Washington needs to return to the foreign policy of a republic, not an empire. It should be a shining city on a hill, an example to others, not the dictatress to the world. □

Isolationism

by Frank Chodorov

Isolationism has been turned (by our politicians, our bureaucracy and its henchmen, the professorial idealists) into a bad word.

And yet, isolationism is inherent in the human makeup. It is in the nature of the human being to be interested first in himself, and second in his neighbors. His primary concern is with his bread-and-butter problems, to begin with, and then in the other things that living implies: his health, his pleasures, the education of his children, wiping out the mortgage on the old homestead, and getting along with his neighbors. If he has the time and inclination for it, he takes a hand in local charities and local politics. If something happens in his state capital that arouses his ire or his imagination, he may talk to his neighbors about the necessity of reform; that is, if the reform happens to engage his interests. Taxation always interests him. But events and movements that occur far away from his immediate circumstances or that affect him only tangentially (like inflation or debates in the U.N.) either pass him by completely or, if he reads about them in the newspapers, concern him only academically. A Minnesotan may take notice of a headline event in Florida, as a conversation piece, but he is vitally interested in what has happened in his community: a fire, a divorce case, or the new road that will pass through. How many people know the name of their congressman or take the slightest interest in how he votes on given issues?

It has become standard procedure for sociologists and politicians to take opinion polls and to deduce behavior patterns from such data. Yet, it is a fact that the subject matters of these polls do not touch on matters in which the questionees are vitally interested, but are topics in which the pollsters have a concern. Putting aside the possibility of so framing the questions as to elicit replies the pollsters want, the fact is that the pride of the questionees can well influence their answers. Thus, a housewife who has been asked for her opinion on South African apartheid, for instance, will feel flattered that she has been singled out for the honor and will feel impelled to give some answer, usually a predigested opinion taken from a newspaper editorial; she will not say honestly that she knows nothing about apartheid and cares less. On the other hand, if she were asked about the baking of an apple pie, she would come up with an intelligent answer; but the sociologists are not interested in knowing how to bake an apple pie.

The scientist immersed in the laboratory will weigh carefully any question put to him regarding the subject matter of his science and will probably not come up with a yes-or-no answer; but he is positive that the nation ought to recognize the Chinese communist regime, because he heard another scientist say so. The baseball fan who knows the batting average of every member of his team, on the

Frank Chodorov (1887-1966) was editor of The Freeman *in 1954 and 1955. This is excerpted from his autobiography* Out of Step *(Devin-Adair, 1962). Reprinted with permission.*

other hand, will denounce the recognition of the regime because he has heard that the "Reds" are no good. The student whose grades are just about passing will speak out boldly on the U.N., reflecting the opinion of his professor on that organization. Everybody has opinions on international subjects, because the newspapers have opinions on them, and the readers like to be "in the swim." That is to say, interventionism is a fad stimulated by the public press, and like a fad, had no real substance behind it. If a poll were to be taken on the subject of our going to war, the probability is that very few would vote for the proposition; yet, war is the ultimate of interventionism, and the opposition to it is proof enough that we are isolationist in our sympathies. A poll on the subject of isolationism—something like "Do you believe we ought to keep out of the politics of other nations and ought to let them work out their problems without our interference?"—might bring out some interesting conclusions; but the politicians and the energumens of interventionism would prefer not to conduct such a poll. Our "foreign-aid" program has never been subjected to a plebiscite.

A Natural Attitude

Isolationism is not a political policy, it is a natural attitude of a people. It is adjustment to the prevailing culture within a country, and a feeling of security within that adjustment. The traditions, the political and social institutions, and the moral values that obtain seem good, the people do not wish them to be disturbed by peoples with other backgrounds and, what is more, they do not feel any call to impose their own customs and values on strangers. This does not mean that they will not voluntarily borrow from other cultures or that they will surround themselves with parochial walls. Long before interventionism became a fixed policy of the government, American students went to Europe to complete their education and immigrants introduced their exotic foods to the American table. But these were voluntary adoptions, even as we welcomed German and Italian operas and applauded the British lecturers who came here to decry our lack of manners. We certainly enjoyed the bananas and coffee imported from Latin American countries, and, while we might deplore their habit of setting up dictatorships, we felt no obligation to inject ourselves into their political affairs; that was their business, not ours.

This was the general attitude of the American people before the experiment in interventionism known as World War I. Before that event, Woodrow Wilson had taken leave of his senses in backing one revolutionary leader against another in Mexico, and had even sent the marines to support his choice; his excuse for opposing Huerta was that that leader had not been "democratically" elected, overlooking the fact that 80 percent of the Mexicans were simply incapable of making a choice, or of caring about it. From that interventionary exploit we garnered a mistrust of American intentions vis-à-vis Mexico which haunts us to this day. But, Wilson's urgency to introduce "democracy" in Mexico was purely a personal idiosyncrasy, shared by his political entourage but not by the American people. We cared little about which brigand, Huerta or Carranza, got to the top, and were stirred up only by the fact that a number of American boys were killed in Wilson's invasion.

When World War II got going in Europe and it became evident that Roosevelt was intent on getting us into it, a group of Americans organized the America First Committee for the purpose of arousing the native spirit of isolationism to the point of frustrating his intent. They were for keeping the nation neutral. For various reasons (particularly Pearl Harbor) their plan failed, even though at the beginning they gained the adherence of many Americans. One flaw in their program was a tendency toward protectionism; the anti-involvement became identified with "Buy American" slogans and with high tariffs; that is, with economic, rather than political, isolationism. Economic isolationism—tariffs, quotas, embargoes, and general governmental interference with international trade—is an irritant that can well lead to war, or political interventionism. To build a trade wall around a country is to invite reprisals, which in turn make for misun-

derstanding and mistrust. Besides, free trade carries with it an appreciation of the cultures of the trading countries, and a feeling of goodwill among the peoples engaged. Free trade is natural, protectionism is political.

The America First Committee's opposition to our entry into the war was based on political and economic considerations. It is a well-known fact that during a war the state acquires powers which it does not relinquish when hostilities are over. When the enemy is at the city gates, or the illusion that he is coming can be put into people's minds, the tendency is to turn over to the captain all the powers he deems necessary to keep the enemy away. Liberty is downgraded in favor of protection. But, when the enemy is driven away, the state finds reason enough to hold onto its acquired powers. Thus, conscription, which Roosevelt reintroduced at the beginning of the war, has become the permanent policy of the government, and militarism, which is the opposite of freedom, has been incorporated into our mores. Whether or not this eventuality was in Roosevelt's mind is not germane; it is inherent in the character of the state. Taxes imposed ostensibly "for the duration" have become permanent, the bureaucracy built up during the war has not been dismantled, and interventions in the economy necessary for the prosecution of war are now held to be necessary for the welfare of the people. . . .

Fatal Conceit

As isolationism is a natural attitude of the people, so interventionism is a conceit of the political leader. There does not seem to be area enough in the world to satiate his desire to exercise his power or, at least, his influence. Just as the mayor of a town hopes to become governor of his state, a congressman, or even president, so does the president or the king of a country deem it his duty to look beyond the immediate job of running his country. Necessity limits the interventionary inclination of the head of a small country, unless, indeed, he finds a neighboring small country incapable of resisting his advances. But, given a nation opulent enough to maintain a sizable military establishment and an adequate bureaucracy, his sights are lifted beyond the borders. To be sure, his interest is always the enlightenment or the betterment of the people over whom he seeks to extend his dominion or influence, never to exploit them. Thus, Alexander the Great offered the benefits of Hellenic civilization to the people of Asia, the Roman legions carried *Pax Romana* at the tip of their spears, and Napoleon imposed French "liberté, fraternité, égalité" on the peoples of Europe, whether they wanted it or not. Hitler tried to extend the influence of Aryanism and the late British Empire was built on the premise that a taste of English civilization would do the natives good.

"Foreign policy" is the euphemism which covers up this inclination toward interventionism. About the only foreign policy consistent with the natural isolationism of a people would be one designed to prevent interference of a foreign power in the internal affairs of the country; that is, protection from invasion. But that is too limited in scope to satisfy the cravings of the government of a powerful country. Theodore Roosevelt's foreign policy was avowedly designed to spread among other peoples the benefits of American civilization—even at the end of a Big Stick. Without an income tax, he could do very little beyond the display of naval might to execute this purpose, and the job was undertaken by Woodrow Wilson. It is interesting to note that Wilson was by persuasion an antimilitarist and an isolationist; yet the exigencies of office induced him to lead the country into war and into the missionary purpose of spreading American democracy far and wide. He failed, partly because the peoples of the world were not willing to adopt the American tradition and partly because he could not break down American resistance to interventionism. It remained for Franklin D. Roosevelt, aided and abetted by the Great Depression and a great war, to do that. And now that a monstrous bureaucracy with a vested interest in interventionism is in control of our "foreign policy," the nation is committed to a program of interference in the affairs of every country in the world. □

How War Amplified Federal Power in the Twentieth Century

by Robert Higgs

After surveying the Western world in the past six centuries, Bruce Porter concluded: "a government at war is a juggernaut of centralization determined to crush any internal opposition that impedes the mobilization of militarily vital resources. This centralizing tendency of war has made the rise of the state throughout much of history a disaster for human liberty and rights."[1] As a cause of the development of big government in the United States, however, war seldom receives its due.

World War I

Despite expansion during Woodrow Wilson's first term as president, the federal government on the eve of World War I remained small. In 1914, federal spending totaled less than 2 percent of GNP. The top rate of the recently enacted federal individual-income tax was 7 percent, on income over $500,000, and 99 percent of the population owed no income tax. The 402,000 federal civilian employees, most of whom worked for the Post Office, constituted about 1 percent of the labor force. The armed forces comprised fewer than 166,000 men on active duty. Although the federal government meddled in a few areas of economic life, prescribing railroad rates and bringing antitrust suits against a handful of unlucky firms, it was for most citizens remote and unimportant.

With U.S. entry into the Great War, the federal government expanded enormously in size, scope, and power. It virtually nationalized the ocean shipping industry. It did nationalize the railroad, telephone, domestic telegraph, and international telegraphic cable industries. It became deeply engaged in manipulating labor-management relations, securities sales, agricultural production and marketing, the distribution of coal and oil, international commerce, and markets for raw materials and manufactured products. Its Liberty Bond drives dominated the financial capital markets. It turned the newly created Federal Reserve System into a powerful engine of monetary inflation to help satisfy the government's voracious appetite for money and credit. In view of the more than 5,000 mobilization agencies of various sorts—boards, committees, corporations, administrations—contemporaries who described the 1918 government as "war socialism" were well justified.[2]

During the war the government built up the armed forces to a strength of four million officers and men, drawn from a prewar labor force of 40 million persons. Of those added to the armed forces after the U.S. declaration of war, more than 2.8 million, or 72 percent, were drafted.[3] Men alone, however, did not make an army. They required barracks and training facilities, transportation, food, clothing, and

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health care. They had to be equipped with modern arms and great stocks of ammunition.

As the mobilization began, the requisite resources remained in the possession of private citizens. Although manpower could be obtained by conscription, public opinion would not tolerate the outright confiscation of all the property required to turn the men into a well-equipped fighting force. Still, ordinary market mechanisms threatened to operate too slowly and at too great an expense to facilitate the government's plans. The Wilson administration therefore resorted to the vast array of interventions mentioned earlier. All may be seen as devices to hasten the delivery of the requisite resources and to diminish the fiscal burden of equipping the huge conscript army for effective service in France.

Notwithstanding those contrivances to keep the Treasury's expenses down, taxes still had to be increased enormously—federal revenues rose by nearly 400 percent between fiscal 1917 and fiscal 1919—and even greater amounts had to be borrowed. The national debt swelled from $1.2 billion in 1916 to $25.5 billion in 1919.

To ensure that the conscription-based mobilization could proceed without obstruction, critics had to be silenced. The Espionage Act of June 15, 1917, penalized those convicted of willfully obstructing the enlistment services by fines up to $10,000 and imprisonment as long as 20 years. An amendment, the Sedition Act of May 16, 1918, went much further, imposing the same severe criminal penalties on all forms of expression in any way critical of the government, its symbols, or its mobilization of resources for the war. Those suppressions of free speech, subsequently upheld by the Supreme Court, established dangerous precedents that derogated from the rights previously enjoyed by citizens under the First Amendment.

The government further subverted the Bill of Rights by censoring all printed materials, peremptorily deporting hundreds of aliens without due process of law, and conducting—and encouraging state and local governments and vigilante groups to conduct—warrantless searches and seizures, blanket arrests of suspected draft evaders, and other outrages too numerous to catalog here. In California the police arrested Upton Sinclair for reading the Bill of Rights at a rally. In New Jersey the police arrested Roger Baldwin for publicly reading the Constitution.[4]

The government also employed a massive propaganda machine to whip up what can only be described as public hysteria. The result was countless incidents of intimidation, physical abuse, and even lynching of persons suspected of disloyalty or insufficient enthusiasm for the war. People of German ancestry suffered disproportionately.[5]

When the war ended, the government abandoned most, but not all, of its wartime control measures. The draft itself ended when the armistice took effect on November 11, 1918. By the end of 1920 the bulk of the economic regulatory apparatus had been scrapped, including the Food Administration, the Fuel Administration, the Railroad Administration, the War Industries Board, and the War Labor Board. Some emergency powers migrated into regular government departments such as State, Labor, and Treasury and continued in force. The Espionage Act and the Trading with the Enemy Act remained on the statute books. Congressional enactments in 1920 preserved much of the federal government's wartime involvement in the railroad and ocean shipping industries. The War Finance Corporation shifted missions, subsidizing exporters and farmers until the mid-1920s. Wartime prohibition of alcoholic beverages, a purported conservation measure, transmogrified into the ill-fated Eighteenth Amendment.

Most important, the dominant contemporary interpretation of the war mobilization, including the belief that federal economic controls had been instrumental in achieving the victory, persisted, especially among the elites who had played leading roles in the wartime economic management. It was hardly surprising that 15 years later, in the depths of the Great Depression, the federal government employed the wartime measures as models for dealing with what Franklin D. Roosevelt called "a crisis in our national life comparable to war."[6]

World War II

When World War II began in Europe in 1939, the size and scope of the federal government were much greater than they had been 25 years earlier, owing mainly to World War I and its peacetime progeny, the New Deal. Federal spending now equaled 10 percent of GNP. Of a labor force of 56 million, the federal government employed about 1.3 million persons (2.2 percent) in regular civilian and military jobs and another 3.3 million (5.9 percent) in emergency work-relief programs. The national debt held outside the government had grown to nearly $40 billion. Most important, the scope of federal regulation had increased immensely to embrace agricultural production and marketing, labor-management relations, wages, hours, and working conditions, securities markets and investment institutions, petroleum and coal marketing, trucking, radio broadcasting, airline operation, provision for income during retirement and unemployment, and many other objects.[7] Notwithstanding those prodigious developments, during the next six years the federal government would assume vastly greater dimensions—in some respects its greatest size, scope, and power ever.[8]

During the war the conscript-based armed force, which ultimately comprised more than 12 million men and women, required enormous amounts of complementary resources for its housing, subsistence, clothing, medical care, training, and transportation, not to mention the special equipment, arms, ammunition, and expensive weapons platforms that now included tanks, fighter and bomber aircraft, and naval aircraft carriers.

For the Treasury, World War II was ten times more expensive than World War I. Many new taxes were levied. Income taxes were raised repeatedly, until the personal income-tax rates extended from a low of 23 percent to a high of 94 percent. The income tax, previously a "class tax," became a "mass tax," as the number of returns grew from 15 million in 1940 to 50 million in 1945.[9] Even though federal revenues soared from $7 billion to $50 billion between 1940 and 1945, most war expenses still had to be financed by borrowing. The publicly held national debt rose by $200 billion, or more than fivefold. The Federal Reserve System itself bought some $20 billion of government debt, thereby serving as a de facto printing press for the Treasury. Between 1940 and 1948 the money stock (M1) increased by 183 percent, and the dollar lost nearly half its purchasing power.

The authorities resorted to a vast system of controls and market interventions to get resources without having to bid them away from competing buyers in free markets. By fixing prices, directly allocating physical and human resources, establishing official priorities, prohibitions, and set-asides, then rationing the civilian consumer goods in short supply, the war planners steered raw materials, intermediate goods, and finished products into the uses they valued most. Markets no longer functioned freely; in many areas they did not function at all.[10]

World War II witnessed massive violations of human rights in the United States, apart from the involuntary servitude of the military conscripts. Most egregiously, about 112,000 blameless persons of Japanese ancestry, most of them U.S. citizens, were uprooted from their homes and confined in concentration camps without due process of law. Those subsequently released as civilians during the war remained under parole-like surveillance. The government also imprisoned nearly 6,000 conscientious objectors—three-fourths of them Jehovah's Witnesses—who would not comply with the service requirements of the draft laws.[11] Signaling the enlarged federal capacity for repression, the number of FBI special agents increased from 785 in 1939 to 4,370 in 1945.[12]

Scores of newspapers were denied the privilege of the mails under the authority of the 1917 Espionage Act, which remained in effect. Some newspapers were banned altogether.[13] The Office of Censorship restricted the content of press reports and radio broadcasts and censored personal mail entering or leaving the country. The Office of War Information put the government's spin on what-

ever it deigned to tell the public, and the military authorities censored news from the battlefields, sometimes for merely political reasons.

The government seized more than 60 industrial facilities—sometimes entire industries (for example, railroads, bituminous coal mines, meatpacking firms)—most of them in order to impose employment conditions favorable to labor unions engaged in disputes with the management.[14]

At the end of the war most of the economic control agencies shut down. But some powers persisted, either lodged at the local level, like New York City's rent controls, or shifted from emergency agencies to regular departments, like the international trade controls moved from the Foreign Economic Administration to the State Department.

Federal tax revenues remained high by prewar standards. In the late 1940s the IRS's annual take averaged four times greater in constant dollars than in the late 1930s. In 1949, federal outlays amounted to 15 percent of GNP, up from 10 percent in 1939. The national debt stood at what would have been an unthinkable figure before the war, $214 billion—in constant dollars, roughly a hundred times the national debt in 1916.

The prevailing interpretation of the wartime experience gave unprecedented ideological support to those who desired a big federal government actively engaged in a wide range of domestic and international tasks. To many, it seemed that a federal government capable of leading the nation to victory in a global war had a similar capacity to remedy peacetime economic and social ills. Accordingly, in 1946 Congress passed the Employment Act, pledging the federal government to act as America's permanent macroeconomic warden.

The Cold War

The end of World War II blended into the beginning of the Cold War. In 1948 the government reimposed the military draft, and over the next 25 years conscription was extended time and again. After 1950 the military-industrial-congressional complex achieved renewed vigor, sapping 7.7 percent of GNP on average during the next four decades—cumulatively some $11 trillion dollars of 1999 purchasing power.[15]

During the Cold War the government's operatives committed crimes against the American people too numerous to catalog here, ranging from surveillance of millions of innocuous citizens and mass arrests of political protesters to harassment and even murder of persons considered especially threatening.[16] *C'est la guerre.* The government's reprehensible actions, which many citizens viewed only as abuses, we can apprehend more plausibly as intrinsic to its constant preparation for and episodic engagement in warfare. □

1. Bruce D. Porter, *War and the Rise of the State: The Military Foundations of Modern Politics* (New York: Free Press, 1994), p. xv.

2. Robert Higgs, *Crisis and Leviathan: Critical Episodes in the Growth of American Government* (New York: Oxford University Press, 1987), pp. 123–58; James L. Abrahamson, *The American Home Front* (Washington, D.C.: National Defense University Press, 1983), pp. 101–12.

3. John Whiteclay Chambers, III, *To Raise An Army: The Draft Comes to Modern America* (New York: Free Press, 1987), p. 338, n. 68.

4. Michael Linfield, *Freedom Under Fire: U.S. Civil Liberties in Times of War* (Boston: South End Press, 1990), p. 65.

5. Ronald Schaffer, *America in the Great War: The Rise of the War Welfare State* (New York: Oxford University Press, 1991), pp. 3–30.

6. Quoted by Porter, *War and the Rise of the State*, p. 277.

7. Higgs, *Crisis and Leviathan*, pp. 159–95.

8. Abrahamson, *American Home Front*, pp. 131, 142.

9. Carolyn C. Jones, "Class Tax to Mass Tax: The Role of Propaganda in the Expansion of the Income Tax during World War II," *Buffalo Law Review*, Fall 1988/89, pp. 685–737.

10. Higgs, *Crisis and Leviathan*, pp. 196–236.

11. Abrahamson, *American Home Front*, p. 159.

12. Porter, *War and the Rise of the State*, p. 284.

13. Linfield, *Freedom Under Fire*, p. 73.

14. Ibid., pp. 102–103.

15. Robert Higgs, "The Cold War Economy: Opportunity Costs, Ideology, and the Politics of Crisis," *Explorations in Economic History*, July 1994, pp. 9–10.

16. Linfield, *Freedom Under Fire*, pp. 113–67.

Another Place, Another War

by Michael Palmer

February 2, 1969: I step off the back of a CH-34, a helicopter that looks like a flying apartment building complete with side-mounted machine guns. It is so muggy you can't catch your breath.

I'm at Camp Eagle, just north of Hue, South Vietnam. It's the year after the Tet offensive of 1968. Eagle had been a holding of the 1st Cav. until the Vietcong and North Vietnamese regular army overran it. Over 3,800 Americans were killed during the 12-week offensive.

Camp Eagle looks as though it's been through a war. Nothing of value is left. The ground is strewn with trash; barbed wire is everywhere littered with blown paper, rags, and plastic sheeting. The place smells dirty, dusty, and rotten. Half-crouching, not knowing what to expect but knowing this is a place where no one likes you and everyone wants to hurt you, you make for some kind of cover. The remains of a set of hooches (wooden, screen-sided, tin-roofed sheds) will suffice. Little do we know they will be our home for the next year.

Once we get inside, the choppers take off, leaving us in a frightening silence. This is a real "what have I gotten myself into?" predicament. The realization is that whatever happens from here on out, all you will have you have now.

As we pull together to organize a cleanup and planning session, the bleakness of the situation hits. This is really it. We have nothing: no toilet paper, no pop, no sheets, no light, no power. What we do have is mud, wet, mildew, nightly sapper raids (Vietcong running through our hooches throwing bags of explosives). We eventually have "122 mm" rocket attacks, where the 'Cong makes a bamboo fork large enough to hold a six-foot-long bottle rocket and tries to hit you with it. From a couple of miles away they are surprisingly accurate—though accuracy doesn't matter. The fear they generate is the real intent.

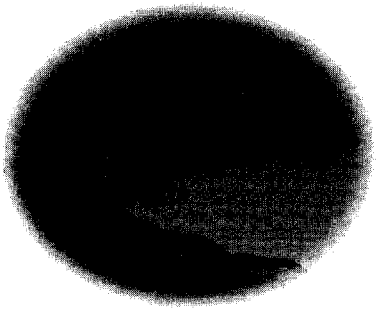
Being in an assault helicopter unit with the 101st Airborne has its rewards. There is a certain military prestige to such an assignment. Reality is less glamorous. Our assignment is the Ashau Valley. We are to support the various firebases and LZs (landing zones) strung out up and down the valley. The Vietcong uses the valley as a highway to supply the south from the north and China. The firebases are small artillery outposts positioned with fire zones to control any traffic.

The living conditions at these firebases are the most primitive any of us have ever seen. Imagine a mountaintop blasted bare of any vegetation, a rough circle of mud ringed with concertina wire and sandbagged bunkers. In the center of this circle is a large sandbagged depression. Artillery of any variety will be found there: eight-inch track-mounted guns, old twin-barreled anti-aircraft guns. Whatever. Everything that goes on here is to protect those guns.

You live in a hole in the ground—mud walls, insects, snakes, and rats. When it is wet it is mud, when dry, red dust. You seldom get to eat hot food, and never get to take a shower. You sleep in a wet sleeping bag night after night, week after week. Everything you own is wet, muddy, and moldy: clothes, food, and equipment.

When you can, you toast your bread. That way you don't notice the weevils. You try to think of it as whole wheat. Your water is always Kool-Aid so you don't see how brown it is. If something doesn't come out of a sealed can you don't trust it.

And you live like this until somebody decides you need to move. Doesn't matter—the terrain will be different but the situation the same.



Thirty years later, are we doing this again? For what? We lost 58,000 of my generation. For what? I lost friends; you lost sons, brothers, husbands.

We went where our government sent us. And we learned; learned not to trust, learned that politicians, out of ignorance and vainglory, can get us into situations they will not allow us to leave for fear of losing face. Who has to clean it up? Our kids, our military, who cannot question their orders.

I have three sons. The oldest is 26 and in the army. The next is 20, and the youngest is 16. My grandfather was in WWI, my dad in WWII; I was in Vietnam. Will my sons end up in the Balkans—even if "only" in a peacekeeping force? Americans will undoubtedly be in Kosovo for a long time.

The politicians wax eloquent about the humanitarian war against Serbia. Where's the humanitarianism in sending Americans to the backwater of Europe while taking sides in a bloody conflict over land? Have they nothing better to do with their lives than become fodder for a president's legacy or an obsolete alliance's credibility?

George Washington, in his Farewell Address in 1796, said that "Europe has a set of primary interests which to us have none or a very remote relation." He wondered: "Why forego the advantages of so peculiar a situation? Why quit our own to stand upon foreign ground? Why, by interweaving our destiny with that of any part of Europe, entangle our peace and prosperity in the toils of European ambition, rivalship, interest, humor, or caprice?"

As a father, as a citizen, I ask, why indeed? □

Michael Palmer lives in Colorado.

War's Other Casualty

by Wendy McElroy

"War is the health of the State." Those famous words are contained in Randolph Bourne's essay "The State," written in response to America's participation in World War I, but left unfinished because of his death from influenza in 1918.

In the introduction to *War and the Intellectuals: Collected Essays 1915–1919*—an anthology of Bourne's writings—editor Carl Resek explains the phrase: "In its proper place it meant that mindless power thrived on war because war corrupted a nation's moral fabric and especially corrupted its intellectuals." Those seven words contain a complexity of meaning that is often overlooked by those who use them. To grasp this complexity, it is necessary to explore the theoretical context within which Bourne, a left-wing writer with individualist sensibilities, wrote.

Bourne argued that in times of peace, the majority of people do not give much thought to the State, but deal instead with the Government, which may be viewed as the practical day-to-day "offices and functions" of a State. He defined "Government" as "a framework of the administration of laws, and the carrying out of the public force. Government is the idea of the State put into practical operation in the hands of definite, concrete, fallible men." The people whose jobs make Government function, such as postal workers and grade-school teachers, have no sense of sanctity about them. They are what Bourne describes as "common and unsanctified men." Even those elected to political office do not generally inspire admiration, but are usually "indistinguishable from the mass." This egalitarian attitude is part of the American republican heritage. Thus in times of peace, "the sense of the State almost fades out of the consciousness of men." People may rise to honor the flag at ball games but they have few practical reasons to contemplate the State.

The American State is more of a concept than a physical reality. It is the political structure established by the American Revolution, the Constitution, and the Bill of Rights. Governments come and go, but the State remains essentially the same. It is the State, not Government, that inspires emotions such as awe or patriotism within its citizenry because the State is considered to be sanctified by history and by the popular will. It is to the concept of the American State—not to any particular Government, Republican or Democratic—that people pledge allegiance with hands placed over their hearts.

Another key to understanding America is the concept of "Society," which Bourne referred to as "nation" or "country." Society is the collection of nonpolitical factors that constitute life in America, including: characteristic attitudes, common lore and literature, a shared history, a unique ethnic mix, the prevailing cultural norms. These nonpolitical

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factors are what make the American society different from Chinese or French society. They constitute "the American way." In times of peace, most people identify more with Society than they do with Government. For example, most define themselves more in relation to a community, religion, or ethnic heritage than in relation to a political party.

For Bourne, Society, unlike Government, is not an expression of the State, nor can it peacefully co-exist with the State because the two concepts are antagonistic. Bourne observed that "Country [society] is a concept of peace, tolerance, of living and letting live. But State is essentially a concept of power, of competition; it signifies a group in its aggressive aspects. And we have the misfortune of being born not only into a country but into a State, and as we grow up we learn to mingle the two feelings into a hopeless confusion."

The Impact of War

Bourne defined war as the ultimate act of statehood. "War is a function . . . of States," he wrote, "and could not occur except in such a system."

He argued that war so blurs the lines separating the State from Government and from Society that the lines virtually disappear in the minds of most people. Filled with emotion, the patriot loses "all sense of the distinction between State, nation and government." As Bourne described the process, "Patriotism becomes the dominant feeling, and produces immediately that intense and hopeless confusion between the relations which the individual bears and should bear towards the society of which he is a part." Thus, "Every individual citizen who in peacetimes had no function to perform by which he could imagine himself an expression or living fragment of the State becomes an active amateur agent of the Government in reporting spies and disloyalists, in raising Government funds, or in propagating such measures as are considered necessary by officialdom."

In times of war, the State and Government become virtually identical so that to oppose the Government is considered to be an act of disloyalty to the State. For example, although criticizing the president is a right regularly exercised by almost every American, such criticism becomes an act of treason when the president has just declared war. Bourne explained that "objections to the war, luke-warm opinions concerning the necessity or the beauty of conscription, are made subject to ferocious penalties, far exceeding in severity those affixed to actual pragmatic crimes."

The impact of war on Society is even more dramatic. Bourne wrote that "in general, the nation in war-time attains a uniformity of feeling, a hierarchy of values culminating at the undisputed apex of the State ideal, which could not possibly be produced through any other agency than war." Instead of its peacetime principle—live and let live—Society adopts the State's principle of a group acting "in its aggressive aspects."

This is the theoretical meaning of "war is the health of the State." In peace, people are largely defined by their Society and they interact with Government, giving little thought to the State. In times of war, the hierarchy and the power of these concepts are inverted. The Government virtually becomes the State, and Society is subordinated to both.

The Individual in Wartime

What happens to the individual when Society and Government are dominated by the State? In times of peace an individual acts according to his own conscience to secure what he believes to be in his self-interest, which usually includes pursuing prosperity and security for the family, engaging in leisure, and the like. Individuals interact peacefully in Society without any imposed coordination because the interactions are sparked by a common desire (such as attending a football game or exchanging goods for money) without any loss of individual choice.

In times of war, individuals become what Bourne refers to as "the herd." "The State is the organization of the herd to act offensively or defensively against another herd similarly organized." Members of the herd may have a

wide range of emotional and intellectual reactions to wartime events and to the war itself. Nevertheless, "by an ingenious mixture of cajolery, agitation, intimidation, the herd is licked into shape, into an effective mechanical unity, if not into a spiritual whole."

Just as the line between the State and Society blurs, so, too, does the line between the State and the individual. The State attempts to draw upon the powerful force of individual choice by appealing to the patriotism of people and asking them to make the "choice" to enlist and otherwise support the war effort. Usually, the individual obliges because in "a nation at war, every citizen identifies himself with the whole, and feels immensely strengthened in that identification." But if the individual makes the wrong choice—the choice to not volunteer, to not cooperate with wartime measures—the State reveals that choice was never the real issue. "Men are told simultaneously that they will enter the military establishment of their own volition, as their splendid sacrifice for their country's welfare, and that if they do not enter they will be hunted down and punished with the most horrid penalties. . . ."

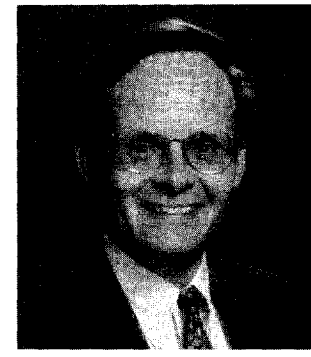
Usually, the individual does not rebel against war's massive violation of rights because he feels what Bourne called "a large element of pure filial mysticism" toward the State, especially the wartime State. Bourne likened this mysticism to the response often offered to religion. "As the Church is the medium for the spiritual salvation of men, so the State is thought of as the medium for his political salvation." The same feeling of patriotism that brings tears to the eyes of those saluting the flag at ball games is magnified by—some would say distorted and exploited by—the wartime State to make individuals conform. Feeling strengthened by "identifying with the whole," people cease to be individuals and become, instead, citizens of the State. The man who dissents and remains an individual feels "forlorn and helpless," while those who think and feel as the others in the herd have "the warm feeling of obedience, the soothing irresponsibility of protection."

Thus, a "people at war become in the most literal sense obedient, respectful, trustful children again, full of that naïve faith in the all-wisdom and all-power of the adult who takes care of them." "[T]his great herd-machine" functions under "a most indescribable confusion of democratic pride and personal fear" that makes the individuals "submit to the destruction of their livelihood if not their lives, in a way that would formerly have seemed to them so obnoxious as to be incredible." The individual became a "child on the back of a mad elephant" that he could neither control nor abandon, but was compelled to ride until the elephant decided to halt.

This, too, is the meaning of "war is the health of the State": war is the death of individualism.

Bourne's essays, written while he was on the editorial staff of the *New Republic*, are not typical of antiwar literature. He did not dwell on the "butcher's bill" of dead soldiers and civilians. He did not rail against the profits reaped by the military-industrial complex, which was collectively called "the munitions makers" in his day. The thrust of Bourne's essays is how war leads to the moral collapse of society by kicking out the props of peaceful interaction.

In essence, Bourne addressed the moral consequences of war on a postwar society that had abandoned individualism in favor of "the herd-machinery." He eloquently argued that postwar America would be morally, intellectually, and psychologically impoverished. By this observation, Bourne did not mean that peacetime America would struggle under the increased bureaucracy that never seems to roll back to prewar levels. Many historians have made this point. Bourne addressed the less tangible, though arguably more significant, costs of war. Post-1918 America, he predicted, would be burdened by intellectuals who had "forgotten that the real enemy is War rather than imperial Germany." In converting World War I into a holy war, the intellectual and psychological groundwork was being laid for future instances of what he termed "the sport of the upper class"—global conflict. □



Clinton versus Cleveland and Coolidge on Taxes

In a post-State of the Union speech in Buffalo, New York, on January 20, 1999, President William Jefferson Clinton was asked why Americans shouldn't get a tax cut since the federal budget is in surplus and the share of personal income taken by the federal government is at a post-World War II high. Is this what he said in response?

> When more of the people's sustenance is exacted through the form of taxation than is necessary to meet the just obligations of government and the expense of its economical administration, such exaction becomes ruthless extortion and a violation of the fundamental principles of a free government.

No, unfortunately, Bill Clinton didn't say that—but how refreshing it would have been if he had! Another Democratic president of long ago, Grover Cleveland (who, ironically, got his start in politics in Buffalo) said it in his second annual message to Congress in December 1886. What Bill Clinton *did* say was this:

"We could give it all back to you and *hope* you spend it right."

He went on to say he wanted to keep the surplus for such government programs as Social Security, and he concluded by tossing a question back to the audience: "I want every parent here to look at the young people here and ask yourself, 'Do you really want to run the risk of squandering this surplus?' "

Bill Clinton is not the only American president who couldn't trust the people with their own money. Nor is Grover Cleveland the only president among the 41 we've had who wanted the people to keep more of what they earned. Clinton's audacious remarks harshly contrast with the perspective of another chief executive more recent than Cleveland: Calvin Coolidge. "Silent Cal" is one of my favorites and a man who would undoubtedly spurn Clinton as a mouthpiece for an arrogant, statist elite. Let me use this opportunity to share with readers what America's 30th president thought about taxes and the people who worked hard to pay them.

"I want the people of America to be able to work less for the government and more for themselves," declared Coolidge in his inaugural address on March 4, 1925. "I want them to have the rewards of their own industry. That is the chief meaning of freedom. Until we can re-establish a condition under which the earnings of the people can be kept by the people, we are bound to suffer a very distinct curtailment of our liberty."

This flinty, frugal New Englander, who grew up respecting the hard-earned property of others, believed that the strength of the American nation was not centered in Washington, D.C. Once, as governor of Massachusetts, he asserted, "In a free republic a great government is the product of a great people.

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They will look to themselves rather than government for success. The destiny, the greatness of America lies around the hearthstone. . . . Look well to the hearthstone; therein all hope for America lies."

Bill Clinton has raised taxes in many forms, several times, and once called taxes "contributions." As one wag put it, "Clinton never saw a tax he didn't like—and hike."

Not Calvin Coolidge. As vice president, he strongly supported the steep reductions in income tax rates proposed by President Warren Harding's treasury secretary, Andrew Mellon. From the time he became president after Harding's untimely death in August 1923 until he left office in March 1929, Coolidge kept Mellon on the job and strengthened his own reputation as a committed tax cutter by urging Congress to enact further reductions. In the 1920s, the top income-tax rate fell from 73 percent to 24 percent. Americans with the lowest incomes benefited even more when the rate at the other end fell from 4 percent to one-half percent.

Between 1921 and 1929, the economy grew by nearly 60 percent, the national debt was reduced by a quarter, and the federal budget was consistently in the black. The depression that came later resulted not from tax cuts, but from unwise monetary policies of the Federal Reserve and destructive interventions by Congress, particularly in the years 1930–33.

Moreover, Coolidge understood that people respond positively to incentives, and negatively to disincentives. He knew that marginal rates of taxation made all the difference in the world in terms of economic behavior. In that sense, he was an early supply-sider—with an important difference. While today's supply-siders support tax cuts as a means to increase government revenue, Coolidge wanted to leverage tax cuts into major spending reductions. Here's what he told an audience on February 12, 1924:

> If we had a tax whereby on the first working day the government took 5 percent of your wages, on the second day 10 percent, on the third day 20 percent, on the fourth day 30 percent, on the fifth day 50 percent, and on the sixth day 60 percent, how many of you would continue to work on the last two days of the week? It is the same with capital. Surplus income will go into tax-exempt securities. It will refuse to take the risk incidental to embarking in business. This will raise the rate which established businesses will have to pay for new capital, and result in a marked increase in the cost of living.

Coolidge told a press conference on October 11, 1927, that he and others "interested in tax reduction ought to be first of all bending their energies to see that no unwise expenditures are authorized by the government, and that every possible effort is put forth to keep our expenditures down, and pay off our debt, so that we can have tax reduction." There was no Coolidge counterpart to Clinton's call for tens of billions of dollars of additional spending in his State of the Union speech last January.

According to Americans for Tax Reform (ATR), the average family today pays more in taxes than it spends on food, clothing, shelter, and transportation combined. The Census Bureau reports that the average household pays $9,445 in federal income taxes alone—twice what it paid just 14 years ago in 1985. The federal tax code is made up of four huge volumes that are each thicker than the Bible, and the tax code is over seven million words long. And ATR reports that if Congress were to adopt the fiscal 2000 budget President Clinton proposed in January, federal bureaucrats will spend more in one second ($56,000) than the average taxpayer earns in a year ($28,000).

Where is Calvin Coolidge when we really need him?! □

THE FREEMAN
Ideas On Liberty

Spontaneous Order

by Nigel Ashford

"Many human institutions are the result of human action, but not of human design."

—ADAM FERGUSON

Order has been a central preoccupation of political thinkers and philosophers throughout the ages. It is widely understood today as a state of harmony between people, or social peace. In the premodern era, however, the concept was understood as the maintenance of a stable, hierarchical order that was pre-ordained by God or nature or both. Order can also be seen as the existence of regularity and predictability in human affairs, the absence of chaos. Although no longer associated with a rigid society ranked by privilege and power, the idea of order is still highly valued. This is because it allows people with different interests and values to live together in society without resorting to discord, conflict, or civil war. This is the modern idea of spontaneous order.

The first thinker to articulate this modern concept of spontaneous order was Bernard de Mandeville, in a book called *The Fable of the Bees* (1714). This work discussed the paradox that "private vices" such as individual self-interest could lead to "public benefits" from which the whole community benefited. He observed that the sum of individuals acting from separate motives produced a commercial society that was no part of any one person's intention. This idea that the evolution of human institutions allowed individuals to serve others, even though their motive might be self-interest, was at the core of the Scottish Enlightenment that grew up around Adam Smith, David Hume, and Adam Ferguson. They sought to apply this idea to a whole range of human institutions, including commerce, law, language, human morality, and even mores and customs. Far from a narrow theory of economics, Smith's *Theory of Moral Sentiments* (1759) argued that morals evolved slowly. The principles that enabled humanity to flourish and prosper were eventually accepted by the community. They stood the test of time.

Smith, Hume, and Ferguson were fascinated at how these values and institutions grew up to greatly benefit mankind despite their being the product of no single mind. Adam Ferguson's observation that human action produced a form of social order superior to that conceived by human design was to echo

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in the thoughts of an Austrian thinker, F. A. Hayek, two centuries later. Hayek took on the ancient idea that institutions were divided between those that are "natural" and those that are "artificial." A third group existed, Hayek said, and these were social institutions. As these are regular and orderly, people suppose that they have been invented by humanity and can therefore be altered or restructured at will. Hayek pointed out that this notion was mistaken because the human mind and society had evolved together. Tearing down the institutions that kept society together and building anew, as socialists advocated, would destroy the order that made society work.

Order Without Commands

Spontaneous order keeps the wheels of society turning without the need to issue commands from the center. A free society is orderly not because people are told what to do but because the evolving traditions and inherited institutions of human society allow individuals to pursue their own ends and by so doing, meet the needs of others. People's behavior follows certain patterns because they have been accepted by society initially as they allowed the groups that adopted them to prosper. It is no accident, said Hayek, that the sharpest differences in material welfare can be seen throughout the Third World where the city meets the countryside and complex rule-guided societies meet intimate communities in which the rules are different.

The rules that allow a complex social order like a city or the global economy to function are not orders in the sense that term is usually understood. Rules that prevent individuals' injuring others or engaging in theft or fraud or breaking promises in fact give people a great deal of latitude in their behavior. They tell people how to do things, but they do not tell them what they should do.

The moral framework for human society is not set in stone, but rather is constantly changing as new rules are discovered that allow the social order to function better. The problem is that we do not know in advance which rules will work and which will not. Our existing laws and customs show us what has worked to get us to the stage society has reached, but innovation and trial and error are required if we are to continue to discover new, effective rules of which we are currently ignorant. Social institutions that keep society orderly—customs, traditions, and values—are like tools. They contain the knowledge of generations before us about how to behave and will be modified by the rising generation and then passed on to the next. Groups that adopt these rules benefit from having done so, without necessarily knowing why. The institutions that transmit information about the rules are the product of human action, but not necessarily the result of human design.

There are three categories of social rules, according to Hayek. The first consists of those that we design ourselves, such as parliamentary legislation. The second, which has been called "tacit knowledge," consists of things like a sense of fair play or injustice that we all understand but cannot put into words. Finally, there is a third group of rules of beneficial behavior that we can observe and write down, but our attempts at codification only approximate the principles. The Anglo-Saxon system of common law is an example of this third type of rule; it evolved through and was gradually refined over centuries by different cases and judgments, and it is open to modification in the future. We learn from these rules and contribute to them even though we often cannot fully explain them. It is the second and third categories that have the power to create a complex order that uses more knowledge than can ever be known by a single human mind.

Why We Need Freedom

Complex social orders require freedom because the information and knowledge that make them work can never be amassed by a central authority. Attempting to use the first category of rules—legislation—to change the second and third categories will fail because the sum total of human knowledge has allowed people in society to live with one another and brought us to the levels of prosperity and population that we now enjoy. This was seen in the old socialist states of the Sovi-

et empire, in which government attacked and undermined traditional morality, justice, and fair play while relying on the economies of the West to keep living standards from falling below subsistence levels. Freedom is critical to the process of achieving spontaneous order in society because we do not know in advance which rules will work, because liberty is essential to the trial-and-error process, and because the creative powers of man can only be expressed in a society in which power and knowledge are widely dispersed. To impose a pre-designed pattern on society would make society cease to function as a creative force. Progress cannot be commanded.

Essential to the progress of an orderly society is the distribution of power among its citizens, as opposed to the concentration of power in the hands of the state. This allows society to experiment in the rules and mores that govern people's behavior. The process of trial and error limits the impact of mistakes to a small segment of society. Rules that work will be observed, imitated, and absorbed into the social framework. Risk-taking and rule-breaking are virtually impossible in small, intimate rural societies, yet these activities are essential to maintaining the large populations that live in the vast impersonal societies of modern life.

The Role of Incentives

Life in a free society can be hard because it forces individuals to adjust to the needs of others. The free society works because it coordinates conflicting desires by creating incentives for people to satisfy their own wants by satisfying those of others. This is the opposite of a state in which one can only achieve one's aims at the expense of others. As if by an invisible hand, Adam Smith suggested, we are moved to serve the needs of others while pursuing our own self-interest.

This complex order that harmonizes and synchronizes the conflicting desires of people who are different from one another can be confusing at first. But it is essential to look beyond that initial confusion if we are to see how a free society works. When Alexis de Tocqueville first disembarked in New York in 1831, he heard what he described as "a confused hum." That great chronicler of American society wrote, "No sooner do you set foot upon American ground than you are stunned by a kind of tumult; a confused clamor is heard on every side, and a thousand simultaneous voices demand the satisfaction of their social wants." Simply trying to work out how society works by watching it and listening to it tells us little. It would be like trying to understand how a clock works by telling the time. It is how people must interact with one another that allows the clockwork of society to keep ticking.

The hum of commerce eases the path of social cooperation in a free society, in part because it offers man opportunities that are simply not available when acting alone or in a state of war of all against all. Incentives allow us to cooperate with others even though our views on political issues or our religious beliefs may radically differ. When people supply goods and services or buy them from others, they may not know with whom they deal. Protestant, Catholic, Jew, and Muslim all benefit from the commercial activity of a free society without altering their fundamental beliefs. Their security and prosperity are interdependent and in free societies far surpass those of nations where conflict marks differences of faith. These differences are resolved peaceably and profitably in a free society, because the benefits of these values have been passed down through society and have become part of the moral framework. The absence of this mechanism for transmitting moral values is one of the reasons that religious strife and social discord mark societies that have never known freedom.

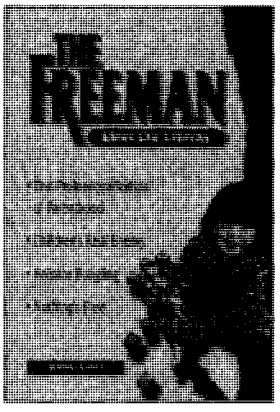
The Law

One key institution that makes the coordination of a free society possible is the law. In a free society, law is not the same as the arbitrary government decrees of totalitarian and autocratic societies or the legislation of Western congresses and parliaments. It is, as we have seen, a code that has evolved not at the hands of politicians but in the decisions of judges. Tocqueville in *Democracy in America*

(1840) described how laws keep order in a free society. He observed that "the spirit of the law which is produced in the schools and courts of justice, gradually penetrates beyond their walls into the bosom of society, where it descends to the lowest classes, so that at last the whole people contract the habits and tastes of the judicial magistrate." The law is respected in a free society not by the use of force (although governments do reserve the right to use force to protect freedom), but because it is based on rules that have grown up and been tested in real life, and because the values and the spirit of the law are closely connected to the moral values of the civilization.

Over-government undermines that respect by imposing controls on society that do not conform to people's inherited sense of right and wrong. Freedom creates order in society. The institutions of a free society give people an interest in keeping the peace, better than any police state or concentration camp. □

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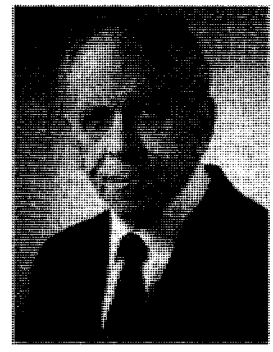
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Suicide as a Moral Issue

"Suicide is an event that is a part of human nature. However much may have been said and done about it in the past, every person must confront it for himself anew, and every age must come to its own terms with it."

—JOHANN WOLFGANG VON GOETHE (1749–1832)

Behind Goethe's simple statement lies a profound truth: dying voluntarily is a choice intrinsic to human existence. It is our ultimate, fatal freedom. That is not how the right-thinking person today sees voluntary death: he believes that no one in his right mind kills himself, that suicide is a mental health problem. Behind that belief lies a transparent evasion: relying on physicians to prevent suicide as well as to provide suicide—and thus avoid the subject of suicide—is an evasion of personal responsibility fatal to freedom.

Not long ago the right-thinking person believed that masturbation, oral sex, homosexuality, and other "unnatural acts" were medical problems whose solution was delegated to doctors. It took us a surprisingly long time to take these behaviors back from physicians, accept them comfortably, and speak about them calmly. Perhaps the time is ripe to rethink our attitude toward suicide and its relation to the medical profession, accept suicide comfortably, and speak about it calmly. To accomplish this, we must de-medicalize and destigmatize voluntary death and accept it as a behavior that has always been and will always be a part of the human condition. Wanting to die or killing oneself is sometimes blameworthy, sometimes praiseworthy, and sometimes neither; it is not a disease; it cannot be a bona fide medical treatment; and it can never justify deprivation of liberty.

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Death Transformed

Increasing life expectancy, advances in medical technology, and radical changes in the regulation of drug use and the economics of health care have transformed how we die. Formerly, most people died at home. Today, most people die in a hospital. Formerly, patients who could not breathe or whose kidneys or livers or hearts failed to function died. Now, they can be kept alive by machines, transplanted organs, and immunosuppressive drugs. These developments have created choices not only about whether to live or die but also about when and how to die.

Birth and death are unique phenomena. Absent celibacy or infertility, practicing birth control—that is, procreating voluntarily—is a

personal decision. Absent accidental or sudden death, practicing death control—that is, dying voluntarily—is also a personal decision. The state and the medical profession no longer interfere with birth control. They ought to stop interfering with death control.

As individuals, we can choose to die actively or passively, practicing death control or dying of disease or old age. As a society, we can choose to let people die on their own terms or force them to die on terms decreed by the dominant ethic. Camus maintained that suicide is the only "truly serious philosophical problem." It would be more accurate to say that suicide is our foremost moral and political problem, logically anterior to such closely related problems as the right to reject treatment or the right to physician-assisted suicide.

Faced with a particular personal conduct, we can approve, facilitate, and reward it; disapprove, hinder, and penalize it; or accept, tolerate, and ignore it. Over time, social attitudes toward many behaviors have changed. Suicide began as a sin, became a crime, then became a mental illness, and now some people propose transferring it into the category called "treatment," provided the cure is under the control of doctors.

Crucial Questions

Is killing oneself a voluntary act or the product of mental illness? Should physicians be permitted to use force to prevent suicide? Should they be authorized to prescribe a lethal dose of a drug for the purpose of suicide? Personal careers, professional identities, multibillion-dollar industries, legal doctrines, judicial procedures, and the life and liberty of every American hang on how we answer these questions. Answering such questions requires no specialized knowledge of medicine or law. It requires only a willingness to open our eyes and look life—and death—in the eye. Evading that challenge is tantamount to denying that we are just as responsible for how we die as we are for how we live.

The person who kills himself sees suicide as a solution. If the observer views it as a problem, he precludes understanding the suicide just as surely as he would preclude understanding a Japanese speaker if he assumed that he is hearing garbled English. For the person who kills himself or plans to kill himself, suicide is, eo ipso, an action. Psychiatrists, however, maintain that suicide is a happening, the result of a disease. Against this mindset, the view that, a priori, suicide has nothing to do with illness or medicine, which is my view, risks being dismissed as an act of intellectual know-nothingness, akin to asserting that cancer has nothing to do with illness or medicine.

We are proud that suicide is no longer a crime, yet it is plainly not legal; if it were, it would be illegal to use force to prevent suicide and it would be legal to help a person kill himself. Instead, coercive suicide prevention is considered a life-saving treatment and helping a person kill himself is (in most jurisdictions) a felony.

Supporters and opponents of policies concerning troubling social issues—such as slavery, pornography, abortion—have always invoked a sacred authority or creed to justify the policies they favored. Formerly, God, the Bible, the Church; now, the Constitution, Law, Medicine. It is an unpersuasive tactic: too many deplorable social policies have been justified by appeals to Scriptural, Constitutional, and Medical sanctions.

The question of who should control when and how we die is one of the most troubling issues we face today. The debate is in full swing. Once again, the participants invoke the authority of the Bible, the Constitution, and Medicine to cast the decisive ballot in favor of their particular program. It is a spineless gambit: persons who promote particular social policies do so because they believe that their policies are superior to the policies of their adversaries. Accordingly, they ought to defend their position on the grounds of their own moral vision, instead of trying to disarm opponents by appealing to a sanctified authority.

For a long time, suicide was the business of the Church and the priest. Now it is the business of the State and the doctor. Eventually we will make it our own business, regardless of what the Bible or the Constitution or Medicine supposedly tells us about it. □

THE FREEMAN
Ideas On Liberty

Storm Trooping to Equality

by James Bovard

Politicians have long enjoyed promising to deliver equality to the American people. In a January speech, President Clinton announced that he is seeking a budget increase to hire more federal agents to penalize more companies for alleged inequalities in their wage and salary structures. Clinton declared, "We have an opportunity now, and an obligation, to make sure every American fairly benefits from this moment of prosperity." However, as usual, Clinton's idea of "fairness" consists merely of politicians and bureaucrats tightening their grip over everyone else.

Clinton is asking for a $14 million increase in enforcement budgets for the Equal Employment Opportunity Commission and the Labor Department's Office of Federal Contract Compliance Programs (OFCCP). While these are small amounts, the feds are certain to use the money to extort far greater sums from private companies.

The OFCCP has jurisdiction over the jobs of 25 million people who work for companies, universities, and other entities with federal contracts. The agency has already announced plans to almost double the number of companies it investigates this year.

OFCCP Director Shirley Wilcher declared in 1995, "Enforcement of equality in the work place includes penalties to deter violations and to get results as quickly and efficiently as the law permits." Not equality of opportunity—not equal chances for equal talent—but equality, plain and simple. The passion for quick results far exceeds OFCCP's devotion to the law. In some parts of the south in the early 1900s, any company hiring a black for certain positions was presumed guilty of breaking a law. Nowadays, thanks to the OFCCP, any federal contractor who does not hire or promote a black, Hispanic, or woman can routinely be presumed guilty of breaking the law.

The OFCCP is legendary for the pretexts it concocts to accuse private companies of violating its regulations. One manager at a Washington, D.C.-area company summarized the attitude of the OFCCP official who descended upon her firm: "We don't need no stinking statistical significance!" As long as there are disparities between male and female salaries, or between the salaries of different races, the company can be proclaimed guilty.

The OFCCP routinely comes in, looks at the median pay rate for a certain job grade, and then fines the company if women or minorities make less than that amount. But this essentially ignores workers' experience, productivity, and a dozen other factors. As American Enterprise Institute economist Diana Furchtgott-Roth told the *Los Angeles Times*, "Measuring so-called discrimination by comparing women's wages to the median wage is like saying there's something wrong with oranges because they are smaller than grapefruits."

James Bovard is the author of Freedom in Chains: The Rise of the State & the Demise of the Citizen *(St. Martin's Press).*

Judging Performance

The Equal Employment Advisory Committee, an organization of large government contractors, reports that OFCCP auditors considered compensation decisions based on "performance ratings history" and "promotion, demotion, or downgrades" might be unacceptable to the OFCCP "because these may be seen as 'subjective' factors over which the employer has some control." Further, "The federal pay system with which compliance officers are most familiar is a very rigid one consisting of 15 grades and 10 steps within each grade. Over time, everyone progresses through the same series of within-grade step increases and/or promotion-related grade increases." The fact that a private company does not treat its employees like government workers—that is, paying them largely according to how long they have loitered around the office—can be interpreted by some compliance officers as foul play.

Because the rules that the OFCCP uses are vague and convoluted, compliance officers exercise arbitrary power over those whom they investigate. Expert after expert whom I interviewed stated that officers routinely grossly abuse their power. (Few people I spoke to were willing to allow their names to be used, since there is pervasive fear of agency retaliation.) One Midwest human-resources director complained of officers "just coming on site and scaring everyone to death and costing them thousands of dollars in time and effort." She observed that the OFCCP official who monitored her company for ten months "felt that he was on a crusade—and therefore the ends justified the means." Another human-resources professional noted that OFCCP agents "wield a lot of power and they know it and they very often don't act in compliance with the law and they attempt to coerce and intimidate employers into doing what they think what they should do." A female lawyer with over a quarter century's experience with OFCCP efforts said that browbeating, intimidation, and lying about the law happens "all the time." In many cases, the OFCCP arm-twists companies into paying "compensation" to people who were never hired and never did a day's work for them.

One district director in a large western state has achieved notoriety for his heavy-handed methods. According to one lawyer, the director shows up at site visits and warns the contractor: "If you get a lawyer, I will make it more difficult for you." The director has proclaimed to harrowed employees during audits: "You won't have a job around here much longer unless you cooperate with us because you are in deep trouble." Contractor employees have been left in tears at the OFCCP district director's bullying. This director's methods have been so successful at racking up settlement numbers that he has reportedly been invited to other OFCCP districts to lecture about his "enforcement model."

Jennifer Taylor, personnel director of City Utilities of Springfield, Missouri, testified to Congress in 1996 of the nightmare OFCCP audit her company experienced. An OFCCP compliance officer visited the company and spent almost an entire year going through files and documentation. After he examined the company's 250-page affirmative action plan and found no violations, he ordered the utility to completely recalculate its analyses, hoping that the revised version would produce some numbers with which he could condemn its hiring and promotion policies. The official demanded "documentation and reasons why virtually every minority and female considered for promotion and new hire was not selected for nearly every opening," Taylor testified. Though the company had roughly the same proportion of minorities on payroll as in the local labor market, the OFCCP demanded that the company in the future recruit from the Kansas City area—170 miles away. Taylor observed, "We must ignore a readily obtainable source of local labor, which is more motivated to remain with us because of our geographical preference, simply because of their race." Though the OFCCP inspector could not even gin up enough evidence to file a notice of violation, the inspection cost the company over $26,000 and tied up key personnel throughout 1995.

Despite the absurdities in OFCCP compensation analyses, many companies settle the

charges by paying the money the agency demands. This is because the agency has the power to debar companies from getting any federal contracts—a power described as a "nuclear bomb" by Assistant Secretary of Labor Bernard Anderson. Company officials routinely complain that there was no justice in the OFCCP charges but that the company cannot afford to fight the federal government and lose all its government contracts.

Clinton justified the new crackdowns last January as part of his plan "to prepare our nation for the 21st century." But if Labor Department bureaucrats are in charge of leading us into the new millennium, Americans should get ready for some thin gruel in the future.

Many OFCCP officials are both lazy and incompetent. One private lawyer who has dealt with the agency for over 25 years complained that OFCCP investigators "show up to do an onsite review at 10 in the morning and leave at 2 in the afternoon to pick up their grandkids from school. There is absolutely no control or monitoring of the kinds of hours that people are allegedly working. You can go months without catching up with someone" at the agency.

Many private lawyers and personnel experts who deal with the OFCCP complain of the extremely poor training of some of the compliance officers. The OFCCP has apparently been careful not to commit the same crime it accuses private companies of committing: requiring excessive literacy or intelligence in the people hired. One lawyer complained, "We have had OFCCP investigators who had disabilities who can't read. We had one case several years ago in which the investigator ruled that the company violated OFCCP policy because an individual was not paid the same amount as someone else working for the company—but the person who allegedly was underpaid never worked for the company. It took forever to straighten out that mess."

Legal Redress Impeded

Unfortunately, it is very difficult to fight the OFCCP in court. Because of the doctrine of "exhaustion of administrative remedies," the Labor Department can hold hostage any complaints or accusations against the OFCCP for years. Companies cannot gain access to a federal court until it has run the gauntlet of pseudo-remedies within the agency itself. Even if a company wins before a Labor Department administrative-law judge, a political appointee can simply write a memo and overturn the judge's decision—thus thrusting the company back in legal purgatory.

Lawyers estimate that legal fees in OFCCP cases can easily exceed half a million dollars before companies reach a federal court. Because of the high costs of reaching a federal judge, there have been few court rulings limiting the agency's power. As a result, OFCCP officials have free rein to twist the law to suit their purposes.

The issue of OFCCP's power cuts to the heart of the coerciveness of the welfare state. The essence of the OFCCP's concept of social justice is compelling companies to pay people for work they never did—based on secret rules the agency continually changes.

This nation does not need a cadre of employment commissars running around inflicting political correctness on American businesses. The methods of the OFCCP should be repulsive to anyone who respects legal rights and due process. As Justice Clarence Thomas wrote in a 1995 Supreme Court opinion, "Government-sponsored racial discrimination based on benign prejudice is just as noxious as discrimination inspired by malicious prejudice. In each instance, it is racial discrimination, plain and simple. Racial paternalism and its unintended consequences can be as poisonous and pernicious as any other form of discrimination."

Clinton, in his announcement of the expanded crackdown on private pay, declared that "it's a matter of principle—a question of what kind of country we want America to be today, and into the 21st century." Unfortunately, Clinton is making this a country in which petty bureaucrats have more and more power to punish other Americans on more and more pretexts. And since the process by which OFCCP settlements are imposed is fundamentally unfair, the larger the settlements, the greater the likely injustice by the government. □

Economics



In the Absence of Private Property Rights

We commonly benefit from things we neither understand nor appreciate. Obviously there are advantages in benefiting from a wide range of things without having to give them much thought. But the danger is that such neglect can often cause us great harm. Good health is an example. For most people, good health is easy to take for granted, and this often results in harmful patterns of behavior. In the case of health, however, most people know something about the risks of unhealthy behavior, and recognize the advantage of healthy habits even if they don't practice them.

Unfortunately, this is not true for maintaining a healthy economy. The productivity and cooperation essential to economic progress depend on things that are not only easily neglected, but also commonly denounced. Private property is a good example. Instead of recognizing private property as the foundation of economic cooperation and progress, people commonly see it as the source of economic problems actually caused by the lack of well-defined and enforced private-property rights.

Pollution and Private Property

Pollution is widely blamed on capitalism, with its emphasis on profits and private property. According to this view, private property rights should be restricted to prevent firms and individuals from putting their private gain ahead of the public's interest in a clean environment. But pollution is actually a problem caused by too little reliance on property rights, not too much. Pollution problems should teach us how much we benefit from private property by illustrating the inevitable breakdown in social cooperation in its absence.

Pollution problems would not exist if we could divide up the atmosphere, rivers, and oceans into separate units owned and controlled as private property. There would still be pollution, but not excessive pollution. If I wanted to discharge pollutants into the air that belonged to others, they would prevent me from doing so unless I paid them a price that covered the cost my pollution imposed on them. So I would pollute only as long as the value I realized from discharging an additional unit of pollutant was at least as great as the cost to others. Private property and the market prices that result would motivate people to take into consideration the environmental concerns of others.

Pollution problems exist because without private property in air sheds and waterways there are no market prices to make polluters mindful of the cost of their polluting activities. The result is that people pollute excessively; pollution continues even though the benefits from additional pollution are less than the costs.

Although we cannot easily imagine treating the atmosphere and waterways as private

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property, the lack of cooperation that underlies pollution problems would extend to all aspects of human action if private property were absent. Instead of seeing pollution problems as an indictment of private property, these problems should give us an appreciation of the wonderful advantages we realize from private property. And once the power of private property to promote cooperation is realized, one can see how pollution policy can be improved through the creative establishment of private property.

Instead of having political authorities dictate how, and how much, polluters have to reduce their discharges (as they do now), it would be far better to create a form of private property in the use of the environment for waste disposal. This private property would take the form of transferable pollution permits specifying how much their owners could legally pollute. These permits would establish the total allowable pollution, but not how much each polluter reduces his discharges or how he does so. With transferable permits, market prices would emerge that force polluters to consider much of the cost of their discharges. Those who could reduce discharges cheaply would reduce a lot, releasing permits to be used by those facing higher cleanup costs. The result would be a pattern of pollution reduction that yields any given level of environmental quality at far less cost than the command-and-control approach that dominates current policy. (A more detailed discussion of the advantages of such a market-based approach to pollution control has to await a future column.)

Private Property and Patience

Another common misconception is that the profits from private property motivate people to ignore the long-run consequences of their actions. Actually, the lack of private property is the biggest threat to future concerns. Consider the captain of a whaling ship who has a whale in the cross hairs of his harpoon. The captain is about to pull the trigger when his first officer points out that the whale is pregnant and if they let it live there will be two whales within a few months. Will the captain save the whale on hearing this information? Not likely. He will correctly conclude that since he has no property right in the whale, if he doesn't kill it today someone else soon will. Being patient and allowing the whale to give birth requires an immediate sacrifice, without permitting him to benefit from that sacrifice in the future. If somehow whales were privately owned, it would then pay the captain to take the future value of the whale and her offspring into consideration, since that future value would be his opportunity cost of killing the whale today.

It is no wonder that many species of wild animals are overexploited, and in some cases threatened with extinction. The situation is very different with domestic animals that are privately owned. There is no worry that chickens, pigs, cows, or goats will be driven to extinction. The future value of these animals is fully considered by owners who can profit from maintaining them. Indeed, the more of these animals we kill, the more of them we have. In the United States alone, approximately 25 million chickens are killed and eaten every day. It has been said that the difference between chicken hawks and people is that when chicken hawks eat more chickens there are fewer chickens, but when people eat more chickens there are more chickens. The more fundamental difference is that people establish private property rights and, as a result, take the future into consideration; chicken hawks don't.

Unfortunately, legislation such as the Endangered Species Act attempts to protect species by undermining private property rights, thereby reducing the motivation of land owners to provide suitable habitat for wildlife, endangered or not.

Private property allows us to solve problems by taking into consideration the present and future concerns of others. Unfortunately, people with good intentions but little economic understanding often call for solving problems stemming from inadequate private property by subverting rights to private property with political restrictions and mandates. □

THE FREEMAN
Ideas On Liberty

Croaking Frogs

by Brian Doherty

It's the kind of story that doesn't often get reported in the media—even though it is largely the media's creation. In February, Interior Secretary Bruce Babbitt made a stirring call for an extra $8.1 million in other people's money—your money and mine—for fiscal 2000 to research yet another potentially earth-shaking environmental crisis: declining and deformed frogs.

It's tiny by federal standards. Still, the federal agency umbrella group created last year for which Babbitt is seeking this new cash infusion, the Taskforce of Amphibian Declines and Deformities (TADD), could portend something big. It certainly seems as if the government is prepared for anything and everything to come out of the issue of unexpectedly disappearing and deformed amphibians: TADD, in an almost archetypal example of federal overkill, has representatives from the departments of state, justice, and defense on the team.

While the Department of the Interior posits this program as an example of pure science, research into a vital issue that only government force can supply, Babbitt's science adviser William Brown let slip the real score to a reporter from *BNA Daily Environment*: "There are a whole set of regulatory initiatives" waiting in the wings for when they find what they set out to find.

Brian Doherty is the Warren Brookes Fellow in Environmental Journalism at the Competitive Enterprise Institute.

The frog situation has gotten just enough media attention—stories in *Newsweek*, episodes of "Nightline"—and is just bizarre and frightening enough that the average man in the street knows there's something funny going on with frogs. There are two potential problems—probably unrelated, but conflated in both media and government—with amphibians: die-offs (frogs no longer appearing in customary numbers in certain habitats) and deformities.

That frogs are disappearing in numbers larger than what herpetologists have come to consider normal is not controversial in the field now; what these observations mean, and what might be causing them, are. A recently discovered chytrid fungus has been found killing frogs in Australia, Central America, and the United States; it is moving to the forefront as a convincing explanation in the scientific debate. Also, there is the possibility that natural fluctuations occur in frog populations that scientists don't understand because they haven't been looking at trend lines long enough. Even the government's own Web site devoted to the nascent frog crisis acknowledges that one of the frog species whose diminution concerns us now, the Northern leopard frog, created an earlier alarm in the Midwest in the 1960s and '70s, and "initiated our concern about amphibian declines, but many of these original declines have stopped and populations have recovered to some extent." These population fluctuations happen in nature, and the workings of nature, like that of the human

economy, are so multicausal and complex that we don't always know why certain things occur. Our intimate knowledge of long-term population trends is so poor that we can't even be sure we are seeing an alarmingly unnatural diminution.

Also, there are a couple of very likely man-caused, though prosaic, problems that could be killing off frogs: general encroachment on habitat and stocking non-native fish in large numbers in frog ponds. Indeed, man's desire for trout fishing could be hurting young tadpoles—but this is a matter of tradeoffs, not unquestionable bads.

Favored Explanations

However, the government frog effort prefers other controversial explanations. Not coincidentally, these explanations—while government researchers admit they have found no causal smoking gun—are those for which industrial society can be blamed: pesticides and ultraviolet radiation. These are the sort of explanations that would inspire the "whole set of regulatory initiatives" Babbitt's science adviser crowed about. It's true that UV radiation can cause problems for frog eggs in labs, but no one has shown that amphibian eggs in nature are actually being exposed to too much of it. (The UV thesis is thought to have more to do with the problem of deformed frogs rather than dying ones, though even there the evidence of real-world exposure is lacking.) Two herpetologists, from Stanford and the Smithsonian Institution, wrote in the journal *Froglog* that "what funding is available tends to be directed toward the most high-profile factors, regardless of whether or not they are the most likely causative agencies." And when government bureaucrats pay the scientific piper, the bureaucrats call the tune—and they tend to love the sweet sound of more regulation. Thus, while even such potential causes as chytrid fungus might have man to blame, in the sense that herpetologists themselves might be spreading the fungus cross-continent, advising scientists to wash their boots more carefully just doesn't pack the regulatory punch of stopping UV radiation or banning more pesticides to stop man's mad, unchecked lust for food not infested with (or eaten by) insects.

The frog deformity problem is the more grotesque and disturbing—freakish frogs with eyes in their mouths, multiple sets of limbs, missing limbs, missing jaws, appearing (or being noticed) in unusually large numbers. Consequently, it has gotten the most attention and money so far. The state of Minnesota alone—where the crisis first hit the media in 1995 after a school field trip found an unusual number of deformed frogs in one pond—has spent around a million dollars investigating the matter, and has already created a public scare on scant evidence. The Minnesota Pollution Control Agency in September 1997 announced that local well water was definitely causing frog deformities (pressuring scientists to go public with studies before they felt they were ready), and began giving out bottled water to frightened residents. The agency later admitted it was mistaken. One of the leading researchers of frog deformity, who thinks that naturally occurring parasites and cannibalism among tadpoles are most likely the main culprits, complains that the information presented to Babbitt was biased in the direction of scary man-caused explanations.



National Biological Information Service

Captain Ribbitt

Young visitors to the FrogWeb are encouraged to "find out how you can SAVE THE FROGS!"

The feds are pulling out the whole panoply of modern devices to create a scare about this issue. They set up a Web site and created a cute mascot to encourage children of all ages to get scared and get active—and, perhaps coincidentally, to become a public constituency for more federal money on matters amphibian.

Captain Ribbitt, a cartoon frog in a spacesuit presented as "Earth's Ambassador from the Planet Amphibian" tells "earthlings" that they "must join Frog Force now, get involved

in finding the cause, and become a friend to frogs everywhere." Some amphibian scientists shudder at the thought of thousands of eager kids recruited by this cartoon commando tromping heedlessly through the habitat of possibly endangered frogs, but you can't get a good environmental scare story rolling without starting a Children's Crusade. One wonders how much of last year's frog budget—your tax dollars at work—went to cutesy absurdities such as this.

When Babbitt first heard about the frog problem, he told the *Washington Post* that it "illuminated a landscape of potential extinction that extends all the way round the world." This is rhetoric of the sort that herpetologists don't necessarily agree with. The government's and media's panic over frog disappearances is based on the oft-repeated rhetorical notion that frogs, because of their permeable skin and water-based and land-based life cycles, function as a sort of canary-in-the-coal-mine early warning system for the biosphere. But herpetologists Joseph H. K. Pechmann and Henry M. Wilbur, writing in the academic journal *Herpetologica*, write that "we are not aware of any evidence available to substantiate it. The toxicological literature does not support a general statement that amphibians are a relatively sensitive group." But because that idea, false as it may be, is widespread, the frog problem could be another global warming in the making—media hype and government science in alliance to condemn industrial society and justify massive government intervention—on questionable evidence.

In federal terms, $9 million makes for a mere tadpole of a program. But tadpoles become frogs. And little government programs have been known to metamorphose into regulatory monsters. □

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THE FREEMAN
Ideas On Liberty

Noah Smithwick: Pioneer Texan and Monetary Critic

by Joseph R. Stromberg

In 1931 F. A. Hayek wrote that although the quantity theory of money as such is an oversimplification, "it would be one of the worst things which could befall us if the general public should ever again cease to believe in the elementary propositions of the quantity theory." His point was that the fundamental idea—that any increase in the supply of money will raise commodity prices in general—is good enough to guide the voting publics of Western nations, even if the unalloyed quantity theory lacks important Austrian insights into the behavior of relative prices. If only the voters understood even that much today!

The lively and colorful memoirs of Noah Smithwick, nonagenarian, ex-North Carolinian, early Texas pioneer, and eventual Californian, take us back to a time when Americans could grasp essential truths about the nature of money. His book, *The Evolution of a State or Recollections of Old Texas Days*, reflects the original value system of the mobile and ambitious Americans of the early nineteenth century. Sometime in 1827 Smithwick set off down the Mississippi River on his way to Texas. Owing to some complication arising on the riverboat, he lost his grubstake and had to take a temporary job as a "mechanic" or "finisher" in an industrial concern in New Orleans. He immediately became the object of resentment on the part of the older, established workers for being too productive. Cautioned to go slower, he responded, "Our employer pays me for my time: do I not owe him all that I am capable of doing in that time?" The other workers' attitude was that "'No sprig of a boy must presume to set the pace for us,' and so I was forced to slow down and drift with the tide. This was Labour Unionism in its incipiency."

Smithwick, born in 1808 in North Carolina, went on to Texas—then part of Mexico—as soon as he could save enough money in New Orleans. He lived through the tumultuous days of the Texan Revolution, the Texas Republic, the Mexican-American War, and the secession crisis of 1861. At that time, the "integral nationalism" that he shared with Governor Sam Houston led him to leave Texas for the more favorable climate of California, where he remained. His eyesight failing him, he dictated his recollections to his daughter in 1899. Smithwick died the next year.

Willingness to Work

Noah Smithwick's life may well stand as an example of what is rapidly disappearing from the American character. Willing to work hard and with a natural mechanical ability, he tried numerous enterprises: blacksmith, gunsmith, soldier, mill owner, critic of land fraud (perhaps the first big "industry" in Texas), independent inventor of the circular saw, and

Joseph Stromberg is a part-time college lecturer in history who has contributed to the Journal of Libertarian Studies, Reason, Independent Review, *and other publications.*

diplomat. (He negotiated an Indian treaty, promptly violated by both sides.) He would undertake any kind of honest work, which probably explains why he was never much of a politician.

As an active and ambitious pioneer, Smithwick calls to mind the "venturesome conservatives" of the Jacksonian period (to use Marvin Meyer's phrase). A canny observer of, and participant in, the economic life of early (Anglo) Texas, he makes sharp comments on many of its aspects. Alongside his interesting passages on ethnic and cultural groups he came to know of (Mexicans, Indians, blacks, Germans, and Mormons), some of his best material and most amusing stories focus on the nature of money.

Smithwick describes the crisis caused in the Texas Republic by the government's issue of inflationary "scrip" (a sort of constant with new regimes). In a textbook demonstration of Gresham's Law, coin (that is, *real money*) disappeared. He recalls: "I received a hatful of new, crisp, one-dollar bills in payment for a horse lost in the San Saba Indian fight, which I immediately turned over to a creditor [!], without ever having folded them. People would almost rather have anything else than the commonwealth paper."

In Travis County, people came up with an alternative: "Under those circumstances, we established a currency of our own, a kind of banking system as it were, which though unauthorized by law, met the local requirements. Horses were generally considered legal tender: but owing to the constant drain on the public treasury by the horse-loving Indian, that kind of currency became scarce, so we settled on the cow as the least liable to fluctuation." Private bills were written against cows (valued at $10 per animal in real money). The system apparently worked well enough as long as it was needed. (Yearlings were also used as a medium of exchange.)

Meet "John Doe"

An even better example of Smithwick's empirical Texan monetary views is found in his discussion of counterfeiting in the Redlands just before Texan independence. In



Noah Smithwick

1831 he ran afoul of the law in San Felipe. Texas was still part of Mexico, and Smithwick thought it best to shove off to the Redlands, which bordered on the American state of Louisiana. There he came to know the local counterfeiter, on whose premises he worked, although he never took part himself in the counterfeiting portion of "John Doe's" business. Doe's product was a copper-sandwich version of the Mexican silver dollar, calling vividly to mind the "Lyndon Johnson" dimes and quarters introduced sometime in the mid-1960s.

Smithwick says of Doe: "There was nothing of the desperado about him. On the contrary, he was pleasant and peaceable and generally liked, and, so far from being looked upon as a malefactor, was considered a public benefactor, in that he furnished the only currency to which the people had access. The country could not be said to be on either a gold or silver basis, copper being the basis of Doe's coinage. . . ."

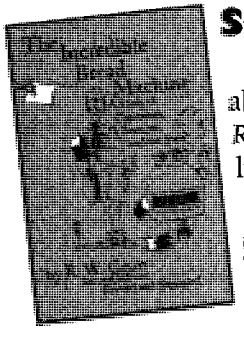
Doe would occasionally call in his worn sandwich dollars and restamp them with a veneer of silver. He made doubloons as well. Clearly in touch with the policy debates of his

last years, Smithwick remarks: "Doe's currency furnishes a good example of the practical working of the populist idea: it was all right in domestic transactions, but when they attempted to discharge foreign [that is, non-East Texan] obligations with it, it got them into trouble."

Doe did not do well when he extended his operations into western Louisiana. On one occasion, however, he won a sizeable bet by stamping a pure silver coin with the same cracked die he used for his copper-sandwich coins and sending a crony into a saloon to spend it. A skeptical bartender announced that the coin was clearly counterfeit, but put to the test, this coin of course proved to be unadulterated silver. (Doe won $500 on the bet.) With this windfall, Doe removed himself west of the Sabine River, where, as Smithwick puts it, "his efforts were more appreciated."

As a moneysmith, says Smithwick, Doe "added materially to the wealth of the colonies . . . by restamping the old hammered dollars, a single blow of the hammer adding 25 cents to the value of each. There were thousands of them thus rehabilitated." (There was apparently no debasing with copper in this operation.) Doe was finally put out of business by counterfeiters in Louisiana, who printed up fake U.S. banknotes and floated them in East Texas. Smithwick observes: "Paper and ink being cheaper even than copper, Doe's currency was given the go-by." Copper, after all, was fairly valuable and Doe, at one time, had to break up a still to keep his copper-sandwich undertaking going.

Smithwick's experience with the counterfeiter suggests a corollary to Gresham's Law: worse money drives out merely bad money. It is refreshing to read the memoirs of a pioneer who could grasp an essential point about the nature of money and use it to cast light on his times. □



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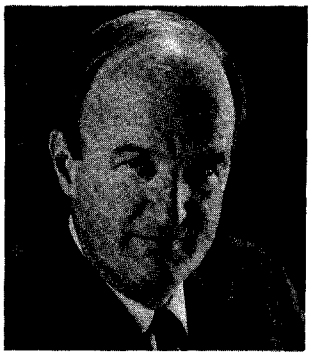
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JULY 1999



Dismal Scientists Score Another Win

"Until a business returns a profit that is greater than its cost of capital, it operates at a loss."
—PETER F. DRUCKER

The English essayist (and economist) Walter Bagehot once remarked, "No real Englishman in his secret soul was ever sorry for the death of an economist."

Quite a few security analysts and fund managers on American shores probably feel that way about the economists who came up with the efficient market hypothesis and proved that 95 percent of professionals can't beat a blindfolded monkey in picking stocks. Highly paid Wall Street analysts don't like being compared to sightless apes. Yet after decades of heated exchange between Wall Street and academia, the eggheads are winning the argument. Today index funds—the professors' favorite investment vehicle—are the fastest growing sector on Wall Street.

The latest group to sympathize with the words of Walter Bagehot are the accountants. Over the past decade, ivory-tower economists (mainly professors teaching modern finance theory at MBA schools) have taken on the accounting departments, damning them for not taking into account the full opportunity cost of capital.

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Are Accounting Profits for Real?

For years, economists have complained that conventional accounting distorts the true economics of the firm by not including a charge for common equity in its earnings reports and balance sheets. Generally accepted accounting principles treat equity as if it were free. Thus, publicly traded corporations release quarterly reports showing substantial earnings that in fact are losses. "True profits don't begin until corporations have covered a normal return on investment," declares Al Ehrbar, senior vice president of consultants Stern Stewart & Co., specialists in EVA—a new performance technique for business.[1]

What is EVA? It stands for "economic value added" (also called economic profit or residual income). Essentially, EVA is a precise measurement of the opportunity cost of capital. For years, opportunity cost was a nebulous concept known only to professors. The term, coined by Austrian economist Friedrich Wieser in the early twentieth century, refers to the universal principle that all human action involves giving up other opportunities. When you invest in a stock, lend money, or create a new product, you give up the chance to invest elsewhere. If you invest in a high-flying computer stock, you can't buy T-bills. If you build

a new office building, your money is tied up for years in concrete and can't be invested in AT&T.

EVA is a practical application of classical economics and modern finance theory. The Austrians elucidated the concept of opportunity cost, and Nobel laureates Merton H. Miller and Franco Modigliani used it in their model of the firm to determine its true value. In the 1980s, G. Bennett Stewart III created EVA as a financial yardstick to measure opportunity costs in business.

EVA is fairly simple to determine: it is after-tax operating profits minus the appropriate capital charge for both debt and equity. If a company issues debt, the opportunity cost is linked to the Treasury rate (currently 5-6 percent), plus the credit risk of the issuer. If the company issues stock, the opportunity cost is measured by the long-term annualized return on the stock market, approximately 12 percent. In short, EVA recognizes that investors must earn enough to compensate for risk of their investment capital.

If a firm earns more than these opportunity costs, it has "added value" to its shareholders and created wealth in the world economy. Hence, the phrase "economic value added." If EVA is positive, shareholders and the economy are making real contributions to the bottom line. Otherwise, the business should shut down and invest shareholders' funds in Treasuries or an index fund. As British economist John Kay declares, "In the long run, firms that fail to add value in a competitive market will not survive, nor do they deserve to."[2]

Okay, so what good is EVA to corporate managers? EVA analysis helps identify potential acquisitions, expansion plans, and nonperforming assets and assists in eliminating low-profit-margin operations that are clearly unprofitable when full costs are taken into account. EVA is also being used as an incentive system for managers and employees. Bonuses are linked to economic earnings, not just accounting earnings, and EVA has proven effective in boosting productivity.

EVA makes a lot of sense and has made significant inroads into the financial world. Already over 300 major corporations, including Coca-Cola, Eli Lilly, and Sprint, use EVA as a capital accountability tool to reinforce the idea that profits don't begin until corporations have covered their normal return. Wall Street analysts at Goldman Sachs and First Boston, among others, use EVA to evaluate stocks. According to Ehrbar, EVA explains stock performance and market value better than any other accounting measure, including return on equity, cash flow, earnings per share, or sales. EVA makes company officers focus more clearly on creating shareholder value and a higher stock price. Stern Stewart issues an annual EVA report on the top 1,000 U.S. corporations. For several years now, Intel has had the highest EVA ranking and GM the lowest.

EVA Wins the Battle

Accountants still have a dominant grip on the way corporate financial statements are submitted, but the popularity of EVA has forced them to take notice. All five accounting firms offer an EVA-type statistic to their clients. Most accounting textbooks now include a significant section on economic value added, economic profit, or residual income. Previous editions did not mention EVA or opportunity cost.

Want more? Check out Al Ehrbar's highly readable *EVA* or John Kay's brilliant *Why Firms Succeed.* See also www.eva.com.

I like EVA. Companies adopting it appear to perform better in creating wealth and shareholder value. But it may have potential drawbacks. EVA puts enormous pressure on managers to overachieve and to create constant above-average profit centers. Imagine not earning a true profit unless your company or division beats last year's Dow Jones Industrial Average. It could be depressing. Wonder what your company's EVA will look like in the next recession? Heads could roll

Some managers may want to join Wall Street analysts and accountants in shooting those dismal scientists. □

1. Al Ehrbar, EVA: *The Real Key to Creating Wealth* (New York: John Wiley & Sons, 1998), p. viii.
2. John Kay, *Why Firms Succeed* (New York: Oxford University Press, 1995), p. 19.

BOOKS

Overcoming Welfare: Expecting More from the Poor and Ourselves

by James L. Payne

Basic Books • 1998 • 243 pages • $26.50

Reviewed by Robert Batemarco

When free-market advocates criticize welfare they are commonly accused of having nothing to put in its place. James Payne meets this objection head-on in *Overcoming Welfare* by making a crucial distinction between "sympathetic giving" and "expectant giving." In so doing, he provides an alternative that is consistent with free-market principles and keeps defenders of the status quo from occupying the moral high ground.

Sympathetic giving means giving out of pity and seeking nothing in return from the recipient. It characterizes all twentieth-century government "anti-poverty" programs. Payne echoes the views of numerous scholars that those programs not only fail to reduce poverty (indeed, by rewarding irresponsible behavior, they generate more), but also lead to resentment on the part of givers, receivers, and intermediaries alike.

Expectant giving means that the giver expects that the receiver will give something back. The quid pro quo, however, is usually not something that directly benefits the donor. What the recipient most often "contributes" is some action that will eventually lead him to overcome his state of need.

It is the demand of something in return that makes expectant giving superior to its alternative. The specific demand—whether swearing off drugs, keeping a curfew, or rendering some useful service—is less important than that the act symbolizes that the recipient is ultimately responsible for himself. That's a heretical idea in an age when everyone is encouraged to label himself a victim to whom society owes a living. But it's an idea that must be revived.

Payne not only shows that expectant giving can work, but also cites much evidence that it *has* worked. Britain's unjustly maligned Reform Act of 1834 actually was a rare governmental effort to replace sympathetic giving (home relief) with expectant giving (the workhouse). Even more important were the "charity theorists"—most notably Octavia Hill—who not only preached the virtues of expectant giving, but also practiced them. By treating the poor as responsible people with problems to overcome, Hill and her fellow poverty fighters were able to elicit constructive responses from them, turning many of the indigent into productive members of society.

Payne's analysis of how we moved from the sound expectant approach to the bankrupt sympathetic approach is equally interesting. He implicates many factors, most important the spread of the idea that income redistribution is an appropriate function of government. Once government programs were in place, whatever lip service was paid to expectant giving was always superseded in practice with government handouts. The political incentives that virtually guarantee this result are well-charted territory in the public choice literature, but Payne presents them with great clarity and force.

He also blames the elite classes' acceptance of moral relativism (the notion that no choice or lifestyle should be judged as any better or worse than any other) and what I call infantile leftism (that no act, however irresponsible, should have any negative consequences for the actor). Both ideas have exacerbated the problems inherent in government programs and infected many privately funded efforts as well.

It is usually easier to diagnose problems than to propose solutions, and this book's less convincing sections are those offering political escapes from our welfare trap. Payne suggests attaching a taxpayer representative to each welfare program to expose the flaws in it. (Admittedly, he does not consider this to be a panacea.) This is a worthwhile objective, but it is hard to imagine that legislators would appoint people who would take on the task with the requisite seriousness. Besides, the flaws in our welfare system have already been exposed for all who care to inform themselves.

Another imperfection in the book is that, as important as the distinction between sympathetic and expectant giving is, there is a parallel distinction the author fails to make. That is the distinction between self-esteem and self-respect. The former refers to feeling good about oneself, regardless of whether those feelings are merited. The latter, on the other hand, must be earned. Self-esteem is bestowed on a something-for-nothing (sympathetic) basis, while self-respect results from constructive effort to better oneself. Payne uses the term "self-esteem" exclusively, when "self-respect" is often what he really means.

Those qualifications aside, *Overcoming Welfare* is an outstanding book. In writing it, James Payne has made a valuable contribution to the debate over welfare policy. □

Robert Batemarco is director of analytics at a marketing research firm in New York City and teaches economics at Marymount College in Tarrytown, New York.

Coolidge: An American Enigma
by Robert Sobel
Regnery Publishing • 1998 • 462 pages • $34.95

The Presidency of Calvin Coolidge
by Robert Ferrell
University Press of Kansas • 1998 • 272 pages • $29.95

Reviewed by Raymond J. Keating

Few U.S. presidents have suffered more at the hands of statist historians than Calvin Coolidge. The reason for the nearly unanimous scorn directed at the 30th president was Coolidge's generally limited government philosophy, which he quietly brandished while in the White House.

Those historians love to criticize Coolidge because he presided over peace and prosperity and had no interest in federal programs to "manage" the economy and "solve" social problems. Recently, for example, Nathan Miller, author of *Star-Spangled Men: America's Ten Worst Presidents*, ranked Coolidge among the worst not for anything he did, but because he supposedly did "nothing." (See the review in *The Freeman*, March 1999.) That's the ultimate source of the discontent regarding Coolidge—he actually accomplished much, but not the government activism desired by so-called liberal observers.

During the Coolidge administration federal expenditures fell from $5.06 billion in 1921 (under President Warren Harding) to $3.12 billion in 1929. Along the way, Coolidge stopped various government boondoggles, most prominently the McNary-Haugen bill, which would have had the federal government buy up farm surpluses to sell abroad and hike prices domestically. The federal debt fell by 30 percent between 1921 and 1929.

At the same time, tax rates were slashed. The top personal income tax rate dropped from 73 percent to 25 percent, and the capital gains tax from 73 percent to 12.5 percent. Coolidge got Congress to eliminate the recently imposed gift tax and to reduce the estate tax. The corporate income tax was also cut.

The consequences of these policies were positive. Real annual economic growth averaged 6.2 percent from 1922 to 1929 and consumer prices fell.

Coolidge's record was not perfect. He favored high tariffs and supported limitations on immigration, although he fought unsuccessfully against an anti-Japanese provision in the Immigration Act of 1924. Initially he opposed federal relief for the Mississippi flood of 1927, but eventually relented under massive congressional pressure. Coolidge downsized the relief plan, but it set an expensive precedent.

Taken as a whole, however, Coolidge's record was admirable, and these two new books take major steps toward a far more just historical assessment.

Robert Ferrell's effort is the more workmanlike of the two. He has a formidable grasp of the period and the key events of the time. Many of his interpretations, however, suggest a strong faith in government action. For example, Ferrell declares that "something had to be done" regarding farmers' woes during the 1920s—the implication being that *government* had to do something.

Nonetheless, he manages to restrain such leanings and provides sound historical report-

ing on Coolidge, his career, and his administration. Of note, Ferrell observes about Coolidge's stint as governor of Massachusetts: "Crowning his accomplishments as governor was consolidation of the commonwealth's 118 separate government departments into 18, a courageous thing to do, for many people lost lucrative posts." He also writes that "Regulation in the Coolidge era was thin to the point of invisibility." And he honestly summarizes Coolidge's fiscal record: "During the 1920s, the Coolidge administration reduced the debt, kept the budget flat, and brought in sufficient revenues through markedly reduced tax rates, both personal and corporate."

Where Ferrell falls far short is in his understanding of economics. He breaks into Keynesian rhetoric, for example, in declaring that Coolidge failed to see the problem of "underconsumption." Based on this Keynesian model, Ferrell concludes: "The economy was the greatest problem of the moment, and Coolidge understood it less than some of his contemporaries. If he failed in the presidency, this was the major failure." In reality, aside from his failure to understand the benefits of free trade, Coolidge may have had the best grasp of how the economy works among all twentieth-century presidents.

Robert Sobel's book is a highly readable popular biography. It is largely based on secondary sources, but the author's interpretations are fresh.

Among the many interesting issues Sobel touches on is Coolidge's request "for legislation to abolish the rights of states and municipalities to issue tax-exempt securities, arguing that new investment funneled into these securities could be better employed in the private sector." Coolidge's argument holds even greater validity today, given the tremendous waste that has been financed by such instruments over the past seven decades.

Sobel also reports that Coolidge believed that "government should remain out of the economy, and businessmen should not interfere with the proper functions of government." Again, given today's convoluted tax system, web-like regulatory regime, campaign-finance controversies, and extensive corporate-welfare expenditures, his philosophy looks very sound.

My sole complaint with Sobel's book again lies with his understanding of economics. While Sobel gets much of Coolidge's economics and its effects right, he asserts that Coolidge was "not a 'supply-sider.' "

However, this statement seems to grow from the standard misunderstanding of supply-side economics. Coolidge, after all, showed a consistent understanding of how high tax rates dulled incentives for working, investing, and risk taking, and thereby restrained the economy's productive capacity.

Ferrell and Sobel manage to grasp the complete Coolidge. While most historians have offered a caricature of a president completely beholden to business interests, both authors understand that at Coolidge's core were his religious beliefs. As Sobel points out, during the same speech in which Coolidge noted in passing that the "chief business of the American people is business," he also declared: "The things of the spirit come first."

In another speech, Coolidge sagaciously observed: "Prosperity is only an instrument to be used, not a deity to be worshiped."

Despite certain weaknesses in both books, they go far toward setting straight the historical record on Calvin Coolidge. □

Raymond J. Keating is chief economist for the Small Business Survival Committee, a columnist with Newsday, *and a contributing editor to* The Freeman.

H. L. Mencken Revisited

by William H. A. Williams

Twayne Publishers • 1998 • 195 pages • $35.00

Reviewed by George C. Leef

Henry Louis Mencken is known to many lovers of freedom as a sharp-tongued satirist who lampooned politicians, crusading moralists, overstuffed intellectuals, and anyone else he thought was a public menace. He is well appreciated for his acidic barbs (FDR, for example, was "King Roosevelt II"), but most people who think well of Mencken do so

just because he disliked big government and its champions. Not many are familiar with his life and career as a journalist.

William H. A. Williams's *H. L. Mencken Revisited* admirably supplies the details of Mencken's life and career. The book is not a detailed biography, but covers the main features of the great Baltimorean's life, with the primary focus on his thought, writings, and battles with the many people he believed were ruining the United States.

One of Mencken's virtues was his consistency. He was a man of principle, and Williams's book makes this very clear. Williams often refers to Mencken's "libertarianism" and quotes him as saying, "My literary theory, like my politics, is based chiefly upon one idea, to wit, the idea of freedom. I am, in brief, a libertarian of the most extreme variety, and can imagine no human right that is half as valuable as the simple right to pursue the truth at discretion and utter it when found." Instances of his commitment to the philosophy abound in the book.

For example, he vigorously opposed all attempts to silence free speech, even for those with whom he was in complete disagreement. During the Red Scare of the 1920s, he not only wrote to condemn the arrest and deportation of anarchist Emma Goldman, but also tried to get the Justice Department to return her papers seized in a raid on the office of her magazine and urged the Bureau of Immigration to allow her to return to the United States to visit relatives. He even contributed money to the Emma Goldman Recovery Committee. Why worry about the treatment of a leftist radical? Because, Mencken knew, preservation of the marketplace of ideas supersedes disagreement with particular ideas. Williams writes, "Mencken belonged to no political organizations, and he invariably had little sympathy for the liberal or radical goals of those he defended. He was motivated by libertarian principles and basic human sympathy." Mencken thought little of most politicians. He subscribed to the belief that "public officials, under democracy, were predominantly frauds, and hence did not deserve to be taken seriously."

He blasted most for what he saw to be their self-serving attempts to manipulate the "booboisie" for their own gain. For instance, he denounced Woodrow Wilson's last attorney general, A. Mitchell Palmer, for his "medieval attempts to get into the White House by pumping up the Bolshevik issue."

Many people at the time, and perhaps to this day, regarded the incessantly satirical Mencken as simply a nihilist. Williams argues otherwise: "Beneath the surface of his satire, Mencken was a very different figure from the cynical nihilist depicted by so many of his critics. He never denied the importance of values or their necessity in society. He never sought to destroy those values in which he believed. He did attack, sometimes ignorantly and intolerantly, ideals that seemed to him hypocritical or false. Even then, he usually produced his condemnation by juxtaposing the qualities he admired against those he rejected. . . . He was in his own way a moralist, angrily decrying the erosion of those values necessary to a humane and civilized society."

Williams also defends Mencken against other attacks by leftists who feel compelled to besmirch the name of anyone who disagrees with them. Mencken died in 1956, but in recent years he has been subjected to charges of racism and anti-Semitism. The "racist label is based on nothing more than snippets of Mencken's colorful writing and hardly squares with a man who helped many black authors, had black friends, testified in favor of an anti-lynching bill, and repeatedly slammed the Ku Klux Klan." As to alleged anti-Semitism, Williams quotes Sheldon Richman's observation that Mencken never blamed Jews for anything. Moreover, he had numerous Jewish friends, and denounced the Roosevelt administration's policy of refusing admittance to Jews seeking to flee Germany, condemning "political mountebanks who fill the air with hollow denunciations of Hitler, and yet never lift a hand to help an actual Jew."

If you are among that group of people who are fond of H.L. Mencken's flamboyant writing but know little about the man, this is a book you would do well to acquire. □

George Leef is book review editor of The Freeman.

Eat the Rich: A Treatise on Economics
by P. J. O'Rourke
Atlantic Monthly Press • 1998 • 265 pages • $24.00

Reviewed by William H. Peterson

Eat the rich. Why not? Everyone knows that they're responsible for the poverty of victimized masses. To their rescue comes Compassionate Government selflessly transferring wealth from the rich to the poor. The transfer, however, comes at a steep price to society in terms of disincentives to the rich (as well as the middle class) but more so to the poor whose plight is compounded by the law of unintended consequences. The poor, you see, get to be truly victimized by the "compassion" of their own government.

This is the theme that P. J. O'Rourke plays, grandly, in this lighthearted work with the tongue-in-cheek subtitle of "A Treatise on Economics." Economics then is taught via numerous examples of official mismanagement and unscrupulousness.

One of the foremost lessons concerns the consequences of living under the rule of men rather than the rule of law. The rule of men, says our hardy world traveler, is the pits. O'Rourke wittily cites his experiences in Albania, Sweden, Cuba, Russia, Tanzania, China, and elsewhere to make his point. There, men in power seem bent on building monuments to themselves—funded mainly by, naturally, the poor.

One such monument is seen in Shanghai's giant new gleaming Pudong business district. The only catch: no business, even though the place boasts of regional headquarters for the likes of Hewlett-Packard, Siemens, Sharp, Coca-Cola, SmithKline Beecham, and Sony. O'Rourke writes:

> Nobody seemed to be there at all. In the middle of a Tuesday afternoon, nothing was going on. We drove up and down empty streets along concrete fences decorated with those international cross-out silhouettes indicating prohibition of this or that: No spitting. No martial arts. No cutting trees. No firecrackers. No breaking the phone.

Yet P.J.'s Chinese escort could brag in the face of this monumental office real-estate glut, rolling his eyes slightly: "The floor space of high-rises in Pudong exceeds New York City." That was in 1997. Office space in Pudong was set to grow by a third more in 1998. The Chinese communists, according to the Asian *Wall Street Journal*, had literally ordered Shanghai to be a world-class city—apparently regardless of cost. The beneficiaries? Certainly not the poor Chinese peasant.

O'Rourke, a roving editor for *Rolling Stone*, has covered such official misdeeds in previous books such as *Give War a Chance* and *Parliament of Whores* (in which he held that the whores include anyone who is on the take from the welfare state). His winking cynicism and irreverence can lift a reader's sense of gloom, on surveying political shenanigans at home and abroad, into laughter at the follies of government. Often, a good horselaugh is a more effective refutation of statist pomposities than a lengthy article, and P.J. lampoons with a Menckenesque verve.

Continuing his economics lessons, P.J. plugs Adam Smith's Invisible Hand idea, quoting the famous passage: "It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest." He rejects the cliché that in free societies the rich get richer and the poor get poorer. He amends that line with a punch line: "The rich are getting richer. The poor are getting richer. And we're all getting older."

With anecdotes and humor he demonstrates that economic liberty makes for the creation of wealth and that economic repression makes for poverty. Thousands of people who would otherwise shun a conventional treatise on economics may learn the fundamentals of human action from this unconventional one.

Lastly, P.J. finds economic virtue in the Tenth Commandment condemning covetousness. He says that if you want a donkey or a pot roast or a cleaning lady every week, "don't bitch about what the people across the street have. *Go get your own.*"

Great message. □

William Peterson is an adjunct scholar at the Heritage Foundation in Washington and Distinguished Lundy Professor Emeritus of Business Philosophy at Campbell University in North Carolina.

Cyber Rights: Defending Free Speech in the Digital Age

by Mike Godwin

Times Books • 1998 • 305 pages • $27.50

Reviewed by Royce Van Tassell

On June 26, 1995, *Time* magazine started the "Great Cyberporn Panic of 1995" with a story legitimizing Martin Rimm's scaremongering study of pornography online. Three weeks later, after Mike Godwin and others in the online community had completely discredited Rimm's study, *Time* realized that Rimm had duped them and issued what amounts to the only full-page retraction in its 70-year history.

In his book *Cyber Rights*, Mike Godwin, chief counsel for the Electronic Frontier Foundation, uses that and other cases to show how important full free speech rights on the Net are. Without them, Godwin maintains, the Net could not help the rest of America hold the mainstream press accountable and facilitate the vigorous, uninhibited exchange of ideas we find there. This book is a passionate argument that speech in cyberspace must enjoy the same protection as "ink on dead trees."

Godwin believes that the Net represents the most complete extension of the American experiment in democracy. It permits everyone, "not just lawyers or journalists or policymakers, or the rich and well-connected . . . to level the playing field, to hold media and political institutions accountable, and to tell the truth." It makes everyone with a computer and a modem a modern "pamphleteer." Anyone who recently logged onto the seattle.general newsgroup saw how vibrant the discussion of racial preferences and affirmative action can be, as opposed to the staid, often redundant discourse found in the traditional media. Without the Net's anonymity, such frankness would never have emerged.

Freedom of speech must be more than a notion to which we sometimes pay lip service. Godwin tells adults to relearn a lesson we've all tried to teach children: "Sticks and stones may break my bones, but words will never hurt me." When we tell children this, we know that the reason some people want to restrict certain kinds of speech is precisely because words can hurt. But just as children must learn to rise above adversity and learn to cope with the power of words, so must adults—even when the words hurt or offend.

Cyber Rights is not without its flaws. Godwin makes the claim that libel law may be coming to an end, but it is rather difficult to take that seriously. Furthermore, his passion for the Net sometimes colors his judgment. He states at one point that, "the Net [is] reducing and perhaps erasing the imbalance of power between mass media and private individuals. The power of the Net allows anyone with a will and the energy to write the opportunity to publish their ideas." While the second half of that statement is true, I am not convinced of the first. Earning a voice in public discourse comparable to the current position of, say, the *New York Times* or Tom Brokaw is as much a product of luck as it is of effort or knowledge.

Godwin's writing is for the most part clear and succinct. He distills the legalese of speech law into simple prose, and then illustrates the application and importance of those principles in cyberspace with well-told stories. On occasion, his transition between the explanation of a principle and the ensuing illustration jarred me, but it was not difficult to pick up the trail again.

Cyber Rights is an enjoyable and important book. For lawyers conversant in First Amendment law, Godwin dispels some of the preconceptions that have led many of them to segregate speech on the Net from speech in the traditional media. For legislators and policymakers, it is an excellent primer on why they must not rashly alter the rules of speech in new media. Lastly, Godwin helps the average citizen understand how the Net can improve society and perhaps re-establish some of the community lost in our increasingly distant society—if it is left free. □

Royce Van Tassell is an analyst with Citygate Associates, a policy and management consulting firm in Sacramento, California.

LEVIATHAN at WAR



"Many men desire peace; but not many desire the things that make for peace."

– Thomas à Kempis

This issue's special section on the war in the Balkans falls squarely within FEE's 53-year tradition of exploring the ideas that make for freedom and peace. As Leonard E. Read, FEE's founder and longtime president, once explained: "War is liberty's greatest enemy, and the deadly foe of economic progress. If war be evil there must be a way to avoid it; there must be a rationale, a type of thinking, patterns for living, that lead to peace."

In 1995, FEE published *Leviathan at War*, an anthology of articles from *The Freeman* and other FEE releases. Edited by Edmund A. Opitz, *Leviathan at War* includes more than 20 essays on the causes and economics of war, free trade as a foundation for peace, war's effect on individual liberty, and related topics.

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Ignorance Is Bliss—Maybe

Not having experienced much of the past is a mixed blessing. What's grotesque, shocking, and unheard of to older Americans might seem normal, perhaps just a bit curious, to younger Americans. For example, last year New Orleans Mayor Marc Morial brought suit against gun manufacturers to recover carnage costs in his city. This January, Philadelphia Mayor Ed Rendell met with his advisers to consider whether the city should sue gun manufacturers for creating a public nuisance since guns were used in its 400-plus homicides. The city would seek to recover the cost of everything from cleanup after bloody murders to court and social workers for victims. Mayor Rendell's imagination has also led him to discover a new liability for tobacco companies: since some of Philadelphia's fires have careless smoking as their origin, why not sue tobacco companies to recover the city's fire losses?

Decades ago anyone suggesting bringing lawsuits against gun manufacturers for homicides, or tobacco companies for fires caused by careless smoking would have been considered a prime candidate for a lunatic asylum. If one generalizes from the lawsuits brought against gun manufacturers because people use their product to commit murder and mayhem, and against tobacco companies for smoking illnesses and fires caused by careless smoking, one would conclude that people are not to be held responsible for anything they do. It is the inanimate object, while incapable of acting, that is responsible. That is, a gun is responsible for murder, not the gun's user. A cigarette is responsible for a fire, not the careless smoker. That being the case, it "logically" follows that manufacturers of the offending inanimate object are culpable. After all, had the manufacturer not produced the gun or cigarette there would be fewer homicides, smoking-related illnesses, and fires caused by careless smoking.

"It's Not My Fault"

This it's-not-my-fault principle can be broadened to include just about anything. If a scantily clad young lady prancing along the street distracts my attention, and I have an automobile collision, the it's-not-my-fault principle would hold the young lady liable for my accident. But she might make the case that it is the manufacturer of her miniskirt who is really liable. If we Americans were to carry the it's-not-my-fault principle to its logical conclusion, we would virtually guarantee poverty. There would be little production. Why should I manufacture irons if I could be held liable for anything a person might do with the iron, including assault or leaving the iron unattended and thereby causing a fire.

Suppose by some miracle a person who died as recently as 1950 were to come back to visit today's America. How might we explain all this to him? At first blush we might tell him that Americans and their leaders have taken complete leave of their senses and wish

Walter Williams is the John M. Olin Distinguished Professor of Economics and chairman of the economics department at George Mason University in Fairfax, Virginia.

to abandon all notions of personal responsibility. But there is a more flattering explanation though nonetheless still troubling: Americans simply want other people's money, and the courts and the legislature have provided them with a mechanism for getting it. I do not believe we have reached a point where the courts would countenance legislatures' brazenly picking out a corporation and saying, "You look as if you have a lot of money; give it to us." Thus, we have to create an aura of legitimacy to extortion. We do it with propaganda impugning the company's moral character and with bogus science. Health and professed concern about the nation's children have been two successful strategies. After all, who can be against health and the welfare of America's children?

Where it all ends is difficult to predict but there are some signs on the horizon. "Caffeine is the new drug of choice among kids," warns Helen Cordes writing in *The Nation* magazine (April 27, 1998), adding, "Caffeine Inc. [soda manufacturers] is raking it in, often targeting teens and younger kids. . . . The major caffeine suppliers to kids have been throwing millions into advertising and give-aways." The Center for Science in the Public Interest (CSPI) agrees and wants the FDA to regulate caffeine content of soda, coffee, tea, and chocolate. Roland Griffiths of Johns Hopkins University is also concerned about coffee's addictive qualities and says, "If health risks are well-documented, caffeine could be catapulted in public perception from a pleasant habit to a possibly harmful drug of abuse." That vision, along with bogus science, might become justification for lawsuits and FDA regulation.

Michael Jacobson, CSPI's director, also thinks Mexican and Chinese restaurants offer servings much too large and says, "It's high time the [restaurant] industry begins to bear some responsibility for its contribution to obesity, heart disease and cancer."

Got Milk?

Since obesity impacts heavily on healthcare costs, why not bring lawsuits against the food industry like those against the tobacco industry? Yale University's Professor Kelley D. Brownell, director of the Center for Eating and Weight Disorders, proposes that foods high in fat or with little nutritional content be taxed. He recommends that the tax proceeds be used to build bike and hiking trails. He also says that since the average child sees 10,000 food commercials each year, 95 percent of them for junk food and sugared cereals, Congress ought to regulate junk-food commercials. The cigarette tyrants got "Joe Camel" advertisements banned. Why not go after Rice Krispies' "Snap, Crackle, and Pop"?

In New York City, Anti-Dairy Coalition Executive Director Robert Cohen, author of the book *Milk: The Deadly Poison*, says that "Milk products, like tobacco, are an enormous threat to the health of both children and adults, yet we see the dairy industry protected by constitutionally questionable laws while the tobacco industry is held accountable."

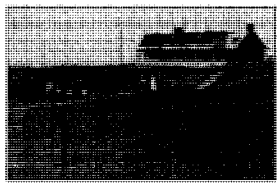
If there is a blessing to being at an age when one contemplates the arrival of the grim reaper, it is the knowledge that one will not be around to witness the end of sanity in America. □

THE FREEMAN
Ideas On Liberty
August 1999 Vol. 49, No. 8

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PERSPECTIVE

Winners and Winners

Books and articles by the dozen bemoan the gap between "winners and losers" in today's economic boom. Even writers not associated with socialism have joined the moaners' chorus. For example, conservative Edward Luttwak writes in his new book, trendily titled *Turbo-Capitalism: Winners and Losers in the Global Economy*, "living in a country that so greatly respects and admires high-earning winners, losers find it hard to preserve their self-esteem."

Let's ignore the psychobabble and look at this idea of winners and losers. In games, the object is to win, which means to fulfill some arbitrary conditions defined by the rules of the game. *Because* one player or team wins, the other loses. The victory and loss are not independent events. That's why we say the Yankees *beat* the Padres in the World Series.

Writers who describe the economic process in terms of winners and losers indicate, intentionally or not, that the same zero-sum principle applies: namely, that people who make high incomes are responsible for others' making low incomes. But how can that be? Is Bill Gates the reason that some people earn only the minimum wage? Does anyone live in poverty because Sam Walton got rich?

That's not only untrue, it's *worse* than untrue. The fortunes of Gates, Walton, and anyone who earns a high income are the consequences of their having enriched a multitude of people considerably less wealthy than themselves. You have to produce things people want if you intend to get rich (unless you find a way to milk the taxpayers). Market activity is a positive-sum, or win-win, process. In a free (or free-ish) economy, the rich get richer by making the "poor" richer. If you don't believe it, ask yourself where would you rather be "poor," here or in India?

To be sure, people with acute entrepreneurial alertness or valuable skills and knowledge will do spectacularly well. By comparison, the people who lack those things will seem to be losers. But they aren't. And since there is unlimited wealth yet to be created, anyone—if

free—can have his shot at being a "winner." Whatever is holding a particular person back, we can be sure it isn't the people who have already succeeded.

* * *

American collectivists have long wanted the government to nationalize the railroads. They finally got their wish in recent decades. As Gregory Bresiger shows, they should have been more careful about what they wished for.

What if family finances were run like the Social Security Trust Fund? William Conerly describes his imaginative method of financing his children's college education without having to give up anything.

The Academy Award for the best movie in 1998 went to *Shakespeare in Love*. The script was co-written by Tom Stoppard, whose plays have a feature that sets him apart from most of the arts world: anti-collectivism. Norman Barry looks at the philosophy that underlies Stoppard's work.

The market order has been credited for many good things. Andrew Cohen finds one more way it benefits us: it provides a foundation for friendship.

Antitrust law's interference with business efficiency has long been documented by economists and legal scholars. What gets far too little attention is its immorality and injustice. D. T. Armentano demonstrates that the law fails the test of ethics too.

Ever since historian Richard Hofstadter wrote his book *The Paranoid Tradition in American Politics*, statists have had a convenient way to smear any uncompromising advocate of individual liberty and limited government. James Bovard takes a close look at the book, the thesis, and the author.

Medical treatment presents many complex ethical issues. State intervention in health care only makes difficult matters worse. Karen Selick discusses a case from Canada.

This month marks the centenary of the birth of the late W. H. Hutt, an important and prolific free-market economist. Richard Ebeling contributes an appreciation of Hutt's long career.

Golf used to be a relaxing pastime. Then the environmentalists came along. Ray Keating explains.

Lawyers have long been jealous of their monopoly in the practice of law. George Leef describes the lengths to which the profession is willing to go to prevent people from obtaining legal advice outside approved channels.

Attempts by states to impede corporate takeovers are presented in humanitarian terms. But as Christopher Mayer explains, they are special-interest bids that undermine property rights.

The clash between academic freedom and freedom of association may seem irreconcilable—until a missing element is brought into the debate. A controversy at the University of Notre Dame prompts James Otteson's discourse on rights real and imagined.

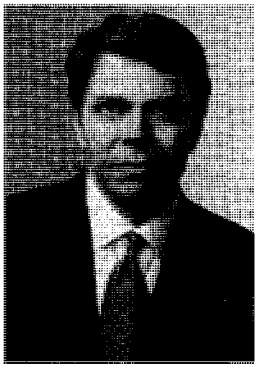
In the columns department, Donald Boudreaux distinguishes real false consciousness from false false consciousness; Lawrence Reed remembers hard-money man James Blanchard; Doug Bandow argues for voluntary voluntarism; Dwight Lee links conservation to speculation; Mark Skousen reminds us of what Say really said; and Charles Baird reads the California legislature the riot act about compulsory unionism for professors. Andrew Morriss wonders if a hidden fist is really necessary to protect the invisible hand and decides "It Just Ain't So!"

Book reviews this month examine the federal government's welfare state for Indians, the Great Depression, the importance of property, the lives of two lucky people, and the global environmental movement.

—SHELDON RICHMAN

Thoughts on Freedom

by Donald J. Boudreaux



True False Consciousness

A few years ago I listened to a professor from a prestigious law school speak on the modern economy. This learned scholar was baffled that people voluntarily shop at Wal-Mart and Home Depot. He asked: "Why do so many people patronize large, impersonal retailers who destroy downtowns and sell goods that destroy the human spirit? Why do consumers and workers willingly permit themselves to be oppressed by capitalism?"

His answer was one that's given with appalling frequency by many statist scholars: false consciousness. This is the notion that people act contrary to their true interests because they don't know what's good for them. Refusing to abandon juvenile notions about the horrors of private property and free markets, radical leftists instead resort to accusing the masses of collective stupidity. "Workers are falsely conscious," intoned the law professor. "Their participation in capitalist institutions and their refusal to revolt against them reflect only the awesome power of capitalism to deceive its victims."

Good heavens! Not only does capitalism oppress the body and soul, it oppresses the mind as well—so much so that its cruelly abused victims remain oblivious to the injustices visited upon them.

The Economist's Reaction

My initial response to hearing allegations of false consciousness is to dismiss the concept out of hand. People, as economists inelegantly say, are rational. They're not so stupid as to be oblivious to being abused.

But the more I reflect on the matter, the more I realize that false consciousness is real. Contrary to statist claims, however, false consciousness arises only in politics and not in the private sector.

When are you most likely to be adequately informed to make choices? When are you most likely to put forth the mental effort necessary to weigh all available information and then exercise the discipline required to make decisions that are best over the long haul? It's when you have a significant personal stake in the outcome *and* when your decision matters.

One of the great benefits of the rules of private-property rights and freedom of contract is that they oblige each decision-maker to bear the bulk of the costs—and permit each decision-maker to enjoy the bulk of the benefits—of each of his decisions. Also, by concentrating decision-making power in individuals rather than dispersing it among collectives, private property gives each individual genuine influence over the outcome of events. Private-property rights promote true, not false, consciousness.

Consider, for example, a woman who voluntarily puts aside a professional career in favor of staying home to raise her children. Many leftists explain this decision as evidence of false consciousness—as evidence that the woman is hoodwinked by the capitalist patriarchy into thinking that raising children is at least as worthy as pursing a career

Donald J. Boudreaux is president of FEE.

outside the home.

Nonsense. The stay-at-home mom makes her choice very carefully. After all, the woman herself bears a large portion of the benefits and costs of the decision, and her decision is decisive: it alone determines what she will do. If she chooses to pursue a career, she pursues a career; if, instead, she chooses to become a homemaker, she becomes a homemaker. These two features—bearing personal consequences and exercising a decisive ability to choose which alternative to pursue—mean that the choice made by any woman in such a situation should be presumed to be the product of rational thought and of a mind cleared of distortions.

Likewise for the other decisions that statists assert to be distorted by false consciousness: people's decisions to shop at Wal-Mart, workers' decisions to take jobs at non-unionized firms, consumers' decisions to smoke cigarettes, and women's decisions to be surrogate mothers. Each such decision has direct consequences for each decision-maker, and each such decision is firmly in the hands of the person who makes it—no one else can lawfully veto it. No other set of circumstances is as likely to prompt humans to be rational, competent, and clear-headed decision-makers.

Political False Consciousness

Compare the private decisions that statists so distrust to those decisions that statists applaud, namely, political decisions. Unlike private decisions, people make political decisions with no incentive to choose wisely. While private decisions are individualized (that is, no person must share decision-making authority), political decisions typically are made collectively, with no individual exercising decisive influence. For example—and most notoriously—no voter determines the outcome of an election. Therefore, unlike in private settings, Jones can vote for A and get B instead. This is so regardless of how passionately Jones desires A. Knowing that his vote will not swing the election, why should Jones bother to become adequately informed about the relevant issues?

In addition, and again unlike in private settings, voters (and legislators and bureaucrats) are permitted to help determine how *other* people will lead their lives. When the issue in an election is, say, whether or not Sunday alcohol sales should be allowed, each voter is given the opportunity to push the government to override the private decisions of individuals, each of whom knows best whether buying alcohol on Sunday is best for him or her.

False consciousness, then, indeed is real. But it afflicts people as voters rather than people as private decision-makers. Only in voting booths are people prone to act consistently contrary to their true interests. Again, if the outcome of an election is unaffected by how you vote—and if the bulk of the consequences of electoral outcomes fall on people other than you—you gain nothing by casting an informed and prudent ballot. Your vote, like everyone else's, will be uninformed and ill-considered.

Statists have it backwards. Capitalism doesn't foster false consciousness; politics does. The political process encourages ignorant and imprudent decisions that often run counter to the best interests of the very voters who cast their ballots in support of such decisions. One of the many splendid benefits of private property and free markets is that these institutions give each person an unambiguous incentive to make wise decisions—that is, not to suffer false consciousness. □

THE FREEMAN
Ideas On Liberty

Markets Need a Hidden Fist?

It Just Ain't So!

When I want to jump-start my Sunday by kicking up my blood pressure a few points, I head down the driveway for the Sunday *New York Times*. Some weeks it is the front page that does the trick, other weeks the op-ed page. Few Sundays have given me a more eye-popping, artery-clearing boost, however, than March 28, 1999.

To mark the publication of *The Lexus and the Olive Tree*, his new book on globalization, *Times* foreign affairs columnist Thomas L. Friedman wrote an extraordinary cover story for that week's *New York Times Magazine*. The magazine was graced with a large photograph of a fist painted with an American flag and emblazoned with the headline: "What the World Needs Now."

The fist symbolizes Friedman's message that what the world needs is for the United States not to "be afraid to act like the almighty superpower that it is." Military strikes against Afghanistan, Iraq, Sudan, and Yugoslavia during the last 12 months suggest one might reasonably at least quibble with the notion that any significant level of fear prevents America from acting like an almighty superpower. Friedman is in no mood to quibble, however. "From supercharged financial markets to Osama bin Laden, the emerging global order demands an enforcer. That's America's new burden."

The world according to Thomas Friedman divides along two dimensions. One stretches between the Separatists and the Integrationists, those who want to wall America away from the world and those who want to plunge in. The other dimension stretches between the Social-Safety-Netters, who "believe globalization will be sustainable only if it is democratized, in both the economic and the political sense," and the Let-Them-Eat-Cakers, who want to let the poor fend for themselves. Bill Clinton, along with Friedman, is a Social-Safety-Netter/Integrationist while Ross Perot is a Let-Them-Eat-Caker/Separatist. You get the picture.

For all his experience in exotic foreign lands and hobnobbing with his big-shot friends, Friedman's problem is that he doesn't really grasp what a market is. Friedman understands that markets "generate the incomes and absorb the technologies needed to keep standards of living rising." What he doesn't seem to have a clue about is how markets do that. Friedman misses two key points.

First, markets are a means to solve what F. A. Hayek called the knowledge problem. Almost anywhere I go, I find an incredible array of goods from virtually every corner of the world. To take just one example, on my daughter's last Girl Scout camp-out we did a global product hunt and found goods from every continent except Antarctica among the (relatively) small amount of stuff we took with us. That all those things get here without our being aware of the alternative uses for those goods elsewhere in the world would be miraculous if it weren't so commonplace. The result is prosperity.

Second, markets create a sphere for human freedom that would justify their existence even if they didn't create prosperity. For many reasons societies that rely on markets are freer than societies that don't. Markets offer the potential for anonymous transactions that free us from accounting to the government for our purchases. Markets also offer us a wider variety of means to pursue our own ends than any alternative form of social organization.

No Force or Fraud

To do those things, markets require remarkably little. In the absence of force and fraud,

markets facilitate voluntary transactions that create wealth. If I sell you one of my widgets, as long as I don't misrepresent what the widget does or hold a gun to your head, we're both better off. I've got your money, you've got my widget. Thus all a market really needs to function is protection against force and fraud. Many institutions can be used to stop force and fraud, and government is one (but only one) of the potential solutions.

Governments create problems as well as solve them (something Friedman never mentions), and we might hesitate to employ government solutions when we think the problems outweigh the benefits. Reasonable people can differ about just where the balance tips, but Friedman wants nothing to do with a comparative analysis of institutional strengths and weaknesses.

According to him, markets need supplementing for two reasons. First, we need to "democratize" globalization by compensating the losers from increased trade, because if we don't "the have-nots, know-nots, and turtles . . . will eventually produce a backlash that will choke off your country from the world." In other words, we need to bribe those who have benefited from stifling tariffs and other special-interest rules to relax their grips on our throats. As a matter of practical politics this may carry some weight; as a matter of principle it is repulsive.

Second, Friedman thinks we need to worry about those pesky foreigners who don't understand the benefits of globalization quite as well as he does. His basic idea boils down to this: "The hidden hand of the market will never work without a hidden fist—McDonald's cannot flourish without McDonnell Douglas, the builder of the F-15. And the hidden fist that keeps the world safe for Silicon Valley's technologies is called the United States Army, Air Force, Navy and Marine Corps." In other words, if it weren't for America the Global Policeman, we wouldn't have all those foreign markets for our goods.

Our armed forces certainly play a major role in the world today—although an important part of their role is subsidizing other nations by freeing them from the burden of providing for their own defense. It may even be that McDonald's gains new markets by our stationing of troops around the world. From Indonesia to Zaire/Congo and other countries where American support has propped up kleptocracies for decades, the hidden fist is a not-so-hidden dead-weight loss that impoverishes both the people of those countries and American taxpayers.

The fundamental premise of Friedman's argument is wrong: McDonald's and Intel, Microsoft and Ford—all are successful or not overseas for the same reasons they succeed or fail at home: because people around the world either want their products or do not. To the extent American companies' success depends on the flexing of our fist to coerce others into buying their products, it is the United States that is engaged in undermining markets, not other countries. If Americans heed the call of people like Thomas Friedman to start swinging our red, white, and blue fists, we are likely to find that among the first casualties are our freedom and our prosperity.

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THE FREEMAN
Ideas On Liberty

Train Wreck

by Gregory Bresiger

"The power to tax involves the power to destroy," Supreme Court Chief Justice John Marshall said. So does the power to regulate.

In the decades after World War II, many American railroads fought a losing battle for survival.[1] Railroad executives had been lulled by strong performances during the war into thinking that good times were back. However, the regulatory and legislative measures were in place in the 1940s and '50s that would destroy dozens of private lines and result in the bankruptcy of the biggest survivor, Penn Central.

Critical elements in the decline of railroads were regulators' saddling them with money-losing operations as well as preventing them from pursuing new profitable ventures.[2] Another important factor was the tax financing of competitors. Those politically adept rivals that persuaded lawmakers to fund them included the aircraft, truck, and auto industries. Labor unions, backed by the government, also insisted on continuing uneconomic practices, such as overstaffed train crews and outdated pay scales. Unions also stopped modernization.[3] They exerted political power and had a say in whether some railroad consolidations took place, such as the Pennsylvania and the New York Central merger.

Governments in this era were committed to the airplane, the car, and the massive construction of highways—especially the interstate highway system that was sparked in part by national security concerns—and were hostile to railroads. Highways, almost all of them owned by governments, were given many advantages. They had dedicated sources of revenues that kept them modern and well maintained. They were untaxed, while railroads paid crushing taxes.[4] These costs for the railroads inevitably discouraged service improvements and triggered a vicious circle. When service declined, passengers and freight customers blamed the railroads, not the lawmakers or regulators. When customer numbers declined, service deteriorated further. The process was irreversible as long as the railroad industry was heavily regulated.

The struggling railroad industry was unable to maneuver. In a free market, businesses expand or contract services based on where managers see profitable opportunities. Nimble entrepreneurs move quickly to add or drop operations. In their fight for survival in the 1940s and '50s, private railroads wanted to fall back on freight service and quickly scuttle many passenger runs because in America freight had traditionally subsidized passenger service. Railroad executives wanted to raise some prices and cut others, trying to find a new formula for success. But they were often blocked by the regulators.

"Railroad management," writes historian Stephen Salsbury, "found their hands tied." He notes that most other American businesses in peacetime had the ability to set their own

Gregory Bresiger is a senior writer with Financial Planning Magazine.

rates and determine "the nature of their service."[5] Railroads didn't have the freedoms of other businesses. If allowed to concentrate on freight service, many roads that died in the postwar era would have had a better chance to survive. Rate deregulation and the freedom to concentrate on more profitable lines were surely the keys for ailing railroads. However, state and federal lawmakers, feeling political pressures, generally blocked these survival efforts. It would take the sudden destruction of some of the biggest lines to awaken lawmakers and regulators to their mistakes, which had been repeated over generations.

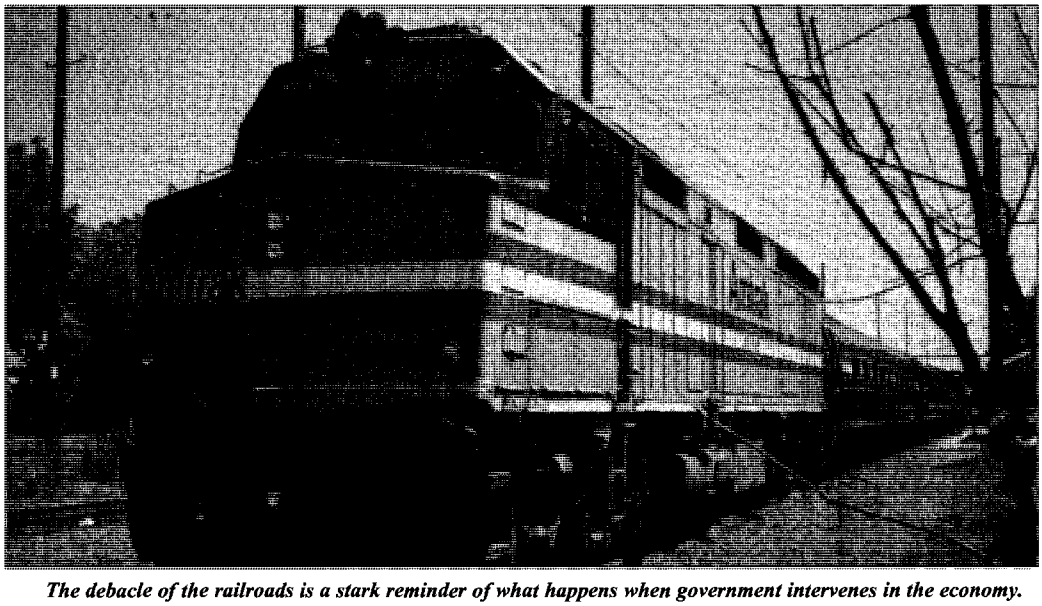
The Death of an Industry

By the late 1950s the regulatory and legislative disasters had come to fruition. Congress had pushed ahead with the Federal Highway Act of 1956 and established a highway trust fund. With up to 90 percent of a superhighway financed with federal money, state officials jumped on the bandwagon and happily paid the rest of the bill. Highways elected lots of politicians and also blinded many Americans to the drawbacks of highways, a point detailed by Robert Caro in his masterful biography of Robert Moses, *Power Broker*, a book about an unelected highway czar with almost unchecked power for 40 years in New York City. By the late 1950s Congress finally noticed what decades of oppressive regulations had accomplished.

There was no doubt that the railroads were in disrepair. "A mighty industry has come upon sick and precarious times," said Senator George Smathers in congressional hearings in 1957.[6] The chairman of the New York Central, Robert R. Young, after a concerted but futile effort to turn the railroad around, shot himself.[7] The chairman of the Pennsylvania Railroad, after detailing the road's skimpy 1956 profits of only $41 million on close to $1 billion in revenues, said government subsidies might soon be needed and that a government takeover was a possibility.[8]

The experience of the once mighty Pennsylvania, a railroad that even in the midst of the Great Depression never missed a dividend, was typical of a sick, over-regulated industry, most of whose leaders just wanted to discontinue money-losing lines in favor of operations with the prospect of earnings. Freight service was hurt by rate regulation, but passenger service was a disaster many railroad executives pleaded for permission to discontinue.

According to the Interstate Commerce Commission, American railroads lost huge amounts of money in passenger service every



COURTESY: THOMAS E. McMASTER

The debacle of the railroads is a stark reminder of what happens when government intervenes in the economy.

year from 1945 to 1970. The industry-wide deficits reached $500 million to $600 million. Only freight and outside investments delayed the death of some railroads.

Highways, airlines, and even pork-barrel waterway projects were the favorites of federal lawmakers. Railroads were the ugly duckling. For instance, in 1958 some $10.3 billion was spent on the national highway program—expenditures that years later led to complaints that cities were drowning in automobile traffic. By contrast, in the same year, railroads paid $180 million in taxes to all levels of government.[9]

A takeover of the railroads, especially the unwanted passenger lines, was discussed at the 1957 hearings. In the 1950s and '60s the problem continued to fester. By the 1970s, the massive train wreck finally happened. Dozens of railroads failed, mostly in the east, where they were more dependent on passenger service. The biggest failure was Penn Central, but others included the Reading; Central of New Jersey, New York, New Haven & Hartford; Erie Lackawanna; Boston & Maine; Lehigh Valley; and the New York, Ontario & Western.

The Promise of Government Railroads

Government railroads had been the dream of American progressives and socialists going back to the early part of the century. Writer Frank Norris had planned a series of novels to depict the predatory nature of railroads but never completed the "Trilogy of Wheat" saga. American socialist parties had consistently advocated nationalization, as did parts of the "progressive" wing of the Republican and Democratic parties. Economic populist William Jennings Bryan advocated government ownership in the 1890s after a visit to Czarist Russia, where the railroads were owned by the state.[10] During World War I the government took over the railroads and approved huge new costs that were imposed on the owners when the roads were handed back after the war.[11]

In *The Promise of American Life* (1909), progressive Herbert Croly opposed outright



W. J. Bryan (1860–1925)

nationalization of the railroads, but argued for gradual government takeover, with the industry slowly accepting a greater role for government management. Croly expected railroad entrepreneurs to dig their own graves; a variant of Lenin's prediction that the capitalist would sell the rope to his murderers. "In return, for instance, for the benefit of government credit, granted under properly regulated conditions," Croly wrote, "the railroads might submit to the operation of some gradual system of appropriation, which would operate only in the course of several generations, and the money for which could be obtained by the taxation of railroad earnings."[12]

This was an amazing scenario, given that in 1909 railroads were one of the more profitable parts of the American economy. Still, Croly could figure a way to nationalize them. A system of "gradual" appropriation would come through intense regulation that turned investors, passengers, and business customers away from railroads. Another destructive form of regulation, a set of outdated accounting standards, had been imposed by the ICC. Those standards made it difficult for railroads to correctly price services. "I.C.C. accounting," complained one railroad executive, "was

not only obsolete, but actually impossible to utilize effectively in controlling costs."[13]

"Be Careful What You Wish For"

When the "promise" of government railroads was achieved in the early 1970s, with the bankruptcy of the Penn Central and the takeover of service by a government corporation, socialists and other friends of government ownership would find they had achieved a Pyrrhic victory. Although Croly and Bryan, among others, had argued that government would bring coordination and better service to the rails, Americans today, after more than two decades of Amtrak, are not impressed.

Government ownership of railroads did nothing to reverse generations of disgust with passenger railroads. Amtrak, which inherited this shaky edifice of regulated railroads, found it was committed to featherbedding practices and lines that could not be discontinued because of political pressure.[14] Frequent promises to run the trains on a self-sustaining basis never were kept.

Amtrak subsidies, which tend to benefit the rich because the ridership is overwhelmingly high income, have totaled some $13 billion between 1972 and 1997.[15] Despite all the marketing efforts and government "investment," only a tiny minority of Americans use the government railroad. An Amtrak president, Roger Williams, conceded that the road's pathetic ridership numbers constitute no more "than a drop in the bucket" in the nation's transportation system.[16] Government ownership and frequent promotion and marketing of Amtrak had done nothing to persuade people to use trains again.

The problem, in a word, was politics. Unlike their transportation rivals, private railroad executives had never been good political players. For instance, in the 1970s and '80s, aircraft and automobile lobbyists effectively argued that Lockheed and Chrysler could not be allowed to fail. Government loan guarantees saved those poorly run corporations. In the Penn Central crisis, there were no loan guarantees. With the birth of Amtrak in 1971, the railroads have become a plaything of politicians, with routes shaped to fit the pressures applied by key congressmen.[17] Red ink exploded.

It was once inconceivable that the government would own and operate America's railroads; they were at the foundation of industrialization and so profitable they were a big part of the early Dow Jones Industrial Average. The debacle of the railroads is a stark reminder of what happens when government intervenes in the economy. The power to regulate is the power to control. It may not be the quickest method, but it is probably the surest way to socialism and then to ruin. □

1. See Ernest W. Williams, *The Regulation of Rail-Motor Rate Competition* (New York: McGraw Hill, 1958).

2. The Interstate Commerce Commission, in decisions in the 1930s, '40s, and '50s repeatedly prevented railroads from moving into other forms of transport such as air and water. See Donald M. Itzkoff, *Off the Track: The Decline of the Intercity Passenger Train in the United States* (Westport, Conn.: Greenwood Press, 1985), p. 49.

3. John F. Stover, *The Life and the Decline of the American Railroad* (New York: Oxford University Press, 1970), p. 217.

4. See Clarence B. Carson, *Throttling the Railroads* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1971), pp. 90–91.

5. Stephen Salsbury, *No Way to Run a Railroad: The Untold Story of the Penn Central Crisis* (New York: McGraw Hill, 1982), p. 49.

6. Itzkoff, p. 44.

7. Salsbury, p. 83.

8. Itzkoff, p.45.

9. Robert Sobel, *The Fallen Colossus* (New York: Weybright and Talley, 1977), p. 222.

10. Charles Morrow Wilson, *The Commoner: William Jennings Bryan* (Garden City, N.Y.: Doubleday), pp. 289–303.

11. Merle Fainsod, *Government and the American Economy* (New York: Norton, 1959), pp. 163–64. Also see Walker Hines, *The War History of American Railroads* (New Haven: Yale University Press, 1928). Hines says private railroads suffered low profits after they were handed back to private control and many managers of private roads "were intensely dissatisfied with the labor situation" (pp. 226–30).

12. Herbert Croly, *The Promise of American Life*, Arthur Schlesinger Jr., ed. (Cambridge, Mass.: Belknap Press, 1965 [1909]), p. 377.

13. Salsbury, p. 151.

14. Rodger Bradley, *Amtrak: The U.S. National Railroad Passenger Corporation* (Dorset, Mass.: Blandford Press, 1985), pp. 123–24.

15. Stephen Moore, "Amtrak Subsidies: This Is No Way to Run a Railroad," "This Just In," May 22, 1997, Cato Institute Web site, www.cato.org.

16. Itzkoff, p. 3.

17. George W. Hilton, *Amtrak* (Washington, D.C.: American Enterprise Institute, 1980), especially pp. 19–30.

A College Fund on the Social Security Model

by William B. Conerly

Thanks to Social Security, my wife and I have discovered how to guarantee our children's college education without any sacrifice on our family's part. No, we aren't so old that our retirement checks will go directly to the university. We have an even better method: our family has adopted the Social Security model for a college trust fund.

It began when our 10- and 12-year-old children started asking us what college is like. After we described the wonders of exciting lectures, late night bull sessions, and the newfound freedom for parents, our older son asked if it cost money to go to college. What an ugly question!

Later that evening my wife and I agreed that we ought to start saving some money for the kids' college education. But how to save? As we walked around the house, we saw the crumbling infrastructure. Well, not really crumbling, but the house is in need of some fresh paint and a decent lawn irrigation system.

Then there were the pressing social needs. The spring-break ski week helps to bring us together as a family, and the evenings out with my wife are vital to maintaining a solid marriage. What more pressing social needs could there be?

My wife proposed cutting back spending on computer games, to which I agreed. But the children pointed out that the games are an investment in the future, because both boys expect one day to make millions as game designers, or at least thousands as professional game testers. Who can be against investments in education and technology? Thus, we just couldn't cut the current budget, despite the looming college crunch.

A Great Idea

The great idea came when I studied the Social Security Trust Fund. I called a family meeting to announce the establishment of the Conerly College Trust Fund.

"Where will the money come from?" my wife asked. I assured her that we would put money into the fund, but not have to cut our current spending.

"How will the trust fund be invested?" asked my older son, who has a budding interest in the stock market.

"The fund will buy Conerly Bonds," I explained, waiting for cries of understanding and adulation. The family fell silent, so I explained: "We're following the Social Security model here. The Social Security Trust Fund buys bonds issued by the U.S. government. So, the Conerly College Trust Fund will buy bonds issued by the Conerly Family."

Still no response. "You see, a bond is just a loan. The trust fund will lend the family the money we need to continue spending on our infrastructure needs, social needs, and investments in the future. That way the fam-

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ily continues to spend as ever before, while the trust fund grows to a nice fat sum. I just hope that you kids can get into a college expensive enough to use up all of our big trust fund."

My younger son, who had been silent up to now, didn't understand. "But how will we pay off the Conerly Bonds? If the family isn't able to pay for our college without the trust fund, how will the family be able to pay off the bonds when we turn 18? I don't get it."

"Don't worry, son," I told him, "there are some things that Daddy just can't explain. But I'm sure you'll be able to understand it after you've gone to college. I suggest you study economics." □

Classic Satires

Every age has its witty fable exposing the reigning fallacies, from Jonathan Swift's *Gulliver's Travels* to George Orwell's *Animal Farm.*

In 1990, ***Princess Navina Visits Malvolia*** joined this list. With its captivating diagnosis of modern political woes, it describes a strange land where politicians are duty-bound to cause harm. Hence, they devise policies to provoke social unrest, encourage idleness, and frustrate entrepreneurs.

Since that first volume, political scientist Jim Payne (who writes these tales under the pseudonym Count Nef) has produced two sequels:

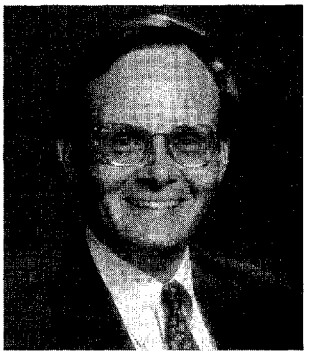
– ***Princess Navina Visits Mandaat*** tells of a country where government tries to fix every problem – yet somehow nothing seems to work.

– ***Princess Navina Visits Nueva Malvolia*** (just published) is about a country where politicians are duty-bound to harm people and stay popular in order to win elections. So they follow the "strategy of good intentions," presenting their vexing schemes as compassionate programs to ensure fairness, guarantee jobs, and protect children.



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James U. Blanchard III: Champion of Liberty and Sound Money

Great movements are marked by the dedication and accomplishments of steadfast individuals who make the most of every moment, every opportunity, and every available resource. When those great men and women pass from the scene, they leave behind untold numbers of friends and followers who derive comfort from their memory and inspiration from their deeds.

Such a man was James U. Blanchard III, who died on March 20, 1999, at the age of 55. The causes to which he devoted ceaseless energy and for which his name will always be associated are liberty and sound money. Jim knew that neither one is long safe without the other, and few American businessmen in the second half of the twentieth century did as much as he to promote them both. The opening sentence of his family's formal notice of his passing summed him up well: "James U. Blanchard III was a man who accomplished much against great odds, and changed more people's lives than he ever knew."

I was privileged to know Jim Blanchard for the last 15 years of his life. For two years I served as an economist for his firm. I spoke at many of his conferences. I traveled with him to Brazil, Nicaragua, and Kenya. Though many others knew him better, it didn't take much acquaintance with him for anyone to marvel at what a man in a wheelchair can get done if he puts his mind to it. Jim was nearly killed in a tragic automobile accident at the age of 17 and was unable thereafter to walk. But if anything, his handicap only spurred him on.

Not once did I hear Jim Blanchard bemoan his physical plight. If he talked about it at all, it was to relate how sitting in a wheelchair gave him time to read. In his 20s he read voraciously. Introduced to the writings of Ayn Rand by a medical student friend, he became an unabashed defender of laissez-faire capitalism. Rand's influence on Jim is perhaps best exemplified by the name he gave his oldest son: Anthem. Jim also became a devoted reader of *The Freeman* and books by FEE's founder, Leonard Read.

In 1974, Gerald Ford signed a bill that restored the right of Americans to own gold. The real hero of that moment was Jim Blanchard, who had formed the National Committee to Legalize Gold in 1971 and spearheaded a nationwide grassroots campaign. He knew that governments don't like gold because they can't print it. He saw gold ownership as a fundamental human right, a hedge against government mismanagement of money, and the first essential step down the long road to monetary integrity.

True to his spirit, some of Jim's efforts were dramatic and unconventional. He arranged for a biplane to tow a "Legalize Gold" banner over President Nixon's 1973 inauguration. He also held press conferences around the country at which he would brandish illegal bars of gold and publicly defy federal officials to throw him in jail. These and many other sto-

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ries about Jim's colorful career can be found in his 1990 autobiography, *Confessions of a Gold Bug*.

Once gold became legal, he held his first annual investment conference in New Orleans. Expecting 250 attendees, he was stunned to see 750 show up. Now in its 26th consecutive year, Blanchard's New Orleans Investment Conference has drawn tens of thousands of individuals from all 50 states and 35 nations. Investment advice comprised most of the 25 programs Jim assembled, but he always made sure that attendees were provided a hefty dose of sound-money and free-market ideas. His speakers included Milton Friedman, F. A. Hayek, Robert Bleiberg, Walter Williams, and many other great economists. Ayn Rand's last public appearance was at a Blanchard conference.

In the meantime, Jim's original $50 investment to begin a coin business in the 1970s blossomed into a giant within the industry. When he sold the business 15 years later, it was a $115-million-a-year precious-metals and rare-coin company. In 1993, he launched a second such firm, Jefferson Coin & Bullion, Inc.; it's already one of the largest in the United States. Other business ventures he helped start were notably successful, including the Blanchard Group of Funds, which held as much as $1.7 billion under management before being sold in July 1995. He cofounded the Industry Council for Tangible Assets to combat unscrupulous business practices in the coin and bullion industry, and he helped reverse several burdensome laws and regulations that afflicted American investors.

Jim's adventurous instincts and love of liberty combined to put him on the front lines of important struggles around the world. On my return in 1986 from visiting with activists in the anti-communist underground in Poland, I went to Jim with a request. I advised him that for $5,000, pro-freedom forces in Warsaw could translate Milton Friedman's *Free to Choose* into Polish and then print and distribute hundreds of copies throughout the country. He wrote that check on the spot, and many others for similar causes behind the Iron Curtain. Not content only to fund these worthy endeavors, he often transported illicit, pro-freedom literature himself when he visited communist countries.



James U. Blanchard III

One of Jim Blanchard's favorite foreign projects was assisting anti-communist rebel forces inside war-torn Mozambique in the 1980s and early 1990s. He once sent a colleague and me on a clandestine journey inside the country to live for two weeks with the rebels in the bush and help spread a pro-freedom message. Once the war was over and Mozambique adopted policies friendly to private property and free markets, Jim pitched in to assist in reconstruction. Through Blanchard Mozambique Enterprises, he obtained a concession to rejuvenate 580,000 acres and create the largest privatized game reserve in the world. His plans for the development of lodges and resort facilities within the reserve will go forward and will in turn support the wide-scale reintroduction and protection of a number of big game animals.

Jim Blanchard overcame personal tragedy to become a powerful figure for liberty and sound money. His indomitable spirit lives on in all those who know that the noble causes to which he devoted his life require both hard work and eternal vigilance. □

THE FREEMAN
Ideas On Liberty

Freedom and Morality in the Plays of Tom Stoppard

by Norman Barry

Most people who were dazzled by the verbal dexterity and comic genius revealed in Tom Stoppard's Oscar-winning movie, *Shakespeare in Love* (his co-writer, Marc Norman, provided the idea but every line of dialogue is quintessentially Stoppard's) do not realize that behind this extravagant frivolity is a serious, indeed political, playwright. Unusual for a British writer, Stoppard is not a man of the left; not since Noel Coward has Britain had an artist so unashamedly "right-wing." He once famously said: "I burn with no causes. I cannot say that I write with any social objectives. One writes because one loves writing."

He displayed a welcome hedonistic approach to life with his reply to a question on his first play, *Rosencrantz and Guildenstern Are Dead* (1966). "What is it all about?" he was asked. "It is about to make me a lot of money," he said. One can't imagine Harold Pinter or Arthur Miller saying that: they are far too "serious" and morally pompous.

But all this is a little disingenuous, for Stoppard is actually much more politically acute than Pinter and Miller, and he is certainly more morally mature and intelligent. He has written at length on political themes, notably in his anti-communist plays *Professional Foul* (1977) and *Every Good Boy Deserves Favour* (1977) and in his memorable dramatizations of modern philosophy, especially *Jumpers* (1972). All these works, and many others, reveal a deep commitment to morality and an intellectually, as well as theatrically, coherent rejection of that relativism which logical positivism and sterile linguistic philosophy have spawned. Above all there is a confident exposure of the dehumanizing aspects of Marxism and its relativistic anti-ethics.

Philosophy and Morality

Undergirding what Stoppard calls his conservatism in politics ("I am a conservative in politics, literature, education and theatre") is a deep and uncompromising view of the morality of freedom; a conception that could almost be called natural law. It enjoins the universal precepts of human liberty and a commitment to a minimalist equality. Equally important is the idea that ultimately morality is individualist; our fundamental values cannot be submerged in a collectivist enterprise and personal responsibility ought not to be diluted by the ersatz ethics of nationalism, ideology, or an overpowering sense of religion (though this is not to say that he has no belief in God). As he said in an interview: "However inflexible our . . . beliefs . . . they owe their existence to individual acts between individuals, which themselves are derived from an individual's intuitive sense of what is right and wrong." Correct values are simple and immediate in their appeal. As Chetwyn says in *Professional Foul*: "A good rule, I find, is to try them out

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on men much less clever than us. I often ask my son what he thinks."

The intellectuals have made morality socially untenable, and in *Jumpers* Stoppard mercilessly and comically exposes the aridity and ethically subversive nature of logical positivism ("truth is an interim judgment," says a leading character). Set in a university, the play features yellow-clad gymnasts who reproduce physically the verbal agility of the positivists ("I have seen the future and it is yellow"). They are opposed by a believer in old-fashioned moral absolutes, Professor George Moore, who points out that the acrobatic team consists of a "mixture of the more philosophical members of the university gymnastics team and the more gymnastic members of the Philosophy School." They are mainly positivists, empiricists, Benthamites, behaviourists, even lapsed Kantians, and they all make fantastic leaps of the imagination along with their gymnastic flights of physical fancy. Their political wing, the Radical Liberals, have just won an election but the positivists' victory is spoiled by the murder of their most prominent member, McFee. They soon discover that there are absolute values; a circumstance the logical positivists normally find difficult to accommodate.

Even worse, McFee had already defected before his death, having himself witnessed a murder on TV. George cannot handle the slickness of the positivists and never makes the final lecture that would restore intellectual respectability to his absolutist beliefs or secure them in a plausible notion of God. George's metaphysical meanderings seem as inconsequential as his zany wife Dotty's badly rhymed rendition of classic musical comedy numbers ("I want to spoon to my honey I'll croon love's June or July"). Both seem out of touch with modernity. The positivists, in their sanitized belligerent way, are as much responsible for the misery in the world as are the overt totalitarians. As Stoppard said, in a fine refutation of moral equivalence: "The point is not to compare one ruthless regime against another—it is to set up one against a moral standard . . . and at least my poor professor in *Jumpers* got that right."

Stoppard's first theatrical onslaught against Marxism is in the extraordinarily adroit *Travesties* (1975). Three famous people, James Joyce, Tristan Tzara (the founder of the anarchic artistic movement, Dadaism), and Lenin are all in Zurich at the same time (1917) and are involved with a British civil servant, Henry Carr, in a production of *The Importance of Being Earnest*. Here one of the targets is Lenin's materialism ("people were a sensational kind of material object") and his dehumanizing theory of art and revolution. Lenin almost sobs with admiration at hearing Beethoven's "Appassionata," but quickly relapses into an ideological harangue against Western capitalism, for example, a free press will be "free from bourgeois anarchist individualism." For him art's only role is to be the servant of the class war. This small speech constitutes an instructive vignette on the depredations of ideology.

As it turns out, Carr is the real hero of *Travesties*. He may have somewhat jejune old-world British characteristics and an odd dress sense, but he does espouse Stoppard's own beliefs in genuine artistic freedom, civil liberties, and a modest patriotism. And the important point is that these values are not negotiable; they are the universal standards by which we assess the *secondary* claims of art and politics.

The Political Plays

Stoppard was originally criticized for his alleged indifference to contemporary social issues; compared to the tedious moralizing and posturing of fashionable left-wing theatrical ranters, his retreat into cleverness, sheer verbal wizardry, and literary adroitness were a welcome relief. But two important plays in 1977—*Professional Foul* (written for TV) and *Every Good Boy Deserves Favour* (with music by André Previn)—firmly established him as an anti-communistic and pro-West writer. Stoppard had long been involved with Czech dissident movements (he was born in Czechoslovakia in 1937 but his family moved two years later) and his political views were not unknown—but he had not let them interfere with his professional work in the theatre.

Professional Foul nicely blends philosophy

and politics. Anderson is an orthodox analytic philosopher who believes that ethics are mere conventions and not really worthy of intense speculation apart from the linguistic puzzles they might generate. He is on his way to Prague to pursue his real interest, football (soccer). There is a game on during a philosophy conference to which he has been invited to give a paper. His smug equanimity is disturbed by his meeting a former student, Pavel Hollar, who has been reduced to a cleaner's job because of his political views: he wants to have his thesis smuggled into the West. Anderson's complacent detachment is counterpoised by the moral absolutist, Chetwyn, and the conceited, amoral Marxist, McKendrick.

But circumstances, mainly the arrest of Hollar and the threat to his son, compel Anderson to engage in substantive moral issues. He changes the subject of his paper from a tame analytic enquiry about nothing important into a ringing declaration of human rights and a strident denunciation of communist tyranny. Against the subjectivism that had previously dominated his metaphysics he now says that "there is a sense of right and wrong that precedes utterance" and, in a neat paraphrase of a famous aphorism of Wittgenstein's, maintains that "whereof we cannot speak, thereof we are by no means silent." Anderson discovers that ethics are not club rules we can change at will; and at some risk to himself, as well as at the cost of missing the football game, he manages to get the thesis out of Czechoslovakia. In a gesture of supreme irony, Stoppard arranges for it to be placed in the luggage of McKendrick. There is redemption for philosophy after all.

In Every Good Boy Deserves Favour, Stoppard mercilessly parodies, with deadly intent, Soviet psychiatry. Mental hospitals are really prisons ("your opinions are your symptons") and the dissident Alexander finds himself alongside a genuinely mentally disturbed patient, also named Alexander, who thinks he is conducting an orchestra. Indeed, an aberrant triangle functions as a discordant element in the grisly order of communism, as well as allowing Stoppard to make some complex wordplay on geometrical configurations. Again, correct morality is presented through a child, Alexander's nine-year-old son Sacha ("Papa doesn't lie").

The ending of the play, in which a KGB official appears to confuse the two Alexanders so that both are released, caused some controversy at the time it was produced. It was said that Stoppard had concocted a bureaucratic bungling to effect a tame happy ending. But this was not so; it was a genuine decision by the regime. It did not want the embarrassment of continuing to persecute a famous dissident. That was the only relief available from the horrors of communism, but as Stoppard well knows, it was a poor consolation for the thousands of unknown victims of tyranny.

Both plays reflect Stoppard's concern to stress the dependency of politics on morality. As he said: "All political acts have a moral basis to them and are meaningless without it." This basis is objective, and Stoppard is disgusted by those people in comfortable situations in the West who think otherwise: Marxism and relativism "are now the quite familiar teachings of well-educated men and women holding responsible positions in respectable universities, and the thing to say about such teaching is not that it is "radical" but that it is not true. . . . It is silly. Daft. Not very bright. Moreover, it is wicked." He knows, and has articulated very well, the absurdity of Marxist economics and sociology. But what he thinks has not been expressed strongly enough is its bankrupt and dehumanizing non-morality.

Stoppard, of course, has had the inestimable advantage of not going to university, yet he is undoubtedly thinking of those contemptible fellow travelers in Soviet Studies at Ivy League universities who were defending communist regimes as late as 1990.

Chaos and Order

In addition to the political implications of his objective ethics, Stoppard is also interested in some more general philosophical themes. An abiding concern is his sometimes comic exploration of the relationship between order and chaos and the possible unreliability of conventional scientific truths. His plays themselves are often constructed out of seemingly bizarre concatenations of events. There

is an order out there, but it often has to be imagined, and although he is conservative about science, as in everything else, he is very much aware of the inadequacy of simple linear theories. It explains his recent excursion into chaos theory in his much-acclaimed play *Arcadia* (1993). But some of the themes here are presaged in his first stage success, later made into a movie, *Rosencrantz and Guildenstern Are Dead.*

One recalls the opening scene where the two hapless Shakespearean courtiers from *Hamlet* keep spinning a coin, which keeps coming up heads. As well as effecting a mild redistribution of income this phenomenon obviously breaches the laws of probability and introduces us to what was to become a familiar Stoppard theme: uncertainty even about our most firmly held and apparently well-established convictions. The play itself is *Hamlet* seen from the wrong end of a telescope: characters come in and out of the action, they do unexpected things, and yet some semblance of order (though indescribable) is maintained. People die as they should, if not quite in the place and at the time that Shakespeare originally intended. Moviegoers will notice how Stoppard uses a similar technique in *Shakespeare in Love*; the *Romeo and Juliet* theme is a convenient peg on which to hang his invented relationship between Will Shakespeare and Viola.

The theme of order out of chaos is much more fully explored in *Arcadia* in which, at the beginning of the nineteenth century, a 13-year-old but precocious schoolgirl, Thomasina, discovers chaos theory while doing her math homework. What is described is a non-linear world that is also further exemplified by a modern character's study of the breeding of grouse: the play is set in two different time periods, nineteenth-century England and the present day. The world may not be Newtonian but it is orderly, a theme that Stoppard directly borrows from James Gleick's book *Chaos*. But in his own imaginative reconstruction of the theory, Thomasina shows how simple rules and equations, which contain apparently no random elements, can generate extraordinary complexity. Also, they have much greater explanatory power than conventional scientific theory.

Stoppard himself veers toward an understanding of the world in terms of a kind of order, though he clearly appreciates the dramatic power that chaos can create: "iterated algorithms" and other paraphernalia of modern mathematics adorn the play. The only philosophical omission in all this is the absence of any consideration of what the debate might imply for freedom. But the implication from his other work is that in politics he is an indeterminist; after all, his fierce anti-collectivism reveals a deep commitment to liberty and personal responsibility.

But *Arcadia* itself is wonderfully complex. Stoppard manages to work in a purported explanation of the mysterious disappearance of Lord Byron after a duel in 1809 alongside the pyrotechnics. The order/chaos dichotomy is further explored with the description of the changes in English social life as evinced by the transformation of the garden from classical symmetry through to "picturesque" disorder. It also contains some of Stoppard's delightfully witty comments on sex, which rival those in *Shakespeare in Love*: "Is sexual congress like love?" Thomasina asks her tutor innocently. "Oh no, it is much nicer than that," he replies knowingly.

Freedom and Literature

It is doubtful that the success of Stoppard will lead to a renaissance of "conservatism" in English literature. Already Shakespeare is being subtly removed from many courses (he was, of course, a racist and a sexist), so what chance does an avowed Thatcherite have of getting on the syllabuses of left-dominated schools? The class war and communism may be over in the regimes Stoppard has so brilliantly, and poignantly, pilloried, but they go on in their enervating ways amongst the British intelligentsia, especially in the arts.

But none of this matters. Stoppard does not work in the subsidized theatre. Nobody who has lived parasitically off the state could venerate freedom as much as he does. He would dazzle us with his verbal dexterity and theatrical innovations even if there were no political problems to worry about. And that, I am sure, would be his own Arcadia. □

THE FREEMAN
Ideas On Liberty

Friendship and the Free Society

by Andrew I. Cohen

Private property and limited government are unrivaled in promoting personal liberty and material abundance. These institutions of a free society also beat the competition in promoting another vital personal and social good, namely, friendship.

Beneath our differences, people understand that self-respect, some wealth, a sense of personal efficacy, and maybe even a dash of luck are among the essential ingredients of a successful life. These values would still seem shallow or pointless without friendship. As Aristotle observed, "No one would choose to live without friends even if he had all the other goods." Our achievements would be emptier and our failures more unbearable without friends by our side. If friendship is then not the supreme good, it is certainly an essential one. Some of us are admittedly less social than others. The companionship that comes in meaningful friendships nevertheless seems to be a key part of the good life.

There are of course many sorts of friendships. Some persons are friends out of convenience. Perhaps our typical "acquaintances" fall into such a category. There are also friendships based merely on what two people find mutually pleasing. Both of these types of relationships help amplify our lives in various ways, but the best sorts of friendships are those where each friend cares deeply and sincerely about the other. In such complete friendships, each friend respects the other person, not as a means to his own ends, but as an end in himself.

A free society is uniquely qualified to promote the most complete friendships because it provides the institutional framework most favorable to them.

Freedom by Degrees

By a "free society," we can speak of a social and political framework with three key features: (1) private property is protected as inviolable, (2) government's role, at most, is to prevent and punish the violation of individual rights, and (3) all human relationships are voluntary. Free societies can exist in degrees. While the United States now is more free than, say, the Soviet Union under Stalin, the United States is not a completely free society. To the extent that a society counts as free, it will provide the best opportunities to nurture and sustain deep friendships.

Consider what is necessary for friendships. Two persons must share some form of good will. There needs to be a certain authenticity to any such mutual affection. This sincere good will helps to nurture a sense of trust and healthy interdependence. Trust is certainly key to building and maintaining any meaningful relationship, particularly in complete friendships where friends have a special respect for each other. But suppose you find yourself in an institutional environment where you have no choice but to interact with some-

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one else. Such a stilted setting will tend to restrict the development of any friendship. While you may still come to be friends with the other person, it is much more difficult for you to do so under such circumstances. First you must overcome some understandable mutual suspicion, but then you must fight the worry that the other merely likes you as a means to some private end.

In all political economies, individuals will sometimes find themselves having to deal with persons somewhat involuntarily. Even in a nearly free society, we may find ourselves working for, going to school with, or just sitting beside persons with whom we would rather have no contact.

Consider just one example. Most municipalities have tightly regulated local telephone monopolies. To a great extent we have no choice but to deal with our telephone repairman. His incentive to engage in gestures of good will, and our reason to show him some sincere regard, are both constrained. The repairman's "have a nice day" rings hollow when we know that we have no choice but to get our telephone service from that one company.

What a free society does is minimize the extent to which human relationships are involuntary. When we have no choice but to deal with someone, sincere good will is often hard to muster. But when individuals are free to come and go as they please and they nevertheless continue to interact with one another, they can be more certain of one another. They might then foster the trust and mutuality necessary for genuine friendships.

Take a lower-level friendship, such as one of mere convenience. We have such friendships with many persons, such as with the family doctor, the corner florist, or (if we are lucky) with car mechanics, plumbers, and carpenters. Our good will toward such persons is mostly based on what they can offer us. Genuine good will is an ingredient in any wholesome friendship. To the extent our displays of good will are sincere, it is because we recognize both the value such persons represent to us and their freedom to do as they wish.

These low-level friendships are often steppingstones toward the more complete friendships where each friend regards the other as an end in himself. People usually do not just fall into friendships. They develop their relationships, often starting out on the fragile and fleeting bases of mutual pleasure or mutual convenience. The trust that comes from freedom of choice can only help foster the good will that gets started in such rudimentary relationships. The enhanced freedom of choice characteristic of free societies also removes several impediments to the deepening of these relationships.

To say that the institutions of a free society best facilitate friendship does not mean that people didn't have good friends in, say, Maoist China. (Perhaps genuine friends were especially valuable there.) But it is far more difficult to discover, nurture, and sustain good friendships when human relationships are not entirely voluntary. What a free society does is enhance our range of freedom of choice. We have more options to select or reject. When you find yourself interacting with persons in this wider range of choice, you have better reason to believe that another's interest in you is genuine. You also have better reason to know that your own interest is genuine. The corner baker is more apt to take an interest in your life when he knows quite well that you could just as well go across the street to a competitor or bake your own muffins. You may also be more likely to feel a mutual good will toward the baker when you know that you are free not to patronize him.

Private Property

Another characteristic of a free society even more important and powerful for advancing friendships is private property.

What good is wealth, Aristotle asks rhetorically, unless we have people we care about with whom to share it? Ambiguously defined property rights and property that is not private notoriously promote waste and neglect. What matters here, however, is that when property is not private, or when it is otherwise not fully protected as private, individuals have diminished opportunities to cultivate the benevolence characteristic of genuine friendships.

There is a certain sort of kindness that helps to nurture and sustain friendships. This is the kindness manifested by freely sharing

one's belongings with others. Unless one owns property, however, it is difficult if not impossible to show benevolence toward another. With what would one be benevolent? It is not benevolence if you grant another access to some good to which you do not have an exclusive, protected claim.

Benevolence is still a vital ingredient in bringing a relationship to a higher level, one where you spontaneously and willingly contribute to a friend's well-being. What property does is give individuals a protected sphere of control over some range of action and material goods. It sets up a divide between what is "mine" (and not yours) and what is not "mine" (but someone else's). "Property" here is not just a material thing but also includes one's freedom, one's time, and one's body. Even the materially poor man can be benevolent toward another; the poor man still owns himself and his time. The authentically benevolent man then freely waives his rights to exclude others from his goods. In doing so, he builds trust and helps to enhance his friend's welfare. Such gestures lay the groundwork for later reciprocal gestures that, in a complete friendship, come freely and without any thought to some payoff.

A free society enhances the quantity of property individuals own and protects as inviolable whatever property rights individuals enjoy. A free society thereby promotes authentic friendships by giving people added opportunities to engage in meaningful sharing. If resources move from one person to another when they do not *have to*, the recipient is better able to gauge the motives of the gesture. Indeed, the one who gave the property away is better able to be sure of his own motives. A free society does well in clearing the air in this fashion. Relationships are voluntary, and property is exchanged and redistributed only through free consent. Such gestures lay the groundwork for the most meaningful sorts of friendships.

Friendships are possible in a variety of circumstances, including in the most repressive of dictatorships. What a free society does is make the discovery, development, and sustenance of friendships of all types—particularly the most meaningful sort—easier. When free, individuals have a diminished need to second-guess the motives of others (and themselves) and they are better in a position to be generous. The freedom not to do what others may want us to do is a valuable liberty. Besides providing a sense of autonomy, that freedom is an important ingredient in expanding the opportunities for the friendships that characterize a successful human life. □

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THE FREEMAN
Ideas On Liberty

The Immorality of Antitrust Law

by D. T. Armentano

The economic inefficiencies associated with antitrust law enforcement are now generally acknowledged. The regulation of mergers and acquisitions hampers the efficient reallocation of corporate assets. The antitrust regulation of product prices and innovation (as in the recent Microsoft case) protects less-efficient business competitors and harms consumers. A century of antitrust litigation—both public and private—confirms that the laws restrain the competitive process and make economic activity less efficient.

Economic issues aside, the antitrust laws also interfere with commonsense notions of liberty and justice, as Adam Smith remarked in *The Wealth of Nations*. Pro-antitrust economists never tire of citing Smith's famous condemnation of price fixers: "people of the same trade seldom meet together . . . but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices." But those same economists rarely acknowledge that Smith immediately went on to assert that "it is impossible, indeed, to prevent such meetings, by any law which either could be executed, or would be consistent with liberty and justice." Smith, a professor of moral philosophy, was opposed to antitrust law on practical *and* ethical grounds.

How do antitrust laws interfere with liberty? All the important antitrust statutes (Sherman Act, Clayton Act, Federal Trade Commission Act) regulate or prohibit purely voluntary or consensual business activity. For example, free-market monopolization implies that consumers choose freely to support only one supplier of some product or service. Free-market prices—whether they are described as discriminatory, or predatory, or collusive—are all determined through voluntary agreement and exchange. Mergers involve voluntary acquisitions of stock or assets. Tying contracts or exclusive dealing agreements are voluntary arrangements to purchase one good and forgo the purchase of another. Since liberty (in a business context) implies the natural right to make any agreement to trade legitimately owned property on any terms mutually acceptable, then antitrust law *must* interfere with liberty.

Microsoft Case

Consider the recent Microsoft antitrust case. The software company clearly has a property right to its software. It has a property right to license (or not license) its software to any PC manufacturers on any terms mutually agreeable. It has a property right to integrate its Web browser, Internet Explorer, into its Windows 98 operating system. And it has a property right to prohibit any licensee's deleting any part of its Windows operating code. The federal government's and the states' attempts to regulate all these peaceful activities (and more) are not only irrational but

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clearly invasive of liberty and property rights as well.

The antitrust suit against Microsoft is also absurdly unjust. Microsoft is the world's premier software corporation. It earned its market position by innovating a user-friendly operating system at minimal cost to the consumer. And rather than "restrain" trade, it has licensed its operating system to hundreds of PC manufacturers here and abroad. That it competed vigorously for market share cannot be doubted; but more important, it committed neither force nor fraud in its commercial activities. Yet for all this, it was rewarded with massive competitor envy and a decade of legal harassment from both the Federal Trade Commission and the Antitrust Division of the Justice Department.

Antitrust and the Rule of Law

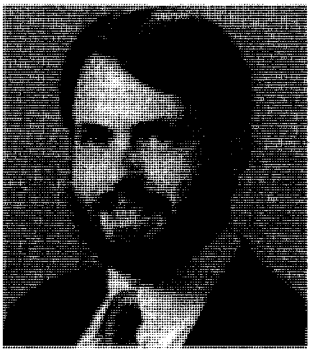
Substantive abuses of liberty and justice occur with antitrust enforcement because owners of property (or trustees standing in for owners) are prevented from engaging in peaceful trade and exchange. But there are also "procedural" difficulties with antitrust regulation. For example, antitrust case law is so inconsistent that it is almost impossible to know from one case to the next which business practices are illegal and which are not. "Predatory prices" are illegal, but how low must prices go (and for how long) before they become predatory? In a "monopoly" case, how will the relevant market share be determined and what percentage of the relevant market will the court determine *is* monopoly? Mergers and tying agreements are illegal if they "substantially reduce competition," but no Congress or court has ever clearly defined that expression with any precision—nor could they. Corporations and businesspeople indicted under antitrust regulation can only discover *after the fact* if they have violated antitrust law. This legal subjectivity is the major reason why those accused of antitrust violations settle their cases pretrial or with a consent decree.

The laws are also inherently discriminatory. In the Microsoft case, for example, the company was accused of entering into exclusive dealing agreements with PC manufacturers; it was also accused of refusing to allow PC manufacturers to delete the Web browser from Windows 98. Yet many of Microsoft's competitors employ similar exclusive agreements with manufacturers, and many refuse to allow a licensee to delete any part of their proprietary software code. If the court rules against Microsoft, the company will have to change those practices—but its competitors will not. They will be perfectly free to engage in the very activity explicitly forbidden to Microsoft. If you think that this is unfair (as you should), remember that this is antitrust. As the judge in the 1953 *United Shoe Machinery* case put it: it was morally acceptable for the court to impose discriminatory requirements on the defendant, United Shoe Machinery Corporation, and not on its competitors since United's unique efficiency *already* put it in a class by itself.

Over 100 years of experience with antitrust regulation confirms Adam Smith's prediction that the laws are inherently abusive of liberty and justice. When our legislators gain the moral courage to repeal the vast antitrust apparatus, both economic performance and individual liberty will be expanded greatly. □

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Voluntarism Should Be Voluntary

Service is good, so government-provided service must be better. That appears to be the motto of the Clinton administration. And the GOP Congress seems to agree.

Shortly after taking office, President Clinton proposed a multimillion-dollar program to hire volunteers: AmeriCorps. As with so many programs, it seemed to be animated by the best of intentions.

Service has a long and honorable history in the United States. Americans' willingness to help their neighbors was noted by Alexis de Tocqueville 150 years ago in his classic, *Democracy in America.*

And so it continues today. Three-fourths of American families donate money to charity. Some 90 million adults volunteer. The Independent Sector estimates the value of their time to approach $200 billion.

But Clinton has never been satisfied with leaving people alone, so in 1993 he suggested putting tens of thousands of "volunteers" on the federal payroll. The prospect of the federal government's becoming a national volunteer coordinator caused some hesitation even in the Democratic Congress, forcing the administration to scale back its proposal to win passage.

Since then, entirely predictable problems have beset the growing program, just as critics warned. For instance, the federal Corporation for National Service treats "public" service as inherently better than private service. Many early AmeriCorps participants were assigned to federal agencies.

The Corporation has turned service into a job that, counting the educational tuition voucher that participants receive, pays more than other entry-level employment. Although some participants undoubtedly think of themselves as "volunteers," others admit that they chose AmeriCorps as a good job option to help them get through college—which is precisely how Bill Clinton pitched the program. In this case, "serving" people through AmeriCorps is no different from flipping burgers at McDonald's, only it's done at taxpayer expense.

There is also the practical question of whether taxpayers get good value for the "service" they pay for. Supporters cite impressive statistics about trees planted and beaches restored, but even the government finds it hard to spend billions of dollars without doing some good. Moreover, the true price of such jobs, however attractive they sound, is the opportunity cost, or the value of other activities forgone.

"Public service" has a nice ring to it, but there is no reason to believe that a dollar going to it will yield more benefits than an additional dollar spent on pharmaceutical research, technological innovation, business investment, or any number of other private purposes. Indeed, the political process almost guarantees that money will be wasted. An AmeriCorps employee who is shelving books in a public library is doing no more than

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someone shelving books in a private bookstore. Nor is it necessarily a good deal to have, say, a potential doctor spend a year surveying residents, handling paperwork, or replacing light bulbs, all tasks performed by Corporation-funded volunteers.

A more subtle problem is the likely long-term effect of federal funding on real volunteer groups and their supporters. It might seem simpler to have the IRS empty people's pockets and hand money to the Corporation, which in turn gives it to charity. But it's better for individuals to send their money directly to deserving groups.

The availability of government support is likely to skew the activities of eligible organizations in an effort to obtain more aid. Moreover, turning the job of funding private groups over to the state encourages people to further abdicate their civic responsibilities. Thoughtfully choosing which charities to support, and monitoring their activities, are themselves important forms of voluntarism. But government-funded service, though implemented in the name of voluntarism, makes it less necessary for people to volunteer time and money in this fashion.

Is it realistic to expect people to volunteer more time and money? They won't if they feel no pressure to do so, and they will feel less pressure if the government not only provides public welfare programs but also funds charitable groups. More fundamentally, people should not be forced to underwrite charities in which they do not believe.

Most Republicans initially opposed AmeriCorps, and they have controlled Congress for more than four years. What has the GOP done with AmeriCorps? Hiked its budget two years in a row. Now the administration is proposing an increase of $113 million for next year, up to $585 million.

At least participation in AmeriCorps, though not the funding, is voluntary. But there are some who would make service mandatory. The state of Maryland, along with as many as 1,200 school districts nationwide, now require that students "serve" in order to graduate from high school. Although constitutional challenges to such programs have failed, Scott Bullock, an attorney with the Institute for Justice, says that lack of popular support compounded by administrative problems has slowed their spread.

Compulsory compassion is a contradiction in terms. There's even increasing evidence that it backfires. A study by Arthur Stukas (University of Northern Colorado), Mark Snyder (University of Minnesota), and E. Gil Clary (College of St. Catherine), published in *Psychological Science*, found that it makes people less likely to volunteer later in life. The authors observe that "limiting an individual's freedom to act may lead to desires to reestablish that freedom, which can be accomplished by derogating the forced activity and by refusing to perform it once the mandate has been lifted." This is not a new view. A 1991 study found that people who were first forced to donate blood were less likely to do so in the future.

Stukas, Snyder, and Clary came to a similar conclusion about broader service mandates. In a review of the effects of one mandatory school program, they found that such a requirement "may reduce interest in an activity." Ironically, the effect was "strongest for participants with greater prior experience as volunteers."

Another study examined the service inclinations of students who both faced and did not face a requirement. While mandates had little effect on students eager to serve, the less-than-eager who were under a mandate were even less inclined to serve in the future than those whose service was voluntary. Thus compulsion drives away the very people it is supposed to attract.

Stukas, Snyder, and Clary suggest "students [be given] a sense of freedom and autonomy in meeting the requirements." But that misses the point. Government should end all such requirements.

There may be no better evidence of the imperialist tendencies of politicians than their attempt to take the voluntary out of voluntarism. People should serve those around them. But they should do so because they believe it to be right, not because the government pays or forces them. □

THE FREEMAN
Ideas On Liberty

Paranoia About Paranoia in American Politics

by James Bovard

Since the 1960s modern "liberals" have often sought to stigmatize those who distrust government as paranoid. This "diagnosis" was first popularized by Columbia University professor Richard Hofstadter (1916–1970). His widely read book *The Paranoid Style in American Politics*, first published in 1965, presented a thesis that is routinely invoked to delegitimize any criticism of government that goes beyond whining about the price the Pentagon pays for toilet seats.[1] It has been the perfect formula to dismiss and deride those who wish to limit government power and expand the sphere of individual liberty.

One of the twentieth century's most respected American historians, Hofstadter is an unrecognized early advocate of politically correct thought. His writing on political paranoia—inspired in part by the 1964 presidential campaign of conservative Barry Goldwater (who had been "diagnosed" from afar as mentally ill by a group of psychiatrists)—has encouraged people ever since to equate aversion to government intervention with pathology. Hofstadter had no such aversion: he was a former member of the Communist Party. When he joined the party in 1938, he wrote to a friend: "My fundamental reason for joining is that I don't like capitalism and want to get rid of it. I am tired of talking."[2] (Hofstadter left the party in 1939, after the Soviet Union signed the Non-Aggression Pact with Nazi Germany.)

Hofstadter's book quickly became sanctified by the academic and political establishment. He acknowledged that "the term 'paranoid style' is pejorative, and it is meant to be; the paranoid style has a greater affinity for bad causes than good."[3] Hofstadter wrote, "What interests me here is the possibility of using political rhetoric to get at political pathology." And in his view, distrust of government was among the worst political pathologies imaginable.

Hofstadter's opinion of the opponents of big government—whom he called "pseudo-conservatives"—was unmistakable: "Pseudo-conservativism is among other things a *disorder* in relation to authority, characterized by an inability to find other modes for human relationship than those of more or less complete domination or submission."[4] (Emphasis added.) He seems to be saying that wishing not to be oppressed by government proves that advocates of a limited state actually want to tyrannize their fellow citizens. The logic was Orwellian, but it played well in academia and in the media.

Hofstadter observed, "The pseudo-conservative is a man who, in the name of upholding traditional American values and institutions and defending them against *more or less fictitious dangers*, consciously or unconsciously aims at their abolition."[5] (Emphasis added.) Hofstadter believed that since the threat of government power is "fictitious," everyone

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who fears government is, by definition, mentally ill. But this diagnosis derived largely from Hofstadter's presumption that people had nothing to fear from government.

Government Spying

The pseudo-conservative, according to Hofstadter, "believes himself to be living in a world in which he is spied upon, plotted against, betrayed, and very likely destined for total ruin. He feels that his liberties have been arbitrarily and outrageously invaded."[6] At the time of Hofstadter's first article on this thesis, in *Harper's* magazine, the Federal Communications Commission was striving to torpedo "right-wing" radio.[7] A few years earlier, President John Kennedy's assistant secretary of commerce, Bill Ruder, had declared: "Our massive strategy was to use the Fairness Doctrine to challenge and harass right-wing broadcasters and hope that the challenges would be so costly to them that they would be inhibited and decide it was too expensive to continue."[8]

Also, the Internal Revenue Service had been carrying out the Ideological Organizations Audit Project to harass and destroy conservative organizations—both nonprofit and otherwise.[9] And it wasn't only "right-wingers" who were the targets of government. J. Edgar Hoover's FBI sought to subvert the civil rights movement by smearing and trying to blackmail Martin Luther King, Jr.[10] In 1962, the Kennedy administration sent FBI officials to do late-night "interviews" with steel company executives who raised steel prices higher than Kennedy approved.[11] The FBI also carried out an extensive surveillance operation at the 1964 Democratic National Convention of a civil rights challenge that President Lyndon Johnson feared would embarrass him.[12] And in 1965, the FBI did background checks on dozens of people who had sent Johnson telegrams opposing his Vietnam policy.[13]

Hofstadter even ridiculed the tendency of big-government critics to heavily document their charges. "The entire right-wing movement of our time is a parade of experts, study groups, monographs, footnotes and bibliographies," he wrote.[14] If "paranoids" offered what appeared to be evidence for their beliefs, that was simply further proof of their mental illness. Once a professor officially attaches the "paranoid" label to a group, no amount of evidence can remove it. And any consideration of the evidence proffered is unnecessary, since the people offering the evidence are known to be crazy.

Some of Hofstadter's criticisms of Goldwater as the archetype paranoid are amusing in hindsight. Hofstadter plinked at Goldwater for his call for the "prompt and final termination of the farm subsidy program."[15] It is difficult to understand why opposition to farm subsidies would be evidence of mental illness, since even wheat farmers decisively rejected federal supply controls on their farms in a national referendum in 1963.[16] Perhaps Hofstadter assumed that the wheat growers who did not want Washington micromanaging their farms were also crazy.

Hofstadter believed that no one could reasonably suspect that government would continue to grow to dangerous proportions, regardless of how rapidly it was currently expanding. Deriding some of the Goldwaterites' fears, Hofstadter remarked: "It reminds me of the people who, because they found several close parallels between the NRA [Franklin Roosevelt's National Recovery Administration] and Mussolini's corporate state, were once deeply troubled at the thought that the NRA was the beginning of American fascism."[17] Yet some of FDR's own Brain Trusters openly admired Mussolini's economic program.

Hofstadter's doctrine rested on his near-boundless faith in the wisdom and benevolence of the ruling class: "American politics is run mainly by professionals who have developed over a long span of time an ethos of their own, a kind of professional code . . . [which] for all its limitations, is an American institution embodying the practical wisdom of generations of politicians."[18] He offered no proof of the wisdom of politicians; instead, it was treated as self-evident. For Hofstadter, fear of losing one's liberty was proof of mental illness—while blind trust in politicians was merely common sense.

Hofstadter also mocked the role of guns in

American life. In one of his last published essays, he wrote, "Every Walter Mitty has had his moment when he is Gary Cooper, stalking the streets in 'High Noon' with his gun at the ready."[19]

Ironically, Hofstadter's article in *Harper's* appeared just two months after the Gulf of Tonkin incident, which led to the congressional resolution authorizing President Lyndon Johnson to fight a war in Vietnam. But there has long been suspicion that the attack never occurred and that an earlier attack had been provoked, contrary to the government's claim. (U.S. ships had been conducting espionage in the Gulf.) Hofstadter ridiculed those who distrusted government, but the Johnson administration's lies and misrepresentations led directly to the deaths of over 58,000 Americans. If Americans of that era had not been so credulous, the Johnson administration could not have railroaded the nation into a futile war. As Army Major H. R. McMaster, author of the 1997 book *Dereliction of Duty*, argued, the failed Vietnam war strategy "was not due just to overconfidence, not due just to arrogance, this was due to deliberate deception of the American public and Congress based on the president's short-term political goals."[20]

Deadly Obsession

Although Hofstadter inspired intellectuals and political leaders to view fear of government as a dangerous pathology, it is the government's obsession over alleged paranoia that can be deadly. This is no better illustrated than by the Ruby Ridge and Waco cases, where government agents provoked and later killed civilians who were seen as threats but who had not initially committed violence. These cases were custom-made to create greater fear of the federal government.[21] Yet political leaders, including President Clinton, use these incidents, as well as the inexcusable bombing of the federal building in Oklahoma City, to smear and dismiss all principled critics of government intervention. For example, in a 1995 speech to a group of federal law enforcement officials after the Waco disaster involving the Branch Davidians, Clinton declared: "There is no moral equivalency between the disgusting acts which took place inside that compound in Waco and the efforts that law enforcement officers made to enforce the law and protect the lives of innocent people."[22] Clinton sought to frame the issue so that no one could criticize what he and the FBI did at Waco—including the gassing of dozens of adults and children—without appearing to favor child abuse.

When Hofstadter's essay was published, three-quarters of the public trusted the federal government to do the right thing most, if not all, of the time. Now only about a quarter of Americans have such trust in government.[23] According to Hofstadter's analysis, distrust of government has grown from the illness of a radical fringe to a mass psychosis of modern Americans. It's regrettable that some people believe things about the government that are not true (the existence of U.N. black helicopters in the United States, for example). But it's almost understandable, considering the routine property violations and deception that have come to light.

Yet much of the academic establishment continues to be mystified by public distrust of government. In 1997 Harvard University Press published *Why People Don't Trust Government*, in which political scientists struggled to discover why so many citizens significantly underestimated the benevolence and trustworthiness of government. The book contained no references to Waco or Ruby Ridge.

For statist academics, paranoia is everywhere. At a 1997 American Society of Criminology conference, one professor argued that among the signs of "hate group ideology" are "discussion of the Bill of Rights, especially the Second Amendment or the Federalist Papers," "discussion of military oppression, in the U.S. or elsewhere," and "discussion of the Framers of our Government."[24]

The Hofstadterian disdain for opponents of big government leads to the Catch-22 of modern statism: anyone who fears government by definition becomes unfit to judge government. Thus, the more people who fear government, the more power government needs because the populace is manifestly unsuited for self-government. Hofstadter's view of those who

distrust government was shared by the KGB, which locked up Soviet dissidents in mental hospitals in the 1970s and 1980s.

This "fear of government-equals-insanity" doctrine is naturally popular among academics and others who prefer not to notice the screws, levers, threats, and pressure valves that government officials use to force compliance with their decrees. The notion that people's attitudes toward government are more important than whatever government actually does is the triumph of the intellectualist perspective on history. According to this view, history consists merely of ideas—some elegant, some trashy—or rather, a series of intellectual poses—some respectable, some gauche.[25]

The Founding Fathers Paranoid?

The easy diagnosis that Hofstadter championed is now embraced by historians who wish to vindicate King George III. Michael Kazin declared in 1997, "In the 1760s, colonists along the Eastern seaboard were convinced that King George III and his ministers meant to abolish their liberties and yoke their economy to the venal desires of the imperial court. The Founding Fathers made a revolution to thwart the wicked plot, one contemporary historians agree never existed."[26] Kazin's statement illustrates how contemporary statist liberals are intent not only on whitewashing today's Leviathans—but governments throughout history as well. That the British were seizing the colonists' firearms, forcibly searching their homes, revoking the rights of local governments, dragooning Americans to England to stand trial, prohibiting them from expanding to the West were, in Kazin's view, no evidence whatsoever of an attempt to destroy American liberties. Perhaps academics should also rewrite the history of the nineteenth-century clashes with Indian tribes, focusing myopically on how Indians distrusted the "Great White Father" in Washington and disregarding picayune details about the Cherokees' Trail of Tears and the massacre at Wounded Knee.

For many statists, distrust of government is the worst conceivable political offense. They are far more skeptical of citizens who distrust government than of government itself. They are willing to forget government lies, but never willing to forget or forgive citizen incredulity. For statists, the highest civic virtue apparently is a bad memory. □

1. The book was republished recently. See Richard Hofstadter, *The Paranoid Style in American Politics and Other Essays* (Cambridge, Mass.: Harvard University Press, 1996).
2. Eric Foner, "The Education of Richard Hofstadter," *Nation*, May 4, 1992, p. 597.
3. Hofstadter, p. 5.
4. Ibid., p. 58.
5. Ibid., p. 44.
6. Ibid., p. 45.
7. Adrian Cronauer, "The Transformation of Television News; the Fairness Doctrine: A Solution in Search of a Problem," *Federal Communications Law Journal*, October 1994, p. 54.
8. Thomas W. Hazlett, "The Fairness Doctrine was Never Quite Fair," *Los Angeles Times*, October 4, 1987.
9. Tom Rhodes, "Kennedys Put Tax Squeeze on Foes," *London Times*, January 29, 1997.
10. Michael J. Sniffen, "Reno Awaits King Family Reaction to Limited Review of Assassination," Associated Press, July 30, 1998.
11. "FBI's 'Political Abuses'; Full Text of Official Report," *U.S. News & World Report*, December 15, 1975, p. 61.
12. Ibid.
13. Ibid.
14. Hofstadter, p. 37.
15. Ibid., p. 98.
16. John Strohm, "The Farmers Vote for Freedom," *Reader's Digest*, September 1963, p. 95.
17. Hofstadter, p. 65.
18. Ibid., p. 102.
19. Quoted in Donald Baer, Ted Gest, and Lynn Anderson Carle, "Guns," *U.S. News & World Report*, May 8, 1989, p. 20.
20. Quoted in John Berlau, "War Planners Carried Out Strategy of Lies, Deception," *Insight*, June 9, 1997, p. 14.
21. See Alan Bock, *Ambush at Ruby Ridge: How Government Agents Set Up Randy Weaver and Took His Family Down* (New York: Berkley Books, 1996) and David Kopel and Paul Blackman, *No More Wacos: What's Wrong with Federal Law Enforcement and How to Change It* (Buffalo: Prometheus Books, 1997).
22. "Remarks to Federal Law Enforcement Officials," *Public Papers of the Presidents*, July 20, 1995, p. 1278.
23. Paul Weyrich, "Who Do Americans Trust?" *Washington Times*, May 21, 1997.
24. Quoted by Joyce Lee Malcolm during an interview with the author, August 5, 1998.
25. When I dedicated my 1995 book, *Shakedown*, "to the Victims of the State," *Entertainment Weekly* (owned by Time Inc.), September 15, 1995, ridiculed the dedication as a "paranoid conclusion."
26. Michael Kazin, "America's Paranoid Streak," *Pittsburgh Post-Gazette*, June 8, 1997.

THE FREEMAN
Ideas On Liberty

Socialized Medicine—One Size Fits None

by Karen Selick

ONTARIO, CANADA—Andrew Sawatzky, an elderly Manitoba man whose wife went to court to fight the "Do Not Resuscitate" order placed on his hospital chart, is probably part of a fairly small minority. His wife says he wants resuscitation if he has another stroke, even though the attempt might fail or leave him permanently unconscious.

I discuss these life-and-death issues frequently with clients when preparing powers of attorney. The vast majority recoil from the thought of becoming brain-dead husks on permanent life support. Most say that if their doctors pronounce further treatment futile, they would rather accept the verdict and "die with dignity."

But what's right or wrong in cases like this can't be determined by public opinion poll. It doesn't matter what 99 people would choose, if the 100th person wants something different. The question remains: what should be done about Mr. Sawatzky?

To me, the ethical principles that should be applied are simple. Everyone should be free to conduct his life however he pleases, so long as he leaves others free to do the same. It's wrong to use force—including the force behind our court system—to bend someone to your will, except to enforce a contract the other person previously agreed to.

The Sawatzkys, if they want heroic and possibly futile measures taken, have the right to try and procure such services. But they don't have a right to force any particular doctor, using the court as their big stick, to render those services. If their current doctors and hospital genuinely believe it's unethical to provide them, all the Sawatzkys can do is look for someone who believes otherwise.

The doctors and the hospital, on the other hand, have no right to impose their will by force on Mr. Sawatzky. For example, they can't refuse to let him leave if he finds an alternative treatment center that is willing to comply with his wishes.

The Money Issue

But there's a good chance he won't be able to find one. Now the secret, unmentionable side of the problem must finally be broached: money.

The hospital couched its objections to further treatment in humanitarian terms, but they rang hollow to me. So what if resuscitation attempts might fail? Why not just try and see? And how can it be "cruel" to treat someone when he understands the risks and still wants the treatment? People make decisions to undergo risky medical procedures every day, and hospitals don't overrule them because the operation might fail or the outcome might be tragic.

If life-support machines grew on trees, and an infinite amount of money earmarked for

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paying doctors' salaries and hospital expenses fell like manna from heaven, we would not be having this debate. Under those conditions, who would deny Mr. Sawatzky his resuscitation request? Why not give him every conceivable chance of survival if he and his wife are willing to risk the possible negative consequences? No one else would be harmed by it.

It's only because medical equipment and human labor are scarce resources that hospitals must make choices about when to use them. And it's the albatross of socialized medicine around our necks that makes us insist on a one-size-fits-all solution. If we give Mr. Sawatzky an unlimited amount of futile medical treatment, how can we ever deny it to anyone else?

Suppose Canadian law permitted the hospital to say to the Sawatzkys, "Okay, we'll furnish heroic measures, provided you pay all the costs—including the cost of all the extra years of hospitalization if he enters a permanent vegetative state." This might well make the Sawatzkys change their minds. Mrs. Sawatzky might not be willing to risk being destitute for the remainder of her life. Her husband probably wouldn't wish to see her sacrifice herself this way. But if the Sawatzkys themselves, the only people who would derive any benefit from the procedure, were unwilling to pay, why should strangers, many of whom would choose death for themselves in comparable circumstances, be forced to?

If people had a choice about what medical care they wished to buy or insure against, different people would choose different plans. Some might purchase the deluxe package—heroic measures and full life support to the bitter end. Others would buy just the basics—painkillers and a quick death. Neither choice is wrong, but the price tags would be very different.

Ironically, those who choose the basic package might end up living just as long as those who choose the deluxe. The money saved on health insurance would allow them to take more leisure, or improve other aspects of their daily lives, or relieve some of their stress, all of which might let them live longer and healthier lives.

This is not a choice the state should be making on our behalf. But socialized medicine takes our choices away—both as to how much we wish to spend, and how much we wish to receive.

There is no moral solution to the Sawatzky case, because we've been dragooned into a system where moral behavior—free, voluntary trade—has been outlawed. The remedy is not to make further bad law in each new case—it's to scrap the whole, immoral system. □

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May the Force *Not* Be With You

I'm just back from seeing *Star Wars: Episode I, The Phantom Menace* with my 11-year-old son, Ben. The space adventure, full of eye-popping special effects, lives up to expectations.

But, alas, I must report on an aspect that will be disappointing to readers of *The Freeman*. The conflict that is the focus of the movie has to do with trade, and the traders are the bad guys. The opening scroll tells the audience that the Galactic Republic has imposed a tax on trade routes to the outer star systems, but "the greedy Trade Federation" is disputing the tax.

The Trade Federation is an organization of merchants so powerful that it has a seat in the Galactic Senate. To challenge the Republic's jurisdiction over the trade routes, the Federation blockades the peaceful planet Naboo, ruled by the teen-aged Queen Amidala. It then invades Naboo, rounds up resisters, and puts them in camps. The Federation seeks to impose a treaty on the planet to legitimate the invasion and persuade the Senate to keep hands off. The Federation's objective is to demonstrate that it controls trade in the outer star systems. The queen refuses to capitulate, and the oppressed inhabitants suffer and starve.

Admittedly, this is a small part of the story. The trade dispute is barely mentioned again. It's simply Lucas's way of getting the story off the ground: the subjugated Naboo must be liberated—a job for the Jedi Knights and their Gungan allies. Lucas's ultimate purpose is to launch the Jedi career of Anakin Skywalker, who will grow up to be Darth Vader. (Whose idea was it to train that kid anyway?)

But militaristic traders? It's oxymoronic. Traders tend to be peaceful. It's hard to conduct business in the midst of combat. Napoleon dismissed capitalist England as a "nation of shopkeepers." Tocqueville and others feared that commercial virtues would drive out martial virtues. Some early Americans shared this view.

The history of trade is a history of peace and cooperation. In the late eleventh and twelfth centuries, traders rebuilt world commerce and developed the transnational "law merchant," the sophisticated, pacific commercial code that plays a role in governing trade to this day. Under that code, traders from different cultures and legal systems resolved their disputes peacefully, swiftly, and efficiently in the merchant-run courts. Form followed function, the function being the facilitating of commerce.

Legal scholar Harold Berman, in *Law and Revolution*, calls the mercantile law "capitalist law par excellence." He notes that "reciprocity of rights" was a key feature of the law. That principle refers to "the element of *equality* of burdens or benefits as between the parties to the transaction—the element, that is, of fairness of the exchange."

The law was not the product of government. Gerard Malynes wrote in 1622 that "it is customary law approved by the authority of all kingdoms and commonwealths, and not a law established by the sovereignty of any

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prince." Berman says that "the initial development of mercantile law was left largely, though not entirely, to the merchants themselves, who organized international fairs and markets, formed mercantile courts, and established mercantile offices in the new urban communities that were springing up throughout western Europe."

I can't imagine these merchants imposing an aggressive blockade on peaceful people. They'd have found other ways to dispute a tax on trade. Maybe someone should send George Lucas a copy of *Law and Revolution*.

I don't wish to single out Lucas. Trade is often misunderstood. While merchants were accused of being pacifists with no loyalty to their nations, they were also suspected of pursuing base and dishonest work. Zero-sum thinking has led people to believe that if a merchant makes a profit, the buyer must lose.

Sometimes the image of trade is ridiculous. If you've ever been to the Federal Trade Commission in Washington, D.C., you may have noticed two statues each depicting a man struggling to hold back a wild horse. The Soviet-style statues are titled "Man Tames Trade." You won't be surprised to learn that they were the winning entry in a sculpting contest during the New Deal. (The winner was the brother of Walter Lantz, creator of Woody Woodpecker.)

Deconstructing the statues is enlightening. The man represents collective Man. The wild horse represents trade. Trade is an activity of individual human beings. Thus, the statue symbolizes collective Man restraining individuals. This puts a new spin on the work of art. Since trade is consensual and occurs only when both parties expect to get more than they give—making the wild horse a poor choice of symbol—we're left with what should have been an ominous (and accurate) message from the government: the Federal Trade Commission exists to restrain free exchange for mutual advantage.

The misunderstanding of trade is on display every time the newspapers announce America's foreign trade deficit. I recall a day when the front page of my newspaper declared in dark tones a record trade deficit, while the business page of the same newspaper pointed out in an upbeat story that since the U.S. economy was doing better than foreign economies, Americans were importing more than foreigners were. Was the trade deficit good or bad news?

In fact, the United States has run both trade surpluses and deficits in good times, but usually surpluses in deep recessions and depressions. More fundamentally, the presence of a deficit or surplus is a sign that one is not looking at a full accounting of economic activity. The trade deficit refers to the merchandise account. We Americans buy more goods from foreigners than they buy from us. But merchandise is not the entirety of economic activity. Foreigners also buy services from us, and they invest here. There's no reason to worry that one account doesn't balance. Foreign merchants have a limited number of ways to dispose of the dollars they earn from sales here. They can buy American merchandise, services, or investments. If they don't want to do any of those things, they can trade their dollars for their own currency. But then the new holder of dollars faces the same choices. However you slice it, there's nothing to worry about.

If everything is counted, the books must balance. It's an accounting imperative. Someone once attempted to do a worldwide accounting of all economic activity. He found that the world was running a deficit in the hundreds of billions of dollars. Who was running the surplus? Naboo? Or were the trade statistics deficient?

While the national trade accounts must balance, that still gives a misleading picture. Nations don't trade. Individuals do, and individuals don't trade in an effort to break even. They trade to come out ahead. And barring error, they do just that.

Forget the Force. May peace and freedom be with you. □

THE FREEMAN
Ideas On Liberty

William H. Hutt: A Centenary Appreciation

by Richard M. Ebeling

In the mid-1980s I had the good fortune to be teaching at the University of Dallas with Professor William H. Hutt as a colleague. By that time he was already in his mid-80s and held the title of "emeritus." Though stricken with an increasingly debilitating case of arthritis, Professor Hutt would be in his office most days of the week working on some article or reading the latest literature on economic theory and policy.

I would ask him to deliver one or two guest lectures in some of my classes each semester, and he almost always graciously consented. In one class I recall Hutt's starting his remarks, in a slightly stammering voice, "Most economists have their works forgotten after they're dead. I've the unique distinction in having had all my works forgotten while I'm still alive."

When Professor Hutt passed away on June 19, 1988, at the age of 88 he left behind a legacy of a dozen books and more than 50 articles.[1] During an academic writing career that began in 1926 he had been a courageous voice for free-market economics at a time when Keynesian economics and interventionist policies dominated both the economics profession and the arena of public policy.

August 3, 1999, marks the 100th birthday of William Harold Hutt, and it seems an appropriate occasion for an appreciation of some of his contributions to twentieth-century economic thought.

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Hutt was born in London to a middle-class family. He joined the Royal Flying Corps in 1916, during the First World War. He would reminisce that he had mastered the art of taking off, but he couldn't quite get the hang of landing; he said his superiors accused him of crashing more planes than the Germans were shooting down.

After the war he enrolled at the University of London and studied with the famous English economist Edwin Cannan. Lionel Robbins, who also studied with Cannan during the same years, recalled that "Cannan was a great teacher. He was a fine economist; he gave one a sense of the sweep and the power of the subject and its relevance to human happiness. . . . I do not know anyone who sat under Cannan in those years who was not powerfully affected by his teaching."[2] What Cannan instilled in Hutt and others who studied with him was a deep appreciation of the miracle of the market economy, which integrated a multitude of global participants in a spontaneous process of coordination.

On to Cape Town

After graduating he worked for four years for Sir Ernest Benn, one of the leading British advocates of laissez-faire economics in the first half of the twentieth century and operator of the Benn publishing house. For part of this time Hutt served as manager of Benn's Individualist Book Club. In 1928 Hutt received a teaching appointment at the University of

Cape Town in South Africa, a position he held until the 1970s, when he moved to the United States, holding visiting positions at several prestigious institutions of higher learning until his appointment at the University of Dallas.

His first published work was an essay on "The Factory System of the Early Nineteenth Century," which appeared in *Economica* (March 1926) and was later reprinted in *Capitalism and the Historians*, edited by F. A. Hayek.[3] He argued that the standard interpretations of early factory life in England during the industrial revolution had often been misrepresentations or exaggerations. He demonstrated that work in the developing manufacturing centers of England had created rising standards of living and improved opportunities for children and women compared to earlier rural life.

His first major contribution was the 1930 book *The Theory of Collective Bargaining*. Hutt challenged one of the most fundamental assumptions underlying interventionist theory: that the individual worker was at an inherent disadvantage in labor negotiations, a disadvantage that could be redressed only through collective bargaining over wages. It was a theme he came back to four decades later in his 1973 work, *The Strike-Threat System: The Economic Consequences of Collective Bargaining*. He explained that supply and demand set wages in the marketplace just as they set all other prices. Wages formed on an open, competitive market assure that no worker is or can be exploited. What determines any worker's worth is the training, experience, and productive capabilities he brings to the marketplace and the value that prospective employers see in those talents and abilities. No employer will offer the worker more than the extra value he is expected to bring to the enterprise. And competition among employers assures that the wage reflects the most highly valued use of his abilities.

Coercive Bargaining

Collective bargaining, Hutt argued, can force wages above market-determined levels only through the use of coercion. Although trade unions threaten to (and do) shut down enterprises through strikes to force employers to acquiesce in their wage demands, wages pushed above market-clearing levels cause some workers who would have found employment to be priced out of the market.

Union apologists have often argued that through collective bargaining and strike threats, organized labor can capture a greater portion of the total revenues earned in an industry at the expense of employers. Hutt demonstrated that at most this tactic can only work in the short run. In the longer run, as profits in an industry fall owing to union wage increases, entrepreneurs will shift to industries where profits are higher. Thus fewer employers will remain in union-dominated industries, potentially reducing total employment opportunities there.

This led Hutt to make the useful distinction between what he called "natural" and "contrived" scarcities.[4] The fundamental problem in society is that means are scarcer than ends. This scarcity is "natural"—an inescapable part of the human condition. The task of the market, through the competitive forces of supply and demand, is to determine how the scarce means of production (including labor) are to be allocated among their alternative productive uses. Scarcities become "contrived," however, when owners of means attempt to withhold part of their supply by politically restricting entry and competition. A special-interest group might do this to boost its income.

Contrived scarcities frustrate what Hutt was the first to call "consumers' sovereignty."[5] In a free market the demands of consumers determine what gets produced and therefore, indirectly, the allocation of naturally scarce resources among their competing uses. When the allocation of resources reflects consumer demand, they can be said to have been fully and properly applied to serve the interests of consumers. The wishes of consumers have been made "sovereign." Politically contrived scarcities frustrate consumers either by withholding some of a resource or by allocating it to a less highly valued use.

Colliding with Keynes

Hutt's criticisms of collective bargaining, strike threats, and the dangers from contrived scarcities meant that beginning in the 1930s he was on a collision course with the emerging Keynesian Revolution in economic thinking. In 1936, Cambridge economist John Maynard Keynes published *The General Theory of Employment, Interest and Money*. He argued that the Great Depression had demonstrated that the market economy could not always employ everyone willing to work at prevailing wages because aggregate demand could be too low. Government would have to fill the gap by increasing its own demand for what the economy produced.

Hutt's first challenge to Keynes came with his 1939 book, *The Theory of Idle Resources*, in which he asked the most obvious question: why would a resource or a worker be unemployed? He responded that workers might be unemployed when: (a) no one has any use for their services; (b) employment opportunities are seasonal and it pays for workers to be idle part of the year; (c) workers won't move to where jobs are, or won't accept the prevailing wages for their skills, or prefer leisure, or have their idleness subsidized; (d) a union pushes wages above market levels and a barrier or incentive prevents the unemployed workers from moving to other jobs; or (e) workers withhold their labor because they are unwilling to accept pay cuts when the demand for their services has fallen.

The crux of the unemployment problem during the Great Depression, Hutt argued, was labor unions' often aggressive resistance to pay cuts in the face of declining demand for various goods and services. The massive unemployment of the 1930s, therefore, was the result of "contrived" scarcities created by government and special-interest groups.

Despite criticisms such as Hutt's, Keynesian economics dominated both economic theory and policy for the four decades after the Second World War. Yet even during the zenith of Keynesianism, William Hutt continued to challenge what was then known as the "New Economics." In a series of articles, such as "The Significance of Price Flexibility,"[6] and in several books, *Keynesianism: Retrospect and Prospect* (1963), *A Rehabilitation of Say's Law* (1974), and *The Keynesian Episode: A Reassessment* (1979), he attacked the fundamental premises of the Keynesian approach.

He argued that Keynes was wrong when he asserted that the classical and free-market economists who preceded him had no theory to explain massive and prolonged unemployment. Hutt said that the economists before Keynes had never claimed that unemployment was impossible or unexplainable. They clearly understood that the selling of goods and labor depended on prices that would find willing buyers. He quoted his old teacher, Edwin Cannan, who had pointed out in 1933 that "General unemployment appears when asking too much is a general phenomenon."[7]

This led Hutt to restate and defend Say's Law. He argued that Keynes's definition, "supply creates its own demand,"[8] is a distortion of its actual meaning. Jean-Baptiste Say and other nineteenth-century classical economists pointed out that people produce only because they wish to consume. What they don't consume they trade for what others have produced. Every offer of supply therefore indicates a demand. Goods of course are typically bought with and sold for money. Unless individuals offer their goods at prices that others are willing to pay and that earn the money they desire, they will be unable to demand what others are selling.

Seen from this angle, Hutt argued that the massive unemployment of the 1930s was not the result of "aggregate demand" being too low, but of prices for goods and labor being too high. Furthermore, these prices created conditions for a cumulative contraction of production and employment. Whenever "inappropriate pricing" results in unsold supplies, Hutt said, the owners of those supplies are less able to demand goods from others. If this second group of suppliers also keeps their prices and wages too high, they also will experience unemployment. The process will repeat itself, widening the circle of unsold goods and unemployed workers.

Flexible Prices and Wages

At the same time, Hutt explained, any lowering of these prices and wages helps release withheld supplies and bring workers back to their jobs. The re-employed workers could then demand goods on the market. Thus flexible prices and wages, adjusting to changing market conditions, would always tend to assure full employment in the economy.

Written during the high watermark of Keynesian economics, Hutt's arguments were often either ignored or rejected as being politically out of step with the times. Yet, this never dissuaded him from defending what he considered to be logically sound and true. In 1936 Hutt published a book titled *Economists and the Public*, in which he insisted that only by ignoring the politically fashionable and expedient could an economist claim to speak with objectivity. The economist's task was to explain the workings of the market process and the consequences that would result from intervention, regulation, and control. Politicians may have to compromise, but not economists. The laws of supply and demand operate regardless of ideological whims and wishes. He defended this position again in *Politically Impossible . . .?* (1971).

As if to illustrate this principle of integrity, in 1964 Hutt published *The Economics of the Colour Bar*, a pro-capitalist challenge to apartheid in South Africa.[9] He showed that race-based government intervention in the economy was bad for both blacks and whites. The book caused a firestorm of controversy and even threatened Hutt's position in South Africa for a time.

Since his death in 1988, traditional Keynesian economics has been eclipsed, union power is no longer viewed as sacrosanct, apartheid has ended in South Africa, and there has been a renewed appreciation and understanding of the free market. To no small extent this has been due to the ideas and principled stance of William H. Hutt. For those of us who had the privilege to know him, his greatest influence was through the wit and humor with which he made his case. Students loved him. In his last years he had to get around the University of Dallas campus in a wheelchair. Some of my students then came up with the following riddle: Why does Professor Hutt always use a wheelchair? Because he hates Keynes.

When told this, Hutt smiled and nodded his approval. □

1. See Richard M. Ebeling, "William H. Hutt, 1899–1988," *The Freeman*, October 1988, pp. 400–401.

2. Lionel Robbins, *Autobiography of an Economist* (New York: St. Martin's Press, 1971), pp. 85–86. Also see my review of *Collected Works of Edwin Cannan* in *Freedom Daily*, August 1998, pp. 41–44.

3. F. A. Hayek, ed., *Capitalism and the Historians* (Chicago: University of Chicago Press, 1954), pp. 160–188; see also W. H. Hutt, "The Poor Who Were with Us," *Encounter*, November 1972, pp. 84–90.

4. W. H. Hutt, "Natural and Contrived Scarcities," *South African Journal of Economics*, September 1935, pp. 345–353.

5. W. H. Hutt, "Economic Method and the Concept of Competition," *South African Journal of Economics* March 1934, pp. 3–23; *Economists and the Public: A Study of Competition and Opinion* (London: Jonathan Cape, 1936), pp. 257–72; "The Concept of Consumers' Sovereignty," *Economic Journal*, March 1940, pp. 66–77.

6. W. H. Hutt, "The Significance of Price Flexibility" (1954), reprinted in Svetozar Pejovich and David Klingaman, eds., *Individual Freedom: Selected Works of William H. Hutt* (Westport, Conn.: Greenwood Press, 1975), pp. 130–46.

7. Edwin Cannan, *Economic Scares* (1933), reprinted in Alan Ebenstein, ed., *Collected Works of Edwin Cannan*, vol. VII (London: Routledge/Thoemmes Press, 1997), p. 38.

8. John Maynard Keynes, *The General Theory of Employment, Interest and Money* (New York: Macmillan, 1973 [1936]), p. 18. For a detailed criticism of Keynes's misunderstanding of Say's Law in the context of what the classical economists really said, see Steven Kates, *Say's Law and the Keynesian Revolution: How Macroeconomic Theory Lost Its Way* (Northhampton, Mass.: Edward Elgar, 1998). Also see Mark Skousen's column in this issue of *The Freeman*.

9. The book is available once again through the Free Market Foundation, Johannesburg, South Africa.

THE FREEMAN
Ideas On Liberty

Greens Against Greens

by Raymond J. Keating

Playing golf on Long Island can be a glorious experience. On this sliver of land in the Atlantic Ocean, golfers are treated to various types of golf, from playing often windswept layouts along the north and south shores, to more inland, wooded, and hilly courses.

Long Island also has a fairly impressive history of professional golf. In addition to hosting an annual Senior PGA Tour stop—the Lightpath (formerly Northville) Long Island Classic at the Meadow Brook Club—Long Island courses have hosted six U.S. Opens and five PGA Championships. Most recently the U.S. Open stopped at Shinnecock Hills Golf Club in 1985 and 1996. The Open will return to Long Island in 2002 on the Black Course at Bethpage State Park, and possibly again at Shinnecock in 2004.

Naturally, Long Island is overflowing with amateur golfers, from occasional duffers to the more serious players.

However, all is not serene on Long Island's greens. Courses are crammed with folks hooking and slicing down the fairway. Waiting times to tee off can run into the hours any day of the week, and many facilities have reservation systems, which means that the spur-of-the-moment round of golf virtually has become a blessing of the past.

Other than at private membership clubs, it is not unusual for a weekend round of golf to stretch out to more than six hours. At such times, even the most passionate lovers of the game become annoyed, with the glory of Long Island golf decaying into one of those headaches usually reserved for errant drives and three-putts.

Of course, slow play and long lines are market signals to build more golf courses. And some golf entrepreneurs are trying to do just that on Long Island. However, in addition to onerous property taxes, they face hazards from local environmentalists and NIMBY (not-in-my-backyard) types who possess absolutely no respect for private property. Even though these crusaders are relatively small in numbers, they are hyperactive and hold considerable sway over lazy, easily frightened politicians. The stories of their assaults on property owners—including those trying to build golf courses—are numerous.

From Racing to Golf

For example, the Bridgehampton Race Circuit had served as a home to big-time auto racing for decades. However, as homes started to spring up around the racetrack where drivers like Mario Andretti competed, complaints about noise increased. Town officials ignored the obvious fact that the raceway was there first and tightened government noise restrictions to the point where the racing left Long Island.

The track owner, Robert M. Rubin, then decided to build a golf course and 20 estate

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homes, even agreeing to set aside some 150 acres as open space. For greedy environmentalists that was not enough. They wanted it all, and they tried to force state and local taxpayers to buy the land even though the landowner declared he had no intention of selling. After years of battling, the golf-course project seems to be moving ahead—an increasingly rare victory for property rights on Long Island.

Brother and sister Barry Bistrian and Bonnie Krupinski in tony East Hampton saw their dream of a golf course finally coming to fruition in 1999. Their environmental battle with local officials and activists lasted over two decades.

Bill Coore and two-time Masters champion Ben Crenshaw are the course designers of the East Hampton Golf Club. Small hills mark the front nine, with more of a links style on the back nine. Krupinski notes that the course was laid out with environmental concerns in mind, using native grass, limiting high-maintenance grass mostly to tees and greens, and building with minimal earth movement. As for other benefits to the community, C.J. McDaniels of Crenshaw Golf, which will manage the course, notes that a caddie program for local kids is being established.

The family did not originally plan for a members-only club, but were forced to go that route because local zoning does not allow courses open to the public in residential areas. After all, the local NIMBY crowd couldn't have golf riffraff from other parts of Long Island invading the very exclusive East Hampton area. The family just wasn't up to a battle on that zoning issue.

Meanwhile, in Baiting Hollow, Long Island, the 117-year-old Talmage family farm has grown so efficient in recent years that land was freed up for a 36-hole golf resort also to be designed by Coore & Crenshaw. The courses would be located in a breathtaking spot overlooking the Long Island Sound.

As news got out about the proposal, local environmentalists sprang into action. They hurled all sorts of irresponsible accusations about environmental catastrophe at the project, with little regard for the truth. For example, Long Island's leading environmental activist, Richard Amper, head of the Long Island Pine Barrens Society, claimed in a 1998 *Newsday* op-ed that the course would destroy a rare dwarf beech forest. But as family spokesman Bill Talmage and I walked and climbed his land, he showed me that the golf course will never disturb this thicket. Indeed, he and his family would never want to ruin the beautiful spot where land meets sea. The Talmage family is rooted in a deep respect for their land. They clearly want to do the right thing for the local environment and economy. They are active members of their community who have no plans of moving. Bill Talmage says he wants his grandchildren to be able to say that Grandpa Bill was pretty smart to build this beautiful golf resort, in which the family is a partner.

To build the rhetorical case against the golf project, Amper classified the area as the "Grandifolia Sandhills," saying this was "one of Long Island's most environmentally sensitive areas." While the name of some of the beech trees is in fact "fagus grandifolia," Talmage says that the "Grandifolia Sandhills" classification is a "complete fabrication." I asked folks at the National Wilderness Institute: they never heard of it. And I couldn't find any reference to it when I did various literature searches.

In addition, the project's opponents said the golf courses would ruin rare migrating sand dunes. In fact, as Talmage points out, beyond the normal changes that nature brings, old trees and massive boulders on the land clearly show that the area is anything but migrating.

Normally, local command-and-control environmentalists and NIMBYists would steamroll the land owner and get him to acquiesce. However, Talmage is in the horticulture business himself, cultivating native, wetland, and erosion-control plants, and is knowledgeable about the issues at hand. He has easily debunked the numerous charges made by his opponents.

Tragically, though, the pseudo-science of Long Island enviro-politics captured many easily duped local politicians, and as a result the resort plan probably will give way to one

golf course, some residential homes, and more greenhouses. Talmage says this accomplishes nothing for the local environment, and winds up being less of a benefit for the local economy.

Big-Government Reactionaries

But that does not matter to these local activists. For the most part, these folks cloak their opposition to change in a concern for the environment. More accurately, they can be categorized as big-government reactionaries. They don't like economic change. One of their costly schemes is to have state and local government buy the development rights of farms on Long Island's east end, so that the land will always stay agricultural—even as the cost of farming on Long Island becomes more and more prohibitive. The landowners actually have little choice in the end; once their land is placed in the cross hairs of local environmentalists and politicians, it becomes costly to do anything else with it.

The local reactionaries want to be Long Island's feudal lords, deciding what can and cannot be done with the land. And golf courses are decreed not to be an option. Indeed, Amper has condemned golf courses as "the biggest drinking-water polluters on Long Island." Groundwater serves as the primary excuse to oppose almost all golf courses, especially on the east end of the island. (The same reason is used to oppose houses, buildings, and most everything else you can think of linked to mankind and civilization.) Indeed, "groundwater protection" has been invoked by opponents of golf course projects in Bridgehampton, East Hampton, and Baiting Hollow.

The environmental activists say that as much land as possible must be left in or revert to a wild state. This demand conveniently ties into their desire to have no more people move into the area and to preserve their way of life.

When I asked about the science undergirding his claim about golf courses and pollution, Amper briefly mentioned pesticides, but then referred me to others for explanation. Speaking with and listening to many of Long Island's leading environmentalists, I quickly discovered they cannot back up their grandiose statements.

Amper's hyperbole is contradicted by more sober assessments. A few years ago hydrologist Robert LaMonica told the local county legislature, "There is no reason ever to use water supply as a zoning tool or a restriction on economic development." And several other local experts note that golf courses are no more polluting than homes or agriculture.

In addition, the protectors of the Long Island pine barrens—essentially large, rather ugly tracts of land made up of little, scruffy pine trees—assert that these areas must be protected because that is where Long Island gets its drinking water. This notion has been the main driving force behind draconian restrictions on land use and the millions of taxpayer dollars spent to buy acres and acres of land. However, knowledgeable experts disagree. Donald Middleton, an environmental consultant and a former regional director of the New York State Department of Environmental Conservation, was even quoted as saying: "The Long Island aquifer system is not one continuous and interconnecting underground reservoir. Contamination in one part does not extend throughout the entire system. . . . Long Islanders do not get their drinking water from the pine barrens and they never will."

Why Worry?

A mid-1980s scientific study of golf courses atop sandy, permeable soil in Cape Cod—similar to what you might find on Long Island—reported "little cause for concern about use of currently registered pesticides." As reported in the September–October 1993 issue of *Audubon*, the study examined four mature golf courses and looked for about 17 different pesticides in soil and groundwater samples. For good measure, many golf-course managers are choosing organic management, minimizing the use of chemicals, and working to preserve local flora and fauna. The United States Golf Association also does research and offers advice on sound environmental golf practices. One might expect local environmentalists to work with golf course owners, but too often that simply is not the case.



COURTESY: USGA

Long Island's Shinnecock Hills early in this century.

About those opposing his golf plans, the owner of the Bridgehampton land, Robert M. Rubin, told the *New York Times* last year, "These people are the lunatic fringe." He continued, "Nobody is more worried about the water than I am. I've spent six figures analyzing the situation, and I'm comfortable with it." The *Times* also reported that a professor of turf grass science and a hydrogeological consulting firm hired by the town to evaluate Rubin's plans "deemed the golf proposal plan to be basically in compliance with the various restrictions on the site."

Undaunted by facts and private property rights, the warriors against golf courses continue to wage their battle on Long Island, aided by politicians unwilling to do the hard work of discovering the truth. And even when property owners come out victorious in the end, the costs in time and resources are tremendous.

What does this all mean for Long Island golfers such as myself? Naturally, if golf entrepreneurs are stymied, golfers will suffer. Limited tee times, long lines, and slow play will remain an aggravating part of the game.

Under these conditions, how am I supposed to get my game in gear for the Senior PGA Tour by the time I turn 50 in about a decade and a half? My wife says I'm dreaming, and she's probably right. But as a golfer ready to fork over greens fees, at least I could have my dreams shattered by my own abysmal putting, rather than by a bunch of reactionary environmentalists and NIMBYists. □

THE FREEMAN
Ideas On Liberty

Banned in Austin

by George C. Leef

People love competition. It is wonderful to have others trying to outdo rivals in finding new and better ways to serve you, giving you more alternatives at lower prices. But people also hate competition. How annoying it is to have others trying to take away "your" customers just so they can make money. What nerve!

In our statist era, people have frequently turned to government seeking to hinder or even eliminate the competition they don't like. Those who are adept at manipulating the political system often succeed, getting statutes or regulations that take from others the freedom to compete. Not surprisingly, the legal profession is particularly good at working the system. Competition-suppressing measures have given licensed attorneys a corner on the legal-services market for decades. But one of the legal profession's most recent attacks against competition is especially noteworthy because it involves nothing less than the First Amendment.

The high cost of hiring a lawyer has led to a growing industry in self-help legal books and software. Companies now market books and computer programs that enable anyone to get answers to legal questions and create legal documents at a price far lower than contracting for the services of a lawyer. Non-lawyers welcome self-help publications because such materials increase the range of options open to them when they need legal assistance. On the other hand, many lawyers fear that they will begin to lose "their" clients to those awful books and CD-ROMs. Time for action—but how do you keep books and software off the market in a nation ostensibly committed to a free press?

A Suit Is Pressed

People always look for the least costly way of accomplishing their objectives—and that includes nefarious objectives like stifling competition. For lawyers, the least costly way of stopping competition is to do what they do best. They file a lawsuit.

In 1998 the State Bar of Texas instituted suits against Nolo Press, a Berkeley, California, firm that publishes an array of self-help books and computer programs, and Parsons Technology, an Iowa-based firm that sells computer software including several legal self-help titles. The ground for the suits? The State Bar argued that the firms had violated the Texas statute prohibiting "unauthorized practice of law (UPL)." This law, some version of which is in effect in every state except Arizona, restricts "the practice of law" to licensed attorneys. It is the equivalent of a "No Trespassing" sign around the entire field of legal services.

Individuals have the right to do their own legal work, whether it's drafting their will or defending against criminal charges in court. Publications that merely inform people about the law are legally unobjectionable—law

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libraries are, after all, open to the public—but they are also less beneficial to laymen than books or software that actually help them navigate through the shoals of the law. Because the Nolo and Parsons products stepped over the line by actually helping individuals, the unauthorized-practice watchdogs argued that they had broken the law.

To briefly recapitulate the argument against UPL prohibitions, they are neither necessary nor sufficient to protect consumers against incompetent or dishonest legal practitioners. A free market backed by the possibility of legal remedies for fraud, negligence, or breach of contract is the optimal system for deterring harm to consumers. It has no need for coercive legal action against any peaceful individual or First Amendment-weakening lawsuits such as the Texas Bar Association's.

But those considerations don't matter when the objective is something as vital as preserving billable hours. The UPL Committee's case against Nolo was argued before the Texas Supreme Court in October 1998 and at the time of this writing no decision had been rendered. However, the suit against Parsons ended in victory when in January 1999, federal district Judge Barefoot Sanders granted the bar's motion for summary judgment. That means he saw no need for a trial; on the facts as presented, Parsons must necessarily lose. Judge Sanders followed up that ruling with a ban against the sale of Parsons "Quicken Family Lawyer" software within the state.

What is frightening about this ruling (which may, of course, be reversed on appeal—or stand as a precedent for future attacks against the freedom to produce and sell informational products) is that it undermines one of the cornerstones of a free society. Let's analyze the decision.

First, there was no showing of any specific flaw in the software that had or even might cause a user to make a legal error and suffer some detriment. Quicken Family Lawyer was written by attorneys who specialize in the areas of law covered, and checked for state-to-state variations. Parsons does not want either a bad reputation or a lawsuit from an individual who made some legal blunder because he followed its software. But care in preparation and lack of harm are no defense. Parsons Technology is not licensed to practice law in Texas (only individuals who graduate from law school and pass the bar exam can be), and that settles it.

Second, Judge Sanders brushed off the company's First Amendment arguments. The First Amendment prohibits Congress from enacting any law that abridges freedom of the press, and decades ago the Supreme Court ruled that this restraint on government power also applies to the states and their instrumentalities. In First Amendment cases, the decision almost always turns on the "level of scrutiny" the court will apply. If the judge decides that the case merits "strict scrutiny," then the government's restriction will be struck down unless the state can show that its action is the least intrusive possible means of accomplishing some "compelling state interest." (Never mind that the First Amendment does not read: "Congress shall make no law abridging freedom of the press unless. . . .") Statutes and regulations that are given "strict scrutiny" almost never survive. On the other hand, if the court decides that the case does not warrant "strict scrutiny," then all the government needs to do to prevail is to show that there is some rational basis for thinking that the law furthers some "important" (or similar adjective) state interest. (Again, never mind that the Constitution draws no such distinctions.)

Content Neutrality

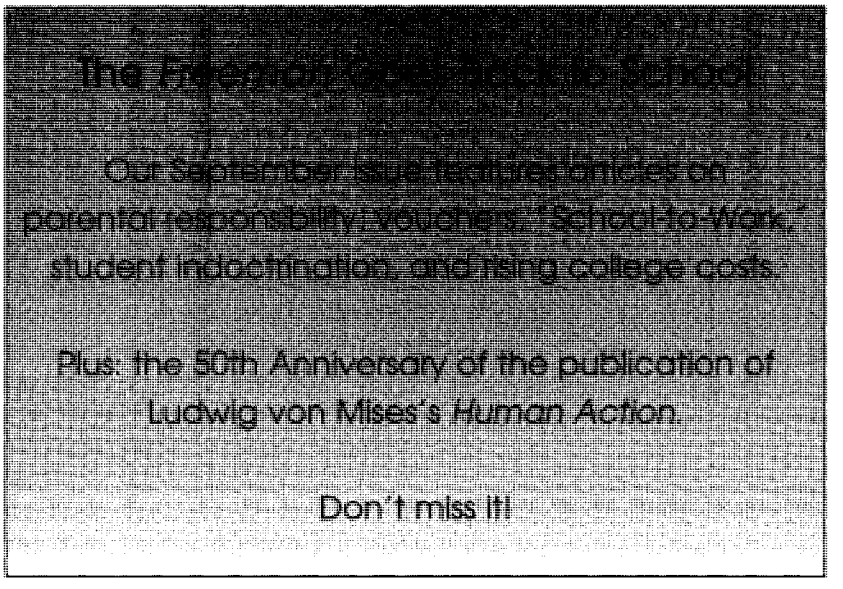
Judge Sanders stated that strict scrutiny would not apply because the restriction sought by the Texas State Bar on freedom of the press was "content neutral." That is, the state was not trying to suppress knowledge or ideas, but merely limiting who was allowed to convey particular knowledge and ideas. In First Amendment jurisprudence, "content neutrality" renders restrictions on freedom of speech or press constitutionally trivial, so the government needs only to meet the easy "rational basis" test in order to prevail. Judge Sanders concluded that the state's "substantial interest" in "eradicating unauthorized practice of law" was justification enough.

The notion that "the state," an abstract entity, can have any interests at all is worthy of debate, but that is a question for another time. Let us ask whether there is in fact some "substantial" public benefit to be achieved in eradicating UPL. Is it something heinous that belongs in the same league as, say, lynching or typhoid fever? Certainly not. What the bar calls "unauthorized" practice is simply a voluntary market transaction. Transactions between consumers and legal practitioners deemed unauthorized by the state turn out satisfactorily as frequently as do transactions between consumers and licensed attorneys. That is one lesson from the free market in legal services that exists in Arizona. The public interest is no more served by eradicating UPL (assuming that the law could do so) than it would be in eradicating, say, unauthorized lawn mowing.

If the state has an interest in the market for legal services at all, it is to maximize access to competent, affordable assistance. That is done not by placing arbitrary restraints on entry into the market, but by establishing the conditions that allow the market to function unhampered. Sadly, public policy is usually made by people who have little or no understanding of economics.

Note also that there are noncoercive means of accomplishing whatever legitimate concerns the State Bar might have, a point that Judge Sanders did not bother with because of his conclusion that the UPL statute was content neutral. (Is it? Texas lawyers evidently have no interest in publishing legal self-help materials, so in saying that only they are allowed to publish something they don't want to publish, the state is in effect suppressing the transmission of knowledge and ideas.) Rather than seeking an authoritarian ban, why couldn't the Texas Bar carefully analyze Quicken Family Lawyer for problems and then bring them to the attention of Parsons? Or lawyers could find QFL users with genuine reasons to complain about its quality and then sue. There is no justification for banning this (or any) product from the market and depriving many people of its benefits just because it might not be perfect for everyone.

Perhaps Parsons will win a reversal on appeal. We should hope so. As it stands, the decision to ban self-help legal software in Texas is a stab wound to the First Amendment, a blow to consumers (especially poorer ones for whom low-cost alternatives are a great boon), and an encouragement to bar associations and other special-interest groups to turn to government whenever they see competition they want to eradicate. □



Economics



Conservation and Speculation

I often ask my students, "How many of you are in favor of conservation?" Except for those who are asleep, every hand goes up. I then ask, "How many of you are in favor of speculators?" and almost no one raises his hand. The students see conservation as a noble activity that prevents people from squandering resources now to insure that adequate quantities will be available in the future. On the other hand, they see speculation as the greedy hoarding of valuable resources now in order to gouge those who will need those resources later. I attempt to explain that if they are serious about conservation, they should also applaud speculation. The speculation that results from private property and the desire for profits is the most powerful force for beneficial conservation.

The Right Amount of Conservation

Without private property rights there could be no speculation for personal profit and no meaningful conservation. As discussed last month, animal species that are *not* privately owned are the ones at risk of extinction. Without private property no one has an incentive to conserve a resource, since no one can benefit from doing so. But if I own a resource and believe its value is going to be greater in the future (after considering the cost of holding it—including the opportunity cost of forgoing interest), I will conserve it for future use or sale. Similarly, even if I don't own a resource, but I believe its value is going to increase, I will buy it at today's price in order to conserve (hoard) it and then sell it at the expected higher price later.

But why should we depend on private property and greed to conserve valuable resources? Why not have the government determine how much of a resource should be conserved and then limit its current use accordingly? Relying on government to enforce conservation would be foolish even if the right amount of conservation were known. If government has enough power to allocate a resource over time, it has enough power to allocate its use to competing alternatives at each point in time. This much power guarantees waste, as special-interest influence replaces the cooperation of market exchange in determining how and where resources are used.

But even if the public interest, rather than special interests, motivated government decisions (dream on), the authorities could never determine the right amount of conservation as accurately as speculators subject to the discipline of the marketplace. There can be too much as well as too little conservation. Just as we don't want to use resources today that will be worth a lot more in the future, neither do we want to sacrifice consumption today to conserve resources that will be worth less in the future.

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Speculators Do It Better

Even if government authorities were not subject to special-interest influence, they would have less motivation to conserve wisely than speculators do. If bureaucrats make wasteful decisions, their salaries aren't reduced. Indeed, their failures often result in larger budgets, supposedly so they can do a better job. In sharp contrast, speculators make money only if they conserve wisely—purchasing resources (holding them off the market) when they are less valuable and selling them (making them available) when they are more valuable. If speculators don't conserve enough they pass up profitable opportunities to buy low and sell high, and if they conserve too much they lose money by buying high and selling low. As opposed to bureaucrats, who can survive despite their mistakes, the speculator who consistently makes mistakes is soon relieved of the money necessary to continue speculating.

Speculators can also act much more quickly than any government agency. For example, at the first indication that next year's Brazilian coffee crop will be devastated by a frost, speculators will immediately purchase raw coffee beans to store them until next year. Consumers will still see plenty of ground coffee in the stores, but suddenly the prices will be higher. What consumers don't see is that coffee prices will be lower next year than they otherwise would have been because they are higher today, and that their reduced consumption today will be more than compensated by their greater consumption later. The complaint will be that greedy speculators have unnecessarily driven up prices. Interestingly, the universal complaint against speculators that they cause current prices to be too high is really a complaint that they conserve too much.

Don't Complain Out Loud

I find it fascinating that people who believe that speculators are responsible for prices being too high complain about it out loud. The last thing you should do if you are convinced that speculators are harming the public by driving up the prices of important resources is to let others know. If you are correct, you can make yourself a fortune by keeping quiet, while providing a valuable public service at the same time. If the public is being harmed by speculative buying, it is because coffee is being taken off the market now when it is worth more than it will be later. If this is so, you would be right to criticize speculators for harmful price increases.

But this is a problem you can help correct. Simply call your broker and sell coffee short. Selling short means borrowing a quantity of coffee (from a speculator) and selling it at the currently high price. When the price falls later, you can buy the quantity borrowed, repay the speculator, and pocket the difference between the two prices. (You will have sold high and bought low.) If you were correct about market conditions, you will have made the coffee available to consumers now *and* made a profit. Why you should keep your criticism of speculators secret is obvious. If others believe you, they will sell coffee short themselves, which will drive down the current price and increase the future price, thereby reducing your profit opportunities.

Too Important to Leave to the "Experts"

Why don't we hear fewer people complaining about speculators and see more people selling short? The answer has to be that most people find complaining easier than understanding what they are complaining about. But the objective here is not to criticize. The important point is that anyone who believes he has better information on the future value of resources or commodities than is reflected in market prices can both profit personally and benefit society by acting on that information—if he is right. So when conservation is left to speculators, far more relevant information from far more people with far more at stake is acted on than if conservation is left to government.

Conservation is important, much too important to leave to government "experts." There is no better way of achieving sensible conservation than through the concern for the future that is motivated by private property, market exchange, and speculators putting their own money on the line. □

THE FREEMAN
Ideas On Liberty

Protection for Bad Managers

by Christopher Mayer

My home state of Maryland is considering adopting anti-takeover legislation to protect the small number of major corporations with headquarters in the state. The legislation would allow the directors of Maryland corporations to adopt defenses against takeovers without the consent of shareholders. Thus the legislation would legally permit company managers to consider interests other than those of the owners—say, the employees, suppliers, customers, the managers themselves—in deciding whether to reject a takeover bid. Managers would be relieved of their legal responsibility to report such bids to their employers, the shareholders.

There is simply no economic benefit to be derived from this legislation, which would put Maryland near the bottom of the list of states with regard to takeover rules. It is the product of parochial state interests and a fundamental misunderstanding of the economic role of the corporate raider. It is also another weapon in the emerging economic war between the states, along with direct subsidies and tax benefits. Such an attempt to prevent takeovers will be self-defeating because consideration of interests other than shareholder interests will result in lower productivity, lower output, and lower living standards. (The federal government already has built obstacles to takeovers.)

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In the interest of full disclosure, I should say that I work for a bank with headquarters in Maryland and I might benefit from such a law. However, I have denounced this legislation at every opportunity. I believe it is a violation of shareholders' property rights.

Why Maximize Shareholder Value?

In the United States it is an accepted fact of corporate life that a firm's mission is to increase shareholder value. Failure to do so results in pressure from the board of directors, activist shareholders, and corporate raiders. The result might be a takeover—the purchase by one person or small group of a controlling share of stock—and the firing of the managers. That's what provides an incentive for managers to perform well.

The role of the corporate raider is therefore essential. Yet the media portray raiders (and those, such as Michael Milken, who finance them) as shortsighted menaces. This makes for lurid journalism and sensationalist storytelling. Recall the bestseller *Barbarians at the Gate* by Bryan Burrough, which chronicled the battle for RJR Nabisco.

However, as G. Bennett Stewart III asks in his book *The Quest for Value,* "Did the 'raiders,' as the pejorative label suggests, pillage companies solely for their personal enrichment leaving a weakened economy in their wake, or did they instead promote improvements in corporate performance and

increases in market values for all to share?"[1]

In his book, Stewart outlines his comprehensive research on nearly 300 financial restructuring transactions completed in the 1980s. In a vast majority of cases the restructuring led to significant increases in market values and operating performance. The restructuring is one reason for the sustained economic growth the American economy has experienced.

The media home in on the job losses that often occur after takeovers. However, jobs are constantly being created as well as destroyed in a market economy. This is a mark of health, since workers are constantly moving to where they do more to satisfy consumers.[2]

Takeovers are generally a threat only to managers whose companies are performing below their potential. Raiders buy stock only from willing shareholders, who surely don't regard the transactions as hostile. The managers whose jobs are at risk understandably see a takeover as hostile to their interests. But they work for the owners. Why are they more deserving of sympathy than stockholders? (Stockholders are not all rich, of course, and managers make well above the minimum wage.)

The potential for a takeover is therefore a strong incentive for management to pursue projects and strategies that maximize shareholder value. Remove the threat of a takeover and you remove one of the shareholders' most effective means of policing management. (It is curious that some of the same people who decry takeovers also, on occasion, decry the lack of accountability of corporate managers.)

Foreign Differences

In other parts of the world, this incentive of managers to maximize stock value is not present. In Germany and Japan managers are expected to consider a more intricate web of stakeholders in the corporation, such as customers, suppliers, government, employees, and even society at large. Maximizing shareholder value is seen as inefficient, shortsighted, or downright selfish and antisocial. However, as authors Copeland, Koller, and Murrin point out, "Shareholder wealth creation does not come at the expense of other stakeholders. Quite the opposite."[3] Research has shown that there is a close link between maximizing shareholder value (which requires an open market for corporate control) and higher living standards and greater productivity. Maximizing shareholder value is especially important in the increasingly global economy, where capital is generally free to seek the highest returns. Societies that do not adopt such a corporate ethic will find it hard to attract and retain investment capital.

Beyond this, there is the ethical matter of property rights. Corporate managers should do what is in the best interest of shareholders because the shareholders own the corporation. Managers work for them. To make a law that weakens this responsibility is to undermine the property rights of the shareholders. When you hire an attorney or an accountant, you expect him to act in your best interests within the framework of the rules. Legislation that permitted your attorney or accountant to consider something other than your interests would be met with derision and disbelief. So should anti-takeover legislation.

In the Interests of State

Why is the state pursuing this legislation? Richard Lewin, the secretary of business and economic development and a prime advocate of the bill, says, "We have very few headquarters companies in this state. They're very important to us. I don't want to lose a Black and Decker or a Mercantile Bank."[4] Thus, stockholders are to be sacrificed to the parochial interests of the state government (and incumbent managers). Unfortunately, the bill's supporters seem to outnumber the detractors. Supporters include the Maryland Chamber of Commerce, the Maryland Bankers Association, and the Maryland Bar Association.

Lewin adds that hostile bidders are "doing it for sheer greed."[5] When badly performing managers try to cling to their jobs at the expense of stockholders, it is never characterized as "greedy."

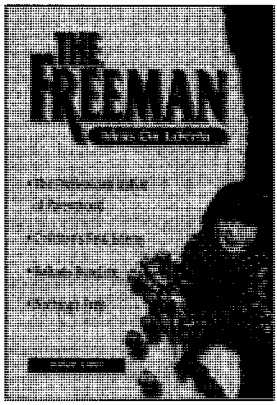
Dan Abramowitz, president of the investment fund Hillson Partners states, "I don't

consider this anti-takeover legislation. I consider it anti-shareholder legislation. I'm a money manager, this is my home state. But if [the bill] passes, I would be far more hesitant to invest in a Maryland company because of the risk that my hands would be tied if something went wrong."[6] The legislation would further re-enforce Maryland's reputation as pro-regulation and hostile to business.

By adopting this legislation with the intent of preserving existing Maryland corporations, the state ignores the long-term dampening affect it will have on new investment in the state and on the probability of new corporate headquarters coming to Maryland. Behold the practical implications of ignoring Frederic Bastiat's great lesson about disregarding the unseen. □

1. G. Bennett Stewart III, *The Quest for Value: The EVA Management Guide* (New York: Harperbusiness, 1991), p. 477.
2. See Charles Baird, "Recycling Labor," *The Freeman*, April 1999.
3. Tom Copeland, Tim Koller, and Jack Murrin, *Valuation: Measuring & Managing the Value of Companies* (John Wiley & Sons, 1995), p. 3.
4. Peter Behr, "Maryland's Hostile Takeover Defense," *Washington Post*, February 25, 1999.
5. Ibid.
6. Ibid.

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THE FREEMAN
Ideas On Liberty

Academic Freedom on Religious Campuses

by James R. Otteson

In a free society adults should be able to associate, establish institutions, and order their lives without interference, provided that in doing so they initiate no violence against others. That indeed is the definition of an open, peaceful society.

One thing in particular that adults are able to do in such a society is establish formal associations and groups. People who share certain views may want to ally themselves to promote and provide a safe haven for their views or just create a place in which like-minded people may gather. Most religious orders, for example, are of that nature: people sharing (some) common interests who establish an association in which they can pursue those interests together. Of course there is nothing wrong with people doing this—in fact, I would suggest that this habit of forming associations, which has been part of human nature for all of recorded history, is an essential element in leading a flourishing, happy life. People need associations and close ties to others to provide them the psychological well-being necessary for being happy.

But trouble can arise in this paradise. What happens, for example, when someone joins an established association and then decides to subvert it? Here we would seem to have a conflict of rights that free people enjoy. On the one hand, the people in the association have the right to maintain whatever kind of group they want; on the other hand, the new member, it would seem, also has the right to express himself as he sees fit. May the other members rightfully expel the newcomer—or does the newcomer have a right to stay and act according to his beliefs? It seems that we cannot have it both ways.

Notre Dame Case

This is precisely the situation in which many religiously oriented colleges and universities find themselves. They were founded and organized to conduct educational activities from within a specific religious framework. They have traditionally appointed presidents and trustees, hired faculty and staff, and admitted students on the basis of their commitment to or at least their tolerance for the school's religious framework.

The University of Notre Dame, for example, has only had Catholic priests of the Holy Cross order as presidents, and it makes explicit its commitment to the Catholic tradition. But Notre Dame now finds itself in a difficult position. It recently hired a faculty member who, it turns out, is not only not a Catholic, but is a Marxist atheist and an open lesbian. To make matters worse for Notre Dame, she is public and militant about her beliefs and practices, and is quite candid about her intention to subvert, as she sees it, the sexist, patriarchal, homophobic tradition of the Catholic church generally and of Notre Dame in particular. And she has further put

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Notre Dame on notice that if it tries to get rid of her, it will be sued before it can say a Hail Mary.

What to do? Notre Dame asserts its right to maintain its Catholic character, which entails, presumably, the right to exclude people who are antithetical to that character. The professor asserts her right to academic freedom, which is guaranteed, she claims, not only by the First Amendment but also by moral principle.

The notion of academic freedom (free speech for professors) was developed and pressed by—who else?—academics who were looking for protection from political persecution. They argued that they should not be punished for the views they hold, even if those views are politically controversial. Moreover, the long-term health of our civilization requires the uninhibited exchange of ideas in the search for truth. Colleges and universities were conceived as safe houses in which even the most outrageous and subversive ideas could be tried and tested. If they were no good, the marketplace of ideas would eventually weed them out; but under no circumstances should ideas be forced out—or worse, not allowed to join the debate in the first place—because they were politically inexpedient or unfashionable. Ideas are just too important to suffer those kind of restrictions, and professors, whose main currency is ideas, therefore deserve special protection on campuses.

This seems to leave us at an impasse, a purported case of rights clashing: the university's right to self-determination and the professor's right to free speech. There is, however, a way out that simultaneously protects the rights—properly understood—of *both* parties. We can eat our cake and have it too.

Misconstruing the First Amendment

The constitutional argument that the renegade professor marshals in her defense does not hold water. The First Amendment says that "Congress shall make no law . . . abridging the freedom of speech. . . ." If Notre Dame fires the professor for her beliefs, how can that be construed as, or even be relevant to, the Congress's making a law abridging speech? Even if we grant the substantial extension of the First Amendment's scope allowed by various twentieth-century court decisions and the "incorporation" clause of the Fourteenth Amendment, it seems plain that the First Amendment does not address private entities. (The emphasis on "private" is crucial. If the entity in question is publicly funded, the picture changes dramatically—and to the extent that Notre Dame accepts governmental funding, its claim to private autonomy is commensurately weakened.[1]) It seems clear that the First Amendment does not even address this professor's case, let alone provide her a protection. But let us not be content to argue about the constitutionality of Notre Dame's proposed action—for in the words of the first Chief Justice of the Supreme Court, John Jay, "anything in the Constitution can be made to mean anything."

Let us focus, then, on the moral issue involved. Would it be a violation of the professor's rights to fire her? And would Notre Dame therefore be acting immorally if it did so? The answer to both questions is no.

Like everyone else, the professor has a right to express herself without restriction from others. But this right does not entail that someone else must listen: included in the right to freely associate is the right to choose *not* to associate with the professor and thus not to listen to her.

To go a step further, although each person has the right to speak freely, no one has a right to demand that someone else provide a forum, for that would violate the other person's right to freely associate. Speech, after all, is merely an expression of belief; speech has been protected throughout the centuries in order to protect the sanctity of conscience. There is nothing special about words (or other sounds) in themselves that warrants protection. Likewise, the freedom to associate is a manifestation of private belief. Thus both the right to speak freely and the right to associate freely protect the right to believe what one wants to believe—and, by extension, to act peacefully on those beliefs.

An example will illustrate my point. Sup-

pose you hire a painter to paint your living room and halfway through you notice that he has painted it all black enamel, though you had told him you wanted a light periwinkle. Suppose, then, you quite understandably fire the painter, at which point he claims that you had no right to fire him because that would abridge his freedom of artistic expression. You would undoubtedly inform him not to let the door hit him on the way out. He does indeed have a right to freedom of expression, but that does not mean he has the right to express himself in your living room. So your firing him does not infringe his rights; it merely asserts yours. It is your house, and you get to say what goes on in it. The painter may express himself elsewhere—in his own living room, perhaps.

The principle can be generalized to all private associations. Any group of adults may unite under any consensual conditions they please and they may include or exclude others as they see fit. Now there is an important restriction: if the group entered into a contract with a new member, it is bound to honor the contract even if the group later regrets the decision. But that has nothing to do with the right to free speech. (The standard pre-tenure university contract permits the dismissal of a professor at the end of an academic year.)

Reconciling the Notre Dame Dispute

The upshot is that Notre Dame can fire the subversive professor *and* respect her right to speak freely. By firing her it is acting entirely within its rights to associate freely. On the other hand, it has not interfered with her right to speak freely. She can continue her mission to subvert the Catholic church and to convince people that Christianity is a superstition. All Notre Dame would be saying is that it chooses not to provide her a forum. She can say what she wants, just not on Notre Dame's nickel.

As a university professor myself, I can assure you this issue is of no little moment for me. I would love to have someone else guarantee a lifelong forum in which I could espouse whatever opinions I wanted. But I, like my colleagues, have no right to force others to provide me with such a forum. If that means that Marxist atheist lesbian professors cannot get jobs at Catholic universities, then I think that is the price we pay for living in a free society. □

1. For an excellent summary of court decisions and other important historical events regarding academic freedom and the scope of the First Amendment, see Alan C. Kors and Harvey A. Silverglate, *The Shadow University: The Betrayal of Liberty on America's Campuses* (New York: Free Press, 1998), chapters 1–3.

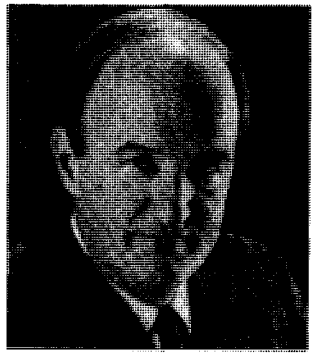
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THE FREEMAN
Ideas On Liberty
AUGUST 1999



Say's Law Is Back

"Keynes . . . misunderstood and misrepresented Say's Law. . . . This is Keynes's most enduring legacy and it is a legacy which has disfigured economic theory to this day."

—STEVEN KATES[1]

In researching my forthcoming book, *The Story of Modern Economics* (to be published by M. E. Sharpe next year), I came across a remarkable new work by Australian economist Steven Kates, *Say's Law and the Keynesian Revolution.* According to Kates, John Maynard Keynes created a straw man in order to produce a revolution in economics. The straw man was Jean-Baptiste Say and his famous law of markets. Steven Kates calls *The General Theory* "a book-length attempt to refute Say's Law."

But to refute Say's Law, Keynes gravely distorted it. As Kates states, "Keynes was wrong in his interpretation of Say's Law and, more importantly, he was wrong about its economic implications."[2] And Kates is sympathetic to Keynesian economics!

How Keynes Got It Wrong

In the introduction to the 1939 French edition of *The General Theory*, Keynes focused on Say's Law as the central issue of macroeconomics. "I believe that economics everywhere up to recent times has been dominated . . . by the doctrines associated with the name of J.-B. Say. It is true that his 'law of markets' has long been abandoned by most economists; but they have not extricated themselves from his basic assumptions and particularly from his fallacy that demand is created by supply. . . . Yet a theory so based is clearly incompetent to tackle the problems of unemployment and of the trade cycle."

Unfortunately, Keynes failed to understand Say's Law. By incorrectly stating it as "supply creates its own demand," he proposed, in effect, that Say meant that everything produced is automatically bought. Hence, Say's Law cannot explain the business cycle.[3]

Keynes went on to say that the classical model under Say's Law "assumes full employment." Other Keynesians have continued to make this point, but nothing could be further from the truth. Conditions of unemployment do not prohibit production and sales from taking place that form the basis of new income and new demand.

Moreover, Say's Law specifically formed the basis of a classical theory of the business cycle and unemployment. As Kates states, "The classical position was that involuntary unemployment was not only possible, but occurred often, and with serious consequences for the unemployed."[4]

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Production and Consumption

Exactly what is Say's Law? Chapter 15 of Say's *A Treatise on Political Economy* describes his famous law of markets: "A product is no sooner created, than it, from that instant, affords a market for other products to the full extent of its own value."[5] When a seller produces and sells a product, the seller instantly becomes a buyer who has spendable income. To buy, one must first sell. In other words, production is the cause of consumption, and increased output leads to higher consumer spending.

In short, Say's Law is this: The supply (sale) of X creates the demand for (purchase of) Y.

Say illustrated his law with the case of a good harvest by a farmer. "The greater the crop, the larger are the purchases of the growers. A bad harvest, on the contrary, hurts the sale of commodities at large."[6]

Say has a point. According to business-cycle statistics, when a downturn starts, production is the first to decline, ahead of consumption. And when the economy begins to recover, it's because production starts up, followed by consumption. Economic growth begins with an increase in productivity, new products, and new markets. Hence, production spending is always ahead of consumption spending.

We can see why this is the case on an individual basis. The key to a higher standard of living is, first, an increase in your income, that is, your productivity, either by getting a raise, changing jobs, going back to school, or starting a money-making business. It would be foolish to achieve a higher standard of living by spending savings or going into debt to buy a bigger house or new automobile before you increase your productivity. You may be able to live high on the hog for a while, but eventually you will have to pay the piper . . . or the credit card bill.

According to Say, the same principle applies to nations. The creation of new and better products opens up new markets and increases consumption. Hence, "the encouragement of mere consumption is no benefit to commerce; for the difficulty lies in supplying the means, not in stimulating the desire of consumption; and we have seen that production alone, furnishes those means." Then Say added, "Thus, it is the aim of good government to stimulate production, of bad government to encourage consumption."[7]

The Cause of the Business Cycle

Say's Law states that recessions are not caused by failure of demand (Keynes's thesis), but by failure in the structure of supply and demand. Recession is precipitated by producers miscalculating what consumers wish to buy, thus causing unsold goods to pile up, production to be cut back, income to fall, and finally consumer spending to drop. As Kates elucidates, "Classical theory explained recessions by showing how errors in production might arise during cyclical upturns which would cause some goods to remain unsold at cost-covering prices." The classical model was a "high-sophisticated theory of recession and unemployment" that with one fell swoop by the illustrious Keynes was "obliterated."[8]

In his broad-based book, Kates highlights other classical economists, including David Ricardo, James Mill, Robert Torrens, Henry Clay, Frederick Lavington, and Wilhelm Röpke, who extended Say's Law. Many classical economists focused on how monetary inflation exacerbated the business cycle. They were precursors of the Austrians Ludwig von Mises and F.A. Hayek.

Free-market economists, such as W. H. Hutt and Thomas Sowell, have tried to rehabilitate Say's Law, but none carries the punch of Steven Kates. □

1. Steven Kates, *Say's Law and the Keynesian Revolution* (Northampton, Mass.: Edward Elgar, 1998), p. 1
2. Ibid., p. 212.
3. John Maynard Keynes, *The General Theory of Employment, Interest and Money* (London: Macmillan, 1936), pp. 25–26.
4. Kates, p. 18.
5. Jean-Baptiste Say, *A Treatise on Political Economy* (Augustus M. Kelley, 1971 [1832]), p. 134.
6. Ibid., p. 135.
7. Ibid., p. 139.
8. Kates, pp. 18, 19, 20.

BOOKS

The Choctaw Revolution

by Peter J. Ferrara

Americans for Tax Reform Foundation • 1998 • 191 pages • $20.00

Reviewed by George C. Leef

The U.S. government's treatment of American Indians was despicable. Everyone knows that, at least in a general way. The forced resettlement of the Choctaws, of which the "Trail of Tears" is the most infamous episode, is undoubtedly among the sorriest instances of governmental duplicity, venality, and incompetence in our abundant history thereof.

We have become accustomed to "oppressed minority groups," with grievances far more imagined than real, demanding compensation at the expense of people who had nothing to do with the alleged injustices, or preferential treatment that necessitates abandoning equality before the law. So it is shocking to read of an instance where a "victim group" has chosen a different path. That is precisely the subject of Peter Ferrara's *The Choctaw Revolution*.

Ferrara relates the intriguing story of how the Choctaw tribe of Mississippi improved their lives not through political coercion, but by freeing themselves from paternalistic, enervating federal policy. It is a story that might just open the eyes of those who always proclaim their compassion for the oppressed, yet clamor for more government intervention to help them.

Ferrara is a well-known Washington policy analyst who has made his name mainly by exposing Social Security as doomed. Now he has given us a detailed look at federal Indian policy, an area as fraught with interventionist nonsense as Social Security is.

Through repeated treaty violations and land grabs, the government turned the Choctaws (and most other Indian tribes) into wards of the state, dependent on Bureau of Indian Affairs (BIA) bureaucrats for education, health care, housing, roads, law enforcement, and more. Ferrara quotes Chief Phillip Martin on the situation they faced: "The government could give us the bare essentials to survive, but if we wanted more, we would have to earn it ourselves." That was easier said than done.

Seeing that the federal government was doing a pathetic job of providing the Choctaws with the essentials, Martin decided that it was time to stop relying on the BIA and to start contracting for services directly. This is a right recognized for Indian tribes under the Indian Self-Determination and Assistance Act, but as the Indians should have known from history, having a right on paper and being able to exercise it are two different things.

Martin found the BIA bureaucrats fighting his efforts to contract for services at every point. That the Choctaws would have been better off without the bureaucrats was irrelevant. Ferrara writes, "Instead of pursuing the broad public interest as they are supposed to do, they pursue their own narrow parochial interest in their own turf, power, funding and jobs." The BIA repeatedly withheld information and technical assistance, arbitrarily imposed onerous requirements, delayed approving Choctaw initiatives, and even threatened retaliation against them for trying to exercise their rights. Eventually, after years of perseverance, the Choctaws were successful in contracting the BIA almost completely off their reservation, but it was a nasty, unseemly battle for freedom. Ferrara quotes one honest BIA official on the results of their fight to run their own affairs: "The tribe is doing an exemplary job. They're a more professional outfit than we ever were."

Another typical political fight the Choctaws (and other tribes) have had to wage is the avoidance of federal taxation of gambling casino proceeds. The profits from casinos go to fund improved housing, roads, education, and other things for Indian tribes. They also represent marginal competition for the big gambling interests in Las Vegas and Atlantic City. Nevada and New Jersey congressmen have introduced bills to subject Indian casinos to federal regulation and taxation, claiming

without any evidence that they are "riddled with corruption." Donald Trump, quite willing to use politics to further his interests, lobbied personally for the bills. So far, however, the Indians have defended successfully against this attack.

Ferrara closes with a list of useful suggestions for improving government policy toward Indian tribes. He argues that "tribes should have the freedom to run their own lands" and advocates treating Indian reservations as enterprise zones free from capital gains taxes and regulations on both Indian and non-Indian business enterprises.

Of course, the entire country should be given that treatment, but if we must proceed in small steps, beginning with Indian reservations is sensible. Why not allow some of the poorest Americans the freedom to prosper, as the Choctaws have begun to? It would be a wonderful demonstration of the benefits of liberty. □

George Leef is book review editor of The Freeman *and director of the Pope Center for Higher Education Policy.*

The Great Depression: An International Disaster of Perverse Economic Policies

by Thomas E. Hall and J. David Ferguson

University of Michigan Press • 1998 • 216 pages • $42.50 cloth; $19.95 paperback

Reviewed by Michael R. Adamson

Thomas Hall and J. David Ferguson state two purposes in writing this book. Their first is to apply macroeconomic theory to an actual event, "the greatest macroeconomic disaster in U.S. history." Their second aim is historical. They seek to tell the story of how powerful officials in several countries "committed an incredible sequence of policy errors that generated a cataclysmic event reaching around the entire globe." The authors succeed admirably in their first objective, but do less well in their second. As economists relying on macroeconomics to explain the decision-making processes that culminated in and sustained the Depression, they demonstrate the limits of macroeconomics alone in analyzing and explaining historical events.

Nonetheless, *The Great Depression* is a valuable book. It is well written and the authors carefully explain many obscure practices of the interwar financial world, such as the Federal Reserve's real bills doctrine. Moreover, they ably marshal the secondary literature in economics to answer such questions as: why the depression was so severe, why it lasted so long, and why it was a global phenomenon.

Their answers to those questions reflect a monetarist consensus that synthesizes the work of Milton Friedman and Anna Schwartz, which focuses on the domestic sources of the depression found in Fed policy, and that of Peter Temin and Barry Eichengreen, whose work indicts the pursuit of the interwar gold standard for making the depression an international phenomenon. Although the authors do not include the analysis of Austrian economists, they rightly point to the role of the Hoover and Roosevelt administrations in perpetuating the Depression. Indeed, the authors reach the conclusion of Murray Rothbard and other Austrians: government intervention made conditions worse.

In applying macroeconomic criteria as the test of policy outcomes, the authors also applaud several federal policies that constituted unprecedented economic intervention. Accepting the idea that a central role of the government in monetary policy is essential, they approve of the banking and financial laws of the 1930s that established federal deposit insurance, and strengthened the power of the Fed. Similarly, given Fed failures, they view the Reconstruction Finance Corporation as a useful alternative lending institution. They also endorse the questionable idea that heavy federal defense spending ended the Depression. As Robert Higgs has argued, the war masked the Depression by putting people back to work, but did not end it in terms of restoring material well-being.

The book also fails to demonstrate the authors' main contention that it was policy errors of well-intentioned officials who were "grossly ignorant about the goals, tools, and

impact of economic policy" that caused the Depression. They suggest that had policymakers just known better, they wouldn't have enacted the series of misguided policies that created "an absolute disaster." The historical literature leads to a rather different conclusion. For instance, as Herbert Stein has shown, New Deal officials were cognizant of monetary policy as a tool, but simply regarded it as ineffective. Holding dim views of financiers and bankers as a class and eager to demonstrate the capability of the federal government in restoring prosperity, they instead developed fiscal policy as a tool to manage the economy. The problem was not so much one of ignorance as of the mindset of the New Dealers.

Economic ignorance alone does not adequately explain historically how the series of misguided policies that caused and sustained the Depression came to be. What may seem today to be misguided policies were not necessarily obvious at the time. During the 1930s, few private or public leaders in America other than a small number of economists, Wall Street bankers, and Fed officials pointed to monetary policy as a primary cause of the contraction. Ultimately, *The Great Depression* fails to clarify for the reader precisely what the authors believe should have been obvious to contemporary policymakers, enabling them to avoid the calamity.

On the whole, the main macroeconomic conclusions of the book are sound: that policy mistakes of the 1920s and 1930s were the most important factors in causing the Great Depression; that the severity of the 1929–1933 contraction in America was due to bank failures that resulted from Fed inaction; and that the duration of the Depression owed to the lack of pro-active Fed policy after 1933 and the economic incoherence of the subsequent New Deal program.

This book, while limited in some respects in its explanatory power, helps to refute the still-popular notion that the Depression was caused by an inherent flaw in the market economy, inexplicably causing economic collapse. □

Michael R. Adamson is a Ph.D. candidate in history at the University of California-Santa Barbara.

The Noblest Triumph: Property and Prosperity Through the Ages

by Tom Bethell

St. Martin's Press • 1998 • 378 pages • $29.95

Reviewed by William R. Allen

Property is a multifaceted and fundamental topic. Tom Bethell here gives us a broad survey, dealing with economic, political, and legal theory; episodes of economic and political activity; and assessments of institutional constraints and procedures from ancient Greece to virtually the day before yesterday.

Since the fiasco in the Garden of Eden, we have lived in a world of scarcity. The ineluctable state of limits implies not only frustration but also conflict. But there are many ways to compete, and communities differ enormously in how the economic/social/political game is played.

How we survey our possibilities and formulate our strategies, how we interact with each other and coordinate our efforts, is determined largely by the rules of the game. Those rules basically are subsumed under "rights to use of property." The right to use property we "own" is necessarily limited—I cannot use my hammer to break your window—but what are those limits, how are they determined, and by whom? Property rights go far to define the nature of the community, providing constraints, opportunities, and incentives with respect to what we do and how we do it and determining how we adapt to our niggardly circumstances. Some systems of property rights are much more conducive than others to living together productively and civilly.

The implications of who has what property rights include subtle aspects of political and social philosophy. "The Western concept of human rights presupposes individualism," Bethell writes, and individualism finds much of its operational manifestation in private rights in property. Equality before the law and freedom of contract are antecedent to a free-market economy.

All this is pursued, elaborated, and illustrated by Bethell with references to a mass of var-

ied literature, from ancient to modern. He is centrally concerned with "the legal and political foundations that are essential to economic growth." In an individualistic open market with well-defined property rights, options can be discovered; opportunities can be identified; negotiations and exchanges can be conducted; division of labor and coordination can be effectuated; long-range plans can be confidently formulated; and credit can be obtained. Moreover, good stewardship of assets is rational. Bethell persuasively argues that "private property is a necessary (but not a sufficient) condition" for a society to enjoy the "four great blessings" of "liberty, justice, peace and prosperity."

Some origins of private property are found in Roman law, but our heritage comes mainly from long-developing English common law. Perhaps the operational high point of private property is seen in mid-eighteenth-century Britain. Unfortunately, intellectuals of the eighteenth and nineteenth centuries—including the classical economists—did not adequately spell out the significance of property relations for a flourishing society.

Here, I believe, Bethell is excessively impatient with and ungenerous toward writers of a century or two ago who did not foresee the insight of a handful of analysts of our own generation. The way was left open for much socialistic silliness in both advocacy and action during the last two centuries, but he is too harsh on good economists for not being better.

The author recounts much of the utopianism provided, before and during modern times, by the Jamestown, Plymouth, and New Harmony experiments; by Sir Thomas More, Jean Jacques Rousseau, William Godwin, Robert Owen, and Karl Marx; by the fiasco of the twentieth-century communism; and by the misdirection and mismanagement of modern "emerging Third World economies." He accounts for the rise and fall of the Ottoman Empire and the Irish famine of the 1840s and tries to explain intricacies of today's "intellectual property" within a framework of property rights. And he devastatingly quotes the naïveté of agitators, politicians, jurists, and economists: see especially Theodore Roosevelt's insidious distinction between "rights of property" and "rights of men."

Seminal work on the implications of property rights is to be applauded, but I fear that such interest is not likely to be sustained. Today's younger economists may not consciously defame private property, but most do little to defend it.

At any rate, innovative academic scribblers can use felicitous help from writers who can reach a wide, non-specialist audience. Mr. Bethell, with a style that is typically graceful but with journalistic assurance, has played his expository role well. □

William Allen is emeritus professor of economics at UCLA.

Two Lucky People

by Milton and Rose D. Friedman

University of Chicago Press • 1998 • 655 pages • $35.00

Reviewed by Bill Field

I still remember, after more than 30 years, my mounting excitement as I read *Capitalism and Freedom* for the first time and discovered the wondrous moral and economic benefits of being "free to choose." Reading it changed my professional life. Here was solid economic reasoning, but economics with a heart, and—unbelievably—economics that was exciting. All my subsequent economic thinking has been driven by this experience. While I eventually wandered off the Friedman reservation, I still have a warm feeling for the book and author who started it all for me.

Two Lucky People, the memoirs of Milton and Rose Friedman, is not a work primarily focused on economic theory or policy. The book assumes that readers are familiar with the Friedmans' economic ideas, although it does provide summaries and defenses of many of their positions. Rather, *Two Lucky People* is an easygoing narrative of the experiences of a happily married couple, with some sections written by each individually and others by the two combined.

The Friedmans clearly qualify as a traditional family unit, with Milton the primary

breadwinner and Rose focusing on homemaking. Milton, despite his obvious affection for his wife and family, is drawn back time after time in his account to his professional experiences and economic ideas. Rose, despite her obvious competence and interest in economics, is drawn back to the family and its experiences. It is heartwarming to see a couple of such extraordinary intellectual ability experiencing the ups and downs of daily life.

As Rose and Milton carry us through their lives and careers, they provide us with glimpses of many of the greatest and not so great economists of the twentieth century. Their reminiscences demonstrate that personal foibles and prejudices exist among the intellectual elite as surely as in the general population. Some instances are touching; others produce a sense of revulsion.

Examples of the latter include the anti-Semitism encountered by the Friedmans in academia in general, faculty cliquishness that escalates into personal animosities, and the incredible close-mindedness of leftists to the failures of socialism.

Milton also provides us with interesting portraits of the presidents he advised. No one should be surprised at the picture of Richard Nixon as having a powerful intellect and vast knowledge, but often carrying out policies he knew were socially undesirable in pursuit of short-run political advantage. Friedman's admiring portrait of Ronald Reagan shows much more respect for his intellect than most Washington commentators.

Of interest is the section devoted to the evolution of the "Free to Choose" television series, especially the resistance encountered from leftists within the public television establishment. While pressure from sponsors and other sympathizers eventually forced almost all public stations to show the series, there was much opposition, as exemplified by the decision of the New York station to run the show's initial program opposite the Super Bowl.

Today, when the Friedmans' ideas are almost mainstream intellectually (if unfortunately not in policy), it is hard for many of us to remember (and for younger people to have any notion of) the long-term resistance they faced. For many years the Duke University library carried none of Milton Friedman's books because of faculty hostility to his ideas. At the same time, the library had a complete collection of the works of Karl Marx. When *Capitalism and Freedom* was published in 1962, it was reviewed in almost no general publications—even though it was obviously aimed at a broad audience and Milton was already known internationally.

Rose and Milton present all this information about their lives with a minimum of malice. The dominant tones of the book are optimism and pride. A sense of vindication is evident: the free market is winning the battle of ideas and ultimately will win the battle over policy. As Milton stresses, advocates of the free market are inherently patient, long-term thinkers. He is perfectly willing to be judged by the economics profession and others 25 to 50 years in the future. He is confident, and surely with good reason, that his work in positive and normative economics will stand the test of time. □

Bill Field is a professor of economics at Nicholls State University.

Global Greens: Inside the International Environmental Establishment

by James M. Sheehan

Capital Research Center • 1998 • 213 pages • $25.00

Reviewed by Jane S. Shaw

Only a policy wonk could love this book, but its contents are vital for understanding a major change underway in environmental and foreign policy. Ahead of many others, James Sheehan has recognized the growing power of the international environmental movement. Sheehan, who directs international policy activities for the Competitive Enterprise Institute, describes the exercise of this power in *Global Greens*.

The book centers on "NGOs" (non-governmental organizations) that emphasize environmental issues. To a person concerned about freedom, the term "non-governmental

organization" may sound benign, but most NGOs are not friendly to liberty at all. They are ideologically committed to greater government control to address environmental problems, and they perceive international pressure as the way to achieve that control.

According to Sheehan, about 4,000 NGOs are actively involved in environmental issues. These include large environmental organizations such as Greenpeace and the World Wildlife Fund, but also an array of others, including labor unions, so-called consumer groups, and women's organizations. In general, their goals are to force changes in people's lives, especially in the industrial countries, supposedly to protect the planet from human-caused harm.

The prominence of NGOs reflects the rise of international treaties as a way of dealing with environmental issues. For reasons that aren't fully clear, the governments of the United States and other industrialized countries now allow international treaties to shape important parts of their environmental policies. According to Sheehan, the momentum began in 1972, with the first United Nations Conference on the Human Environment. It slowed during the Reagan administration, when President Reagan withdrew from negotiations over the Law of the Sea Treaty, but picked up again with the Clinton administration. Today, many NGOs are official participant-observers at United Nations conferences, summits, and functions. As the U.N.'s influence grows, so does theirs.

As a result, an ever-growing collection of summits, conventions, treaties, and frameworks undergird environmental policy in the United States. During the 1980s, Sheehan reports, 250 environmental treaties or conventions were enacted. Treaties, to cite just a few examples, limit the use of chemicals that are believed (by many) to deplete stratospheric ozone, ban trading in certain animal species, and have begun to influence the use of fossil fuels. Forty-seven places in the United States are now designated U.N. Biosphere Reserves (including the Everglades) and 19 are World Heritage Sites (including Yellowstone National Park). These give the green NGOs leverage to control land use in and around those places. The international noose is tightening.

In 1992, the Rio Summit (the U.N. Convention on Environment and Development) took center stage. This meeting launched a proliferation of activities and agreements, including a global-warming treaty (signed by President Clinton, but not ratified by the Senate); a U.N. commission on sustainable development; conferences on such topics as women, housing, and population; and the World Bank's Global Environment Facility (which Sheehan calls a "$2 billion slush fund for Third World environmental projects").

Sheehan describes in detail several important international treaty negotiations of recent years, including the 1994 International Conference on Population and Development, the 1996 World Food Summit, and the 1997 Kyoto Protocol on global warming. He observes that NGOs did not always achieve their goals at such meetings. However, as time goes on, they have become increasingly adept at influencing treaties in the direction they want, a fact that bodes ill for our freedom and prosperity.

Sheehan's reporting of each event is thorough and well-footnoted. In some of the negotiations he discusses, he was a firsthand observer. His book is clearly written and has no visible gaffes. It includes lists of prominent NGOs (including information about their funding) and other reference material.

Why then is it not more exciting? The reason is probably that it deals mostly with facts—a lot of facts—rather than with ideas. Sheehan provides extensive details that illustrate his theme: the growth of international environmental organizations. He doesn't explore the reasons behind this growth or speculate on its future directions. Such discussion would have added interest.

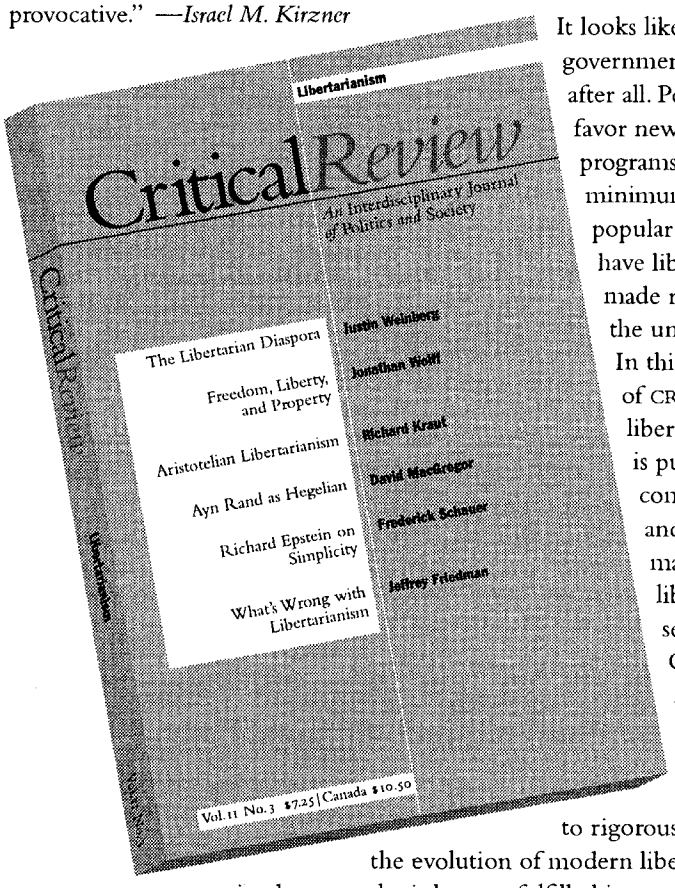
Still, Sheehan has provided a valuable service in marshaling so much information about the network of environmental NGOs. His descriptions of the Greens in action around the world throw light on activities that have to date escaped widespread scrutiny, and provides material that I and others will draw on in the future. □

Jane Shaw is a senior associate of PERC in Bozeman, Montana.

What's wrong with libertarianism...

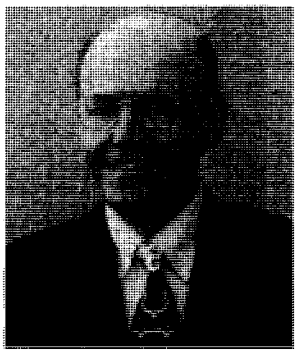
...And how to fix it

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An Open Letter to the California Legislature

As a student of public choice theory, I understand why you support SB 1241, a mandatory agency-shop bill for California State University (CSU) faculty. After all, in the words of Ambrose Bierce, "politics is a strife of interests masquerading as a contest of principles." The California Faculty Association (CFA) supports you in the political marketplace, so it is quite natural for you to give them the power to extract more dues money from faculty. If they have more dues money, they can give more to you. I imagine from your perspective this is a virtuous circle.

I have written extensively on the issue of so-called union security. I know you understand the main argument in favor of union security—the so-called free-rider problem—but I would like to give you the other side of the story.

First, there could be no free-rider problem if it were not for the principle of exclusive representation. If we had a system of members-only bargaining (sometimes called proportional representation), the CFA would not have to bargain on my behalf. I could not receive any of the alleged benefits of their representation services, because I would be responsible for bargaining for myself or for selecting some other representative to bargain for me. In other words, the union's free-rider problem is an artifact of the law. It is not a problem inherent in collective bargaining.

Charles Baird is a professor of economics and the director of the Smith Center for Private Enterprise Studies at California State University at Hayward.

Workplace Democracy

Now, you are probably thinking that exclusive representation is simply majority rule in the workplace. It is economic democracy. After all, as I have heard many of my debate opponents say, we elect members of the legislature by majority vote. A winning candidate represents all eligible voters in his or her district notwithstanding that many voted for another candidate and many more didn't vote at all. That is what democracy is all about. The majority rules. If it is good in politics, it must be good in unionism too. But that conclusion is a non sequitur.

Government is a natural monopoly. It has a monopoly on the legal use of force. There can be only one government at a time. Like all monopolists, governments have a tendency to abuse their monopoly power. Historically, democracy evolved as a way for the governed to have some ability to protect themselves against governmental abuse. Democracy—the mandatory submission of minorities to the will of majorities on all matters that are within the constitutional scope of governmental authority—was never intended to be imposed in the private sphere of human action. There, individual autonomy and free choice are the proper rules. Private persons are free individually to associate with private groups that use majority rule to make decisions, but they are also free not to do so.

Unions are not governments. They are private associations. (The last time I checked, civilian employees of government were still

private citizens.) To impose mandatory submission of minorities to the will of majorities in private affairs by statute is to breach the constitutional wall of separation between government powers and individual rights. On this reading therefore, exclusive representation is illicit. (You cannot take refuge in the U.S. Supreme Court's 1937 ruling in the *Jones & Laughlin Steel Co.* case, which upheld the National Labor Relations Act. We all know that decision was made possible by the switch of votes by Chief Justice Charles Evans Hughes and Associate Justice Owen J. Roberts in an effort to avoid Roosevelt's court-packing plan. This was the switch in time that saved nine.)

Do you realize that the United States and Canada are the only two countries in the world with exclusive representation unionism? I have given lectures all over the world on this issue. From South Africa to New Zealand to Austria to England, audiences are appalled that America, supposedly the most free country in the world, denies to individual workers the right to designate workplace representatives of their own individual choosing.

Forced Riders

The second reason the free-rider argument is false is the problem of the forced rider. Unions claim to confer net benefits on all workers whom they represent. That is nothing but a big lie. For example, the CFA does not confer net benefits on me. To the contrary, I am much worse off having the CFA represent me than I otherwise would be. Just the psychic cost of being forced to have people with whom I have profound educational and philosophical differences speak for me far outweighs any monetary benefits they claim to have secured on my behalf. (Incidentally, I deny that the CFA has secured any monetary benefits for me.) So I suffer net harms from the CFA, and now you want to force me to pay for those net harms through so-called "fair share fees." In economics a forced rider is a person who suffers net harms from some collective action and is forced to pay for them. There may be free riders, but there are also forced riders. Don't you, as elected officials, have a moral responsibility to protect the rights of forced riders? We are citizens too.

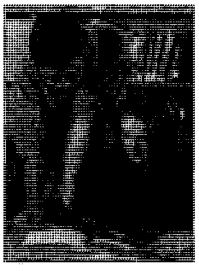
It is telling that SB 1241 doesn't even make the agency shop a subject of bargaining between the CFA and CSU. Instead, it imposes the agency shop burden by force of statute. I guess you don't have much confidence in the CFA's bargaining abilities. The CFA has never been able to accomplish anything without you, their political patrons, giving it special privileges under the law. That is why I have always called the CFA the Cabal of Feckless Academics.

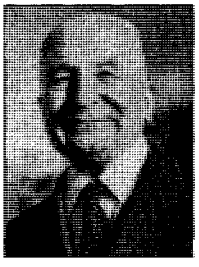
Finally, as soon as you empower the CFA to steal money from my paycheck, I and several like-minded colleagues on many CSU campuses will, with pro bono representation, initiate legal proceedings based on the following Supreme Court decisions: *Abood v. Detroit Board of Education* (1977), *Chicago Teachers Union v. Hudson* (1986), and *Lehnert v. Ferris Faculty Association* (1991). These public-sector rulings guarantee that no agency fees extracted from public employees can be used for any purpose other than collective bargaining, contract administration, and grievance processing. In *Lehnert*, for example, your favorite type of union expenditure—lobbying—was declared to be an impermissible use of forced union fees. In that same case 90 percent of union expenditures were held to be impermissible uses of such fees. You'd better tell your union partners to keep good books. The measly 15 to 20 percent difference between union dues and agency fees you wish to write into the law will not stand up in court. And I, for one, am going to enjoy proving it.

Sincerely,
Charles W. Baird

THE FREEMAN
Ideas On Liberty
September 1999 Vol. 49, No. 9

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Ideas On Liberty

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PERSPECTIVE

Voucher Advocates, Take Heed

As if we needed more proof that with government money come regulations, the U.S. Department of Education says that colleges and universities may not use standardized admissions tests that have a "significant disparate impact" on any race, sex, or national origin. Unless a test is indispensable—a matter to be decided by the department—its use will be regarded as invidiously discriminatory, resulting in loss of federal money.

The premise is that admissions tests on which particular groups do relatively poorly—the SAT and ACT—must be culturally biased. The assertion that these exams somehow give a cultural advantage to white males of European ancestry and Asian males is bunk, but that's inconvenient to the social engineers. The tests *must* be biased.

The consequences of the prohibition are predictable. Students will be admitted to schools for which they are unqualified. Then they will flunk out. There's benevolent social policy for you. After California's state colleges and universities were forced to stop using race as a criterion for admission, it was pointed out that minority groups lost "representation" at the top schools, UCLA and Berkeley. But Thomas Sowell noticed that there are now more blacks, Mexican-Americans, and American Indians than previously at other schools, such as the University of California at Irvine. The opponents of quotas were right: instead of going to Berkeley, for which they are unqualified, minority youth who are not top students, like their white counterparts, will go to schools where they have a chance to succeed.

David Friedman, the economist and author of *Hidden Order*, once formulated Friedman's Law: government is so incompetent, it can't even give something away. Government may promise to give all students a shot at a top college, but clearly it can't make unqualified students qualified simply by forcing their admission to top schools.

Government should not be dictating who should be admitted to which schools. It shouldn't be operating schools. Period. Where

there is government, there is control. Voucher advocates, take heed.

* * *

September is back-to-school month, a fitting time to again put government control of education on the examination table.

Private schools are better at educating children than government schools. But why? Because they're private? Marshall Fritz thinks that answer misses a big point and distorts the school-reform movement.

The rule about pipers, payers, and tunes is endlessly cited in the analysis of government policy. But it's curiously neglected in discussions about what to do about the "public schools." Jacob Huebert reminds us that it's applicable there too.

The logic of government education leads inexorably to wider intervention in the economy. The "School-to-Work" program of the Clinton administration shows that only too well. Gary Wolfram explains.

Government schools are reliable for at least one thing: teaching children the government's line on everything from taxes to war. Daniel Hager says this is nothing new.

Higher education is also increasingly a creature of public policy. Through loans and grants, government helps a lot of people go to college who otherwise wouldn't be there. Russell Madden is not so sure this is a good thing.

The battle in the Balkans is a reminder that governments, never trustworthy, are least credible when they go to war. H.L. Mencken knew this well. Unable to write about war, he found a more subtle way to comment on the state's lack of veracity and the people's inclination to believe whatever it says. Wendy McElroy explains.

This month marks the 50th anniversary of perhaps the greatest achievement in economics in the 20th century: the publication of *Human Action* by Ludwig von Mises. Richard Ebeling explains why this book and this occasion are so important.

It was Mises who pointed out that socialism would have no way to intelligently plan an economy because the abolition of the market would eliminate the tools of calculation: prices. Manual Ayau revisits the calculation debate and notes that it applies to any system other than laissez-faire capitalism.

Most of us are taught that before the Europeans intruded, American Indians lived communally with individuality submerged in the tribal soup. Amy Sturgis writes that, on the contrary, Indian life was yet another source of the freedom philosophy for the European settlers in North America.

Nothing could be more different than the way business and government account for their activities. James Bovard demonstrates that in each case, form follows function.

One of Washington's hottest ideas is to invest some of the Social Security tax revenue in the stock market. Great idea, right? Not so fast, says Deroy Murdock.

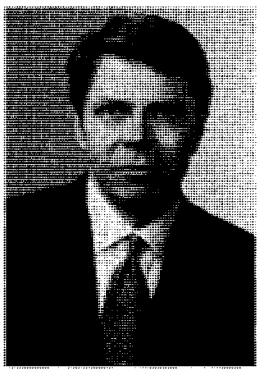
Our columnists have been busy the last month. Donald Boudreaux finds the government's method of detecting victimless "crimes" horrifying. Lawrence Reed sees nothing but bad news in the coming explosion of bogus liability suits against business. Doug Bandow revisits the U.S. bombing in Sudan. Thomas Szasz warns that speaking truth can land you in trouble. Dwight Lee examines the relationship between speculation and risk. Mark Skousen looks back at anticommunism. Russell Roberts imagines a world without the FDA. And Michael Cox and Richard Alm consider the claim that wealthy people hurt the middle class, concluding "It Just Ain't So!"

In the book section, reviewers provide the scoop on works dealing with liberty, socialism, protectionism, and FDR.

—SHELDON RICHMAN

Thoughts on Freedom

by Donald J. Boudreaux



Break This Vile Addiction

Janneral Denson, who is black, was seven-months pregnant when she returned to her home in Florida after visiting Jamaica. U.S. Customs agents at the Fort Lauderdale airport greeted her with accusations that she had swallowed packets of drugs to smuggle them into the United States.

Ignoring a physician's opinion that Ms. Denson's stomach contained no prohibited substances, Customs Service agents denied her request to call her mother, spirited her away against her will to a Miami hospital, handcuffed her to a bed, and forced her to down laxatives. Careful inspection of the results of their handiwork finally persuaded them that Ms. Denson was, in fact, no drug smuggler. She was released the next day.

Eight days later, following bouts of bleeding and diarrhea, Ms. Denson required an emergency Caesarean section. Her premature son weighed only three pounds, four ounces. It is still unknown whether or not her child's health will be permanently impaired.

In May, Customs Commissioner Raymond Kelly testified before Congress about this and similar episodes. Asked about his agency's handling of Ms. Denson, Mr. Kelly denied—unbelievably—that the Customs Service uses racial profiling. But he defended the practice of strip-searches as a necessary weapon in the "war on drugs."

Reflect on this episode—reflect that government officials waylaid an innocent woman, chained her to a bed, and fed her laxatives so that they could inspect the contents of her bowels. Reflect that this woman's disgraceful experience isn't unique: innocent people are routinely subjected to such humiliating treatment. Reflect also that a high government official unabashedly tells Congress that such searches are necessary.

Freedom Requires Tolerance of Foolishness

Ms. Denson's experience shows that the war on drugs is no such thing: it is, like all wars, a war on people. But the people targeted by government drug warriors don't threaten anyone's peace and prosperity. These people merely seek to do as they please without interference from the state.

In a free society, even people who recklessly risk self-destruction should be free to do so. (Of course, taxpayers owe such abusers neither aid nor comfort.) Not only is freedom meaningless if the government assumes the paternalistic power to protect us from ourselves, but a wise people will never trust government with that power.

This wisdom motivated Ludwig von Mises to write that "A free man must be able to endure it when his fellow men act and live otherwise than he considers proper. He must free himself from the habit, just as soon as something does not please him, of calling for the police." Without this tolerance for the freedom of others, no one's freedoms are

Donald J. Boudreaux is president of FEE.

secure. As the government's increasingly belligerent "war" against tobacco demonstrates, powers ceded to the state so that it can behave paternalistically on one front will inevitably be abused and extended to other fronts. The reason is that no sound principle is available to constrain these powers. If the state presumes to protect me from destroying my life with heroin or marijuana, why should it refrain from protecting me from tobacco, alcohol, animal fat, or a sedentary lifestyle? Each can ruin lives and upset friends and loved ones.

Innocent People Victimized

It's important also to be aware of another heavy cost of the "drug war": government's weaponry in this war necessarily is fired scattershot. These bullets too often hit people—such as Janneral Denson—who are innocent of any drug offenses. And Customs Commissioner Kelly's defense of strip-searches is evidence that such scattershooting is inevitable as long as the government wages its "war on drugs." Here's why.

Drug traffickers don't tell government authorities about their illegal activities. And there are no victims to complain. Seldom is there a participant in a drug deal who has an interest in reporting it. This fact distinguishes drug selling (and other victimless "crimes") from true crimes such as murder, rape, kidnapping, and robbery.

Because drug dealing involves only willing participants, drug warriors *inevitably* must guess whether or not an offense is occurring and who is committing it. Such guessing, of course, involves choosing targets according to their racial, sex, and age profiles. This is why Commissioner Kelly's denial of racial profiling is unbelievable (and why Congress can end it only by ending the "drug war"). No matter how refined the technique for selecting targets, large numbers of innocent people will be detained, strip-searched, and humiliated à la Janneral Denson. After all, if Customs agents could identify drug traffickers without strip-searches, there would be no need for such searches.

Some well-meaning people argue that statistical errors are the price we must pay for law enforcement. But surely the degree to which we should tolerate such errors ought to be determined by the importance of the law-enforcement effort. If the effort itself is highly questionable, then there's no need to tolerate these errors.

The plain fact is that drug prohibition *is* highly questionable. At bottom, it is an attempt not to protect each individual's property and person from the aggression of others, but, rather, an attempt to engineer social behavior. It's an attempt at the impossible, protecting people from themselves.

"Drug war" proponents often retort that without this social-engineering effort our society would descend into a grim incivility. They insist that with drug legalization our streets would teem with disgusting junkies and our storefronts would crassly advertise the sale of deadly narcotics.

For various reasons, I dispute these predictions. But let me assume here that these are valid. So what? Would a world with more wasted junkies and crass drug merchants be as vile as what we have now? Today, our prisons are chock-full of non-violent offenders. Our inner-city streets are battle zones. Young blacks and Hispanics are suspected criminals simply because they are young blacks and Hispanics. Our courts permit government to seize and keep properties that are merely *suspected* of having been associated with drug offenses. Many ill citizens cannot get the drugs they need to cure their illnesses or to relieve their suffering. And U.S. Customs agents kidnap innocent young women and men, chain them to beds, pump laxatives down their throats, and inspect the contents of their stomachs.

These and countless other consequences of the "war on drugs" are vastly more uncivil, grim, vile, degrading, unsightly, dangerous, costly, and immoral than even the worst-case scenario of widespread drug abuse.

Let's break our unholy and repellent addiction to the "war on drugs." □

THE FREEMAN
Ideas On Liberty

The Wealthy Hurt the Middle Class?

It Just Ain't So!

Bashing the rich just ain't as easy as it used to be. With the stock market at record levels, unemployment low, and wages rising, most Americans are busy trying to become rich, not brooding over how much others earn. Most of us are better off, so why begrudge those who, through hard work or sheer luck, are making lots of money?

Well . . . Cornell University economist Robert H. Frank has found a reason. Frank, coauthor of 1995's anti-capitalist manifesto *The Winner-Take-All Society*, argues in the April 12, 1999, *New York Times* that the wealthy harm the middle class. They do so simply by spending money on such ordinary things as bigger houses, heftier cars, and nice clothes, which raises a sort of "entry barrier" to the good life for the rest of us.

Pity the unfortunate middle-class families that can't buy houses in the best school districts, whose puny sedans share the roads with 6,000-pound Lincoln Navigators, and whose children don't wear the hippest clothes. "The gifts you give, the night out at the theater, the family vacation—all are affected by the upward pull exerted by the sharply higher affluence of top earners," Frank contends.

Defending the upper classes doesn't provide the same feel-good factor as standing up for the poor and downtrodden. Yet it's dangerously wrong to malign the rich and their spending as some sort of hindrance to the rest of society. Fact is, Frank has it backwards.

We'd all be a lot poorer if not for the rich. Let us count the ways. First, the rich give generously to charity. Households making $100,000 or more donate over five times as much as middle-class families making $30,000 to $50,000—supporting hospitals, libraries, homeless shelters, research, schools and universities (including Frank's own privately endowed university, Cornell, named for the generosity of its chief benefactor, Ezra Cornell, who earned his fortune laying telegraph lines). Second, the rich start new businesses, which create jobs for the rest of us. Third, the rich deliver goods and services to society's rank and file. Indeed, we routinely fill our homes with the products the rich have invented, improved, or simply made more affordable: Colgate (toothpaste), Borden (milk), Campbell (soup), Gillette (razors), Heinz (ketchup), Maytag (appliances), Mars (candy), Dell (computers), Turner (entertainment), Mrs. Fields (cookies), Mary Kay (cosmetics), and on and on. The rich have virtually "branded" America with their gifts.

Fourth, and perhaps most important of all, the rich play a subtle but vital role in funding economic progress—not by their saving but by their *spending*! By and large, economies move forward by introducing waves of new products. New goods and services typically enter the market very expensive, with sales to only a small number of consumers—generally the wealthy. The rich are able to buy, even at what would for most of us be prohibitive prices, simply because they've got the money.

Henry Ford's first Model T hit the market at $850 in 1908, a sum that would take an average factory worker two years to earn. Not surprisingly, Ford sold only 2,500 cars that year, and critics dismissed the early automobile as a "rich man's toy." The sticker prices for today's cars may cause buyers to gag, but they actually take less of a toll on the family budget. A 1997 Ford Taurus required only a third of the work time of the first Model T.

Few entrepreneurs get rich selling only to the rich, even at extravagant prices. The big money—and the greater benefit to society—lies in bringing products within the reach of the masses. The "rich man's toy" will remain so forever unless it gets cheaper—if not in

dollars and cents at least in the currency that really matters: hours of work.

America's free-enterprise economy routinely makes what were once luxuries for the few affordable to the masses. Videocassette recorders fell from 365 hours of work in 1972 to a mere 15 hours in 1997. A cellular telephone dropped from 456 hours in 1984 to nine hours in 1997. An IBM computer declined from 435 hours to under 60 hours (while being jazzed up with 20 times more power). So many goods and services that middle-class America takes for granted started out as niche products for the rich—electricity, telephones, washers, dryers, dishwashers, televisions, microwave ovens, answering machines, compact disc players, airline trips. Today's "jet set" includes not just society's wealthy but middle- and lower-income workers as well. Over four-fifths of Americans earning $20,000 to $40,000 annually have flown on commercial airlines. For those earning under $20,000 a year, the fraction is nearly two-thirds.

Even families at the lower end of the income distribution can count on eventually having goods and services once bought only by those with fat wallets. Indeed, 97 percent of American households in poverty have color TVs, nearly three-fourths own one or more cars, two-thirds have microwave ovens and live in air-conditioned dwellings. It wasn't a government welfare program that cut the price of these items to where they're affordable by the masses in America. It was that "unfair" capitalist system against which Frank so pugnaciously loves to rail.

More to Come

And what about the future? Will the spoils of an increasingly wealthy nation go only to a few? Again, of course not. What the wealthy have today will someday be common on middle-class incomes and below. Take high-definition television, which delivers crystal-clear images. HDTV sets are selling for $5,000 to $10,000, well beyond the means of the average household. Only the rich will buy the first sets. In time, though, we'll repeat the experience of past innovations. Prices will drop quickly, allowing the typical U.S. family to own a high-definition set within a decade or so. If history has anything to teach us on this score, it's that the capitalist booty is spreading *faster* through society today than in the past, making its way to middle- and lower-income Americans in half the time it did a century ago.

In *Capitalism, Socialism and Democracy*, Joseph Schumpeter offered a succinct capsule of the benefit of a free-market economy: "Queen Elizabeth owned silk stockings. The capitalist achievement does not typically consist in providing more silk stockings for queens but in bringing them within the reach of factory girls in return for steadily decreasing amounts of effort."

Frank doesn't tell us how to rid society of the inequality that imposes the burden of keeping up with the rich. Those who buy into his argument are likely to advocate penalties on the wealthy—steeply progressive taxes on income or sky-high excise taxes on luxury goods. These measures might very well reduce rich people's spending. But they're not likely to do the middle or lower classes any good. Quite to the contrary, stopping the rich from spending would retard progress and reduce the general standard of living. We'd all end up worse off.

—W. Michael Cox,
Senior Vice President and Chief Economist,
Federal Reserve Bank of Dallas
Richard Alm,
Business Writer
Coauthors of *Myths of Rich and Poor*
(Basic Books)

THE FREEMAN
Ideas On Liberty

A Better Brand of Parent

by Marshall Fritz

After World War II, aborigines in New Guinea scraped clearings in the brush in hopes that planes would land and bring "cargo." They'd seen U.S. forces do similar scrapings, and soon thereafter, great silver birds landed and disgorged "cargo," some of which was left behind and was quite useful.

Of course, they were perpetually disappointed. No combination of width, length, slope, and decoration ever brought in a single silver bird because they didn't know the real source of "cargo." From their standpoint, however, they were doing reasonable things.

I used to push for tax-funded school vouchers. My logic was that since most times the private schools do better than the government (a.k.a. "public") schools, why not use the tax funds to allow parents a choice? Like the New Guinean who had limited understanding of "cargo," I had limited understanding of "private education."

Let's ask what is the real source of why private schools have better results overall than government schools? Is it the private ownership? Competition and the profit motive? Uniforms? Curriculum? Smaller class size? Prayers and Bible verses? Typically lower spending on teachers? Stricter discipline? Unity of worldview between parent and teacher? Charging tuition of their customers?

Of all of these, only the last gets us near the heart of the watermelon.

Unfortunately, like Cargo Cultists, most of the conservative and libertarian—and recently, "liberal"—proponents of tax-funded school vouchers have not figured out *why* private schools, on balance, outperform government schools.

So what does cause, or at least allow, private schools to have better students? Douglas Dewey, executive vice president of the Children's Scholarship Fund, put it simply: home and private schooling use a better brand of parent.

Wealth No Indicator

By the way, my one-year experience as a teen in an expensive Swiss boarding school convinced me that wealth is not an indicator of good parenting, and my experience running a private school where 71 of 72 students received financial assistance showed me that poverty is not an indicator of weak parenting.

The Reverend E. Ray Moore, founder of Exodus 2000, and I worked up a thought experiment to help explain Dewey's Dictum. Here it is:

1. Come up with five or more indicators of "good parenting." Our list includes: (1) getting married before you have children;

Marshall Fritz is the founder of the Separation of School & State Alliance in Fresno, California (www.sepschool.org).

(2) staying married; (3) giving children authoritative discipline; (4) earning a living, as opposed to living on welfare; (5) taking virtues seriously and working to transfer them to your children.

Imagine a distribution of American parents measured on *your* indicators of good parenting. I suspect your estimates will probably look something like Ray's and mine. We think just a few parents are excellent, the majority are merely good or weak, and more are bad parents than are excellent. Chart 1 attempts to picture this as a histogram.



Chart 1: Moore/Fritz Estimate of Distribution of 1990s American Parents by Quality Level

2. Now invent five measurements of "good children." Our list included: (1) lack of arrests for drug use, theft, and assault; (2) diligently prepare themselves for adult status, as measured by getting good grades, staying in school, and getting a part-time job; (3) care about the world around them, as measured by how much of their income and time they volunteer to helping their fellow man compared to how much they spend in self-indulgent activities; (4) are happy and cheerful; (5) attend the church or temple of their or their parents' choice and make sincere efforts to understand and live by its teachings.

Next, estimate the percentage of children from each of the four quality levels of parenting that you think would measure up as "good or excellent children." In other words, how many children of the bad parents are excellent children, how many of the weak parents, and so on. You can see our estimates in Chart 2.

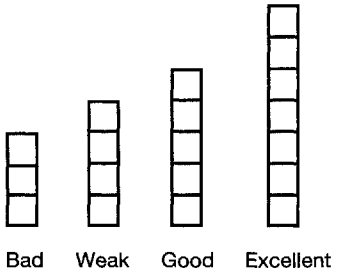


Chart 2: Moore/Fritz Estimate of Distribution of Good or Excellent Children from Each Group (each segment represents 5%)

3. Finally, estimate the percentage of children in private schools that come from the four quality levels of parenting. If your guess is like ours, the vast majority come from the best parents, and practically none from the worst parents. See Chart 3.



Chart 3: Moore/Fritz Estimate of Distribution of Quality Levels of Families with Children in Private Schools

This exercise illustrates Dewey's Dictum that, by and large, private-school children come from better parents and are already better quality children. In other words, the main source of quality in private schooling is that they use better raw material. It's not what's *in* the school as much as what goes *into* the school.

The obvious next question is, how do the private schools get the better pupils? Let's compare the school situation to Chinese restaurants.

Chinese restaurants take measures to filter out diners who want Mexican or other non-Chinese food: In designing their restaurant sign, they usually use a Chinese-sounding

name. Sometimes they employ some Chinese characters and they almost always blatantly use the words "Chinese Food." Because of this filtering out of most diners, rarely do customers complain about the lack of burritos on the menu.

School Filter

Back to our question: from the millions of parents who might like private schools, how do the private schoolmasters find the better ones and filter out the poorer ones? Can they use the Chinese restaurant approach and do it with a sign such as "Polite Children Lutheran School"?

We know better. We know the answer. They put certain demands on parents. Most of these schools expect payment in the form of tuition. Some allow parents and older children to work off part of the tuition. Some require parental involvement. For instance, the Hyde School in Bath, Maine, requires parents to attend several full weekend classes the first year that their child is in the school.

I know one New Yorker whose Jamaican doorman works two jobs in order to keep his children in a tuition-charging religious school. He sacrifices* his leisure time because his children's education is more important to him.

When parents sacrifice their time and money to put their children into private schools, the children see that education is important and they tend to get with the program.

Now, we're getting to the subtle-but-important facts of life about vouchers: even if there were never any strings attached, they would destroy private education in three ways:

1. For today's parents who are sacrificing to send their children to private schools, that sacrifice would be reduced or even eliminated when government funding is available. Their children give up the paper route before breakfast and dad quits his second part-time job. They also stop cleaning the school on Saturday. And when their parents no longer live out their concern for education, the students' eagerness for school is diminished.

2. The schoolmasters can no longer differentiate between better and weaker parents. They must, in effect, take down the sign, "Tuition-paying parents only." Children raised without a spirit of respect for others and their property will have equal access to their school. Children who are thugs and thieves, instead of being the rare exception, will form a quorum, just as they do today in many government schools. (The much-touted "Milwaukee system" even requires schools to accept all children and if oversubscribed, to choose by lottery.)

3. Worst of all, government subsidy transforms good parents into poor parents. When today's poor, even working two jobs, can't afford to put all their children into private schools, they must depend on charity. They go to their pastor or a private scholarship program, which funnels money to them that some other person sacrificed to give. The advantage of charity over government funds is that the recipient keeps a sense of proportion, even gratefulness, when receiving volunteered money. With welfare, however, the recipient concludes he has a "right" to the money and often gets angry because he believes he deserves more. The subsidy transforms him into an angry parent. And when government funding ruins the attitude of the parent, the parent ruins the attitude of the child.

Do I speak from experience? I've run a school, and I had to close it because I accepted way too many children who were morally and emotionally messed up by their parents. In my written analysis of lessons learned at Pioneer Christian Academy, I confessed: "I apologize to all public school people who I accused of overstating the case of 'children unprepared to learn.'"

Destructive Vouchers

Tax-financed vouchers will destroy the very private education that their proponents so

*sac' ri . fice: Surrender of some desirable thing in behalf of a higher object (*Webster's New Collegiate*, 1949).

much desire. The goose that is laying the golden eggs is the combination of voluntary parental sacrifice and the ability of schools to locate those parents. Converting this "sacrifice system" to a "welfare system" with school stamps, a.k.a. vouchers, will kill this goose. The aborigines of New Guinea learned about cargo. I learned about vouchers. So must we all.

If vouchers aren't a solution to the school mess, what is? If government funding of parental duties weakens parents, would removal of government funding enable them to regain parenting strength? I think so. Parents who increase their sacrifice for their children subsequently work to become better parents. The evidence for this is particularly clear if you listen to a few dozen homeschooling parents describe the changes in their families once they began homeschooling. Fathers in particular "turn their hearts toward their children."

The key to good education is good parenting, and the key to good parenting is for parents to reassume the burden of decision-making and financing their children's education. The separation of school and state is a necessary step to improve parenting in America. □

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THE FREEMAN
Ideas On Liberty

Independent Schools at Risk

by Jacob Huebert

As discontentment with government schools grows, tax-funded "school choice" has emerged as the leading reform proposal. School-choice programs typically include a voucher plan, although some would make direct payments from the government to private schools. Those proposals are intended to give parents new school alternatives, which are sorely needed, particularly in inner cities. Yet at the same time, private schools, by accepting the money, would become much like the public schools against which they are supposed to compete. Historical examples of government-sponsored school choice, here and in other nations, show that when private schools sign on to such programs, they often sign away their independence.

What has happened in American higher education provides strong evidence that accepting government money leads to a loss of independence. In the 1950s and 1960s, both public and private colleges and universities began accepting direct aid from the federal government.[1] Nevertheless, it caused alarm among many college presidents, prompting a commission consisting of the presidents of Johns Hopkins University, Union College, the California Institute of Technology, the University of Missouri, Stanford University, and Brown University; the former president of Columbia University; and the provost of Harvard University to declare:

> We are convinced that it would be fatal were federal support to be substantially expanded. Power means control. Diversity disappears, as control emerges. Under control, our hundreds of universities and colleges would follow the order of one central institution and the freedom of higher education would be lost.[2]

Their concerns would prove to be legitimate. As schools quickly became increasingly dependent on government money, the feds began to exert an ever-increasing amount of control over the recipient institutions.

Today, the dependence of schools on federal funds has become such that formerly independent schools are willing to do nearly anything to appease the government in order to retain their funding. William McGill, president of Columbia University in the 1970s, admitted that when the federal government threatened to take away his school's funding, which constituted half of its budget, he was ready to "promise almost anything" in order to get the government off Columbia's back.[3] The government was threatening the university because of concerns about minority representation in its student body and faculty. This was despite the fact that Columbia was already "trying every means" to increase minority representation.[4] It would thus appear that the government was not interested in Columbia's attitude toward minorities. It was interested in control.

Jacob Huebert is a student at Grove City College and an intern at FEE.

The Power to Define

As federal control over public and private education expanded, so did the very definition of a "recipient institution." In 1975, the Department of Health, Education, and Welfare (HEW) sent a letter to all colleges and universities asking them to sign an "assurance of compliance" that would guarantee they were complying with federal regulations under Title IX of the Educational Amendments of 1972. Although Title IX was only to apply to programs and activities directly receiving aid, HEW now said the regulations could be applied to an entire institution if even one part received federal aid.[5]

The majority of schools simply signed the form and returned it. Most of the scant few that saw the form as a threat to their independence did nothing at all with it and hoped no one would notice. One school, Hillsdale College, wrote to HEW refusing to sign because of the control that would follow.[6]

Eventually, after another school, Grove City College, became involved, the matter was litigated and ultimately appealed to the Supreme Court of the United States in *Grove City College v. Bell* (1984). In that case, the court ruled that a school could be considered a recipient institution if *any* student on campus received an education loan or a grant, and that funds could be withheld from school programs that were found to be not compliant with regulations.[7]

In another blow to private independent schools, Congress passed (over President Ronald Reagan's veto) the Civil Rights Restoration Act of 1987, which made it explicit that any school (including any elementary or secondary school) that enrolls students who receive federal aid is subject to regulation by the federal government.[8] Hillsdale and Grove City were presented with a choice: they could accept government control or they could accept only students who received no government aid. Although it would give them a disadvantage in the market, both schools chose the latter.

Advocates of voucher programs often assume that any school could follow this path and choose not to participate, nullifying concerns about independence. Joseph L. Bast and David Harmer insist: "Participation in voucher plans is never mandatory: those who manage private schools are free to remain outside the program if they believe the [inevitable] accompanying regulations are too burdensome."[9]

What Bast and Harmer fail to account for is that schools which refuse vouchers will be at an enormous disadvantage with those that are less concerned about independence, eager to accept vouchers, and happy to offer a "free" education to any student.

Replacing Government Money

Hillsdale president George Roche has been forced to deal with loss of federal student-aid funding since the *Grove City College* decision and the passage of the Civil Rights Restoration Act. In 1992, the school had to raise $1.4 million to replace the money students would otherwise have received through federal grants and loans. This figure is likely to rise because the government has the unfair advantage of being able to supply as much money as it wants to students who choose to accept its aid and who, accordingly, go to other schools. As Roche notes, "It's impossible to make money as fast as a counterfeiter."[10]

Hillsdale and Grove City have managed to get by without government money, but they are schools with long histories and many generous alumni benefactors. Under "school choice" for primary and secondary education, a new school wishing to remain independent would face a far greater disadvantage.

The implications for primary and secondary education under voucher programs are clear. By the logic of *Grove City College* and the Civil Rights Restoration Act, any school that accepts a voucher would also almost certainly have to accept what Sheldon Richman calls "a raft of government standards that before long would make the private schools virtually indistinguishable from the public schools."[11] Former voucher advocate David Barulich changed his views on the issue when he realized that since, under a "school choice" program, the government would inevitably define the sort of organization that would be eligible to accept vouchers, it would essential-

ly turn private schools into clones of public schools.[12]

Even the cases in which the federal government uses its power over private schools to prevent discrimination (ostensibly the purpose of Title IX and the Civil Rights Restoration Act) could seriously affect a school's ability to maintain its independence and standards, as anti-discrimination statutes have recently been extended to protect "rights" of "new" minorities, that is, claims from special-interest groups.[13]

Further, the U.S. Task Force on Assessing the National Goals Relating to Post-Secondary Education has called for "uniform standards" for all colleges—standards that go well beyond matters of putative civil rights.[14] There is no question that these developments could undermine the goals and independence of private schools.

Experience Abroad

Government money has been used for "private" education in certain other nations for some time, with predictable results. In France and Germany, for example, differences between Catholic schools and ordinary government schools have essentially disappeared since government funding of private religious education began. In these and other European countries, government-enforced uniformity has resulted in the weakening or even the elimination of religious teaching in private religious schools.[15] When Australia attempted a government-funded "privatization," the results were similar. Economist Estelle James of the World Bank notes that with the program came "increas[ed] regulation and centralization of decisions and the loss of private school autonomy."[16]

James also did an extensive study of the government-funded school choice program in the Netherlands. She notes that with the high level of government funding for private schools has come an amount of regulation that is virtually directly proportionate. Not only do the regulations for recipient schools specify required numbers of teachers, salaries, and conditions of work, they also limit schools' authority to fire teachers and never allow schools to fire teachers for lack of competence.[17] Further, all schools are forced to follow a "uniform curriculum" prescribed by the government.[18]

The record of American higher education and of government-funded private schooling around the world reveals that government money inevitably leads to government control. While free choice is a worthy cause for those who support liberty and quality education, it may reasonably be concluded from all available evidence that voucher programs and other government subsidies to private schools will lead to increased bureaucracy, increased controls over the lives of individuals, and quite possibly the end of independent private schooling in America. If greater educational freedom and diversity are desired, government money and control are not the means to achieve it. □

1. George Roche, *The Fall of the Ivory Tower* (Washington, D.C.: Regnery Publishing, Inc., 1994), p. 99.
2. Ibid., p. 100.
3. Ibid., p. 105.
4. Ibid.
5. Ibid., p. 112.
6. George Roche, *One by One* (Hillsdale, Mich.: Hillsdale College Press, 1990), p. 4.
7. Ibid., p. 5.
8. Douglas D. Dewey, "Separating School and State: A Prudential Analysis of Tax-Funded Vouchers," *Vouchers and Educational Freedom: A Debate.* Cato Policy Analysis No. 269, March 12, 1997. See www.cato.org/pubs/pas/pa-269.html.
9. Joseph L. Bast and David Harmer, "The Libertarian Case for Vouchers and Some Observations on the Anti-Voucher Separationists" in *Vouchers and Educational Freedom.*
10. *The Fall of the Ivory Tower*, p. 115.
11. Sheldon Richman, *Separating School and State: How to Liberate America's Families* (Fairfax, Va.: The Future of Freedom Foundation, 1994), p. 83.
12. Dewey.
13. *The Fall of the Ivory Tower*, p. 128.
14. Ibid., p. 129.
15. Charles L. Glenn, *Choice in Schools in Six Nations* (Washington, D.C.: U.S. Department of Education, 1989), pp. 41–42, 115, 189; cited in Dewey, p. 37.
16. Estelle James, "Private Education and Redistributive Subsidies in Australia" in *Privatization and Its Alternatives*, W. Gormley, ed. (Madison: University of Wisconsin Press, 1990), p. 108, cited in Dewey, p. 38.
17. Estelle James, "Public Subsidies for Private and Public Education: The Dutch Case" in *Private Education: Studies in Choice and Public Policy* (New York: Oxford University Press, 1986), p. 122.
18. Ibid., p. 123.

THE FREEMAN
Ideas On Liberty

School-to-Work: A Large Step Down the Road to Serfdom

by Gary Wolfram

It's been five years since Congress enacted the "School-to-Work Opportunities Act." School-to-Work is a federal program that ostensibly is designed to improve the work skills of children in the nation's government schools. The theory is that our education system should prepare children for jobs in today's society. This is funded by the billions of dollars the federal government is willing to provide states that adopt approved plans and programs for channeling students into occupations.

By inducing individual states to participate, the federal government can establish a "national framework" for "comprehensive reform." To date all 50 states, Puerto Rico, and the District of Columbia have received state development grants, and 43 states have received implementation grants. In addition, 61 communities have received local partnership grants.

The heart of this reform is to require each K–12 student to have comprehensive career guidance by no later than the seventh grade and to adopt a "career major" within an occupation area. The choice of occupation areas is to be made by a local planning board based on government economic projections of "need." On graduation, students receive "certificates of mastery" that are linked to national skill standards being developed by the federal government's National Skill Standards Board.

The certificate of mastery is designed to create a system of certification for all occupations. Once every state and every student are involved in School-to-Work, the federal government can, through its taxation and regulatory power, "encourage" businesses to require that new hires have a certificate of mastery.[1]

The Federal Role in Education

As Nobel laureate F. A. Hayek made clear in his 1960 book, *The Constitution of Liberty*, the federal Constitution was meant to provide a written foundation to protect the individual from his government. As such, the Constitution provides the federal government with explicit powers and through the Tenth Amendment clearly states that "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." One would search in vain through our Constitution for a statement that the federal government has been delegated power over the education of our children. That is why, traditionally, government control of education has been at the state and local levels.

For a number of reasons, the founding fathers were correct in not assigning the federal government a role in education. The first can be classified under what Hayek, in his final book, called "the fatal conceit."[2] It is impossible for a central planner to know what is the appropriate education for the millions of individual children who are in school every day. Only parents can know what is appropri-

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ate for their child. To think that a federal bureaucracy in Washington, D.C., can better determine even a portion of what is to be taught in schools from Miami, Florida, to Anchorage, Alaska, is at best misguided and at worst a threat to our liberty.

In the context of the School-to-Work Act one might argue that the federal government is not mandating a particular program. Indeed, states may choose not to participate at all, though naturally they find the money irresistible. But this is too superficial a view. Most state governments succumb to what I call the buffalo strategy. If I don't shoot the buffalo someone else will. If Kansas does not adopt an approved plan, it will not receive the taxpayers' money and some other state will. The strategy may be rational from the perspective of a state government, but there are costs. In the short run, educational priorities will be altered to fit the terms of the federal program. In the long run, there will be a further loosening of our constitutional moorings and another step toward government planning of the economy.

The statute requires that each state's plan be approved by the federal government for the state to receive the money. Thus, it is likely that the federal bureaucrats who approve the state plan may influence what the state program will be. Indeed, the statute itself has some requirements to indicate what the plans should look like. For example, students are to be counseled in their career plans by not later than the seventh grade in an attempt to get them to identify their career majors (Section 102), and students are to be encouraged to enter nontraditional careers (Section 4).

One cannot read the Act without getting a clear indication that the Congress is attempting to redirect education into a worker-training role and away from a classical liberal-arts curriculum. Whether this is good public policy is not the question at this point; the issue is whether the federal government was intended under the Constitution to engage in it.

As Frederic Bastiat wrote some 150 years ago in *The Law*, when government becomes involved in education, people begin to lose a sense of whose responsibility it is to educate their children.[3] Education becomes thought of as the responsibility of government; all education issues will become political issues; and people will blame the government for its inevitable failure to do what it claims it can do. Today we prove that Bastiat was right as we engage in a political discussion about whether a primary mission of schools should be specific job training, as opposed to providing general knowledge such as reading, writing, history, mathematics, art, music, geography, and so on.

Are schools likely to be any more efficient at job training than they are at basic classical education? If not, the short-run response may be to call for more resources to go into education, but the long-run response will be further complaints and dissatisfaction with government's actions.

The Political Economy of School-to-Work

Public-choice theorists have recognized that all state action is human action, again something that Bastiat made clear a century and a half ago. This means that the political process is determined by the incentives created within the system. Federalist No. 10 warned us that factions or special interests will attempt to use the political system to direct resources to themselves.[4]

School-to-Work is a case where special-interest groups, in particular business, will have every incentive to influence the curriculum of the schools. Once we have opened the door wide to the business community to help determine what job skills will be taught in the schools, each employer will attempt to get the specific training used in his particular industry into the curriculum. Employers will also assist in determining which "career majors" the seventh-grade students will be steered into. It is only rational that each employer should seek to have students directed into his industry in order to increase the supply of skilled labor. This reduces job-training costs and wages.

The issue is not whether this is illegal or immoral. The issue is that the system is

designed for this to happen and thus it is likely to happen. This leads us to question whether dollars are likely to be spent better by School-to-Work bureaucrats than by taxpayers. The answer is no.

Markets versus Central Planning

In *Socialism*, his seminal work on the failure of central planning, and in later works, Ludwig von Mises showed conclusively that government planners cannot succeed because information indispensable to efficient production is always decentralized and beyond anyone's capacity to gather.[5] Hayek followed Mises in analyzing how the price system allows the market process to solve this problem and make the most efficient use of resources. He warned against attempting to plan a society rather than relying on markets.

The collapse of socialist Europe proved Mises and Hayek to be correct. Yet the lesson has not been fully learned in the United States. The School-to-Work program is embedded in the paradigm of central planning. It is based on the idea that businessmen and educators can get together and plan a curriculum that will teach specific skills for specific industries and assist 12- or 13-year-olds in finding their careers. This is the antithesis of the market process and cannot possibly result in an efficient use of resources.

Markets are dynamic. Those who were in seventh grade ten years ago and are now graduating from college could not have known the many new jobs that would be created. Whole industries have arisen, and some have collapsed. The Bill Gates of the future will not be represented at the committee determining the right career for the right child. To think that today's educators and businessmen are capable of advising young students on career choices is to engage in the fatal conceit.

Schools should provide a strong education in basic academic skills. A person well grounded in these can easily be taught the specific skills needed for a particular job. High job-training costs, often used to rationalize School-to-Work, can easily be lowered if graduates are taught to read, write, and think well. We already ask too much of schools in a vain attempt to replace the family. To burden them with job training is asking more than can be delivered.

There are hundreds of proprietary schools in the United States that can provide job training for students, and they have every reason to respond to changes in market circumstances. No one can realistically believe that the political process of "cooperation" between schools and business can result in anything other than a political outcome.

Finally, we must also beware of "scientific results" showing that students who go through School-to-Work programs get jobs at faster rates than students who don't. This is a case of what Bastiat called the seen and the unseen. We can see the positive results from an expenditure by the government, but we cannot see what would have been done with the money had it remained in private hands. □

1. The National Center on Education and the Economy has been the driving force behind the School-to-Work program. It is committed to developing an integrated system of education, job training, and employment. For further discussion see Diane Fessler, "School-to-Work: It's the Law," at www.fessler.com.

2. F.A. Hayek, *The Fatal Conceit: The Errors of Socialism* (Chicago: University of Chicago Press, 1988).

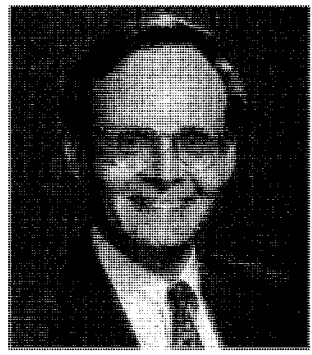
3. *The Law* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1998 [1950 translation of 1848 French version]).

4. For a survey of the economists' analyses of this phenomena under the title "rent seeking," see Robert Tollison, "Rent Seeking: A Survey," *Kylos*, 1982, pp. 575–602.

5. Ludwig von Mises, *Socialism: An Economic and Sociological Analysis* (Indianapolis: Liberty Fund, 1981 [1922]).

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Taxation by Litigation Threatens Every American Business

Abusing the legal system for political, social, or greedy ends is fast becoming America's favorite pastime. Billions of dollars, millions of jobs, and the survival of legitimate businesses are at stake. And if the Clinton administration's latest lawsuit fantasy proceeds, Katie bar the door: government itself will become the biggest abuser of them all—with the potential to threaten dozens of industries from fast food to automobiles.

Lawsuit abuse will end up costing the Dow Corning Corporation billions of dollars. Even though no reputable scientific study to this day has ever shown a connection between the company's breast implants and disease, the litigation lottery forced Dow Corning into bankruptcy in 1995. Science took a back seat to the greed of trial lawyers and plaintiffs looking for deep pockets.

Gun manufacturers are now facing a similar plight, as a growing number of cities file suit against them for making a product that kills. Never mind that just about any product can kill if that's the intent of its user. City officials claim they are simply trying to recover public health and safety expenses that are associated with gun crimes. According to the National Center for Policy Analysis, the costs to society of firearms violence are *one-fifth* the savings that accrue from the crimes that firearms ownership prevents. But there's no guarantee that gun makers won't have to cough up millions anyway.

Now comes the Clinton administration to raise the stakes in the national Blame Game. The Justice Department is preparing a lawsuit against tobacco companies for the stated purpose of recovering Medicare costs attributable to smoking. Picking on an unpopular industry with a charge that sounds superficially defensible may be politically shrewd, but the evidence suggests this is nothing more than a grab for cash with sweeping implications for every American business.

It's no secret that the Clinton administration would like to put the tobacco industry out of business or rake in lots of revenue trying. Its efforts to impose massive new taxes on cigarettes, however, went up in bipartisan smoke last year in Congress. It was also rebuffed in its efforts to have the Food and Drug Administration (FDA) regulate tobacco products as medical devices. The administration apparently sees a new lawsuit, buttressed by dubious and far-reaching legal theories, as a way to do an end run around Congress, even though Attorney General Janet Reno has testified that "the federal government does not have an independent cause of action" to sue tobacco firms for health-care cost reimbursement.

This is the same government, incidentally, that for decades until 1974 gave free cigarettes to the military—even after ordering warning labels on cigarette packages in 1966. The Clinton administration that is contemplating a new lawsuit against tobacco compa-

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nies is the same administration that has denied veterans' requests for coverage of diseases thought to be related to smoking. Indeed, President Clinton's secretary for veterans affairs called it a "borderline absurdity" to compensate veterans for their "personal choice to engage in conduct damaging to their health."

Writing in the *Wall Street Journal* (February 8, 1999), constitutional scholar Robert A. Levy of the Cato Institute explained the attenuated legal notions on which a suit against tobacco firms for health care expenses would have to rest:

> In effect, Justice will assert that it can recover merely because smoking injured someone protected by Medicare—even though that person, having assumed the risk, would have no right to recover on his own. The same tobacco company selling the same cigarettes to the same smoker and resulting in the same injury will be liable only if the smoker is a Medicare recipient and the government is the plaintiff. Liability thus hinges on the injured party's Medicare status, a happenstance utterly unrelated to any misbehavior by the industry.

What makes the threat of a new lawsuit even more ludicrous is that after factoring in health-care costs, the federal government actually *makes money* on every pack of cigarettes sold. That's because the heavy excise taxes smokers pay add up to more than the health-care costs associated with their smoking. According to the FDA, "the most detailed research on the issue of whether smokers pay their own way is the 1991 study by Manning, et al., who concluded that 'there is no net externality, because the sum of all smoking-related externalities is probably less than the added payments imposed on smokers through current Federal and State excise taxes.'"

Moreover, because they don't live as long as nonsmokers, those who smoke contribute far more in Social Security taxes than they get back in benefits. The Congressional Research Service concluded last year that "all in all, smoking has apparently brought financial gain to both the federal and state governments."

Clearly, the Clinton administration seeks to further corrupt the legal system to get the cash it has not been able to secure through higher taxes via the democratic process. If it succeeds in its vendetta against tobacco, who might be next? Michael Baroody, senior vice president of the National Association of Manufacturers, rightly fears that this action "would set a precedent for federal litigation against industries an administration—this or any other—might not politically favor."

The Surgeon General and the FDA warn against high-fat diets; should the Justice Department sue the fast-food industry, bakeries, or the makers of Ben & Jerry's Ice Cream? Why not sue GM, Ford, and Daimler-Chrysler to recover the medical costs caused by auto accidents? Cholesterol has been implicated in heart attacks and too much alcohol causes cirrhosis of the liver; perhaps cattle ranchers should be sued for selling artery-clogging beef and winemakers should be hauled into court and made to pay the hospital bills for every wino in America. And how about the makers of fertilizer: shouldn't they be forced to provide compensation for any medical costs incurred in the 1995 Oklahoma City bombing?

Whether the subject is breast implants, guns, tobacco, or any other product, abusing the legal system is not a harmless lark. It is an exercise in intellectual corruption, an attack on the democratic process, and a manifestation of greed run amok that every consumer and businessman in America ignore at their peril. □

THE FREEMAN
Ideas On Liberty

The Central Fallacy of Public Schooling

by Daniel Hager

When World War II ended, Congress authorized a tax cut to take effect January 1, 1946. *Young America,* a publication distributed through public schools, ran an article in its December 13, 1945, issue discussing the measure and presenting a brief history of American taxation. The article concluded with a section titled "Then & Now: Taxes Serve Us."

"One hundred years ago," the writer stated, "our government helped the citizens by maintaining order. It did little else. Its expenses were low, and so taxes were low." He then quoted Benjamin Franklin's observation in *Poor Richard's Almanack* in 1758: "It would be a hard government that should tax its people one-tenth part of their income." The *Young America* writer continued, "In 1940, our Federal, State and local governments taxed us *one-fifth* of our incomes. But Franklin could not have guessed the tremendous growth of this country." (Emphasis in original.)

The writer then offered justification for such high taxes: "As students, our young citizens are given school buildings. Our government does hundreds of things for us in our everyday life." He finished with a quotation from Supreme Court Justice Oliver Wendell Holmes, Jr.: "I like to pay taxes. It is purchasing civilization."

The article vividly illustrates the overriding intent of public schooling, which has always been indoctrination of the young.

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Who's in Charge?

Indoctrination itself is not illegitimate. In fact, it is an intrinsic part of child rearing. Out of love and concern, parents explicitly or implicitly formulate desired outcomes for the young lives they have created. Parents generally hope their children will adhere to their own traditions and belief systems, which they attempt to inculcate.

The question parents must face is, "Who will do the indoctrinating?" Schooling is an adjunct to child rearing. The schooling options available force parents to make decisions regarding the level of autonomy they wish to exercise. They retain the greatest control over their children's developing beliefs by schooling them at home. An alternative is to enroll their children in an institution where they are certain the indoctrination conforms to their own values, such as a religious school.

When parents send a child to a tax-funded school, they sacrifice their autonomy to alien interests. The state has goals of its own that are distinct from those of parents. Parents are able to economize by availing themselves of a "free" school, but the bargain is Faustian. The child is subjected to indoctrination outside parental control. The price of tax-funded schooling is that parents give up their children to become instruments of the state.

Under totalitarian regimes, the subjugation of parental belief systems to those of the state is blatant. Schoolchildren are propagandized into the doctrines of the

leadership, their thoughts molded to the state's purposes.

But even under a "democratic" regime the state operates manipulatively for its own ends. Those who govern generally like to continue governing. Their governance is more easily maintained when the governed are passive and docile. The state propaganda machine must convince the citizenry of government's benevolence. Schoolchildren are taught, as in the *Young America* article, that government "gives" them things and "does" things for them.

Government schools inevitably become battlegrounds for control by ideological adversaries. The nature of the indoctrination changes as advocates of particular ideologies wax and wane in their power to influence curricula. The constant is that parents have relinquished direct control over what their children are taught to believe.

This battle has been going on ever since the modern public school emerged in the first half of the 1800s. Education historian Joel Spring stated, "In the Western world of the nineteenth century, various political and economic groups believed that government-operated schools could be a mechanism for assuring the distribution of their particular ideology to the population. In this sense, public schools were the first mass medium designed to reach an entire generation."[1]

Early Theocracy

Indoctrination through compulsory schooling originated early in the nation's history. Massachusetts Bay Colony was organized unabashedly as a theocratic government that required citizens to adhere to stipulated religious beliefs. In 1642 the Massachusetts General Court passed an act requiring compulsory education of children and giving town selectmen the authority to maintain orthodox teaching and punish recalcitrant parents. The civil government was in charge of the schools, which were supported by taxes. R. Freeman Butts and Lawrence A. Cremin wrote, "Here was the principle that government had authority to control schools, and it was well enunciated in the New England colonies early in their histories. It was a principle of great importance, for it set a precedent in American life establishing the authority of the state to promote education as a public and civil matter."[2]

However, private schoolmasters were in business in Boston by the mid-1660s, according to records examined by Robert Francis Seybolt. The number of private teachers gradually enlarged to the end of the seventeenth century, partly in response to market demand. He wrote, "The two public schools [in Boston] . . . admitted only boys who were at least seven years of age and had learned to read. Girls as well as boys were welcome, at any age, in the private schools."[3]

In the 1700s in New England, Butts and Cremin noted, private schools flourished as "colonial legislatures showed a slackening of effort to require compulsory education and gave greater freedom to private groups to educate children in schools of their own preference."[4]

A wide variety of curricula was offered in eighteenth-century Boston private schools, Seybolt found. "Unhampered by the control of the town meeting, and little influenced by traditional modes of procedure, these institutions were free to grow with the town. This they did as conditions suggested it. The result was a remarkably comprehensive program of instruction which appears to have met every contemporary educational need."[5]

Seybolt articulated the benefits of private-sector schooling. "The private schools were free to originate, and to adapt their courses of instruction to the interests of the students. The masters sought always to keep strictly abreast of the time, for their livelihood depended on the success with which they met these needs. No such freedom or incentive was offered the masters of the public schools."[6]

This principle was overwhelmed by the swelling tide of nationalism of the early 1800s. Proponents of common schools, or tax-funded elementary schools requiring compulsory attendance, viewed them as crucial vehicles for indoctrinating young people in Americanism. The movement intensified as immigration increased from continental European cultures that lacked democratic tradi-

tions. Benjamin Labaree, president of Middlebury College in Vermont, expressed popular fears in an 1849 lecture before the American Institute of Instruction. He asked, "Shall these adopted citizens become a part of the body politic, and firm supporters of liberal institutions, or will they prove to our republic what the Goths and Huns were to the Roman Empire?"[7]

Wartime Indoctrination

Chauvinistic indoctrination becomes a useful tool of the state in wartime, as when President Woodrow Wilson created the Committee on Public Information (CPI) to build support for American participation in World War I and to blunt opposition by constituencies with European roots. The nation's high schools were prime propaganda targets and received hundreds of thousands of copies of a CPI-produced pamphlet designed to stir anti-German sentiment. "Germany does not really wage war," the pamphlet stated. "She assassinates, massacres, poisons, tortures, intrigues; she commits every crime in the calendar, such as arson, pillage, murder, and rape."[8] Joel Spring commented, "From the standpoint of the public schools, [the CPI] was the first major attempt to bring the goals of locally controlled schools into line with the policy objectives of the federal government."[9]

An influential CPI official was William Bagley, who "believed that local control of educational policy was a major hindrance in adapting the public schools to the needs of the United States as a world leader. . . . The combination of the war and the new national spirit opened the door for the federal government to exercise leadership in a national educational policy. Included in Bagley's proposals was a call for federal financing of the public school system."[10]

During the 1920s, local schools suffered for being dominated by the wrong kinds of people on their boards, according to public-school champion George S. Counts. His research showed that "for the most part, [board members] are drawn from the more favored economic and social classes. They are also persons who have enjoyed unusual educational advantages. . . . No longer is the ordinary American community homogeneous as regards interests, philosophy, and ideals. Hence the need of guarding the integrity of the various minority groups."[11] The laboring classes were expressing "lack of confidence in the public school on the ground that it is under the control of the great capitalistic and employing interests."[12] As the high school of that era evolved and expanded in curricula, he noted, "the institution offers itself as a powerful agency of propaganda to any group able to secure dominion over it."[13]

Since then the dominion of the federal government over schooling has grown to a scope of which Bagley would approve. Its power, abetted by the activism that the collectivist Counts advocated for teacher organizations, enables it to be the leading propagandist in educational policy.

But the nationalist Bagley would be disappointed in the ideology that has accompanied the federal growth. The current pre-eminent public-school propaganda indoctrinates students in an anti-nationalistic collectivist environmentalism. Meanwhile, Counts's "capitalistic and employing interests" attempt to re-establish influence because so many products of public schools need remediation before they can become employable.

Proponents of public schooling argue against the complete privatization of schooling on the grounds that the poor would not be able to afford tuition and that some parents would not provide schooling for their children, leaving them "uneducated." However, the rampant levels of ignorance, subliteracy, and hostility to learning that characterize tax-funded schools argue that the present system is itself not serving the best interests of students.

Instead it is clear whose interests are being advanced. Fifty-four years ago the writer in *Young America* was moved to emphasize in italics that era's apparently high tax rates. Since then the average tax burden has doubled. Yet, as one of my acquaintances has commented, "Americans today are in a stupor." In other words, the tax-supported school system has triumphed. Americans are behaving exactly the way those who govern desire them to behave.

Children who are turned over to the state become molded by the state. Most parents cannot conceive of a totally privatized alternative because they themselves have been indoctrinated by public schooling to believe in its alleged necessity. However, it is fallacious for parents to think that children can escape government schooling without having their traditions and beliefs subverted. "Free" schooling is seductively attractive in the short run, but it has long-term costs. The dismantling of tax-funded schooling will not be accomplished until more and more parents say, "My child does not belong to the state." □

1. Joel Spring, *Images of American Life: A History of Ideological Management in Schools, Movies, Radio, and Television* (Albany: State University of New York Press, 1992), p. 2.
2. R. Freeman Butts and Lawrence A. Cremin, *A History of Education in American Culture* (New York: Holt, Rinehart and Winston, 1953), p. 103.
3. Robert Francis Seybolt, *The Private Schools of Colonial Boston* (Cambridge, Mass.: Harvard University Press, 1935), p. 9.
4. Butts and Cremin, p. 103.
5. Seybolt, p. v.
6. Ibid., p. 92.
7. Quoted in Butts and Cremin, p. 192.
8. Quoted in Spring, p. 25.
9. Ibid., p. 27.
10. Ibid., p. 21.
11. George S. Counts, *The Social Composition of Boards of Education* (Chicago: The University of Chicago, 1927), pp. 82, 97. See also Daniel Hager, "Educational Savior?" *The Freeman*, June 1999.
12. Ibid., p. 86.
13. Ibid., p. 91.

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THE FREEMAN
Ideas On Liberty

Subsidized Education

by Russell Madden

It's an annual ritual. With a sense of dread tinged with resignation, college students, or their parents, wait to discover how much this year's tuition will rise. Unlike their experience with new computers, they entertain no expectation that rates for their education will decrease. The upward spiral in prices appears inexorable.

Yet is that the way it must be?

For a student in college between 1997 and 2001, average total costs will be nearly $46,000 at government institutions, reports *Investor's Business Daily* (December 8, 1998). For those in private schools, the news is even bleaker. Students face expenses approaching $97,000. Twenty years from now, graduates may well be staggered by costs of $157,000 and $327,000, respectively.

In the past four decades, the total yearly spending on higher education increased from $7 billion to $170 billion a year. Financial aid at both the state and federal levels reached $60 billion in 1998, with guaranteed student loans comprising nearly 60 percent of that aid, a six percent increase from 1997. Many people would contend that such a bump in financial aid is justified given the price hikes in tuition and other costs. Not only would they adamantly resist any attempt to lower that aid, they actively lobby for more.

Unfortunately, the first or most obvious answer to a problem is not necessarily the correct one. The reality is that government subsidies not only lead to ever greater educational costs, but also threaten the very existence of private institutions of higher learning.

Two things need to be considered in this matter: basic economic principles and individual freedom.

Supply and Demand

The price we pay for any good or service is essentially determined by relative supply and demand. Other things being equal, the greater the supply of a product with a given demand, the lower the price the supplier will ask and obtain. Conversely, when demand rises relative to supply, prices will increase.

This is as it should be. Through this process, consumers indicate the importance they attach to a certain product or service by their willingness to purchase it at a given price. This insures that economic goods flow to the people who will pay the most for them. Those who are outbid will turn elsewhere to satisfy their desires.

Under normal circumstances, when a product's price is high and supply relatively low, more producers move into that line of work, hoping to cash in on greater returns than they might obtain producing other goods or services. This increased supply then tends to bring down prices. Left to operate on its own, supply and demand will bring goods and prices into equilibrium until all the supply is purchased by those willing to pay the price.

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What happens, though, if the price of a product is artificially set below its clearing price?

If music CDs usually sell for, say, $15, there will be a given number of people willing to purchase them at that price. However, if a third party decides to subsidize music lovers to the tune of $5 per CD, more people will decide they can afford to purchase CDs. Demand will increase. Delighted producers will make more of them. Sales will increase.

Before long, producers will realize that all those people willing to buy CDs at the unsubsidized price of $15 are paying less than they are willing to pay. So the producers will start increasing their prices, say to $17 at first, then $19, then $20. After all, with the subsidy, the consumer has to pay only $15.

But some consumers who have grown accustomed to buying cheaper CDs will have to cut back on their purchases or stop entirely. They are unhappy about seeing their living standard fall. So they demand a larger subsidy, joined by the producers, who face declining sales. If the buyers succeed in getting the "music they deserve" at the price they want, the whole cycle begins again.

So it is with government programs that mask the true costs of college for students. State and federal grants, guaranteed student loans, and direct subsidies to public colleges and universities lower the apparent price of obtaining a college education. This leads to a higher demand. College administrators then feel justified in increasing tuition and fees, realizing that many if not most students are subsidized in one form or another.

The cycle is born: raise tuition; give out more aid; raise tuition again.

Lesser Students

A side effect of this policy is that it attracts more poorly qualified and less motivated students who value higher education less than others who are willing to pay the full price. Colleges have to devote more resources to remedial programs, and students in these programs have a greater dropout rate.

Another problem is that since public administrators do not have to show a profit to stay in business, they are less concerned with the satisfaction of their customers. (Remember the last time you had to wait in an interminable line at the post office or department of motor vehicles?) Administrators also have incentives to increase their budgets needlessly. After all, increased "costs" translate (through a kind of self-fulfilling prophecy) into increased subsidies.

According to the Heritage Foundation, in the 30 years since its inception in 1965, the federally guaranteed student loan program subsidized 74 million students to the tune of $180 billion. By artificially lowering interest rates and insuring banks against defaults, this program has actually raised the total cost of a college education in the long term for *all* students—whether they receive guaranteed loans or not.

While the short-term direct costs of subsidized loans are less than for loans obtained in a free market, the long-term result is to reinforce a cost spiral that outpaces the general price rise (as outlined above). With less attention paid to restraining spending—by administrators and students—waste and unnecessary expenses tend to increase more than they would in a market-based environment.

When combined with direct subsidies to government-owned colleges and universities, the loan program makes such institutions more attractive to students than they might otherwise be. Private colleges find it difficult to compete against public institutions whose price is lowered by taxpayers' money.

At the beginning of this century, 80 percent of students enrolled in private schools. Now that same percentage of students enters government-owned colleges. In the past 30 years, over 300 private institutions closed.

It is as if the government decided to subsidize one supplier of CDs and not another. Who would want to buy more expensive (unsubsidized) CDs? The second supplier would soon be out of business.

When government interferes in the supply of any good or service—whether it be CDs, food, or education—it distorts the behavior of consumers and producers alike. When the product is education, this process becomes outright dangerous. A vital society depends on

a diversity of viewpoints and ideas. With government largesse comes government control. But government has no business regulating ideas. That is the essence of the First Amendment to our Constitution. Political leaders should not be picking winners or losers in the realm of education. Diversity in approach, attitude, and emphasis should be left to the producers and consumers of education.

Besides that encroachment on liberty, no one has a right to anyone else's money. The taxes diverted toward education are taken not only from those who *do* attend college but also from those who do not. No one should be forced to pay for something he does not use. Even less should anyone have his wealth, and the portion of his life which that wealth represents, taken from him to pay for the teaching of ideas he does not support.

Liberty, intellectual independence (personal and institutional), economic efficiency, and educational diversity and quality all argue that government subsidies and guaranteed student loans should end. Only in this way will the unceasing upward surge in tuition be moderated. Even more important, we can begin to restore respect for the freedom and dignity of each individual. □

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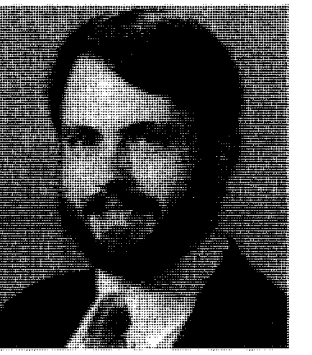
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A Superpower's Prerogative

Being in love means never having to say you're sorry. Being a superpower apparently means the same thing. At least, that appears to be the lesson of President Bill Clinton's promiscuous use of force.

It seems almost unpatriotic to suggest that a president would attack other nations for political purposes. Yet Bill Clinton's conduct regularly raises this suspicion.

Shortly after testifying before the federal grand jury and giving his disastrous televised speech to the nation in August 1998, the President launched air strikes against both Afghanistan and Sudan. The timing seemed more than coincidental, since there was no compelling reason to attack when he did; indeed, the Joint Chiefs of Staff saw no need for immediate action.

Clinton's sustained bombing of Iraq on the eve of Congress's impeachment debate last fall seemed equally questionable. Nothing was gained by striking at Iraq at that moment. The alleged justification was a U.N. paper reaffirming what was already known about Iraq's resistance to arms inspections. Moreover, *Insight* magazine reported that the decision to attack preceded release of the study.

Then there's the war on Yugoslavia, which began in March. There were several embarrassing events that the President might have hoped to push off the front page—such as China's spying and contributions to his campaign, and Judge Susan Webber Wright's contempt citation against him in the Paula Jones case.

Clinton might be blameless, but his record of dissembling denies him any benefit of the doubt. The possibility that the President has been misusing the military for political purposes surely warrants at least a cursory examination by Congress, which is charged with declaring war and raising armies.

The assault on Sudan, in particular, brings up another profound issue of national abuse of power. Even if the President genuinely believed that the attack was necessary at the time, overwhelming evidence indicates that Washington hit the wrong target. Yet no one has been held accountable.

Of course, this isn't the first time that America demonstrated that it can bomb—or shoot—with impunity. In 1985 a U.S. Navy ship on patrol in the Persian Gulf downed an Iranian airliner. Washington claimed that the plane was descending, outside of normal civilian flight paths, and not emitting normal civilian signals. It turned out that the government lied on every count. Washington eventually paid compensation to Iran, but never owned up to the American people.

Similarly, the Clinton administration doesn't seem willing to confront its apparent mistake in Sudan. On August 20, 1998, a U.S. cruise missile destroyed the Ashifa Pharmaceutical Plant. American officials claimed that it produced nerve gas.

As with the Iranian airliner shoot-down, Washington offered a host of seemingly plau-

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sible justifications for its action. The plant was heavily guarded, run by the Sudanese military, financed by Saudi Arabian terrorist Osama bin Laden, produced no commercial products, and yielded a soil sample containing the chemical EMPTA, which is used in the production of VX, a nerve gas, and has no nonmilitary purpose.

Alas, as with the Iranian airliner, everything Washington said was subsequently disproved. Those who visited the plant said it was not guarded; even the administration abandoned its claim that bin Laden was behind the plant, shifting to the charge that the Sudanese military or Iraq was involved. But there was no evidence that Khartoum was involved and the alleged Iraqi connection was limited and seemingly innocuous. Sudanese dissidents said the new plant owner was nonpolitical.

It turns out the Ashifa factory did produce pharmaceuticals and veterinary drugs. Moreover, architects, engineers, and suppliers all said the plant lacked the extra space, equipment, materials, and air-sealed doors necessary for chemical weapons work.

Most important, EMPTA is difficult to isolate in soil; in fact, the incriminating soil sample could have resulted from the breakdown of common pesticides. EMPTA's composition resembles that of several herbicides and pesticides, and could be confused with them in an imperfect test. Moreover, it turns out that there are legitimate, though limited, commercial uses of EMPTA.

All told, observed Oxford chemistry professor R. J. P. Williams: " 'Trace' elements in adjacent soil are of no use. Either the administration has something to hide, or for some reason is withholding the evidence." Indeed, in February American chemists brought in by the plant's owners announced that their tests didn't detect even trace elements of EMPTA.

Yet the administration refused to accept any outside inquiry. Even as Washington demanded an international review of alleged Serb atrocities in Kosovo, it rejected Sudan's offer to open what remained of the plant for inspection, a dangerous course if the American charges were true.

Why did Washington reject Sudan's proposal? National Security adviser Sandy Berger declared that "we had overwhelming grounds to strike this facility."

Not that every administration official was so confident. One told the *New York Times*: "As an American citizen, I am not convinced of the evidence." In fact, the administration eventually dropped its freeze on the plant owner's assets—without, however, acknowledging fault.

Of course, maybe the administration was right. But Washington has no right to be judge and jury in its own case. First, bombing other nations should be a last rather than first resort. Yet the United States never demonstrated why it could not have achieved the same result through diplomatic pressure, which has worked in the past in Sudan. (That government previously expelled bin Laden.)

Second, targets should be chosen carefully. Even if Sudan was rightly attacked, there were other suspicious facilities—one near Khartoum that is tied to the military, for instance. One Pentagon official admitted: "There may have been better places to go."

Third, launching a military strike should require evidence that satisfies someone other than just Washington. In 1986 President Reagan was willing to release confidential information to justify the assault on Libya as retaliation against the bombing of a disco frequented by Americans in Berlin.

The administration's refusal to make a case to other nations strengthens the claim of Sudan's ambassador to the United States, Mahdi Ibrahim Mohamed, who argued that the attack "was an act of lawlessness against the Sudan." Even Milt Bearden, the CIA's former station chief in Khartoum, said that he had his doubts about administration claims.

Yet today the issue lies forgotten. Washington has moved on; it has bombed Yugoslavia into rubble, making such inexcusable mistakes as hitting the Chinese embassy along the way.

This situation obviously isn't good for other nations. It also isn't good for America. For a government willing to act lawlessly abroad is likely to do the same at home.

Being the world's only superpower yields responsibilities as well as benefits. One of those is admitting when it is wrong. □

THE FREEMAN
Ideas On Liberty

The Bathtub, Mencken, and War

by Wendy McElroy

"Not a plumber fired a salute or hung out a flag. Not a governor proclaimed a day of prayer," wrote H.L. Mencken on December 28, 1917, in the *New York Evening Mail*. The occasion for the iconoclastic journalist's lament was "A Neglected Anniversary," so titled because, as Mencken declared, America had neglected to celebrate the 75th anniversary of the invention of the modern bathtub, which had occurred on December 20, 1842, in Cincinnati, Ohio.

He proceeded to offer a history of the bathtub in the United States. President Millard Fillmore had installed the first one in the White House in 1851. This had been a brave act on Fillmore's part, since the health risks of using a bathtub had been the subject of great controversy within the medical establishment. Indeed, Mencken observed, "Boston early in 1845 made bathing unlawful except upon medical advice, but the ordinance was never enforced and in 1862, it was repealed."

"A Neglected Anniversary" was the direct result of the anti-German propaganda that dominated the newspapers in the years before and during America's involvement in World War I. Mencken was an established and respected newspaperman. He had started his career as a reporter for the Baltimore *Morning Herald* in 1899, becoming city editor in 1904. In 1906 he began his long association with the Baltimore *Sun*. Yet during America's anti-German period, he could not get material on World War I published because of his pro-German views, which sprang from a love of the culture rather than from its politics. Mencken was enraged by the popular portrayal of Germans as "barbarous Huns" who committed atrocities such as the widely reported bayoneting of Belgian babies. (Although this accusation had been absolutely accepted by the American people, it was later proven to be pure Allied propaganda.)

Mencken attempted to infuse some real-world perspective on the war into American newspapers. Near the end of 1916 he traveled as a reporter to the eastern front to cover the hostilities, but the breakdown of diplomatic relations between Germany and America forced him to return. At home he discovered to his horror that most of his dispatches had not been published. Edward A. Martin writes in *H.L. Mencken and the Debunkers*, "It was 1917; Mencken, passionately pro-German, felt muzzled by the excesses of patriotism that dominated the attitude of Americans. The 'Free Lance' column [Mencken's daily column in the *Evening Sun*] had been a casualty, in 1915, of his unpopular views of the war. The war and all of its ramifications were excluded from his writing until after 1919."

Thus, Mencken—a political animal to the core—turned to nonpolitical writing in order to publish. A *Book of Prefaces*, a collection of literary criticism, appeared in 1917. His book on the position of women in society, *In Defense of Women*, was issued in 1918. And

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the first edition of Mencken's magnum opus, *The American Language*, emerged in 1919. He also wrote for the literary magazine he co-edited with George Nathan, *The Smart Set*.

But Mencken was far from sanguine about having his political views suppressed. He complained to Ellery Sedgwick, editor of *The Atlantic Monthly*, whose pages were also closed to him: "It is, in fact, out of the question for a man of my training and sympathies to avoid the war. . . . How can I preach upon the dangerous hysterias of democracy without citing the super-obvious spy scare with its typical putting of public credulity to political and personal uses?"

Seeking an Outlet

His restless frustration found vent in "A Neglected Anniversary." Like so much of Mencken's writing, the article was not quite what it seemed to be on the surface. It had levels of meaning. "A Neglected Anniversary" was a satire destined to become a classic of this genre of literature in much the same manner as Jonathan Swift's "A Modest Proposal," which satirized English policy in Ireland. In the article, Mencken spoke in an eloquent tone of mock reason, which was supported by bogus citations and manufactured statistics.

In short, his history of the bathtub was an utter hoax set within the framework of historical fact.

The modern bathtub had not been invented in Cincinnati. Fillmore had not introduced it into the White House. The anti-bathtub laws Mencken cited were, to use one of his favorite words, "buncombe."

Calling the hoax "an amazing mixture of obvious fact and hard to refute fiction," the author of *An Un-Neglected History*, P. J. Wingate, observed, "The story said that Millard Fillmore became President in 1850. True. It was easy to look that up. Also it said, obliquely, that Gen. Charles M. Conrad was Secretary of War under Fillmore. True again." As for the "hard to refute fiction," Wingate continued: "Mencken set a couple of very carefully hidden traps. He quoted from *The Western Medical Repository* of April 23, 1843, and the *Christian Register* of July 17, 1857. No editor or scholar in the land could find these imaginary journals but they had plausible names." Moreover, Mencken's citation of specific dates lent credibility to the quotations so that researchers might well assume that their own archives were incomplete.

The journalist's purpose was not "good clean fun," though it is certain Mencken enjoyed the hoax. "A Neglected Anniversary" was an act of merry contempt directed at journalists who blithely reported fiction as fact and at readers who were so gullible as to believe blatantly false reports without question. As he later wrote, "One recalls the gaudy days of 1914–1918. How much that was then devoured by the newspaper readers of the world was actually true? Probably not one per cent. Ever since the war ended learned and laborious men have been at work examining and exposing its fictions."

Through his hoax, Mencken demonstrated to himself and to selected friends that the American public would believe any absurdity, as long as it appealed to their imagination or emotions. They would even believe a nonexistent inventor in Cincinnati, Adam Thompson, had hired blacks to haul water "from the Ohio river in buckets" to his bathtub because the city then lacked running water.

Keeping Quiet

Content with his private joke, Mencken remained silent about the hoax until a follow-up article, "Melancholy Reflections," appeared in the *Chicago Tribune* on May 23, 1926, some eight years later. This was Mencken's confession. It was also an appeal for reason to the American public.

His hoax was a joke gone bad. "A Neglected Anniversary" had been printed and reprinted hundreds of times in the intervening years. Mencken had been receiving letters of corroboration from some readers and requests for more details from others. His history of the bathtub had been cited repeatedly by other writers and was starting to find its way into reference works. As Mencken noted in "Melancholy Reflections," his "facts" "began to be used by chiropractors and other such

quacks as evidence of the stupidity of medical men. They began to be cited by medical men as proof of the progress of public hygiene." And, because Fillmore's presidency had been so uneventful, on the date of his birthday calendars often included the only interesting tidbit of information they could find: Fillmore had introduced the bathtub into the White House. (Even the later scholarly disclosure that Andrew Jackson had a bathtub installed there in 1834—years before Mencken claimed it was even invented—did not diminish America's conviction that Fillmore was responsible.)

Mencken speculated on the probable response to his confession, "The Cincinnati boomers, who have made much of the boast that the bathtub industry, now running to $200,000,000 a year, was started in their town, will charge me with spreading lies against them. The chiropractors will damn me for blowing up their ammunition. The medical gents, having swallowed my quackery, will denounce me as a quack for exposing them." He wondered whether disclosing the truth about the bathtub would lead to a renewed cry for his deportation to Russia as a Bolshevik.

One can only speculate on whether the actual response to "Melancholy Reflections" surprised Mencken, who was a practiced cynic by then. Many people believed that his confession, and not the original article, was the hoax. Mencken felt impelled to pen a second follow-up appeal, titled "Hymn to the Truth." Writing in the *Chicago Tribune* of July 25, 1926, he commented, "The Herald printed my article ["Melancholy Reflections"] on page 7 of its editorial section . . . with a two column cartoon labeled satirically, 'The American public will swallow anything.' And then on June 13, three weeks later, in the same editorial section but promoted to page 1, this same Herald reprinted my 10 year old fake—soberly and as a piece of news!"

Mencken's history of the American bathtub had been so graceful and charmingly constructed that people simply wished to believe it. Since then, curious researchers have thoroughly discredited Mencken's bathtub "facts." Biographies of Mencken feature the hoax he had played so well that even he could not debunk it. (All the bathtub pieces and more are compiled in *The Bathtub Hoax and Other Blasts and Bravos*, edited by Robert McHugh.) Yet references to Fillmore's first bathtub still can be found. That piece of fiction has even made it into the Age of the Internet. The Internet Public Library's page on Fillmore, part of its series on presidents, lists under "Points of Interest" the following: "The White House's first library, bathtub and kitchen stove were installed by the Fillmores." (See http://www.ipl.org/ref/POTUS/mfillmore.html.)



H. L. Mencken (1880–1956)

It is easy to laugh and lose sight of the motive behind "A Neglected Anniversary." Mencken wished to demonstrate the dramatic inaccuracies of many newspaper accounts, which are too often swallowed whole by uncritical readers. This phenomenon is especially prevalent in periods of war, when great efforts are made to stir the public's emotions so that it unquestioningly supports the government's policies. When reading accounts of war, it is valuable to consider Mencken's estimate that "probably not one per cent" of it is true. □

THE FREEMAN
Ideas On Liberty

Ludwig von Mises's *Human Action*: A 50th Anniversary Appreciation

by Richard Ebeling

Fifty years ago, on September 14, 1949, Yale University Press released a major new work—*Human Action* by the Austrian economist Ludwig von Mises.[1] The following week, in his regular *Newsweek* column, Henry Hazlitt referred to this book as "a landmark in the progress of economics. . . . *Human Action* is, in short, at once the most uncompromising and the most rigorously reasoned statement of the case for capitalism that has yet appeared. If a single book can turn the ideological tide that has been running in recent years so heavily toward statism, socialism, and totalitarianism, *Human Action* is that book. It should become the leading text of everyone who believes in freedom, individualism, and . . . a free-market economy."[2]

It is useful to recall the state of the world when this book first appeared. The Soviet system of central economic planning had been imposed by Stalin on all of eastern Europe. In Asia, Mao Zedong's communist armies were just completing their conquest of the Chinese mainland. In western Europe, many of the major noncommunist governments were practicing what the German free-market economist Wilhelm Röpke called at the time "national collectivism"—a "combination of repressed inflation, collectivist controls, 'full employment,' exchange control, state monopolies, bilateralism, subsidies, fiscal socialism [and] 'cheap money' policies." In the United States, government policy was guided by what Hazlitt referred to in *Newsweek* a few weeks before his review of *Human Action* as "ultra-Keynesian ideology."[3]

In *Human Action*, Mises opposed every one of these trends and policies, plus many others in contemporary social philosophy, philosophy of science, and economic theory and method. He challenged the foundations, logic, and conclusions of every facet of twentieth-century collectivism. As F. A. Hayek explained, in reviewing the German-language version of the book:

> There appears to be a width of view and an intellectual spaciousness about the whole book which are much more like that of an eighteenth-century philosopher than that of a modern specialist. And yet, or perhaps because of this, one feels throughout much nearer reality, and is constantly recalled from the discussion of technicalities to the consideration of the great problems of our time. . . . It ranges from the most general philosophical problems raised by all scientific study of human action to the major problems of economic policy of our own time.[4]

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And as his American student and friend Murray N. Rothbard pointed out, "*Human Action* is it: Mises's greatest achievement and one of the finest products of the human mind in our century. It is economics whole . . . and provided a way out for the discipline of economics, which had fragmented into uncoordinated and clashing sub-specialties. In addition to providing this comprehensive and integrated economic theory, *Human Action* defended sound, Austrian economics against all its methodological opponents, against historicists, positivists, and neo-classical practitioners of mathematical economics and econometrics. He also updated his critique of socialism and interventionism."[5]

Early Career

Ludwig von Mises was born in Lemberg, Austria-Hungary, on September 29, 1881. Though originally interested in history, he turned to economics shortly after entering the University of Vienna in 1900 and reading *Principles of Economics* by Carl Menger, founder of the Austrian school of economics. While at the University he studied with Eugen von Böhm-Bawerk, the person perhaps most responsible for establishing international respect for the Austrian school. In 1906 Mises was awarded a doctoral degree in jurisprudence (at that time economics was studied as part of the law faculty at the university).

Beginning in 1909 Mises worked at the Vienna Chamber for Commerce, Trade, and Industry as an economic analyst within its department of finance. In this capacity he evaluated and made recommendations about various legislative proposals in the areas of banking, insurance, monetary and foreign-exchange policy, and public finance. In the years between the two world wars, he was a senior secretary with the Chamber, enabling him to argue with some authority on the economic policy issues confronting the Austrian government.

The consensus of economists and others who knew Mises during this time is that he was extremely influential in moderating collectivist and inflationary policies in Austria. He was instrumental in preventing the full nationalization of the Austrian economy by a socialist government immediately after World War I. He helped to redirect public and political opinion to bring the Great Austrian Inflation to an end in 1923. And in the aftermath of this monetary disaster, he played an important role in writing the statutes and bylaws of the reconstructed National Bank of Austria, under the auspices of the League of Nations in 1924.

In 1913, Mises had been given the right to teach at the University of Vienna as a *Privatdozent* (an unsalaried lecturer); in 1918 he was promoted to the title of "Professor Extraordinary." Almost every semester until 1934, he taught a course that influenced a new generation of young Viennese and foreign scholars. He also co-founded and served as vice president of the Austrian Economic Society.

Influential Seminar

In 1920 Mises began a private seminar that normally met twice a month from October to June at his Chamber office. It brought together a group of Viennese scholars in economics, political science, philosophy, sociology, and law, many of whom became world-renowned scholars in their respective fields. The participants, almost to a man, recalled the seminar as one of the most rigorous and rewarding experiences of their lives.

One other important activity undertaken by Mises during this period was his founding of the Austrian Institute for Business Cycle Research in 1926. With 27-year-old F. A. Hayek as the first director, the institute was soon internationally recognized as a leading center for economic forecasting and policy analysis in Central Europe.

In 1934 Mises was offered and accepted a position as professor of international economic relations at the Graduate Institute of International Studies in Geneva, Switzerland. Shortly after arriving in Geneva he set about a project he long had in mind, the writing of a comprehensive treatise on economics. Most of his time during the next six years, outside of his light teaching responsibilities, was devoted to this plan. In May 1940, as Europe was falling under the dark cloud of Nazi occupation, this monumental work, *Nation-*

alöknomie, was published in Switzerland. It served as the basis for his later English-language treatise, *Human Action*.

In the summer of 1940 Mises resigned from his position at the Graduate Institute and left for the United States.[6] His first years in America were not easy. He experienced great difficulty in finding a permanent teaching position, partly because of his age (he was 58 when he arrived in America) and partly because of the intellectual climate prevailing in America. His was a voice for an older classical liberalism and free-market capitalism that was out of step with the popular trends of socialism, interventionism, and Keynesian economics that were embraced by a large majority of American academics and policymakers.

Not until 1945 did he receive an academic appointment as visiting professor in the Graduate School of Business at New York University, a position and status he retained until his retirement in 1969 at the age of 87. During this almost quarter-century of teaching in the United States, Mises trained a new generation of economists in the tradition of the Austrian school.

International Reputation

In Europe, Mises had already established an international reputation as one of the most original and controversial economists of his time. Before World War I, in 1912, he had published *The Theory of Money and Credit*, in which he successfully applied the concept of marginal utility to explain the demand for money, demonstrated the process by which the interaction of the demand and supply of money established the purchasing power of the monetary unit, and developed a theory of the business cycle which showed that government manipulations of the market rate of interest was the primary cause of economy-wide fluctuations in production, investment, and employment.[7]

In the early 1920s Mises also challenged the most fundamental assumptions of a socialist planned economy. In his article on "Economic Calculation in the Socialist Commonwealth" (1920) and in his treatise *Socialism: An Economic and Sociological Analysis* (1922), he showed that socialism's abolition of private property, the market economy, and money prices for both consumer goods and the factors of production meant the end of rational economic calculation. Rather than ushering in a utopian epoch of material plenty, socialist central planning would create economic waste, inefficiency, and stagnant or falling standards of living.[8]

In later books, *Liberalism* (1927) and *Critique of Interventionism* (1929), Mises argued that only free-market capitalism could create a social order of individual freedom, material prosperity, and domestic and international peace. A regulated and "hampered" market economy could only produce an economy of distortions, imbalances, political corruption, and abuse.[9]

And in 1933, Mises published a series of essays under the title *Epistemological Problems of Economics*, in which he argued that economics was a distinct science derived from the insight that all social processes derive from the choices and actions of the individual participants in the social and market order. Attempts to reduce conscious and intentional human conduct to the physicalist methods of the natural sciences would not merely distort any real understanding of human decision-making and activity, it would also create a serious false impression that social and market processes could be manipulated and controlled much like inanimate matter in a laboratory experiment.[10]

Integration of Themes

As both Hayek and Rothbard clearly understood, however, it was in *Human Action* that all these themes were integrated into a systematic conception of man, the social order, the market economy, and its alternatives. Mises explained that our knowledge of the logic of human action is fundamentally different from the way scientists acquire knowledge about the physical world. The inanimate matter of the external world can be measured, quantified, and organized on the basis of various hypotheses concerning the nature of and relationships between the physical entities of

the universe. But we have no way of determining the "real" or "true" causal reasons why the elements of nature have the properties and relational characteristics they seem to possess. We can only observe, hypothesize, quantitatively test, and draw tentative conclusions that may be falsified tomorrow.

Human sciences like economics, however, have a radically different starting point. Here we have the ability to know the nature and properties of the causal factor that generates the complex relations of the social and economic processes. All the social processes have their origin in and can be reduced to the actions and reactions of individual human beings. Being human, the social scientist can draw on a source of knowledge unavailable to the natural scientist: introspection. That is, the social scientist can look within himself and trace out the logical and formal characteristics of his own mental processes.

As Mises expressed it, "action" is reason applied to purpose. By understanding the logic of our own reasoning processes, the social scientist can comprehend the essentials of human action: that man, as a conscious being, invariably finds some aspects of his human condition unsatisfactory; he imagines ends or goals that he would like to attain in place of his present or expected circumstances; and he perceives methods and means to try to achieve them. But he soon discovers that some of the means with which he could attain ends are limited in quantity and quality relative to their potential uses. Hence, man is confronted with the necessity to choose among desired ends, and has to set some goals aside either for a day or forever, so those means can be used for the pursuit of other ends to which he has assigned greater importance. Few human decisions, however, are categorical—all or nothing. Most are incremental, giving up a little of one attainable end so as to possibly attain a little bit more of some other desired end; thus, most choices are made at the "margin."

From these elementary and self-evidently true foundations, all the complex theorems of economics can be traced out. But the resulting "laws" of economics are not open to quantitative verification or prediction. The laws of economics, in other words, are logical relationships, and not empirical ones. Why? Because man has volition, free will, and the ability to change his mind and imagine new possibilities that make his actions and responses in the future different in their concrete form from what they were yesterday or are today. Hence, the search for a quantitative economics for deterministic prediction of what men and markets will do today, tomorrow, or a year from now is the pursuit of the unattainable.

Division of Labor

For Mises, one of the greatest accomplishments of mankind was the discovery of the higher productivity arising from a division of labor. The classical economists' analysis of comparative advantage, under which specialization in production increases the quantity, quality, and variety of goods available, was more than merely a sophisticated demonstration of the mutual gains from trade. In Mises's view, the law of comparative advantage was in fact "the law of human association." The mutual benefits resulting from specialization, he argued, were the origin of society and the starting point for the development of civilization.

The rationality of the market economy arises from its ability to allocate the scarce means of production in society for the most efficient satisfaction of consumer wants in a complex division of labor; that is, the market sees to it that the means at people's disposal are applied to their most highly valued uses. This requires some method to discover the alternative uses for which those scarce means can be used and their relative value in those competing applications.

Competitively determined market prices, in an institutional setting of private ownership of the means of production, provides the means for solving this problem, Mises said. On the market for consumers' goods, people express their valuations for commodities in the form of the prices they are willing to pay for various quantities and qualities of finished goods. On the market for producers' goods, entrepreneurs express their appraisal of the relative future profitability of factors of production in

the manufacture of various goods through the prices they are willing to pay for those factors.

Those prices, expressed through the common denominator of money, make economic calculation possible. The relative costs and expected revenues from alternative productive activities can be compared with ease and efficiency. The competitive processes of the market tend to assure that none of the scarce means of production are applied to any purpose for which there is a more highly valued use as expressed in a rival entrepreneur's bid for those factors. Through competition among entrepreneurs, the means derive their value from their ability to produce goods desired by consumers. Thus the means available in society are put in the service of people's ends. And the relative values assigned to those means in their alternative uses reflects the relative valuations of the consumers who desire the products that can be manufactured with them.

Mises concisely summarized the role and nature of competition and the competitive process in the market order:

> Competitors aim at excellence and preeminence in accomplishments within a system of mutual cooperation. The function of competition is to assign to every member of a social system that position in which he can best serve the whole of society and all its members. It is a method for selecting the most able man for each performance. . . .
>
> The pricing process is a social process. It is consummated by an interaction of all members of the society. All collaborate and cooperate, each in the particular role he has chosen for himself in the framework of the division of labor. Competing in cooperation and cooperating in competition all people are instrumental in bringing about the result, viz., the price structure of the market, the allocation of the factors of production to the various lines of want-satisfaction, and the determination of the share of each individual.[11]

Mises's crucial argument against both socialism and interventionism was that they



Ludwig von Mises (1881–1973)

prevented the effective operation of this market process, and thus reduced the rationality of the social system. The triumph of socialism—with its nationalization of the means of production under government control and central planning—meant the irrationalization of the economic order. Without market-based prices to supply information about the actual opportunity costs of using those resources as estimated by the competing market actors themselves, decision-making by socialist central planners would be arbitrary and "irrational." The socialist economy, therefore, was fundamentally anti-economic.

Deflecting the Market

Interventionism does not abolish the market economy. Instead, it introduces various forms of controls and regulations that necessarily deflect production from the paths that would have been followed if entrepreneurs had been left free to more fully follow their own judgments concerning the use of the factors of production in the search for profits through the best satisfaction of consumer demand. Price

controls, in particular, Mises argued, distort the competitively determined relationships between selling prices and cost-prices, resulting in severe misallocation of resources and misdirected production activities.

Mises also restated and refined the Austrian theory of money and the business cycle in *Human Action.* He developed a dynamic sequence analysis enabling him to explain the process by which changes in the quantity of money brought about redistribution of wealth and relative price changes that modified the allocation of resources; his analysis also explained how monetary changes introduced through the banking system could distort interest rates and generate business cycles. A central conclusion was that business cycles were not a phenomenon inherent in the market economy. Rather, they were caused by government mismanagement of the monetary and banking system. Only a separation of money and the banking system from all government control and influence could reduce, if not eliminate, the recurring patterns of inflation and depression.[12]

In 1949 Mises's arguments were ignored or scorned as the reactionary misconceptions of a man out of step with the more enlightened ideas and economic policies of the postwar era. But now, in 1999, it is evident that it was Mises who understood far better than the vast majority of his contemporary economists and policy advocates the fundamental flaws in socialism, interventionism, and the welfare state.

Since Mises's death on October 10, 1973, at the age of 92, the world has seen the collapse of socialist central planning and the economic and ideological bankruptcy of the interventionist welfare state. The superiority of the market economy, the competitive process, and private entrepreneurial creativity is widely admitted if, alas, still far from being allowed to freely function. No small credit is due to Mises, the clearest, most uncompromising voice for economic reason and respect for the freedom and dignity of the individual in our century.

It is *Human Action* that for half a century has served as the medium through which tens of thousands have learned these lessons of a society of peace, freedom, and prosperity. Like Adam Smith's *Wealth of Nations*, it stands as one of the great works not only of economics but also of human and social understanding. And like Smith's book, it will remain a classic, as read and as influential in the 21st century as in our own time, because it speaks to and about the most fundamental and universal truths of man and the human condition. □

1.The first edition of *Human Action: A Treatise on Economics* has recently been reprinted in a handsome edition by the Ludwig von Mises Institute of Auburn, Alabama. The last edition revised by Mises in 1966 is available from the Foundation for Economic Education, prepared by Bettina Bien Greaves.

2. Henry Hazlitt, "The Case for Capitalism," *Newsweek*, September 19, 1949.

3. Henry Hazlitt, "Wrong Diagnosis, Wrong Remedy," *Newsweek*, August 15, 1949.

4. F. A. Hayek, review of *Nationalökonomie: Theorie des Handelns und des Wirtschaftens* in *The Economic Journal*, April 1941, pp. 125, 127.

5. Murray N. Rothbard, *Ludwig von Mises: Scholar, Creator, Hero* (Auburn, Ala.: Ludwig von Mises Institute, 1988), p. 64.

6. See Ludwig von Mises, *Notes and Recollections* (South Holland, Ill.: Libertarian Press, 1978 [1940]) for his own memories of his life, work, and contributions before he left Europe in 1940.

7. Ludwig von Mises, *The Theory of Money and Credit* (Indianapolis: Liberty Classics, 1981). On Mises's contributions to monetary theory and policy, see my "Ludwig von Mises and the Gold Standard," in Llewellyn H. Rockwell, ed., *The Gold Standard: An Austrian Perspective* (Lexington, Mass.: Lexington Books, 1983), pp. 35–59.

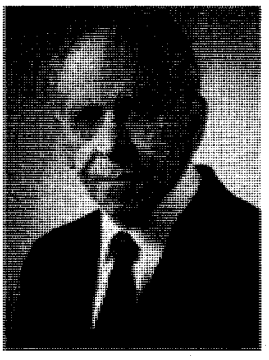
8. Ludwig von Mises, "Economic Calculation in the Socialist Commonwealth," reprinted in Israel M. Kirzner, ed., *Classics in Austrian Economics*, vol. 3 (London: William Pickering, 1994), pp. 3–30; and *Socialism: An Economic and Sociological Analysis* (Indianapolis: Liberty Classics, 1981). On Mises's contribution to the theory of socialism and the planned economy, see my "Economic Calculation Under Socialism: Ludwig von Mises and His Predecessors," in Jeffrey M. Herbener, ed., *The Meaning of Ludwig von Mises* (Norwell, Mass.: Kluwer Academic Press, 1993), pp. 56–101.

9. Ludwig von Mises, *Liberalism: The Classical Tradition* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1996 [1985]); and *Critique of Interventionism* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1996); also, *Interventionism: An Economic Analysis* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1998 [1940]).

10. Ludwig von Mises, *Epistemological Problems of Economics* (New York: New York University Press, 1981). On Mises's conception of human action and his contributions to the theories of the market economy, socialism, and interventionism, see my "A Rational Economist in an Irrational Age: Ludwig von Mises," in Richard M. Ebeling, ed., *The Age of Economists: From Adam Smith to Milton Friedman*, Champions of Freedom Series, vol. 26 (Hillsdale, Mich.: Hillsdale College Press, 1999), pp. 69–120.

11. Ludwig von Mises, *Human Action: A Treatise on Economics* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1996), pp. 117, 338.

12. For an exposition of the Austrian theory of money and the business cycle and its explanation of the causes and duration of the Great Depression of the 1930s, see my "Monetary Central Planning and the State," parts 1–12, *Freedom Daily*, January–December 1997.



The Hazards of Truth-Telling

Language is a priceless gift we inherit from people who came before us and bequeath to those who come after us. Language is a human product, but it is not made by any particular person or group. Because the meaning of what is said depends both on the speaker and on the listener, language is a special kind of patrimony. We receive it in trust, as it were. We use it. And we pass it on when we die. Do we leave language better or worse than we have received it? This choice is part of our destiny as language-using beings. Our contact with language—like our contact with persons—is rarely neutral: either we use language well and improve it, or we use it badly and disimprove it. What is our criterion, you may ask, for making this judgment? Our criterion is our sense of what is right and what is wrong.

I believe that plain speaking and truth-telling are good and improve language, and that equivocating and prevaricating are bad and debauch language. Many people say they agree with this judgment, but they do not mean it, and for good reasons. It is dangerous to speak plainly and to tell the truth, not just in far-off totalitarian societies but in the United States today.

This brings me to remark on one of the great paradoxes of education in our society. We ceaselessly exhort young men and women to think for themselves. However, once people think for themselves, their thoughts—and hence what they say and what they write, and how they speak and how they write—are likely to differ from what passes as politically correct. "To write in plain, vigorous language," wrote George Orwell, "one has to think fearlessly, and if one thinks fearlessly one cannot be politically orthodox." This paradox seems to be an intrinsic part of our ambivalence about daring to face the truth. The lives of many persons we now revere illustrate the sad or even tragic consequences of truth-telling.

For example, Socrates liked to go for walks with his pupils who were eager to hear his reflections about the perennial moral dilemmas of life. The Athenian senate considered his behavior subversive—a corruption of youth, a charge not unlike that now leveled against tobacco companies—and sentenced Socrates to death. He chose to kill himself, instead, an option then accepted as honorable and legal, now rejected as mentally disordered and illegal.

John Huss (c. 1370–1415) was a Bohemian priest. Influenced by the writings of John Wycliffe, he expressed doubts about the dogma of transubstantiation and opposed the sale of indulgences. Charged with heresy, he was burned at the stake.

Galileo Galilei (1564–1642) was not only a brilliant astronomer, but also a gifted popularizer, in Italian, of the Copernican theory of the solar system. For this, he was denounced to the Inquisition. Led by Cardinal Robert Bellarmine (1542–1621), the church's chief theologian, the Vatican declared Copernican-

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ism "false and erroneous" and placed Copernicus's writings on the Index. Bellarmine—by all accounts a decent man—asked Galileo to neither "hold nor defend" the heliocentric theory, a request Galileo honored. After Bellarmine died, he was sainted.

Punished for Doing Good

The life of the truth-teller punished for his good deeds whose story has touched me the most deeply is that of the Hungarian physician Ignaz Philipp Semmelweis (1818–1865). Semmelweis's crime was twofold. He discovered the cause of puerperal fever, which, in the early decades of the nineteenth century, killed poor women who delivered their babies in teaching hospitals rather than in their homes by the tens of thousands. That was bad enough. What made it worse was that he also discovered—before it was discovered that bacteria cause diseases—that, by washing their hands in a disinfecting solution, physicians could prevent the disease. Unable to reconcile himself to the rejection of his simple remedy and the continuing wholesale medical killing of parturient women, Semmelweis's behavior became increasingly "abnormal." He was incarcerated in an insane asylum and soon thereafter died. The cause of his death remains a matter of controversy among medical historians. Today, the medical school in Budapest bears his name.

A less familiar but no less instructive example of the hazards of truth-telling is the experience of Oliver Wendell Holmes (1809–1894), father of the famous Supreme Court justice of the same name (1841–1935). Trained as a physician, Holmes was professor of anatomy and physiology at Harvard from 1847 until his retirement in 1882. In 1843, he produced his most enduring medical work, an essay titled *The Contagiousness of Puerperal Fever,* in which he maintained that the disease was transmitted from patient to patient by the obstetrician. This proposition, like Semmelweis's, met vigorous opposition from leading American obstetricians. However, unlike Semmelweis, Holmes was unruffled by entrenched professional ignorance and added to his achievements by becoming a celebrated author.

Three of France's most famous men of letters—Voltaire (1694–1778), Victor Hugo (1802–1885), and Émile Zola (1840–1902)—had to leave their homeland to write freely. Zola's encounter with the official deniers of truth is the most dramatic. At an early stage in the proceedings, he decided that Captain Alfred Dreyfus was innocent. In 1898, he published his famous open letter—which began with the words "J'accuse"—denouncing the French General Staff of having framed Dreyfus. The publication of this piece led to his being prosecuted for libel and convicted of the charge. He fled to England.

Twain's Advice

What, then, are young men and young women to do when they heed the advice to think for themselves and arrive at thoughts that differ from what passes as politically correct? One of their choices is to follow Mark Twain's advice. He wrote: "It is by the goodness of God that in our country we have those three unspeakably precious things: freedom of speech, freedom of conscience, and the prudence never to practice either."

Had Mark Twain heeded his own advice, he would not have been the great writer he was. He spoke freely, albeit some of his most heretical thoughts were published only posthumously. And he followed his conscience, often choosing to express himself cautiously and humorously, rather than recklessly or polemically.

"The truth," said Jesus, "shall set you free." Jesus did not say it will make you popular, or rich, or happy. He said it will set you free—and that it will do. And while freedom—true, inner freedom, what people used to call serenity—may not win you fame or fortune, it will enable you to look yourself in the mirror and to sleep at night.

In short, be courageous, but be careful. □

THE FREEMAN
Ideas On Liberty

Economic Calculation Revisited

by Manuel Ayau

Now that outright socialism has failed, the quest for a third way has gained prominence. Political leaders insist that a free society is inherently unjust and the privileged prosper at the expense of the unfortunate many. Thus the state must correct the failures of the market.

The critics of the modern version of Western "capitalist" (properly called "mercantilist") societies are right on the issue of privilege, but they are wrong when they identify it with the free society, for in a truly free society privileges would be absent. It is precisely the injustice of state-granted privileges, such as corporate welfare, that gives the "capitalist" system its bad name. That deserves to be cleared up. But it is just as important to understand why the seemingly plausible intervention of governments in the quest for a third way is not the solution for the wrongs perceived. The case against that intervention is the same as the one that was brought to bear against socialism at the peak of its popularity.

In the 1920s a debate on "the problem of economic calculation" took place in Europe. The essence of the controversy was the thesis that without private property in the means of production, and its concomitant exercise of free exchange, no meaningful price structure could evolve to permit the economic allocation of resources. "Economic allocation" means that the products are of more value than the effort and the resources spent in production; it also means that these products are the best of the possible alternatives. Thus human cooperation and use of resources would enrich society. If the allocation was not "economic," for lack of a way (relative prices) to determine what continual adjustments must be made in the use of resources as conditions changed, society would impoverish itself and eventually collapse.

Socialist countries could indeed manage to survive by using the price structure of capitalist countries and copying (and sometimes improving) the scientific inventions and methods of production of the West. With a little bit of economic assistance, they could postpone the day of reckoning. Indeed, the United States provided aid to the Soviets in the 1920s, '30s, '40s, and so on until the '80s, in addition to large amounts of resources to prop up their satellites and semi-socialist countries in Africa and Latin America.

Debunkers Shunned

Since the argument regarding economic calculation was a logical and systematically articulated prediction of the failure of the socialist experiment in vogue at the time, its proponents became unpopular in academic circles. Initially, the problem of socialism was expounded by Austrian economist Ludwig von Mises. He sparked a lively debate, which F. A. Hayek (who won a Nobel prize in 1974) later joined to refute the outstanding socialist

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theoreticians Oskar Lange and Fred Taylor. Independently, T. J. B. Hoff in Norway argued the same point. Others, including the distinguished mathematician Leonid Kantorovich, also addressed the problem, to no avail. The debate was interrupted by World War II and many consider it now only a theoretical relic.

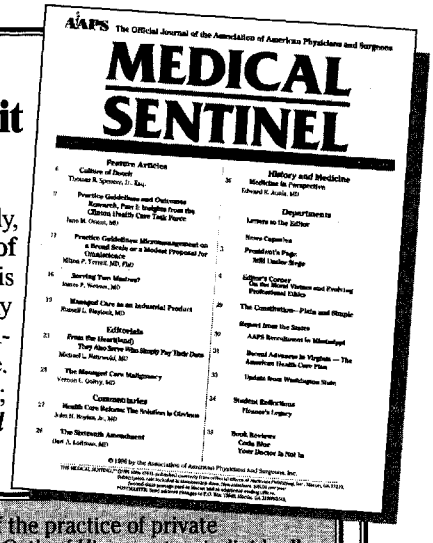
That the "the problem of economic calculation" critique is not exclusive to socialism is a point that has been largely missed. It is perhaps the most rigorous analysis of why an economy becomes inefficient and ultimately cannot function to the degree society departs from the legal system of private property and contracts; that is, to the degree government attempts to plan the economy. The discussion is pertinent not only to full socialism, but also to the mixed economies of today.

In the meantime it is sad to see the media full of news regarding economic crises all over the world. The economic woes of Russia, Asia, and Latin America are ever present. Most amazing was that almost everyone was surprised by the sudden demise of the Soviet socialist empire a decade ago. Immediately, the Eastern bloc countries swarmed with university professors and economic advisers from the World Bank, IMF, and agencies, all competing for opportunities to dispense wisdom, along with bundles of money from the U.S. taxpayers. Unfortunately only a handful of those advisers sought market solutions based on the sanctity of property and contracts, and the rule of law. True, most of them suggested privatization but with the same stifling economic regulations that pervade the "capitalist" countries, supposedly to correct the market's failures.

The analysis of the calculation problem is still pertinent, for it helps us to understand why crises recur all over the world, why the transition from socialism to capitalism without the rule of law has not been and cannot be successful, why Japan fails in its never-ending attempts to manage its economy, and why government economic intervention (planning) is bound to produce unintended and undesirable consequences. □

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"Liberty in Perfection": Freedom in Native American Thought

by Amy H. Sturgis

Preacher Samuel Peters's encounter with a free society was a memorable one. In 1781, he wrote in awe: "The conscious independence of each individual warms his thoughts and guides his actions. . . . Here is liberty in perfection!"[1]

Though he wrote in the shadow of the War for Independence, Peters was not praising the American colonists-turned-rebels. Instead, he had found life in the American Indian villages of New England to be the true experiment in liberty. He even went so far as to credit Amerindian rights theory as the catalyst for the colonial break with England, saying that the colonists "discovered that they themselves were men, and entitled to the rights of that race of beings; and they proceeded upon the same maxims which they found among the Indians."[2]

Samuel Peters's words exhort us to remember that we have inherited the language of liberty in many tongues. From the Greek Sophists and Roman orators to the Islamic economists and Patristic theorists, ancient and medieval thinkers led the inquiry into the nature of freedom. In the modern era much of what we recognize as classical-liberal thought flowed through nationalistic European streams: the realistic English tradition of law, the rationalistic French tradition of humanism, and the organic German tradition of individualism. Few scholars and students of liberty today, however, turn their eyes to North America to investigate the Amerindian contribution to the philosophy of freedom. Far from primitive or forgotten, the New World's indigenous legacy of individual liberty, limited government, and legitimate law offer insights as fresh and relevant as the new millennium.

Many Currents

Of course native American thought cannot be adequately simplified into one monolithic river any more than European or Anglo thought can be. Specific currents are more easily identified and discussed, however, thanks to the persistence of languages, written and oral records, third-party documentation, as well as the survival of political institutions today. Among these currents are the *Haudenosaunee*, or Iroquois Confederacy, of the northeast, and the *Tsalagi*, or Cherokee Nation, of the southeast. Together, they offer valuable examples of the first American republics.

In 1727 political theorist and scholar Cadwallader Colden wrote of the Iroquois Confederacy: "The Five Nations have such absolute Notions of Liberty that they allow no Kind of Superiority of one over another, and banish all Servitude from their Territories."[3] The five nations of what is today the Finger Lakes region of upstate New York—the

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Onondagas, the Senecas, the Mohawks, the Cayugas, and the Oneidas—had ended their intertribal warfare and formed a federal union in approximately 1200. The constitution uniting the nations was called *Kaianrekowa*, the Great Law of Peace. Recorded and preserved in wampum, this document codified laws for each nation, rules for the confederacy, and consistent rights protection for all citizens. National membership remained open, and other peoples joined the confederacy. The northeastern body eventually became known as the Six Nations after the formal addition of the Tuscaroras around 1714.

Of the Cherokee Nation in which he practiced, mid-eighteenth-century colonial surgeon George Milliken Johnson wrote: "Subjugation is what they are unacquainted with . . . there being no such thing as coercive Power among them."[4] In 1757, Raymond Demere agreed, saying there was no "Subjugation among them, they can't be compelled to do any Thing nor oblige them to embrace any Party except [as] they please."[5] The Cherokee Nation, located in the Appalachian region of what is today Virginia, North and South Carolina, Georgia, and East Tennessee, had like the Iroquois formed a republic centuries before Columbus. By the time of European contact, a complex clan-based common law provided national, regional, and local governance for four distinct regions and over 60 discrete towns. In 1827, the Cherokee Nation became the first native polity to write and ratify a national constitution in the European sense.

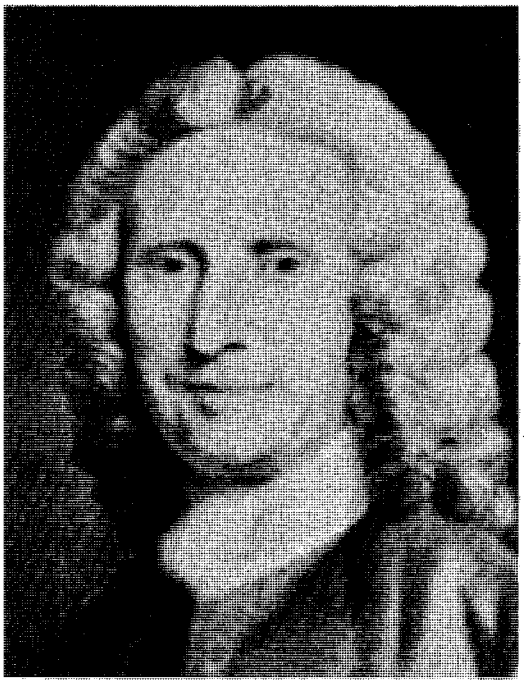
Scholars of the Iroquois and Cherokees have discovered what *Haudenosaunee* and *Tsalagi* descendants have reiterated for generations: these nations developed a consistent and sophisticated understanding of liberty in pre-contact North America.[6] We can learn much from Amerindian notions of the individual, the group, and the law.

Individualist Culture

Native American culture and politics revolved around the individual. The Cherokees used the metaphor of seven directions to explain this emphasis: North, South, East, West, Up, Down, and Where You Are. The position of Where You Are put the individual at the center of her universe, with the other six directions dependent on her. While this symbolic position honored the individual as the star in her own universe, it also implied that she possessed the power and the opportunity to keep that universe in balance. The Cherokees, like the Iroquois and others, viewed this balancing act as the product of lifelong self-discovery. To this end, the cultures offered a tolerant environment for artistic, sexual, philosophical, and spiritual experimentation. To reflect this they also allowed children to change their names as they grew and explored themselves. An act of heroism, a discovered talent, a cultivated physical or spiritual trait, even a famous relative could be cause for name-changing. The community thereby encouraged the individual to define and redefine himself freely throughout the course of his life.

This concern for individual liberty translated into politics. The Great Law of Peace included a section akin to the U.S. Bill of Rights, protecting the freedom of worship, speech, and assembly. The Cherokees limited town size so that all citizens could have the opportunity to speak in each council session if they so desired. Both republics were gender-blind, allowing women and men the same opportunities to participate and, if elected, to lead. (Indeed, the Cherokee language had no gendered pronouns. "He speaks in council" and "she speaks in council" both translated as "a Cherokee speaks in council.") This inclusiveness led to political equality under the constitutions. Divorce law and property law, for example, unlike its counterparts across the ocean, recognized no difference between men and women.

The value the Amerindians placed on the individual meant that the power of the group, be that the town, region, nation, or confederacy, had to remain limited. Participation was one check on the power of government. Control could not rest with one party or faction alone because any leader had to build a coalition to survive. The Great Law of Peace required the consent of leaders from all five (later, six) nations for any law or action, and



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Cadwallader Colden
(1688–1776)

Cherokee tradition required the consent of representatives from all seven clans, even at the town level. Beyond the need for coalition, the Iroquois maintained a structure of checks and balances not unlike the U.S. tripartite system. The Cherokees' right of dissent and withdrawal, a version of conscientious objection, further protected the rights of those in the minority.

Legitimate legal decisions, then, had to pass through coalitions from the local democracies to the greater republics via systems of checks and balances. Without taxes or full-time police forces or similar instruments of coercion, the governments of the Iroquois League and the Cherokee Nation did little save physically defend against external attack and internally protect the negative rights of the citizens. And what of illegitimate law? The Cherokees' system of individual and corporate withdrawal afforded the equivalent of "no confidence" votes. The Iroquois League had processes for the impeachment and removal of leaders who failed to uphold the constitution.

A combination of catastrophic depopulation (from massive epidemics following the introduction of smallpox and other diseases from Europe), imperial and colonial warfare, violent cultural miscommunications, and blatant bigotry prevented many Amerindian nations from enjoying economic and political development in tandem with European colonists and, later, U.S. citizens. Yet, despite these obstacles, some native Americans became capitalistic and constitutional powerhouses in their own right in the age after Columbus. The Cherokees, for example, developed a written language, a bilingual press, a ratified constitution, and the infrastructure of a modern nation-state. Thomas Jefferson was a particular admirer of such Cherokee leaders as Ostenaco and Doublehead. As President he praised the Cherokee Nation, acknowledging that its progress had "been like grain sown in good ground, producing abundantly," and extended his personal invitation to its members to join the United States as full citizens.[7]

It was, in fact, the Cherokees' very prosperity and success that later made them the target of the state of Georgia. By stripping the Cherokee citizens of their property and forcibly removing them to Indian Territory via the infamous Trail of Tears of 1838–39, U.S. citizens transferred Cherokee plantations, businesses, and other wealth to their own pockets. Even the U.S. Supreme Court's ruling in the Cherokees' favor was not enough to protect the Amerindians' rights. President Andrew Jackson encouraged the illegal removal and the theft of property that it facilitated.

Those Cherokees who survived relocation ratified another constitution and reassembled their economy, only to have their property redistributed yet again by Washington. In the years since then, the United States, primarily through the Bureau of Indian Affairs, has repeatedly pursued policies that punish American Indian moves toward political self-determination and economic growth. But old ways die hard. Today Amerindian entrepreneurship and political theory are once again reasserting themselves through such disparate avenues as oral history and cyberspace.

Protecting Individuality

In the modern era, much of the mainstream has fallen prey to the stereotype of the native American as the proto-socialist communitarian whose sense of self was irretrievably anchored in his polity. It is true that the Amerindians valued civic participation, but not for the same reasons as the orators of Western antiquity. The Iroquois and the Cherokees did not value the process of a democratic republic because it consumed their identity; they valued it because it protected their individuality. The political debate from the Cherokee town council to the Iroquois Grand Council limited by law what the group could do to the person. Participation ensured liberty. It was for this reason that Colden explained: "When Life and Liberty came in competition, indeed, I think our Indians have outdone the Romans."[8]

Much of what has been learned of late about Amerindian political theory has been overshadowed by the multicultural debates surrounding history and education. Opponents of multicultural approaches fear that exploration into systems such as the Great Law of Peace will draw credit for the U.S. Constitution away from European antecedents. While few if any scholars claim sole Amerindian influence for the Constitution, Benjamin Franklin's writings on the Albany Plan of Union, Thomas Jefferson's *Notes on the State of Virginia*, and other framers' works make it clear that native American nations did indeed offer some inspiration.[9]

For the student of freedom, however, the idea of liberty in Amerindian thought should remain a worthy inquiry for its own sake. Some of what we find appears familiar to us today: tripartite governments, bills of rights, checks and balances. Other aspects of Amerindian thought—the truly gender-blind polis, the commitment to participation, the encouragement of self-cultivation and self-exploration—should challenge us as we approach the new millennium. The Iroquois and Cherokees of the past and today offer us alternate visions of freedom, other voices to add to our language of liberty. In the words of nineteenth-century theorist Matilda Joslyn Gage, it is fitting that we remember native American thought, for it brought the New World "its first conception of inherent rights, natural equality of condition, and the establishment of a civilized government upon this basis."[10] □

1. Kenneth W. Cameron, ed., *The Works of Samuel Peters of Hebron, Connecticut* (Hartford: Transcendental Books, 1967), pp. 37–38.

2. Ibid.

3. Cadwallader Colden, *History of the Five Indian Nations Depending on the Province of New York in America* (Ithaca: Cornell University Press, 1968 [1727 and 1747]), pp. xvii–xix. Colden would later correspond about the Iroquois with Benjamin Franklin, who pondered the native "confederate republics" while planning his own intercolonial confederation. Donald A Grinde, Jr., and Bruce E. Johansen, *Exemplar of Liberty: Native America and the Evolution of Democracy*, Native American Politics Series No. 3 (Los Angeles: American Indian Studies Center, University of California, 1991), pp. 93–110.

4. Cited in Fred Gearing, *Priests and Warriors: Social Structures for Cherokee Politics in the Eighteenth Century* (memoir 93, AAA, vol. 64, no. 5, part 2, October 1962).

5. Letter from Raymond Demere to W. H. Lyttekton, July 30, 1757. "Indian Books," manuscript collection, vol. 3, William L. McDowell, ed. 1970, Columbia, South Carolina State Archives, pp. 391–92.

6. Some pathbreaking works include Grinde and Johansen, *Exemplar of Liberty*; Bruce E. Johansen, *Forgotten Founders: How the American Indian Helped Shape Democracy* (Cambridge, Mass.: The Harvard Common Press, 1982); Rennard Strickland, *Fire and the Spirits: Cherokee Law from Clan to Court* (Norman, Okla.: University of Oklahoma Press, 1975); John Phillip Reid, *A Law of Blood: The Primitive Law of the Cherokee Nation* (New York: New York University Press, 1971).

7. "An Address 'To The Chiefs of the Cherokee Nation,'" January 10, 1806, in Thomas Jefferson, *The Complete Jefferson*, Saul K. Padover, ed. (New York: Duell, Sloan, and Pearce, Inc., 1943), p. 478.

8. Colden, p. vi.

9. For a discussion of this debate in light of the evidence and charges of "political correctness," see Bruce E. Johansen, *Debating Democracy: Native American Legacy of Freedom* (Santa Fe, N.M.: Clear Light Publishers, 1998).

10. Matilda Joslyn Gage, *Woman, Church, and State* (Watertown, N.Y.: Persephone Press, 1980 [1893]), p. 10, from manuscript.

THE FREEMAN
Ideas On Liberty

Political Accounting

by James Bovard

Why does the federal government, according to its own auditors, squander tens of billions of tax dollars year after year? Attempts to understand the actions of politicians and bureaucrats on the basis of private-sector decision-making are doomed to failure. Efforts to "fix" government by ending specific boondoggles are quixotic crusades. Government will continue to be profoundly wasteful because that is how politicians maximize their power—a subject that interests politicians far more than do General Accounting Office reports.

"Political language . . . is designed to make lies sound truthful and murder respectable, and to give an appearance of solidity to pure wind," observed George Orwell.[1] Ruth Grant wrote that "hypocrisy and politics are inextricably connected on account of the peculiar character of political relationships."[2]

Since government is coercion, politics is largely the exercise of deception regarding the intended use of coercion.

The benevolence of government rarely transcends the venality of politics. Paternalism seeks to generate mass happiness by forcibly sacrificing as many people and groups as necessary to the Greater Good. And who defines the Greater Good? The same people who benefit from maximizing the sacrifices.

The amount of power a politician can seize over other people is inversely related to the politician's honesty. If the politician openly tells people how much more coercive power he seeks and how he intends to use it, there will likely be strong opposition to the expansion of government. Politicians rarely wish to admit that they are pursuing a larger "market share" in the life of the average citizen. Because politicians and government officials often seek more power than they publicly admit, many, if not most, of their analyses of government policies are skewed.

The Social Security Model

If a politician camouflages his plans, people may fail to resist the increased power until it is too late. This is the thumbnail history of Social Security, a program that illustrates the natural combination of paternalism and political fraud. As the Brookings Institution's Martha Derthick observed, "In the mythic construction begun in 1935 and elaborated thereafter on the basis of the payroll tax, Social Security was a vast enterprise of self-help in which government participation was almost incidental."[3] The Social Security Administration for decades told people that their payroll taxes were being held for each citizen in individual accounts; in reality, as soon as the money came in, politicians found ways to spend it.[4]

Social Security Commissioner Stanford Ross, after he announced his resignation, conceded in 1979 that "the mythology of Social

James Bovard is the author of Freedom in Chains: The Rise of the State and the Demise of the Citizen *(St. Martin's Press, 1999).*

Security contributed greatly to its success. . . . Strictly speaking, the system was never intended to return to individuals what they paid."[5] Ross said that Americans should forget the "myth" that Social Security is a pension plan and accept it as a tax on workers to provide for the "vulnerable of our society." But Senator Daniel Patrick Moynihan of New York accurately characterized Social Security taxes as "outright thievery" from young working people.[6]

American citizens now shoulder over $17 trillion in unfunded liabilities.[7] The General Accounting Office issued the first comprehensive report on government assets and liabilities in 1998—and curiously left Social Security obligations out of the liability column. A *New York Times* article noted,

> A footnote in a draft portion of the report released Monday notes that after 2029, the Social Security trust fund will be "totally exhausted" and "current tax income will be sufficient to pay approximately 75 percent of the benefits due." But that is not really a liability, the administration's accounting experts explained Monday, because technically the government owes the money to itself, not the pensioners, and because Congress is free to change the amount paid Social Security recipients. After thinking about the political implications of that statement, however, more politically sensitive administration officials called reporters late Monday to stress that the government did not really have plans to cut back on Social Security payments. "It's an accounting device," one official said. "That's all it is."[8]

If the defenders of Social Security insist that the fraud was justified because otherwise the American people would not have accepted the coercive redistribution scheme, the question arises: What future limits should there be on government's prerogative to deceive the people? If Social Security is an acceptable fraud, what would government have to do before it was considered to have gone too far? Social Security is a perfect symbol of political generosity: it robs scores of millions of young people, it halves the national savings rate, and thereby sabotages investment and productivity increases,[9] and it maximizes bureaucratic and political discretion over people's fortunes. If the average worker had a dollar for every time a congressman lied about Social Security, his retirement would be safe. There is no "Honesty in Intervention Act" governing new laws or political action. Current taxpayers are still paying for the lies that politicians told to get re-elected in 1936, 1938, 1940, ad nauseam. The fact that politicians replace old lies with new lies does not reduce the burden on citizens of laws that were enacted on false pretenses generations ago.

Business Accounting versus Government Accounting

Paternalism will always be based on political accounting, which is practically the opposite of private accounting. Businesses prosper by reducing costs, while politicians prosper by denying that costs exist. For politicians, it is more important that spending forecasts be popular than accurate. The more that politicians and bureaucrats underestimate the cost of their favored policies, the easier it becomes to hustle those policies to voters and other legislators. Medicare—one of the largest expansions of government power since the New Deal—steamrolled through Congress in 1965 in part because of a spending forecast that made the expansion of handouts seem easily affordable. By 1990, however, Medicare was costing almost ten times more per year than the 1965 forecast had predicted it would cost.[10]

The political concept of waste is almost diametrically opposed to the economic concept of waste. In economics if an activity produces something that other people value, it can be successful; in politics if a program garners votes, campaign contributions, or power, it is successful. Government programs are often effectively designed to waste money because politicians benefit from an inefficient, spendthrift program as much as or more than they would benefit from an efficient, well-targeted program. Congressmen brag about the amount of federal money spent in their

districts, not about whether audit reports found minimal fraud.

Political accounting means that government leaders will be ignorant or misled or dishonest about the true cost of policies they impose. The GAO's financial report concluded: "Because of the government's serious systems, record-keeping, documentation, and control deficiencies, amounts reported in the consolidated financial statements and related notes do not provide a reliable source of information for decision-making by the government or the public."[11] GAO found that "significant financial systems weaknesses, problems with fundamental record keeping, incomplete documentation, and weak internal controls . . . prevent the government from accurately reporting a large portion of its assets, liabilities, and costs."[12] Senator Fred Thompson of Tennessee declared, "We are spending almost $2 trillion a year and managing a $850 billion loan portfolio based on erroneous or non-existent information. It means basically that we don't know what the government's assets are, we don't know what the government's liabilities are, we don't know what it costs to run government."[13]

After the audit was released, a senior Clinton administration official told the Associated Press: "This is an old closet that we haven't cleaned out in 200 years."[14] If politicians are going to have the closet cleaned out only once every couple centuries, maybe they have no right to control the house. A report that should have been proof of the political class's incompetence instead merely evokes another round of promises to try harder next time.

Cost Is No Object

Paternalism presumes that government agencies judiciously weigh costs and benefits before extending their power. However, many bureaucracies have little or no curiosity about the impact of agency actions on private citizens. The House Commerce Committee surveyed federal agencies and concluded in a 1997 report, "Where costs [of regulation to private companies] are addressed, they represent only the smallest and most insignificant portion of total costs. . . . With little or no documentation on the costs of regulation, agencies have no basis to judge whether any possible benefits from a new regulation would outweigh the possible costs of the regulation."[15] Because government agencies do not have to pay for the costs they impose, they have no incentive to track the burdens. The committee warned that "federal agencies may inadvertently be exposing our Nation to incalculable economic harms."[16] The only way such government ignorance could not be harmful is if it were true that government dictates are always superior to private decisions.

Efforts to evaluate government programs by private accounting standards are always contrary to how government agencies gauge their own successes. Government agencies measure their achievements by how much they prohibit; private companies gauge their accomplishments by how much they produce. Government bureaucracies brag about the number of fines they have imposed; private companies brag about the number of inventions they have created. Government bureaucrats pride themselves on forcing private citizens to obey orders; private companies pride themselves on discovering ways that help each person find his own path.

Governments do not squander money in a vacuum. The more of an economy that is subject to political command and control, the greater the opportunities and prosperity forgone. Wasteful government spending crowds out productive private investment; as a result, the entire society becomes increasingly impoverished compared to what people could have achieved.

The supposed benefits of the tradeoff between freedom and political control is based almost entirely on the bogus premise that politicians will provide more welfare (after seizing increased power over everyone else) than private citizens can generate through their voluntary agreements and hard work. A 1998 report by economist James Gwartney and colleagues for the congressional Joint Economic Committee found that since 1960, average government expenditures for the 23 major industrial countries had risen from 27 percent of GDP to 48 percent of GDP in 1996—while the average economic growth rate "fell from

5.5% in the 1960s to 1.9% in the 1990s." Gwartney observed: "While growth has declined in all [23] countries, those countries with the least growth of government have suffered the least."[17] Gwartney concluded: "If government expenditures as a share of GDP in the United States had remained at their 1960 level, real GDP in 1996 would have been $9.16 trillion instead of $7.64 trillion, and the average income for a family of four would have been $23,440 higher."

Squandering Lives

The failure of a government policy does not merely reduce the number of bureaucrats who receive "outstanding achievement" job evaluations. Governments cannot waste tax dollars without squandering part of the lives of the people who earned those dollars. There are human costs to every government snafu. A billion tax dollars wasted pre-empts 10,000 families from buying starter homes, or pre-empts 100,000 people from buying bottom-of-the-line new cars, or pre-empts a million people from taking a summer vacation, or pre-empts citizens from buying 40 million new books or 80 million cases of beer.

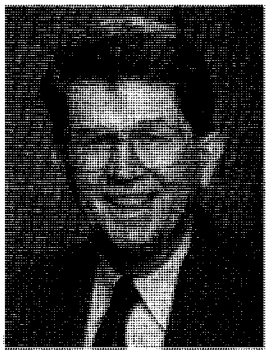
The value of liberty and personal independence is almost never factored into the calculus of paternalism. Social scientists, politicians, and bureaucrats consider the expected benefits of any proposed new rule and ignore the effect of its forcible imposition. Every government program, every government intervention, every government penalty carries a hidden cost of pre-emption. The fact that people prefer to live as they choose and not as others command never shows up on intellectual radar screens. If the costs do not show up in the official government budget, they do not officially exist. Any government cost-benefit analysis of a proposed new rule or regulation that disregards the value of individual freedom implicitly assumes that private freedom is a good at the disposal of the political class.

Since most politicians—simply by their career choice—indicate a desire for power, any measure that increases power will be considered a success. If a policy increases the number of people beholden to them, then it is good as an end in itself. The ultimate conflict of interest that subverts paternalism is that government officials want power and citizens want freedom.

There is no reason to expect contemporary Leviathans to become significantly more efficient in the future. The only way to fix most government programs is to repeal the underlying law and abolish the government agency. Anything less will be little more than a future full-employment program for investigative journalists. □

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15. House Commerce Committee, *Survey of Federal Agencies on Costs of Federal Regulations*, House Report 97-H-272-1, January 1997.
16. Ibid.
17. "On average, government expenditures in 1995 consumed only 20% of GDP in the five economies with the most rapid real economic growth rates during 1980–95: Hong Kong, Singapore, South Korea, Taiwan and Thailand. In these countries, the size of government in 1995 was virtually the same as in 1975." James Gwartney, "Less Government, More Growth," *Wall Street Journal*, April 10, 1998.

Economics



Speculation and Risk

Last month I showed that speculators are best thought of as conservationists. They are constantly looking to the future and conserving resources they believe are becoming more valuable. Since no one can predict the future with full confidence, speculators necessarily take risks. And when a speculator misjudges the future, he moves resources from periods when they are worth more to periods when they are worth less. But speculators who consistently make mistakes are soon left without the finances to continue speculating, and their mistakes create profitable opportunities for better prognosticators to take corrective action.

Recall last month's advice not to complain out loud about the mistakes that you think speculators are making. If your criticism is correct, you can make a fortune by not sharing your information and entering the market yourself. You will increase the value realized from our scarce resources. If you are wrong, however, you can lose lots of money. Again, speculation is risky.

Many people disapprove of speculative markets because of the risk associated with them. They believe these markets are little more than gambling havens on par with Las Vegas and Atlantic City casinos. The critics fear that allowing speculative markets to proliferate, as they have in recent years (allowing people to speculate on such things as foreign currencies and the rate of inflation, as well as on resources such as petroleum and agricultural products), creates harmful levels of risk in society. Wrong! There is a fundamental difference between the risks in Las Vegas casinos and the risks in speculative markets.

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Craps versus Crops

A crucial difference between the risk of playing craps and the risk of speculating on the price of wheat is that the game of craps creates a risk that otherwise would not have existed. Creating risk for the enjoyment of people who like to take chances is the purpose of gambling games. Of course, some people also enjoy the risks of "betting" on the future price of wheat in speculative markets. But speculative markets do not create risks. The risks associated with speculative markets are inherent in the act of growing crops and are necessarily borne by someone. If speculative markets were outlawed, farmers would have to take the risk of "betting" that the cost of planting a crop today is less than the unknown "payoff" from selling it at harvest. Only those who hate gambling more than they love eating should criticize the risks associated with speculative markets. Actually speculative markets lower the cost of unavoidable risks.

Consider the farmer who invests most of his wealth in planting wheat each spring. Taking a risk on the future price of wheat is extremely costly for him. He could win, of course, if the price of wheat is higher than expected. But the price might plummet, in

which case he could lose everything. Even enthusiastic gamblers are reluctant to put their life savings on one roll of the dice. Thus our farmer would like to eliminate the risk of declining wheat prices so he can concentrate on growing wheat, which is risky enough. And that is exactly what he can do in the speculative (futures) market for wheat. In the spring he can arrange to sell his harvest for the fall price that currently prevails in the futures market for the type of wheat he is growing. The farmer eliminates the risk he faces from declining prices by locking in his sales price.

This doesn't eliminate the risk of price declines. The farmer has simply passed that risk on to those who agreed to pay the specified future price. If the price of wheat increases above that price, the buyers of the futures win; but if it falls below that price, they lose. This is not just a game of "hot potato" in which the cost of holding the risk is the same no matter who holds it. Those who accept the price risk have a lower cost associated with that risk than the farmer does; maybe they are less averse to risk. Also, the farmer passes the risk to many people, each of whom takes just the amount he wants. Finally, those accepting the risk can diversify, agreeing to buy many different products. Because of speculative markets, the "hot potato" of risk ends up in the hands of those with the thickest gloves.

In some cases, speculative markets allow risk to be eliminated almost entirely. In fact, the term "speculative market" can be a misnomer, since parties on both sides of the market often use them to avoid speculating. Those who agree to pay a wheat farmer a specified future price for his harvest may do so to avoid speculating in wheat prices themselves. Consider bakers whose profits are reduced if the price of their primary ingredient, wheat, increases in the future. The risk bakers want to avoid (wheat prices going up) is exactly opposite to the one wheat farmers want to avoid (wheat prices going down). So farmers and bakers can eliminate the risk they fear most by using "speculative" markets to agree now to a specified price in the future. The risk of fluctuating wheat prices isn't eliminated—the farmer risks losing the gain from rising prices and the baker risks losing the gain from declining prices. But the degree of risk has been greatly reduced for both.

Derivatives Don't Cause Risk

Agreements to buy and sell agricultural products at specified future prices are made with futures contracts. These contracts are traded on markets, and their prices fluctuate over time with changes in the expected prices of the products. So the value of each of these futures contracts is derived from the value of something else. Any contract whose value is derived from something else is called a derivative. Derivatives have proliferated in recent years, allowing people to speculate on the future prices of a wide range of things (including interest rates). Unfortunately derivatives are widely blamed for the risks that have resulted in a few large losses suffered by businesses and governments that speculated in them. This criticism reverses cause and effect. Increased risk caused the derivative, not the other way around. The increase in the numbers and types of derivatives was the predictable response to the increased risks caused by such things as the uncertain value of the dollar due to the inflation of the 1970s and '80s, the volatility of prices of resources such as oil, and the move to floating exchange rates for foreign currencies. These risks were not caused by derivatives. Derivatives emerged as a way of reducing risks in the same way farmers and bakers reduce the cost of fluctuating wheat prices with futures contracts.

Blaming risks on derivatives is as silly as blaming diseases on doctors. □

THE FREEMAN
Ideas On Liberty

Bad Investment

by Deroy Murdock

In his State of the Union address, President Clinton proposed to invest some $700 billion of the Social Security Trust Fund in corporate equities through 2014. Give the President credit for finally conceding that the largest federal program generates returns that would cost a Wall Street money manager his job. However, Clinton's scheme to make Uncle Sam the biggest trader on Wall Street is riddled with economic and political perils.

True, pumping public pension money into stocks promises better returns than do Special Issue Treasury Notes, the non-marketable IOUs that accumulate as Washington spends today's FICA taxes on foreign aid, food stamps, and more. However, individuals who invest their assets privately tend to see them outperform those supervised by government functionaries. Unlike private portfolio managers—who legally must maximize returns for future retirees—public pension administrators often pursue other agendas. Many strive for "collateral benefits," as former Labor Secretary Robert Reich endearingly calls them, such as "affordable housing, infrastructure improvements and jobs."

According to Marquette University finance professor John R. Nofsinger, these "economically targeted investments" (or ETIs) typically reduce average annual yields by 1.5 percentage points below their expected returns. Alicia Munnell, a former Clinton Treasury official, discovered that the returns from pension investments funneled into home-ownership programs fell between 1.9 and 2.4 percentage points annually. With compounding, such seemingly small gaps swell into wide gulfs between the retirement incomes of workers who control their assets and those whose futures are left to bureaucrats.

Bigger Menace

But the menace of government equity ownership goes beyond rates of return. President Clinton's desire for a Social Security portfolio "free from politics" is fanciful at best, another lie at worst. In a January 28 Senate Budget Committee appearance, Federal Reserve Chairman Alan Greenspan hosed down this idea with ice water. Federal investment of FICA funds, Greenspan said, "would arguably put at risk the efficiency of our capital markets, and thus our economy." He also was metaphysically skeptical of politically neutral government investment: "Even with Herculean efforts, I doubt if it would be feasible to insulate, over the long run, the trust funds from political pressure—direct and indirect—to allocate capital to less than its most productive use."

Social Security's cheerleaders call privatizers paranoid for imagining that the Clinton administration might, for instance, liquidate Microsoft and Philip Morris shares to express solidarity with Macintosh users and non-

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smokers. But the privatizers reply that politically driven public investment is all too common in cities and state. These include assets "targeted" at local economic development, as well as politically correct investment decisions that promote pet causes. Some officials simply have misallocated pension funds. Add to this mix the usual graft and corruption that make government itself such a dreary proposition.

State efforts to steer pension assets into local economic activity have imploded as if they were abandoned public-housing projects. In recent years, according to Heritage Foundation analyst Daniel Mitchell, the Kansas Public Employees' Retirement System lost $65 million in the Kansas-based Home Savings Association, $14 million in Tallgrass Technologies, and about $8 million in a local steel mill. With at least $138 million in losses, this economic targeting missed the bull's-eye by miles.

In 1988 the Missouri State Employees Retirement System launched a venture-capital fund to lure companies to the Show-Me State. Three years and two lawsuits later, the failed fund was shown the door. In 1990, the State of Connecticut Trust Fund spent $25 million for a 47 percent stake in Colt Industries, a local gun maker. In 1993, Colt misfired, and the money vanished.

According to the Cato Institute's Michael Tanner, 42 percent of state, county, and local pension fund systems currently practice this kind of cronyism. Such ETIs, Yale law professor Roberta Romano reports, generated $28 billion in losses between 1985 and 1989.

Politically Correct Investment

As if incompetent investment were not enough, public portfolios also are battered by politically correct decision-making. Public equity ownership became a white-hot political potato during the divestment movement of the mid-1980s. At least 30 states and many more cities and public universities ditched their shares in companies that conducted business in apartheid-era South Africa. (Perhaps in the name of equal opportunity, 11 states also curbed investments in firms that violated the "MacBride Principles" governing commerce in Northern Ireland.)

Tobacco, of course, is a smoldering bugaboo for public pension managers. Minnesota lost $2 million last year when its employees' fund dumped its tobacco holdings. Some public managers have done more than simply wash the tobacco stains off their hands. On April 10, 1998, New York State Comptroller Carl McCall said he would withhold his support from the boards of Philip Morris, RJR Nabisco, and Loew's at shareholders' meetings if they did not "reach a prompt settlement that effectively reduces youth smoking and ends the lingering controversy. . . . It is not in the best interest of the tobacco companies to just stop talking to Congress." New York's state pension fund then owned 11 million shares of those firms' equities worth some $450 million.

Conservative activists have joined in the fun, too. The American Family Association of Texas sent the State Board of Education taped highlights of recent films distributed by Miramax, a Walt Disney subsidiary, including the violent hit *Pulp Fiction*. On July 9, 1998, the board decided to sell the $46.4 million of Disney stock in its Permanent School Fund. "It's not Mickey Mouse and Donald Duck anymore," board member Richard Neill said at the time. "It's blowing people's heads off."

Political pressure needn't be applied to be effective. Like a cocked gun that is never discharged, the mere threat of a politically inspired investment decision can advance desired outcomes. When politicians snarl, executives dive beneath their desks.

On July 2, 1998, Carl McCall and New York City Comptroller Alan Hevesi threatened to exclude Swiss banks and financial advisers from managing municipal pension funds and other state assets. McCall and Hevesi wanted the Swiss to settle a lawsuit with Jewish groups involved in the Holocaust-era dormant accounts controversy. The Swiss banks caved in like chocolate soufflés. "The first set of measures was supposed to begin September 1," a Swiss source close to the talks told me. "That boycott schedule had an impact on the speed of the negotiations, without a doubt." The final deal was unveiled

August 12, 1998, just five weeks after McCall and Hevesi huffed and puffed.

Squandered Assets

While Congress routinely squanders tomorrow's Social Security assets on today's goodies, state and local officials have learned from the big boys. In 1997 California's Supreme Court let stand a lower court ruling that Sacramento had violated public employees' rights. Then-Governor Pete Wilson and the state legislature diverted $1.36 billion in pension contributions to balance the state budget in fiscal years 1993 and 1994. New York State similarly siphoned $230 million from its employees' retirement fund in 1995. In the summer of 1998, Chicago authorities used $12.5 million in pension contributions for interest payments on a $175 million infrastructure bond issue.

Can anyone trust Congress and the White House not to use a federal pension portfolio to balance future budgets? This $700 billion honey pot also will attract lobbyists and PAC men like grizzly bears. This would be a golden opportunity for presidents and congressmen to sell "access" to Wall Street firms—one banquet table at a time.

Free-marketeers should be frightened by those who already are licking their chops over what could become government's biggest chow-down yet. Savoring this potential federal feast, Representative Jerrold Nadler told *The Village Voice*: "You're saying the government will have more influence to pressure for more decent, socially responsible corporate behavior. That's terrible?" The AFL-CIO's Gerald Shea predicts federal investment will "have a good effect on how corporate America operates." That depends on what your definition of "good" is. □

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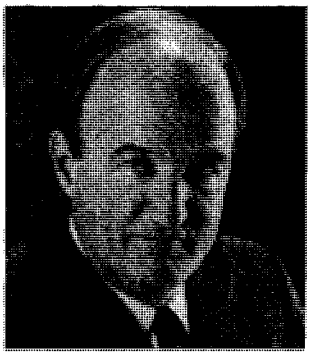


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THE FREEMAN
Ideas On Liberty
SEPTEMBER 1999



"They Were Right"

"Americans need to know the history of American anticommunism if they are to understand the great role they have played in ridding the world of the most murderous of the twentieth century totalitarians."

—RICHARD GID POWERS[1]

On October 16, 1961, thousands of people packed the Hollywood Bowl. The occasion was not a rock concert or a sporting event but the biggest anticommunist rally in the country. "Hollywood's Answer to Communism" was carried on nationwide television. Actor George Murphy was the master of ceremonies and other speakers included Herb Philbrick, Congressman Walter Judd, Dr. Fred Schwarz, Senator Thomas Dodd, and my uncle, W. Cleon Skousen, a former special assistant to J. Edgar Hoover and author of the bestseller *The Naked Communist.*

I was in my early teens when the anticommunist movement was at its zenith and remember seeing my uncle on TV. I watched shows like *I Led Three Lives* and read books like John Stormer's *None Dare Call It Treason*, J. Edgar Hoover's *Masters of Deceit*, and Whittaker Chambers's *Witness.*

But despite this groundswell of concern over the threat of communism, communist sympathizers at high levels combined with media forces to ridicule and vilify patriotic conservatives. Most historians deplored the anticommunist movement of the 1950s and 1960s as "extremist," "paranoid," "right-wing" hysteria. Accordingly, there was little credence given to this alleged vast communist conspiracy; reaction went rarely beyond references to McCarthyism, redbaiting, and blacklisting. They challenged the anticommunists' claims that the Soviets had planted numerous agents in government, that Stalin had infiltrated the film industry as a means of promoting communist propaganda, that the Communist Party USA was a pawn of Moscow, and that the Soviet Union was a serious military threat.

They depicted the anticommunist era as an unwarranted "witch hunt" against liberal progressives and idealistic movie stars and a groundless attack on patriotic government officials who they say were falsely accused of espionage. They carried on a 40-year campaign to prove Alger Hiss and Julius and Ethel Rosenberg innocent. My uncle's book so angered members of the political science and history departments at Brigham Young University that Richard D. Poll, a history professor, wrote a scathing critique of his "extremist" views on Karl Marx and communism.

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Mises and Socialism

In those days, the economics profession also cast doubt on free-market criticisms of socialism and the Soviet economy. Half a century earlier, Ludwig von Mises and F. A. Hayek were lone voices in charging that socialist central planning could not work. According to conventional wisdom, Mises and Hayek had lost the debate with the socialists in the 1930s, and in 1985 Paul Samuelson reported in his popular textbook that the Soviet Union had grown faster than any other industrial economy since the 1920s. As late as 1989, Samuelson claimed that "The Soviet economy is proof that, contrary to what many skeptics had earlier believed, a socialist command economy can function and even thrive."[2]

But then, following the collapse of the Berlin Wall and Soviet communism in 1989–90, economist Robert Heilbroner shocked his colleagues in the socialist world by boldly declaring that the long-standing debate between capitalism and socialism was over. "Capitalism has won," he confessed. "Socialism has been a great tragedy this century." Furthermore, Heilbroner was forced to change his mind about Mises and the debate over socialism. Following the unexpected collapse of communism, Heilbroner admitted, "It turns out, of course, that Mises was right."[3] And it wasn't long before Paul Samuelson did an about-face in his textbook, labeling Soviet central planning "the failed model."

Revelations from the Soviet Archives

The fall of the Soviet Union brought about another dramatic outcome that would have far-reaching effects on modern history. The Russian government opened up thousands of secret KGB files in Moscow, revealing what one historian called "stunning revelations" about espionage and the Soviet economy under Stalin. This new information has sparked a harsh reevaluation of the anticommunist movement by historians and the media. As one reviewer put it, "It's like looking into the new edition of a book from which half the pages had previously been torn out."[4]

The KGB files prove beyond doubt that Alger Hiss, the Rosenbergs, and numerous other Americans accused of spying for the Soviets were guilty. They confirm what J. Edgar Hoover and the House Un-American Activities Committee were saying all along: that spies reached the highest levels of the State and Treasury departments, the White House, and the Manhattan Project, and that the Communist Party USA (which had 50,000 members in World War II) got its marching orders from Moscow.[5]

Stalin's Economic Disaster

Based on research at the Soviet archives, historian Sheila Fitzpatrick has written a pioneering account of everyday Russian life in the 1930s: "With the abolition of the market, shortages of food, clothing, and all kinds of consumer goods became endemic. As peasants fled the collectivized villages, major cities were soon in the grip of an acute housing crisis, with families jammed for decades in tiny single rooms in communal apartments. . . . It was a world of privation, overcrowding, endless queues, and broken families, in which the regime's promises of future socialist abundance rang hollow. . . . Government bureaucracy often turned everyday life into a nightmare."[6] What a sharp contrast to Samuelson's glowing account of the Soviet economy.

After writing three books on the Soviet archives, historians John Earl Haynes and Harvey Klehr summed it up this way about the anticommunists: "They were right."

And being right, they deserve our praise and gratitude. □

1. Richard Gid Powers, *Not Without Honor: The History of American Anticommunism* (New York: Free Press, 1995), p. 428.

2. Paul A. Samuelson and William D. Nordhaus, *Economics*, 13th ed. (New York: McGraw-Hill, 1989), p. 837.

3. Robert Heilbroner, "Reflections After Communism," *The New Yorker*, September 10, 1990, and "The Triumph of Capitalism," *The New Yorker*, January 23, 1989.

4. Joseph E. Persico, "The Kremlin Connection," review of *The Haunted Wood: Soviet Espionage in America*, by Allen Weinstein and Alexander Vassiliev, *New York Times Book Review*, January 3, 1999.

5. Several books have been published detailing new findings from the Russian archives, including John Earl Haynes and Harvey Klehr's *Venona: Decoding Soviet Espionage in America* (New Haven: Yale University Press, 1999) and *The Soviet World of American Communism* (New Haven: Yale, 1998).

6. Sheila Fitzpatrick, *Everyday Stalinism* (Oxford University Press, 1999), flyleaf.

BOOKS

Keeping the People's Liberties

by John J. Dinan

University Press of Kansas • 1998 • 259 pages • $35.00

Reviewed by George C. Leef

The title of this work comes from a 1792 essay by James Madison, "Who Are the Best Keepers of the People's Liberties?" How best to secure the rights of people was a question that bore heavily on the founders and still bears heavily on us today. Wake Forest University professor John Dinan examines the success—and lack thereof—of three different political regimes in their ability to "secure the rights" of citizens. The book is a valuable historical investigation, but is sadly disappointing in that it fails to give much help to those who search for political arrangements that will really *secure* our rights and not trample on them.

The first of the regimes Dinan examines is republicanism, that is, a system of elected representatives. The author finds that in the early days of the nation it was widely believed that elected representatives were best suited to the job of protecting the rights of the people. "[O]f the various public officials who might be charged with this responsibility," Dinan writes, "legislators were thought to be most capable of representing the popular understanding of rights; legislative assemblies were considered the proper forum for deliberating about the content of rights; and statutes were seen as providing the most effective means of securing their protection." Neither judges nor the general public were widely looked to as protectors of rights.

How well did republican institutions protect rights? Not too badly, Dinan concludes. Studying a limited number of state legislatures (principally Massachusetts, Virginia, Michigan, and Oregon), he shows that there were some signal successes achieved through legislation—for instance, freedom from ministerial taxes. Dating back to the seventeenth century in both Massachusetts and Virginia, taxes had been levied for the support of the official church. The battle to liberate people from such taxes was won in the legislatures, with the courts fighting a rearguard action on behalf of the vested interests that wanted the taxes to continue.

Another intriguing case Dinan presents is the controversy over protecting citizens against unlawful searches and seizures. Today we think of such protection as a judicial function of relatively recent origin, but that is far from the case. In the nineteenth century the problem of illegitimate searches and seizures by police and officials was much on the minds of the people, and the legislatures acted. The legislative remedy was to make public officials liable for wrongful invasions of individual liberty and property. It was not until the mid-twentieth century that the courts entered the scene with the controversial exclusionary rule, which forbids the use of evidence obtained illegally.

In the latter half of the nineteenth century, a growing dissatisfaction and impatience with legislatures led to the rise of the populist movement. The populists argued that legislatures were too beholden to special-interest groups and their own interest in re-election to do a good job of securing the rights of the people. Accordingly, many advocated popular initiatives and referenda as a means of bypassing or overriding the legislature.

In some instances, it worked. In 1921 a statute in Massachusetts established a censorship board to license movies that did not contain "indecent" material. The people promptly repealed the law by referendum in 1922.

The problem with populism is that it can result and frequently has resulted in laws that are incompatible with any respectable theory of rights. Dinan reports that when the Oregon legislature declined to enact a workmen's compensation system, "the people resorted to the initiative process to secure their rights." Compelling employers to obey a government edict on the treatment of injured workers is not a matter of "securing rights," however. It is a matter of one group's using the power of the state to get what it wants, overriding the

freedom of others. This is a repeated failing in the book: Dinan does not distinguish between true rights and governmentally decreed pseudo-rights.

Finally, Dinan looks at judicial protection of rights. This is also a mixed bag. Sometimes courts have struck down laws that interfered with rights, as in the "substantive due process" decisions of the pre-New Deal Supreme Court. On the other hand, courts have often been guilty of infringing rights in their quest for "fairness." The Oregon Supreme Court ruled that shopping malls were required to allow people to solicit petition signatures. This, of course, is not "securing a right," but rather violating the rights of mall owners.

Dinan tamely concludes that his analysis "suggests that an ideal regime of rights protection would combine the advantages of each of these institutions." Given the sorry record of all three, one might better conclude that all political institutions are dangerous to and have permitted a steady erosion of the people's liberties. □

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

The Structure of Liberty: Justice and the Rule of Law

by Randy E. Barnett

Oxford University Press • 1998 • 368 pages • $29.95

Reviewed by Bruce L. Benson

In *The Structure of Liberty*, Boston University law professor Randy Barnett identifies the fundamental problems that must be recognized in order to create a proper foundation for society: the problems of knowledge, interest, and power. Those problems arise because both physical resources and human abilities are scarce, because altruism is limited, and because humans are vulnerable. They mean that individual conduct must be constrained in some ways or else society will collapse.

But just as "good" buildings require different floor plans depending on their purpose, the structure of a "good" society also depends on the objectives of the society's occupants. Barnett attempts to describe the structure of a society that will allow "each person to pursue [his subjectively determined perception of] happiness, peace, and prosperity while acting in close proximity to others." Such a society requires justice and the rule of law, as the subtitle of the book suggests, so Barnett focuses on the necessary components of the structure of liberty in the face of the problems of knowledge, interest, and power. The result is an insightful, often brilliant presentation that deserves serious attention from those of us who share this vision of the good society.

Barnett is not attempting here to convince modern liberals or modern conservatives to become classical liberals or libertarians. Instead, he is writing to classical liberals and libertarians who already share his vision in an effort to show them what the structure of liberty requires. Convincing people that particular laws or policies are undesirable will have little long-term benefit if we do not have institutions of governance that sustain better rules and policies. Barnett argues that those institutions must be structured to handle the problems of knowledge, interest, and power.

Other political philosophers, of course, have wrestled with the problem of structuring liberty, but most who have preceded Barnett have not focused adequately on power. By bringing all three problems into the analysis Barnett is able to offer new insights regarding the kinds of institutions that are likely to produce justice and the rule of law in support of liberty. He questions some widely accepted principles of governance long cherished by classical liberals and proposes replacements.

Perhaps the best examples of this are in chapters 12 and 13, where Barnett turns to the problem of enforcement abuse and the nature of effective constitutional restraints on power. He challenges the argument by John Locke and other classical liberals who contend that a coercive monopoly of power is necessary to handle the problem of enforcement abuse. The "single power principle" has led classical liberals to focus on designing constitutional rules to shackle the monopoly in various

ways. Barnett explains that the single power principle is itself a primary source of abuse and that the rule of law is not likely to be maintained even with such constraints as periodic elections and checks and balances.

Furthermore, the single power principle is inconsistent with other liberal tenets. For instance, as Barnett explains, "Some think that law enforcement and adjudication are so important that we must make an exception to the background right of freedom of contract and permit a coercive monopoly to provide such services. . . . [But] the more vital a good or service is, the more dangerous it is to let it be produced by a coercive monopoly."

Barnett also points out that the reality of Western legal tradition is one of polycentric law, not monopolized law, and the competition between legal jurisdictions is actually the source of much of what is good about our modern legal system (many aspects of which are being undermined by increasing centralization of law). The rule of law, he argues, actually requires a polycentric constitutional order.

A brief review cannot possibly do justice to Barnett's analysis. The two chapters devoted to the importance of the rule of law are truly outstanding, but I would not hesitate to say the same about many other of his arguments. This book makes an important contribution toward a more complete understanding of the structure that must underlie a society in which individuals can live in peace and prosperity. I strongly recommend *The Structure of Liberty* to anyone who seeks such a society. □

Bruce Benson is DeVoe Moore Distinguished Research Professor at Florida State University.

The Lost Literature of Socialism

by George Watson

The Lutterworth Press • 1998 • 144 pages
• $50.00 cloth; $30.00 paperback

Reviewed by Antony Flew

The literature of socialism is lost only in the sense of not having been read for a very long time. George Watson has been re-reading this literature as a professional literary critic, with strong interests in both political affairs and the history of ideas. Many of his findings are astonishing. Perhaps for readers today the most astonishing of all is that "In the European century that began in the 1840s, from Engels' article of 1849 down to the death of Hitler, everyone who advocated genocide called himself a socialist and no conservative, liberal, anarchist or independent did anything of the kind." (The term "genocide" in Watson's usage is not confined to the extermination only of races or of ethnic groups, but embraces also the liquidation of such other complete human categories as "enemies of the people" and "the Kulaks as a class.")

Although Watson himself unfortunately never defines the key word "socialism," he is apparently following throughout the usage of the old British Labour Party. From its foundation, it proclaimed itself a socialist party and stated its aim in Clause IV of its constitution—thereafter printed on every membership card—as being "the public ownership of all the means of production, distribution and exchange."

Watson distinguishes three periods in the history of this socialist idea. The first, the Age of Conception, runs from the 1840s to the Bolshevik coup of 1917; the second, the Age of Fulfilment, continues until the Communist seizure of power in China in 1949; the third, the Age of Decline, continues until the fall of the Berlin Wall in 1989.

During the Age of Conception, many were attracted to socialism precisely because they already saw it as what Watson calls a "Tory project," a project necessarily involving rule by an irresponsible elite. Some of these elitists, such as the science fiction writer H.G. Wells and the dramatist Bernard Shaw, lived long enough into the Age of Fulfilment to welcome this aspect of the realization in the USSR of the socialist vision. Before World War I, other socialists, such as the novelist Jack London and the psychologist Havelock Ellis, saw socialism as leading both fortunately and necessarily to the triumph of the white races over the black and the brown.

For those of us born before World War II, the most interesting section of the book is that

dealing with the intellectual relations between the teachings of Adolf Hitler and those of Marx and his professed followers among Hitler's contemporaries. In his autobiography, and in recorded conversations with intimates among his own followers, Hitler said such things as, "I have learned a great deal from Marxism, as I do not hesitate to admit," that "the whole of National Socialism is based on Marx," and that without racist commitments his own political movement "would really do nothing more than compete with Marxism on its own ground."

Hitler was not in these statements saying that he either was or ever had been a Marxist. From his first political activity, he had always been opposed to communism, but that was not because it was socialist, but because it was internationalist. Hitler, although born and raised in Austria, had always been a dedicated German nationalist.

Even those who are aware that Hitler's party was the *National Socialist German Workers' Party* have doubted the sincerity of its socialist professions. This is in part because Hitler, upon coming to power, refrained for tactical reasons from launching an immediate and extensive program of state takeovers of private industries, and in part because these skeptics have not enjoyed the benefits of Watson's re-readings of the lost literature of socialism.

His chapter on "Marx and the Holocaust" begins by telling us that Rudolf Hoess, commandant of the infamous Auschwitz death camp, recalled in his memoirs that even at the height of the Nazi-Soviet war of 1941-45, his colleagues had respected the socialist example of an exterminatory program based on forced labor. Watson then proceeds to deploy further evidence of Soviet influence on the Nazis and to cite other relevant passages from the works of Marx, Engels, Lenin, and other socialist luminaries, all presenting candidates for or possible methods of genocide. The connection between socialism and genocide could hardly be made any clearer.

From all this, Watson concludes that "it is becoming ever more probable that it was not just the idea of genocide that the Nazis owed to Marx and the Marxists, but its detailed practice too, not excluding camps and gas chambers. The shadow of the socialist idea grows longer and longer." □

Antony Flew is Emeritus Professor of Philosophy, University of Reading, England.

Freedom to Trade: Refuting the New Protectionism

edited by Edward L. Hudgins

Cato Institute • 1997 • 88 pages • $10.00 paperback

Reviewed by Charles K. Rowley

Free trade against protectionism is one of those few issues over which economists have reached consensus. Free trade attracts the vote of the very large majority of economists, whereas protectionism typically attracts the support only of those who are paid mouthpieces for the special interests. Yet this remarkable consensus belies the facts of the international trade reality. The guns of the economists, like the French guns of the Maginot Line, appear to point in the wrong direction. International trade is highly regulated; and protectionism dominates free trade despite the cogent economic arguments against it.

The book under review represents a sterling effort to carry the case for free trade forward to the general public in language stripped of the jargon of economics. It is written well and cogently argued. Chapter one, written by Edward Hudgins, director of regulatory studies at the Cato Institute, focuses attention on the fundamental freedom to trade, correctly stressing that the *individual* trades and not the *nation*. Although the concept of comparative advantage strangely is never mentioned, the classical case for unilateral free trade is outlined, briefly but accurately, both in terms of static specialization and in terms of dynamic market discovery criteria.

The second chapter, written by Bruce Bartlett, briefly reviews the trade history of the Netherlands, Great Britain, the United States, Japan, and Germany, and succinctly demonstrates the close correlation between periods of relative free trade and periods of

relative prosperity in each of these nations. The aim of this chapter is to show that generally nations rise to power and wealth through free trade and decline when protectionism takes over. In my opinion this case holds least well for the United States, whose dramatic advance between 1875 and 1900 coincided with Republican high-tariff policies justified by infant-industry rhetoric. Of course, it is the elementary *post hoc ergo propter hoc* logical fallacy to conclude, as some do, that protectionist tariffs were the cause of our economic growth. It is also questionable whether rising German economic power between 1871 and 1939 was based on free trade policies. It is always satisfying when the facts fit our predilections; equally, however, it is unwise to force the fit.

Chapter three, written by Hudgins, attempts to refute the myth of the "race to the bottom," which charges that U.S. free trade policies result in a loss of jobs to other countries and in declining real wages in the United States. Using simple charts to excellent effect, Hudgins makes a strong case that recent job creation in the United States has far surpassed that of its major international rivals and that real wages in the United States, correctly measured, have increased at approximately the same rate as underlying productivity. Hudgins also fingers the explosive growth of government in the United States over the past three decades as the major single factor depressing productivity and obstructing the growth in real wages. Undoubtedly, this is the best chapter in the book, and one that should be read by any intelligent adherent to the intellectually confused trade policies of Ross Perot and Pat Buchanan.

The next chapter, also written by Hudgins, changes direction into a surprisingly vigorous defense of recent trade treaties entered into by the United States, arguing that they do not infringe national sovereignty. I have no dispute with the author in this judgment. However, I contest his view that certain of these treaties are supportive of free trade. In particular, the regional trade agreements, epitomized by NAFTA, divert U.S. attention away from genuinely multilateral trade agreements; for example, excessive attention to NAFTA almost aborted the Uruguay Round. They also provide a regulatory conduit through which the forces of protection obstruct the flow of imports into the United States. The post-Uruguay shift from the informal General Agreement on Tariffs and Trade to the much more bureaucratic World Trade Organization as an enforcement agency is also not a change with which genuine free traders should be enamored.

Among the remaining essays, the best is chapter eight, written by James Dorn, providing a compelling analysis of the relationship between trade and human rights based upon a study of the People's Republic of China over the period 1978 to 1997. Dorn makes an eloquent case in favor of keeping trade open between the United States and China as a basis for promoting liberty in the latter country. This is a refreshing change from the self-serving arguments in favor of such open markets typically advanced by U.S. export interests.

Edited volumes typically suffer from unevenness of quality and lack of cohesiveness. This monograph, despite its brevity, is no exception. In addition, the monograph is weak in its use of public-choice analysis, which is unfortunate since public choice goes far to explain why the guns of the Maginot Line indeed point in the wrong direction.

Nevertheless, I recommend this book to anyone who is eagerly searching for a short volume capable of explaining in nontechnical language the case for free trade and the arguments against trade protection. □

Charles Rowley is a professor of economics at George Mason University and general director of the Locke Institute.

The Roosevelt Myth

by John T. Flynn

Fox & Wilkes • 1998 • 437 pages • $24.95 cloth; $14.95 paperback

Reviewed by Lawrence W. Reed

For every thousand books written, perhaps one may come to enjoy the appellation

"classic." That label is reserved for a book that through the force of its originality and thoroughness, shifts paradigms and serves as a timeless, indispensable source of insight.

Such a book is *The Roosevelt Myth* by John T. Flynn. First published in 1948, Flynn's definitive analysis of America's 32nd president was reissued last year in a 50th anniversary edition by Fox & Wilkes, with a new foreword by Ralph Raico. It is the best and most thoroughly documented chronicle of the person and politics of Franklin Delano Roosevelt.

John T. Flynn was a successful and influential journalist with a reputation for candor and first-rate research. He was neither a shill for Big Government nor a puppet of Big Business. He railed against both when they conspired to undermine the Constitution, erode our freedoms, or suck the nation into foreign entanglements. He saw right through the public relations job depicting FDR as a valiant crusader for noble causes.

Was FDR a man of principles, a man guided in his thinking by a fixed set of lofty and noncontradictory ideas? Far from it, Flynn proves, in what is an important theme of the book. FDR's thinking and behavior show him to be a real-life exemplar of an old Groucho Marx wisecrack: "Those are my principles. If you don't like them, I have others!"

Running against Herbert Hoover in 1932, Roosevelt campaigned as an advocate of limited government, even (correctly) accusing Hoover of "reckless and extravagant spending" and of thinking "that we ought to center control of everything in Washington as rapidly as possible." After being elected, however, FDR promptly championed reckless and extravagant spending and tried to centralize just about everything in Washington. He did so not because he had become a scholarly statist intellectual, but simply because he was an opportunist capitalizing on the public's demand for "action."

Yet the depression that FDR inherited was still very much with us after two terms in the White House. He zigged and zagged from one Rube Goldberg policy contraption to the next. His elitist brain trusters covered for his failures and cooked up new schemes, in what Flynn called "the dance of the crackpots."

Flynn's critique of the Mussolini-inspired New Deal's two main hallmarks—the National Recovery Administration (NRA) and the Agricultural Adjustment Act (AAA)—remains one of the most devastating ever penned. The "crazy antics" of the NRA put a New York tailor behind bars for pressing a suit of clothes for 35 instead of 40 cents. With the AAA, "we had men burning oats when we were importing oats from abroad on a huge scale, killing pigs while increasing our imports of lard, cutting corn production and importing 30 million bushels of corn from abroad."

Flynn's view of FDR's coterie of planners was right on target, each "a kind of little man who will tell you that he can't hit a nail straight with a hammer, but who loves to spread a big country like the United States out before him on top of a table, pull up a chair and sit down to rearrange the whole thing to suit his heart's content."

Flynn leaves the reader with a sense of disgust that the liberties and the pocketbooks of a nation were placed in the hands of so beguiling a schemer as Franklin Delano Roosevelt. Not even America's entry into World War II was without its shameful lies and prevarications from an administration whose one consistency was to place its own preservation above the long-term welfare of the nation.

Given the ongoing deification of FDR (there's even been a rumor that he'll be *Time* magazine's Man of the Century), John T. Flynn's *The Roosevelt Myth* is as relevant and necessary today as it was a half-century ago. Americans who prefer their history not be twisted to serve statist ends or sanitized by the politically correct should be sure to stock their libraries with this classic. No one who reads it with an open mind will ever think of Franklin Delano Roosevelt the same way again. □

Lawrence Reed is president of the Mackinac Center for Public Policy (www.mackinac.org), a free-market research and educational organization in Midland, Michigan, and chairman of FEE's Board of Trustees.

Government



A World Without the FDA (Plus a Contest!)

Back in 1980 I had the good fortune to spend a summer in Santiago, Chile. My woeful high-school French produced an even more woeful Spanish, but I was able to travel about that beautiful country with wonderful people.

In the middle of my stay I developed a fearful cold and wandered into what looked like a drugstore in search of comfort for my ailing throat, nose, and head. I picked up a bottle of this, a bottle of that, and tried to puzzle out their purposes. I quickly realized that my command of Spanish, while adequate for getting around on the bus or in the grocery, was a major handicap when trying to figure out the ingredients and expected impact of any of the products lining the shelves.

As I stood there peering at labels, it occurred to me that there probably was not a Chilean equivalent of the Food and Drug Administration. I remembered the time my father had surgery overseas. His post-operative condition was an emotional roller coaster: he found out later that he had been given cocaine as an anesthetic.

My problem went beyond my language deficiency: I was about to take on more risk than I was accustomed to in the United States. After years in the risk-free world of the American pharmacy, I was uneducated and unprepared for the choices on the shelves before me. I decided to endure my ailments drug-free.

My ignorance was the rational result of growing up in a world where the drugs that have any impact are only available by prescription and the ones available over the counter are about as dangerous as the candy in the next aisle. But if there were no FDA and if any drug were available over the counter, my incentives to become educated would change.

Voluntary Testing

The world would change in all kinds of interesting ways. Let's try to imagine what that world might look like. No FDA. No prescriptions. Any drug could be sold over the counter. And for simplicity, when I speak of drugs I mean purely medicinal drugs, even though my father's experience might make that a tough line to draw in practice.

Would drug companies test their drugs if tests were voluntary? I don't think drug companies' profits would be enhanced if their customers died from using their products. They would test their drugs. Would they test them as thoroughly as they are required to do now by the FDA? I doubt it.

Drugs would be riskier. Is that good or bad? We tend to think of drugs as safe or unsafe. But no drug is completely safe. The only way to avoid the side effects of drugs is not to take them. And most of us understand that as long as the risk is small enough and the benefits

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large enough, putting foreign substances into our bodies is a good idea.

What is more difficult to accept is the possibility that a drug can be "too safe." Under current drug regulations, it takes years of testing to get FDA approval. There is no free lunch: making drugs as safe as the FDA requires has costs.

Some worthwhile drugs for uncommon diseases never make it to market because the costs of proving their safety and effectiveness aren't worth it. Other drugs are worth it, but while waiting for FDA approval, people are dying or suffering. Finally, there are risky drugs the FDA rejects but that a patient might be willing to take a chance on. Without the FDA, there would be a lot more choice in the marketplace.

And with choice comes a lot more risk. That increase in risk would encourage consumers to become more educated. You could insulate yourself from that risk by using your doctor as you do now: as the gatekeeper to the dangerous world of drugs. But we would have the freedom to have a different relationship with our doctors. Many of us would take greater responsibility for our decisions by using a doctor as a resource rather than as a surrogate parent.

Most of us will not want to master the effects of drugs, even with a doctor's help, so we will also have a demand for other sources of good information. With the government out of the business of risk control, there will be a large profit opportunity to provide reliable information on drugs and how they work. The Internet is one way to provide that information.

Perhaps a private nongovernmental version of the FDA would come into existence akin to Underwriters Laboratory or *Consumer Reports*, certifying drugs as having a particular effect on an ailment or not having particular side effects. Such testing would be expensive, but drug manufacturers and consumers might be willing to pay a premium for drugs that had been extensively tested and certified independently. There might be different organizations with different standards of effectiveness or safety certifying the effects of drugs.

All of the above is mere speculation, an attempt to fathom how the market might respond to the intense demand for information in a riskier world. I can only begin to guess how the market might solve that problem.

All I know for certain is that a world without the FDA and without prescriptions would have more personal responsibility and more choice.

I also know for certain that there would be tragic outcomes as well. Without the protection of the government, some people would be taken advantage of by unscrupulous drug manufacturers and deceptive marketing. Some people would hurt themselves taking the wrong drugs or neglecting various drug interactions.

But others would be saved by the wider and earlier availability of life-saving drugs.

Would a world without an FDA and prescriptions be a better world? The answer depends on how many lives would be lost from mistakes and how many lives would be saved by the wider and earlier availability of drugs. It would also depend on the value you place on putting responsibility in our own hands rather than having the government take responsibility for us.

Here is my challenge to you, the thoughtful reader. I would like to hear from you as to which world you prefer: the current world or the one I have sketched above. What are the reasons for your choice? As a final challenge, I'd like to hear from you as to how you think the market would handle the informational challenges of a world without the FDA. The best submissions will be mentioned in my next column and the writer of the most interesting response will be given a choice of books from the FEE Bookstore. Send them to me at FEE, 30 S. Broadway, Irvington-on-Hudson, NY 10533, or e-mail freeman@fee.org, with "FDA Contest" in the subject line. □

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PERSPECTIVE

Ever Striving

It is not "mere theory" to say that entrepreneurs, lured by the prospect of pure profit, constantly strive to make our lives better. It happens somewhere every moment of the day, usually out of sight. It is so ubiquitous we take it for granted.

One of the most fascinating lectures I ever heard was about how the Coca-Cola Company works assiduously to make cans and bottles with fewer materials and less energy. A few decades ago, only an arrogant he-man could crush a can against his head. Today, a 90-pound weakling can do it. As a result of Coca-Cola's efforts, we have lighter containers and more resources for other things that enhance our lives. (Why environmentalists think business has an interest in using more resources than necessary continues to mystify me. Are businessmen "greedy" or not?)

Now comes news that Hewlett-Packard is developing computer parts the size of—hold on—molecules. According to researchers, we could someday have computers 100 billion (that's not a typo) times faster than the best personal computers available today. (Prediction: We'll still be impatient.) Not only that, these computers will be cheap. John Markoff of the *New York Times* writes that the researchers "envision a world in which supercomputing power is so pervasive and inexpensive that it literally becomes an integral part of every man-made object."

Markoff explains that today's computer technology is limited by the wavelength of light, which is used to create integrated circuits on silicon chips. But the research team "has found a way to build circuits using chemical processes rather than light, making the switches as small as a molecule," Markoff writes. "As a result, the researchers believe that they can make components for future computers several orders of magnitude tinier than today's smallest transistors."

The smaller integrated circuits will work much faster and use less electricity. The marginal cost of production will approach zero. Researchers say such tiny computers will per-

mit vast increases in the storage of data. But it gets more exciting than that. Markoff reports that they "could create a new class of 'Fantastic Voyage'-style machines, like sensors traveling within a person's bloodstream, issuing alerts if health problems are encountered." Who can predict what other valuable services they will render?

Scientific problems remain to be solved, and it will be several years before the tiny computers become consumer products, but we'll be hearing more about this. Watch for the term "moletronics" (molecular electronics).

Isn't capitalism wonderful?

* * *

It seemed liked a good idea. At a small, isolated private college, students were invited to use any of 20 collectively owned bicycles to get around campus. What could go wrong? Plenty, write Daniel Alban and E. Frank Stephenson in their story of the relationship between private property and responsibility.

The Clinton administration wants to make sure it can unscramble your encrypted e-mail and computer files. That requires controls on security programs that the government can't crack. Claude Morgan has a status report on this latest power grab.

The "war on drugs" has eroded property rights and a host of what are called civil liberties. Now it even jeopardizes freedom of the press. Paul Armentano demonstrates that in the name of keeping young people from using drugs, the federal government is undermining the integrity of the news media.

Wilhelm Röpke, an important German classical liberal during the darkest days of the twentieth century, would have been 100 years old this month. Richard Ebeling's appreciation of Röpke's life and work brings to our attention one of the intellectual heroes of our time.

At the center of capitalism is the entrepreneur. While big entrepreneurs like Microsoft's Bill Gates and Wendy's Dave Thomas get lots of attention, little ones, like the barber on the corner, are usually taken for granted. Joseph Fulda pays proper tribute.

Did the Federal Reserve expand or restrain the supply of money in the fateful 1920s before the stock market crash and Great Depression? In recent months, Richard Timberlake argued in these pages that the Fed practiced restraint to a fault. In a rebuttal this month, Joseph Salerno argues that the Fed was the engine of inflation that wrecked the American economy and paved the way for the New Deal.

Understanding the Fed and the depression requires an understanding of the nature of money. Bettina Bien Greaves offers a primer in the tradition of Ludwig von Mises.

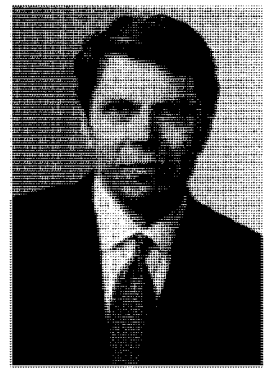
In our columns this month Donald Boudreaux discusses government, markets, and the real source of "inefficient lock-in"; Lawrence Reed asks where the omelets are; Doug Bandow documents the Medicare nightmare; Dwight Lee takes up the law of comparative advantage; Mark Skousen aims at gun control; and Walter Williams identifies a conflict of visions. Thomas DiLorenzo, contemplating the alleged need for the government to give away other people's money, declares: "It Just Ain't So!"

In the book section, reviewers evaluate works on philanthropic foundations gone astray, George Soros's lament about global capitalism, Nixon's economic record, criminal justice, the conduct of states, attempts to impede scientific progress, and the literature of the decline of Western civilization.

—SHELDON RICHMAN

Thoughts on Freedom

by Donald J. Boudreaux



Who's "Locked In" to What?

Politicians and bureaucrats are prone to overemphasize problems with the world and to propose command-and-control "solutions." Economists, sad to say, have aided and abetted that mindset with a series of suspect theories of how markets are doomed to perform inadequately.

Thankfully, not all economists have played this game. Many of the better ones have done outstanding research showing that free markets consistently deliver maximum value.

For example, while most economists 50 years ago were convinced that only vigorous antitrust enforcement could keep industries from becoming monopolized, far fewer economists today hold such a belief. One reason for this change is that a handful of researchers during the mid-century wisely re-examined the theoretical grounds supporting antitrust. (Aaron Director, Milton Friedman's brother-in-law, deserves special recognition for conveying to countless law students a deep understanding of how free markets keep unregulated industries from becoming monopolized.) But another reason is that—guided by these better theories—other researchers found persuasive evidence that the market doggedly resists monopolization. Faced with solid evidence of the robustness of unregulated markets, most economists grew appropriately skeptical of claims that markets are prone to monopolization. The perceived need for antitrust enforcement declined.

Donald J. Boudreaux is president of FEE.

New Justification for Government Activism

But government's thirst for power is unquenchable, as is the willingness of some economists to provide intellectual cover for regulatory activism. Evidence of how such activism is bolstered by new theories is the current antitrust case against Microsoft. Critical to this case is the government's charge that consumers continue to purchase Microsoft software *only* because they are "locked in" to these products.

The allegation is that most consumers want to purchase software from other suppliers, but Microsoft's very dominance locks these consumers into its products, now and forever. After all, the story goes, because a great majority of other computers currently use Microsoft's Windows operating system, it doesn't pay for you to buy another software-maker's less-expensive or technically superior operating system. If you did, your computer couldn't communicate with all those many others that use Windows.

The market, therefore, locks consumers into products and suppliers that by right ought to lose their market shares to firms offering superior deals. Naturally, the story concludes with the assertion that such inefficient "lock-in" is a widespread threat in markets and that only government can spring consumers from these traps.

This "lock-in" theory is dead wrong.

Anyone who cares to look will discover the incredible entrepreneurial dynamism that has

long characterized our market economy. If the "inefficient lock-in" tale were true, we would all still be listening to AM radio, for no one would have built an FM transmitter when virtually no one owned an FM receiver. And no one would have bought an FM receiver when virtually no one broadcast FM signals. Likewise for color televisions. And for CD players. (I recall a conversation during the early 1980s with a fellow graduate student who insisted that compact-disc recordings would never catch on because too many people owned vinyl LPs. I hope he isn't now an investment adviser.) In each of these cases, the market smoothly performed the complex task of coordinating the switch by millions of people from a less desirable to a more desirable product standard.

Not surprisingly, there's no evidence that the market dynamism that assured substantial progress for consumers in the past isn't working now in the computer industry. In a thoroughly researched new book, economists Stan Liebowitz and Stephen Margolis document not only how the market has never been inefficiently locked into old technologies or products, but also that Microsoft owes its current success to its consistency in offering quality deals to consumers.[1]

Stuck with Government

Ironically, those who demand that government police against inefficient lock-in are oblivious to the fact that it is government, not the market, that locks people into bad situations. Once created, government power seldom disappears. Statutes, regulations, and bureaucracies remain cemented in place long after their original justifications have evaporated. In short, government—not the market—is the principal source of inefficient lock-in.

Consider, for example, one of America's most regrettable government programs: Social Security. Aside from those with naked political or material stakes in this deluxe boondoggle, no one today argues that it works. That argument would be ludicrous—as was shown recently by Professors Richard McKenzie and Dwight Lee, who calculated that a 38-year-old worker today, earning no more than $40,000 annually, must live to be 143 years old before getting as good a return as he would by investing. And a worker of the same age earning at least $68,400 per year has to pray for true earthly immortality, for only if he or she lives forever will Social Security pay off.[2]

Social Security has long been known to be disastrous for young people. No sensible person would today voluntarily join this system. But join they must. The reason is that Social Security—by its very existence, by the fact that it transfers wealth from the many to the few—has created its own hardcore constituency who benefits directly from its forced continuation. Because of the gargantuan political clout of today's Social Security recipients, Americans are locked into this nefarious scheme.

Of course, there are good people working now to help liberate Americans from the Social Security trap. (For two excellent efforts, see www.socialsecurity.org and www.praonline.org.) These efforts, though, ultimately require politicians to release citizens from Social Security. Perhaps it will happen. I'm hopeful.

But no significant scale-back in government power can occur until large numbers of people are educated and mobilized to support the change. In contrast, inferior products and programs supplied by the market are assuredly and quickly doomed. No political consensus is necessary to free consumers from unresponsive suppliers. All it takes in the market is a creative idea, entrepreneurial gumption, and consumers who recognize superior bargains.

If government is to launch a campaign against programs, products, and institutions that are protected from competition—"locked in"—it had best look in the mirror. □

1. Stan J. Liebowitz and Stephen E. Margolis, *Winners, Losers, and Microsoft* (Oakland, Calif.: The Independent Institute, 1999).

2. Richard B. McKenzie and Dwight R. Lee, "Security in Old Age—and We Mean Old Age," *Wall Street Journal*, June 17, 1998, p. A16.

THE FREEMAN
Ideas On Liberty

Legalized Theft Is Good for the Poor?

It Just Ain't So!

Former U.S. Secretary of Labor Robert Reich spent the 1980s at Harvard's Kennedy School of Government spreading lies in the service of socialism. Not socialism as government ownership of the means of production but rather, as F. A. Hayek defined it in *The Road to Serfdom*, "chiefly the extensive redistribution of incomes through taxation and the institutions of the welfare state." He's at it again now that he's back in academe as a professor of social and economic policy at Brandeis University.

Reich began the decade of the '80s writing books and articles with the Marxist economist Barry Bluestone about the "deindustrialization of America," which, in their view, could only be stopped by the introduction of central planning, euphemistically called "industrial policy." But America wasn't deindustrializing. In a 1984 study published by the Heritage Foundation, I showed that the U.S. Commerce Department's Index of Manufacturing was at an all-time high, and that manufacturing as a percentage of GDP was about the same in 1980 as it was in 1950. American industry was evolving, as it always has, but it wasn't disappearing.

Then came the myth of the "great U-turn" in wages, with the average worker allegedly suffering a decline in wages and living standards. This myth was debunked by Richard McKenzie, who showed that if one considers total employee compensation, and not just wages, there is no "U-turn."

Reich and Ira Magaziner also championed the view that the Japanese system of crony capitalism was the key to that country's economic success and should be imitated by the United States. Now that the Japanese system has collapsed in a sea of corruption and bankruptcy, Reich is silent on the issue.

The late Murray Rothbard once asked Ludwig von Mises if he thought there was one single thing that designated an economy as primarily capitalist. Mises's response was yes, a vigorous private capital market. For it is capital markets that facilitate the constant reallocation of capital, guided by consumer sovereignty, in a capitalist economy. So, naturally, Reich next wrote a book and a series of magazine articles criticizing private capital markets as essentially useless, part of a "paper economy" that supposedly adds nothing to production.

The Latest Crusade

In a May 16, 1999, *Washington Post* article titled "To Lift All Boats," Reich is back to his old tricks. This time he endorses the Clinton administration's scheme to use tax dollars to set up "Universal Savings Accounts" worth up to $2,000 for citizens with incomes under $40,000 per year. Another variant of this scheme that Reich writes approvingly of is Senator Bob Kerrey's plan to give each newborn child $1,000 in tax money, along with $500 per year every year until age 21, to be deposited in a government-operated "savings account." Then there's Yale Law School's Bruce Ackerman, who favors giving every 21-year-old $80,000 of someone else's hard-earned income, no questions asked. This latter proposal really gets Reich excited. It can be funded, he says, with a mere "2 percent wealth tax on the wealthiest 40 percent of Americans." That's any family with an annual income of more than $40,000 per year, hardly what one would consider to be "wealthy." (For those who believe the tax rate under such a scheme would remain at 2 percent, I've got some oceanfront property in Arizona I'd like to sell you.)

All these socialistic share-the-wealth plans are based on profound economic ignorance. The most fundamental problem is a problem of socialism generally, as Mises pointed out in his 1922 classic, *Socialism*: "The socialist community is characterized by the fact that in it there is no connection between production and distribution. The magnitude of the share [of income] which is assigned for the use of each citizen is quite independent of the value of the service he renders."

Reich's share-the-wealth plans are just another "entitlement" (to other people's money) that will continue to destroy the work ethic by paying people for not working. Since economic reward is divorced from one's service to consumers, the principle is the antithesis of how a market economy works. Reich, however, absurdly claims that it would *expand* "the benefits of a market economy."

It would induce people to save less on their own, just as Social Security does. But once again, Reich gets everything backwards, arguing that it would "encourage saving." In reality, the reduced savings rate would diminish the rate of capital accumulation and reduce economic growth. The annual cost of the programs, which would run in the tens of billions of dollars, would in itself depress the private sector because the opportunity cost of such programs is returning those tax dollars to their rightful owners, the people who earned them.

Static View

Reich's case is based on a static view of the economy and the old socialist canard that there is a "lump" of wealth out there: if one person has more, others must have less. But the economy is dynamic; there is great mobility in a capitalist economy, and that mobility is driven by people's desire to better themselves financially and materially. Giving some of them something for nothing, as Reich's proposal does, can only diminish that incentive.

In their book, *Myths of Rich and Poor*, Michael Cox and Richard Alm examine a sample of more than 50,000 Americans from all socioeconomic backgrounds whose incomes have been tracked for more than 20 years. They found that those who started out in the bottom fifth of income earners in 1975 gained more than four times the income by 1991 than did the top fifth in 1975. In a dynamic, capitalist economy the "rich" may get richer, but the "poor" do even better.

Reich argues that the enormous flow of funds into the stock market in recent years doesn't seem to have benefited "the bottom 30 percent" very much. But those funds have financed the capital expansion and job creation that have made the U.S. economy the envy of the world. The "bottom 30 percent" has benefited as much as anyone, if not more.

Reich's share-the-wealth plan is nothing but another Ponzi scheme, not unlike Social Security, that is designed to help politicians buy the votes of a majority (the "bottom 60 percent") by taxing a minority. As Rothbard wrote in *The Ethics of Liberty*, "the State is a coercive criminal organization that subsists by a regularized large-scale system of taxation-theft, and which gets away with it by engineering the support of a majority . . . through securing an alliance with a group of opinion-moulding intellectuals whom it rewards with a share in its power and pelf." Professor Reich, take a bow.

—Thomas J. DiLorenzo
Professor of Economics
Loyola College, Maryland

THE FREEMAN
Ideas On Liberty

The "Berry Bikes": A Lesson in Private Property

by Daniel L. Alban and E. Frank Stephenson

Berry College is a private college located on a large campus adjacent to Rome, Georgia. In March 1998, the Berry College Student Government Association (SGA) used student activity funds to purchase 20 bicycles for student use on campus.

The bright red bicycles, each with an identifying plate reading "Berry Bike," were available to all students on a "first-come, first-served" basis, making them a common property resource. In spite of the relatively favorable environment for common-property bicycles at Berry, it took less than two months for many of the bikes to be lost, stolen, or abused. This story illustrates the importance of private property rights and the folly of common property.

The SGA purchased 20 Schwinn Cruiser bicycles for $190 each. The rationale for spending student fees was that the distance between some buildings on campus made getting to classes on time difficult. Several factors would seem to favor the plan. The campus is relatively self-contained; it is unlikely that townspeople would enter college property to use the bikes or that students would ride them off campus where they could be abandoned, lost, or stolen. Berry students probably have a more cooperative ethic than students at many other colleges. For example, there is relatively high participation in student organizations, many of which are campus religious groups. Observers report a tendency for students there to split the difference during in-class market simulation exercises, rather than compete to maximize personal gain, suggesting that Berry students are not unusually self-centered.

Moreover, the student body is relatively small. Anyone who abused a bicycle could be readily identified, and the students harmed by having bicycles mistreated would not be strangers. These factors would presumably deter would-be vandals. Finally, and directly pertinent, privately owned bicycles were not being lost or abused.

Dismal Results

Unfortunately, the results of the Berry bike project were dismal. It took little time for the misuse of the bicycles to become evident. Writing in the April 2, 1998, *Campus Carrier,* student Liz Hill reported that "Chains have been broken, tires punctured, handlebars bent, and seats torn" after "only a couple of weeks." Recognizing the underlying cause of the mistreatment, Hill implored students to "treat the bikes as if they were your own property." Evidently, her column spurred little change.

On April 21, SGA President M. Lynsey Morris e-mailed all students that "It has come to our attention here in the SGA office that many students are failing to take care of the Berry Bikes. . . . These bicycles are top quality and should not be bending and breaking

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COURTESY: BERRY COLLEGE

the way they are. The [SGA] officers and other students have seen many people riding the bikes at absurd speeds, doing tricks, and just abusing the bicycles in general." She too requested that students "treat [the bikes] as you would your personal property." Morris's appeal apparently met with little success; a survey at the end of the semester revealed that four of the 20 bikes were lost or stolen and 11 were in a state of disrepair—a 75 percent casualty rate in a mere two months.

Undeterred, the SGA had the bicycles repaired over the summer recess and resumed the program in the fall. It soon became apparent that the abuse would continue. The September 10 *Campus Carrier* editorialized about "mangled corpses of twisted red metal that lie about campus" and concluded that "Perhaps SGA put too much trust in human nature and Berry students' respect for property." Was that the problem? Or was it that the SGA did not understand the role of incentives? Only a month into the new semester, the SGA suspended the program with the intention of leasing the remaining bicycles to students on a semester-by-semester basis, thereby alleviating the problems associated with common-property resources.

Although it may seem cynical or impolitic to point out the failure of the project, we think just the opposite. A primary goal of college is for students to learn, both in and out of the classroom. At a cost of about $2 out of each student's activity fees, the failed Berry bike experiment provides an inexpensive example of the "tragedy of the commons" that students can remember vividly for the rest of their lives. □

THE FREEMAN
Ideas On Liberty

The Encryption Scramble

by Claude V. Z. Morgan

When law professor Peter Junger penned a small computer program for his computer-law class at Case Western Reserve University School of Law, he never dreamed he'd be battling the U.S. Commerce Department for the right to post it on his Web site.

In 1997 the Commerce Department informed Junger that he would need a special munitions export license to publish "Fiddle"—a small encryption program that scrambles computer files into gibberish—over the Internet. "When I realized that I could not publish my little program, or any other encryption program, without asking for permission from the bureaucrats," he says, "I was shocked and angry."

Junger sued the Commerce Department for violating his First Amendment rights—the fifth freedom-of-speech case filed against the department in as many years. As he argues that "Fiddle" is protected speech, U.S. software makers gather at the sidelines to await the outcome of his case. They say that the very same export regulations that prevent Junger from posting "Fiddle" on the Net could cost their industry as much as $60 billion and 200,000 high-end jobs by next year.

Domestic software makers currently command 70 percent of the world's software market, with sales that topped $135 billion at home and abroad in 1997 alone. In fact, U.S. software makers are so adroit at capturing the world market that they are currently growing at two-and-a-half times the rate of other U.S. industrial sectors. But hampered by the current regulations, they have so far managed to win only a meager portion of the world's booming encryption software market.

Critics of the Clinton administration's communications and technology policies charge that backward export regulations are blocking the industry from competing in the world market. Furthermore, they say, lagging behind in encryption sales isn't just about losing profits, it's about undermining national security.

Protecting Data

"Encryption really is the backbone of effective privacy on the Internet," says Linda Bloss-Baum, manager of public policy at the Business Software Alliance (BSA), a public-policy group representing 17 leading U.S. software makers. By converting data in files to gibberish and requiring mathematical "keys" to unlock them, encryption products have protected sensitive data from unauthorized users since the earliest days of computing, says Bloss-Baum.

Encryption guards flight-control data, telephone networks, and power grids from mishaps and sabotage. It cloaks online financial transactions, trade secrets, and sensitive business and military data. It can also be used to scramble telephone calls and e-mail. In fact, Bloss-Baum says, "without strong encryp-

Claude Morgan writes on culture and technology from his home in Portland, Maine.

tion, anyone would be able to break into your files and gain access to your identity."

But if encryption software protects sensitive data from saboteurs and high-tech mischief-makers, it can also be used to conceal that information from law-enforcement agencies, the Clinton administration argues. Citing national security and endorsements from the National Security Agency (NSA) and FBI director Louis Freeh, the administration in 1996 banned the export of all "strong" encryption software and technology to U.S. subsidiaries, trading partners, and all foreign markets. The administration defined "strong" encryption as any software with key lengths of 40 bits or more. (Each bit represents an order of magnitude in the complexity of the decoding key.)

Domestic sales and the domestic use of strong encryption remain exempt from Commerce Department regulations. Banks and other financial institutions have been given special dispensations to glide the Internet safely with strong encryption.

The administration only briefly considered raising the export bar to 56 bits when a graduate student cracked the 40-bit code in three-and-a-half hours using simple desktop computers. After similar demonstrations and pressure from high-tech industry, the administration presented software makers with this proposal: Software stronger than 56 bits can be exported to friendly nations only after a Commerce Department review and only if the code-breaking key can be held in "escrow" by a government-authorized third party. This so-called "key recovery," or "key escrow," plan would allow law-enforcement agencies to obtain keys from escrow agents in much the same way that police currently obtain evidence through search warrants or wiretaps.

So far, the plan has won few friends among industry, public-interest groups, or private citizens. The key recovery plan is riddled with administrative and ethical flaws, says David Banisar, policy director at the Electronic Privacy Information Center. It calls for centralized databases—places to store keys—that would make appealing targets. Key recovery is therefore a bad strategy that jeopardizes national as well as corporate security, says Banisar, who recently gained national notoriety spearheading a boycott against the Intel Corporation for loading its new chip, the Pentium III, with trail-blazing serial numbers. "From a social and ethical standpoint," he says, "the concept that your communication should never be private, but subject to the whims of government, turns the basic principles of free speech and privacy on their heads."

Impeding the Market

That's not the only principle turned upside down, Bloss-Baum says. Current regulations prohibit American companies from competing against foreign firms. "There are a lot of 128-bit products already out there in the marketplace," she says. "Products are being manufactured by foreign providers in countries that have no export controls on how long the bit-strength is on their encryption." Because that technology is already widely available, she says, American companies should be allowed to compete with the same types of products.

More than 900 software makers in nearly 70 countries currently produce and market strong encryption software. Foreign competitors also produce "patches" and "plug-ins" to boost weak encryption exports from the United States.

Bloss-Baum, who has been lobbying Congress to lift the ban on encryption exports for three years, says that most U.S. intelligence agencies support industry's position that encryption software can be widely and safely distributed. She, Banisar, and others point fingers at Louis Freeh for driving the administration's policy into its current regulatory waters.

"The law enforcement argument has been wagging the Administration's whole Internet policy," says Alan Davidson, counsel for the Center for Democracy and Technology (CDT), a nonprofit public-research group promoting constitutional liberties on the Internet. Davidson argues that a lack of security and privacy actually slows economic growth on the Net, leaving consumers distrustful and U.S. technology and infrastructure vulnerable.

"There are serious inconsistencies between the administration's free-market version of the Internet and the administration's law enforcement version," says Davidson. "Encryption is only the most glaring example."

Davidson believes that the export controls are destined to fail because ideas cannot be stopped at the border. "People have good encryption outside of the U.S. and they're going to keep having that," he says. "Key recovery is a real problem because it builds a backdoor that people don't like, and that jeopardizes their privacy. As a whole, the policy really leaves people without the tools they need to protect themselves on the Internet."

Vulnerability has never appealed to the pioneers of the Internet. As early as 1990, Netsurfers began inventing their own tools to shield themselves from observation.

In 1990, Phillip Zimmermann, a Denver-based software engineer, wrote a small but powerful encryption program called Pretty Good Privacy (PGP) and distributed it to friends. The program found its way onto the World Wide Web in 1991, and the Commerce Department found its way to Zimmermann in 1993.

He became the focus of a two-and-a-half-year Justice Department investigation during which he gained cyber-folk-hero status, as well as a $35 million offer from a leading software maker to purchase and distribute PGP. Zimmerman fought the Justice Department's charges, which were dropped unexpectedly in 1996.

In 1995, university professor Daniel Bernstein filed suit against the government for prohibiting him from publishing "Snuffle," another homemade encryption program. A federal judge ruled in favor of his First Amendment suit in 1997. The government promptly appealed, but in May the Ninth Circuit Court of Appeals upheld the decision. There are currently three constitutional cases challenging the export regulations in court, says Banisar. The Supreme Court is likely to hear all three.

"The government has never demonstrated, and can never demonstrate," says Junger, "any threat to security interests that would arise from my publishing my little programs. As to more serious programs, they are all available on Web sites outside the United States anyway, so allowing their publication on Web sites within the United States could not possibly endanger any United States security interest."

Government Waffling

Since April 1996 the administration has waffled on its export policy at least four times, amending, changing, updating, even reversing the Commerce Department's complicated application process. Loopholes in the regulations make it possible to export strong encryption software, says Banisar. But that process can be expensive. Software makers must document that they are trying to comply with the key recovery plan before export licenses are granted.

Loopholes have led to skirting the law. Network Associates, the current distributor of PGP and popular software like the McAfee anti-virus programs, exports PGP's 6,000 pages of raw binary code to a Swiss subsidiary, which then compiles, packages, and sells it to foreign markets. That's legal. Yet U.S. regulations forbid the California-based company from e-mailing the small compiled program abroad.

But using loopholes and complying with regulations are too expensive, software makers say. The regulations are opaque, and the review process often runs late. Foreign manufacturers are not bound by similar restraints.

It's not just encryption software like PGP that gets snared by the regulations, says Bloss-Baum. Mass-market software like Lotus Notes and Microsoft Word have encryption capabilities built into them for the domestic market. "So those parts of these programs would also be subject to the export regulations," she says.

That means that when U.S. companies submit operating systems or Internet browsers for export, says Banisar, "they either have to find an overseas partner who can provide the encryption part of the system, or they forgo the whole contract altogether."

Who currently outside the United States buys American encryption software and tech-

nology? The answer is no one. Foreign buyers show little or no interest in the bit-strength of American exports or in the prospects of handing over their keys to a U.S.-based escrow agent. CDT says not one major key recovery product is being widely used by consumers today.

The cost of buying American can be prohibitive, as well, says the BSA. U.S. industry can plan on shelling out $4.2 billion annually for the first five years to set up and maintain the key recovery system. Start-up costs for small businesses will average $2,500. Large corporations may have to cough up as much as $25,000.

Consumers will chip in $1.8 billion annually for the first five years. Escrow agents will earn $6 billion a year for keeping the consumer and business keys available to law-enforcement agencies.

Who exactly is a key recovery agent? While details of the plan remain sketchy, many analysts believe that contracts will be awarded to banks, post offices, or private mail handlers like Mail Boxes Etc., according to a security spokesman for a leading software maker. Large corporations may be allowed to "post their own centers" provided investigations and warrants can be conducted discreetly—that is, without alerting the bosses upstairs.

Freedom of Speech

Despite the business concerns, free-speech arguments will likely play a decisive role in overturning the regulations. But the law is not clear on high-tech definitions of "speech" in the information age, says Davidson. "We think that there are free-expression issues implicated by the export controls," he says. "But we're treading on new legal ground here. Its difficult getting courts to understand why there's an expressive quality to Professor Junger's little programs."

If the legal issues surrounding encryption software aren't complicated enough, says Davidson, philosophical issues about privacy in the information age are about to muddy the waters further. "This is really about some very different views of how we protect privacy online," he says. "There are two different visions: one is where individuals have the tools to be able to protect themselves; another is where we build backdoors to the system, where we rely on government to be the protector. One minute I'm e-mailing somebody down the street, but the next minute that message is going across ten different countries. And each of those countries has different laws."

Getting the lawmakers to understand that has been difficult enough, says Bloss-Baum. But for the time being, she and her colleagues plan to focus the argument on free-market principles. In 1997, she says, a handful of lawmakers endorsed federal legislation to lift the ban on encryption strengths already available on the world market. That bill failed with 205 supporters.

This year a similar bill was introduced with 210 endorsements. The Safety and Freedom through Encryption Act of 1999 (SAFE), which in March passed the House Judiciary Committee, would prohibit the government from requiring keys to be held in escrow, but the secretary of commerce would still have the power to review encryption products and control exports. On the Senate side, the PROTECT Act of 1999 (Promote Reliable On Line Transactions To Encourage Commerce and Trade) would immediately raise the bar to 64 bits and open the floodgates for exports of *any* strength by 2002. Bloss-Baum says she's optimistic that the ban will be lifted this year.

"People are already moving their lives online," says Davidson. "There has to be a very broad discussion about how we're going to protect what's seen of us online. Encryption is just one small piece of it. I think this is the first skirmish in a very long campaign." □

THE FREEMAN
Ideas On Liberty

Bought and Sold: Drug Warriors and the Media

by Paul Armentano

Americans pride themselves on their independent press. Yet some media outlets and networks are compromising their autonomy and objectivity by welcoming the federal government as a major paying advertiser. This alarming union is the latest outgrowth of the "war on drugs," and the launch of a new $775 million White House campaign to promote its objectives through television, radio, and print advertising.

The message to media moguls is simple: Promote the continuation of the drug war in advertisements, editorial content, and features, and we, as federal officials, will reimburse you by spending millions of taxpayer dollars for ads. The better government mouthpiece you are, the more advertising space we will buy.

Not surprisingly, America's print and television media hierarchy are lining up for a slice of the pie.

Last fall, the board of directors of the Magazine Publishers of America announced their participation in the federal crusade, dubbed the "National Youth Anti-Drug Media Campaign," by agreeing to run "compelling ads in their magazines and providing editorial support for their audiences." Their decision came immediately after a meeting with White House drug czar Barry McCaffrey, who urged the industry to begin a "nationwide antidrug publishing strategy."

McCaffrey found the MPA more than willing. "[We] accept the challenge presented to the magazine industry by the General [Barry McCaffrey] to join with the Ad Council, the Partnership for a Drug-Free America, and the Office of National Drug Control Policy [ONDCP]," a spokesperson for the MPA board of directors announced following the drug czar's visit. "The MPA will use its best efforts to coordinate member participation in a national magazine 'roadblock' . . . to raise the level of awareness of the campaign among parents and kids."

Disturbing Implications

The implications of the publishing industry's new alliance with the federal government are disturbing. Michael Hoyt, senior editor for the *Columbia Journalism Review*, warns that the industry's involvement sacrifices credibility and journalistic integrity. "I don't think that the MPA should be urging members to provide editorial support for anything at all," he says. "And it doesn't matter how worthy they think the cause is. That's particularly true where there can be a perceived conflict of interest, such as urging that support in return for tax dollars."

Indeed, federal officials made it clear that the MPA's portion of the White House's war chest hinged on its willingness to espouse the government's party line. "We want . . . the magazine industry to be a critical player in

Paul Armentano is the publications director for The NORML Foundation, a Washington, D.C.-based research and legal foundation that examines drug policies.

this effort," McCaffrey told the publishing heads. "However, . . . we have yet to determine exactly how much of the roughly $775 million ad dollars will go to magazines. . . . That proportion depends on your response. If you deliver the commitment of your industry, we will provide the [financial] resources necessary to deliver the message on your pages."

As expected, the drug czar's bribe achieved the desired union. Unfortunately, this is not the first time the media have enlisted in this governmental campaign. Previously, the National Association of Broadcasters announced that it would cooperate with the U.S. Department of Health and Human Services and the advertising conglomerate Partnership for a Drug-Free America to launch a nationwide television campaign demonizing marijuana's alleged dangers. The ABC television network also broadcast a month-long federally backed antidrug media blitz two years ago that raised eyebrows among many media critics.

"All of us can benefit from an honest message about the risks of substance abuse, but it must be credible," wrote national columnist Robert Scheer, who called the earlier ABC/Partnership for a Drug-Free America effort a "propaganda campaign." "The government-sanctioned anti-drug message, inserted by corporate fiat into all [ABC] programming, including news, criticizes only those vices that are not legally profitable, while the network's advertising continues to glorify those that are. Surely, those sales people at ABC know that a warning that is transparently dishonest is worse than useless."

Apparently not. Today, the White House drug-control office is one of ABC's best-paying clients. ABC accepted over $14 million in paid ads from the ONDCP in the first five months of the federal advertising campaign, more than twice as much as any other network.

ABC also combined efforts with Disney Online to establish the drug propaganda Web site, Freevibe.com, which targets visitors with baseless drug "facts" like: "Pot turns people into potheads." This statement, like most others appearing on this and other government-influenced sites, conveniently ignores the science exonerating marijuana of such "reefer madness" inspired allegations. For example, visitors will find no mention of a May 1999 John Hopkins University cognition study, the first ever to investigate the long-term effects of marijuana on mental function in a large epidemiological sample, that found "no significant differences in cognitive decline between heavy users, light users, and nonusers of cannabis."

The White House drug control office spent an additional $5.5 million on Fox, $1.8 million on NBC, $600,000 on CBS, and $800,000 on the WB Network, according to *USA Today* columnist Melanie Wells. In return, the major networks "donated" $24.4 million of free air time to promote the feds' political antidrug agenda. This public-private partnership makes the White House campaign one of the top 15 single-brand campaigns in the nation, even outspending (in unadjusted dollars) the public service campaign run during World War II in support of the war effort.

Tom Haines, chairman of the drug-policy alternatives group Partnership for Responsible Drug Information, denounces the emerging alliance among the government and media as a threat to America's free press. "We are seeing the unification of the business end of the media community and the government for an advocacy campaign where only one point of view is coming across," he says. "If this were happening in any other country, it would be denounced as propaganda."

Shifting Roles

Also critical is *New York Times* writer Frank Rich, one of the few columnists to question the shifting roles of the government and the media. This new ad campaign "may introduce a new economic model to the long and tortured history of the drug war," he wrote in a syndicated column. "Where we once had companies that laundered drug money, we now have corporations synergizing anti-drug money."

One thing is for certain, as long as there are dollars to go around, expect the networks and much of the Fourth Estate to keep buying. "One of the most surprising results we've seen has been the tremendous response by the media and entertainment industry," Alan

Levitt, who oversees advertising for the ONDCP, said in a recent interview. "They're willing to listen to what we're saying . . . and they [are] willing to change storylines."

Such may have been the case last spring when the NBC show "Hang Time" aired an ONDCP-friendly episode regarding marijuana. "When kids and teens across the nation tuned into the popular TV show, they saw a group of high schoolers catch their friends smoking marijuana, witnessed the negative consequences of drug use, and saw some real friends convince their pal to get help," the drug czar's office bragged after NBC aired the show, declaring the network had "adopted" the prevention theme in their broadcasts. Other NBC shows followed suit, including "One World," "City Guys," and "Saved by the Bell: The New Class," each emphasizing the "negative consequences" of drug use. The network and the White House also combined efforts to produce and distribute "study guide" pamphlets to public high-school students. Teachers were encouraged to use the materials as a basis for initiating drug "education" classroom discussions. "The programming and surrounding activities were made possible by a unique collaboration among the ONDCP [and] NBC television . . . , arising from the powerful messages of the National Youth Anti-Drug Media Campaign," the White House summarized.

Is the campaign really propaganda rather than good science? The federal government's marijuana policy has long been based on propaganda. Government witnesses advocated passage of America's first prohibitive federal marijuana law in 1937 by telling Congress that marijuana consumption inevitably causes violence, insanity, and death among users.

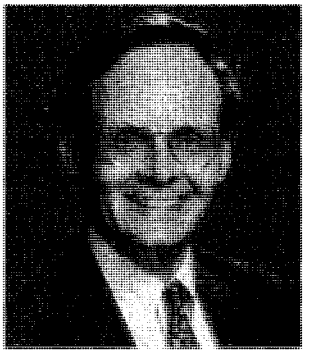
In different eras, various other myths have gained prominence (marijuana kills brain cells, marijuana causes amotivational syndrome, marijuana harms sexual maturation and reproduction, and so on), but few have been abandoned. Indeed, many of the "reefer madness" tales that were used today to generate support for early anti-marijuana laws continue to appear in the government's media campaign and bureaucratic reports today, despite scientific studies demonstrating the contrary. For example, just one month after the May 1999 National Academy of Sciences Institute of Medicine report concluded that marijuana withdrawal symptoms evidenced in humans are "mild and subtle," the federal National Institute on Drug Abuse said that marijuana smokers who abstain from the drug become aggressive. Assertions like those form the backbone of the federal antidrug campaign, while nongovernment studies that fail to find deleterious or toxic effects from marijuana and other drugs are ignored.

The unholy taxpayer-financed alliance arising among federal drug warriors and the media threatens to usher an unparalleled campaign of government propaganda into our homes, lives, and public schools. In addition, by waving taxpayer dollars, federal officials are presenting many within the Fourth Estate with a conflict of interest that threatens not only their credibility and objectivity, but also their ability to maintain a proper role as a watchdog over big government and its policies. How likely is the media to question the drug-war party line when the warriors are some of their biggest advertisers? The feds are spending $775 million of your hard-earned dollars to find out. □

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Government



Where Are the Omelets?

"On ne saurait faire une omelette sans casser des oeufs." Translation: "One can't expect to make an omelet without breaking eggs."

With those words in 1790, Maximilian Robespierre welcomed the horrific French Revolution that had begun the year before. A consummate statist who worked tirelessly to plan the lives of others, he would become the architect of the Revolution's bloodiest phase—the Reign of Terror of 1793–94. Robespierre and his guillotine broke eggs by the thousands in a vain effort to impose a utopian society based on the seductive slogan *"liberté, égalité, fraternité."*

But, alas, Robespierre never made a single omelet. Nor did any of the other thugs who held power in the decade after 1789. They left France in moral, political, and economic ruin, and ripe for the dictatorship of Napoleon Bonaparte.

As with Robespierre, no omelets came from the egg-breaking efforts of Lenin, Mao, Pol Pot, Adolf Hitler, and Benito Mussolini either.

The French experience is one example in a disturbingly familiar pattern. Call them what you will—leftists, utopian socialists, radical interventionists, collectivists, or statists—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 other people in the process. If socialism ever earns a final epitaph, it will be this: "Here lies a contrivance engineered by know-it-alls and busybodies who broke eggs with abandon but never, ever created an omelet."

Every collectivist experiment of the twentieth century was heralded as the Promised Land by statist philosophers. "I have seen the future and it works," the intellectual Lincoln Steffens said after a visit to Uncle Joe Stalin's Soviet Union. In *The New Yorker* in 1984, John Kenneth Galbraith argued that the Soviet Union was making great economic progress in part because the socialist system made "full use" of its manpower, in contrast to the less efficient capitalist West. But an 846-page authoritative study published in 1997, *The Black Book of Communism*, estimated that the communist ideology claimed 20 million lives in the "workers' paradise." Similarly, *The Black Book* documented the death tolls in other communist lands: 45 to 72 million in China, between 1.3 million and 2.3 million in Cambodia, 2 million in North Korea, 1.7 million in Africa, 1.5 million in Afghanistan, 1 million in Vietnam, 1 million in Eastern Europe, and 150,000 in Latin America.

Additionally, all of those murderous regimes were economic basket cases; they squandered resources on the police and military, built vast and incompetent bureaucracies, and produced almost nothing for which there was a market beyond their borders. They didn't make "full use" of anything except

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police power. In every single communist country the world over, the story has been the same: lots of broken eggs, no omelets. No exceptions.

F. A. Hayek explained this inevitable outcome in his seminal work, *The Road to Serfdom,* in 1944. All efforts to displace individual plans with central planning, he warned us, must end in disaster and dictatorship. No lofty vision can vindicate the use of the brute force necessary to attain it. "The principle that the end justifies the means," wrote Hayek, "is in individualist ethics regarded as the denial of all morals. In collectivist ethics it becomes necessarily the supreme rule."

The worst crimes of the worst statists are often minimized or dismissed by their less radical intellectual brethren as the "excesses" of men and women who otherwise had good intentions. These apologists reject the iron fist and claim that the State can achieve their egalitarian and collectivist goals with a velvet glove.

But whether it is the Swedish "middle way," Yugoslavian "worker socialism," or British Fabianism, the result has been the same: broken eggs, but no omelets.

Have you ever noticed how statists are constantly "reforming" their own handiwork? Education reform. Health-care reform. Welfare reform. Tax reform. The very fact that they're always busy "reforming" is an implicit admission that they didn't get it right the first 50 times.

The list is endless: Canadian health care, European welfarism, Argentine Peronism, African postcolonial socialism, Cuban communism, on and on ad infinitum. Nowhere in the world has the statist impulse produced an omelet. Everywhere—it yields the same: eggs beaten, fried, and scrambled. People worse off than before, impoverished and looking elsewhere for answers and escape. Economies ruined. Freedoms extinguished.

It is a telling conclusion that statists have no successful model to point to, no omelet they can hold up as the pièce de résistance of their cuisine. Not so for those of us who believe in freedom. Indeed, economists James Gwartney, Robert Lawson, and Walter Block in their survey, *Economic Freedom of the World: 1975–1995*, conclude that "No country with a persistently high economic freedom rating during the two decades failed to achieve a high level of income. In contrast, no country with a persistently low rating was able to achieve even middle income status. . . . The countries with the largest increases in economic freedom during the period achieved impressive growth rates."

Perhaps no one explained the lesson of all this better than the French economist and statesman Frederic Bastiat more than 150 years ago:

"And now that the legislators and do-gooders have so futilely inflicted so many systems upon society, may they finally end where they should have begun: May they reject all systems, and try liberty; for liberty is an acknowledgment of faith in God and His works." □



THE FREEMAN
Ideas On Liberty

Wilhelm Röpke: A Centenary Appreciation

by Richard M. Ebeling

On January 30, 1933, German president Paul von Hindenburg appointed Adolf Hitler chancellor of Germany. One week later, on February 8, Wilhelm Röpke, a 32-year-old professor of economics at the University of Marburg, delivered a lecture in Frankfurt am Main with the title "End of an Era?"

Röpke told his audience that Germany was in the grip of a "revolt against reason, freedom and humanity." The National Socialists under Hitler were now the dominant force in an attack against the fundamental principles of liberalism and Western civilization. Liberalism, correctly understood, represented a 2,000-year-old intellectual heritage of political, civil, and economic liberty. Liberty required the rule of reason, resting on "truthfulness instead of obscurantism, clarity instead of hysteria, the advancement of knowledge instead of sensationalism for the masses, logic instead of wallowing in moods and emotion. . . . It is only the liberal ideal of the use of Reason in the service of truth that has engendered science . . . that alone has liberated Europe from the stupor and wretchedness of barbarism."

An additional element in the philosophy of liberalism, rightly understood, Röpke explained, was the idea of humanity. "The idea of humanity is seen in all its full significance when conceived as the rejection of the principle of violence in favor of the principle of reason. Violence is relegated to the very bottom of the scale of value; its use is admitted only as a last resort and with the utmost reluctance. This, ultimately, is the essence of civilization."

But Nazism was the culmination of Germany's sinking into "illiberal barbarism," Röpke said, the elements of which were based on: (1) "servilism," a "longing for state slavery," with the state becoming the "subject of unparalleled idolatry"; (2) "irrationalism," in which "voices" in the air called for the German people to be guided by "blood," "soil," and a "storm of destructive and unruly emotions"; and (3) "brutalism," in which "The beast of prey in man is extolled with unexampled cynicism, and with equal cynicism every immoral and brutal act is justified by the sanctity of the political end." Röpke warned that, "a nation that yields to brutalism thereby excludes itself from the community of Western civilization." He hoped Germany would step back from this abyss before its people had to learn their mistake in the fire of war.[1]

Röpke also spoke out against the Nazi dismissal of Jewish professors and students from German universities, which began in April 1933. The Nazis denounced him as an "enemy of the people" and removed him from his professorship at the University of Marburg. After an angry exchange with two SS men sent to "reason" with him, Röpke decided to leave Germany and accept exile rather than live under National Socialism.[2]

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Leading Figure

Wilhelm Röpke was a leading intellectual figure of twentieth-century Europe. He combined conservatism with classical liberalism to develop a political philosophy he called a market-oriented "middle way" between nineteenth-century capitalism and twentieth-century totalitarian collectivism. He also became a spiritual guide and political-economic architect of Germany's "social market economy" in the post-World War II era. As Ludwig von Mises wrote when Röpke died in 1966 at the age of 66,

> For most of what is reasonable and beneficial in present-day Germany's monetary and commercial policy credit is to be attributed to Röpke's influence. He—and the late Walter Eucken—are rightly thought of as the intellectual authors of Germany's economic resurrection. . . . [T]he future historians of our age will have to say that he was not only a great scholar, a successful teacher and a faithful friend, but first of all a fearless man who was never afraid to profess what he considered to be true and right. In the midst of moral and intellectual decay, he was an inflexible harbinger of the return to reason, honesty and sound political practice.[3]

Röpke was born October 10, 100 years ago in Hanover, Germany. He grew up in a rural community of independent farmers and cottage industry craftsmen. His father was a country doctor. That upbringing can be seen in his later belief that a healthy, balanced, small community is most fit for human life.

The event, however, that shaped his chosen purpose in life was his experience in the German army in the First World War. War was "the expression of a brutal and stupid national pride that fostered the craving for domination and set its approval on collective immorality," Röpke explained. The experience of war made him decide to become an economist and a sociologist when the cannons fell silent. He entered the University of Marburg, from which he earned his doctoral degree in 1921. At first, Röpke thought that socialism was the answer to the world's problems. But he soon discovered that the only realistic solutions were to be found in classical liberalism and the market economy.[4] Among the most important influences in that discovery were the writings of Austrian economist Ludwig von Mises. "It was his book, *Nation, State and Economy* (1919) . . . which was in many ways the redeeming answer to the questions tormenting a young man who had just come back from the trenches," Röpke wrote. And it was Mises who "rendered me immune, at a very early date, against the virus of socialism with which most of us came back from the First World War."[5]

In 1922, Röpke became an adviser to the German government on the problems of reparation payments resulting from the Treaty of Versailles. From 1924 to 1928 he was a professor at the University of Jena, spending part of the time, in 1927–1928, in the United States studying American agrarian problems under the auspices of the Rockefeller Foundation. After returning to Europe he was a professor of economics at the University of Graz, Austria, in 1928–1929. In 1929 he was appointed professor of economics at the University of Marburg, a position he held until his expulsion by the Nazi regime in 1933. He also served as a member of the German National Commission on Unemployment in 1930 and 1931, and as an adviser to the German government in 1932.

After leaving Germany in 1933 he accepted a position at the University of Istanbul, Turkey, which he held until 1937, and during which he undertook the reorganization of its department of economics. He also founded and was the first director of the Turkish Institute of the Social Sciences.

Teaching Career in Geneva

In 1937 he was invited to become a professor of international economic relations at the Graduate Institute of International Studies in Geneva, Switzerland, a position he retained until his untimely death on February 12, 1966. The Graduate Institute had been founded in 1927 by the famous economic historian Paul Mantoux and the internationally respected economist, political scientist, and leading

classical liberal William E. Rappard. In the Graduate Institute's comfortable building overlooking Lake Geneva, Röpke took up his teaching duties. He was in the company of such colleagues as Mises, the eminent Italian historian Guglielmo Ferrero (an exile from the fascist regime in Italy), the Polish free-market economist Michael Heilperin, and the Austrian legal philosopher Hans Kelsen.

After the German occupation of France, Röpke was three times offered a teaching position at the New School for Social Research in New York (in 1940, 1941, and 1943) as a means of escape from Nazi-occupied Europe. But each time he turned down the invitation to leave neutral Switzerland, having decided to continue to be a voice for freedom and reason in a totalitarian-dominated Europe. In the immediate aftermath of the Second World War, Röpke circulated a memorandum offering a "plan for an international periodical" that would be devoted to the restatement and defense of classical liberalism and the free-market economy against all forms of political and economic collectivism. The journal was never established, but the ideas conveyed in the memorandum served as support for F. A. Hayek's successful founding of the Mont Pelerin Society in 1947, an international association of scholars and opinion makers dedicated to the philosophy of freedom. Röpke served as the society's president from 1960 to 1962.

In the 1950s, he was an economic adviser to the government of West Germany. He also was one of the leading figures of a group of market-oriented German economists who in the postwar period became known as the Ordo-liberals; their purpose and goal was the construction of a "social market economy" that assured both an open, competitive order and minimal social guarantees.[6]

Business-Cycle Theory

In the 1920s and for part of the 1930s, a primary focus of Röpke's writings was business-cycle theory and policy. His most significant work in this field was his 1936 volume *Crises and Cycles*, which summarized and elaborated on his earlier writings, mostly in German, on the subject.[7] Röpke argued that a complex division of labor with a developed structure of roundabout methods of production, held together by the delicate network of market prices for finished goods and the factors of production, had the potential to occasionally suffer from the cyclical waves of booms and depressions. The cause of such cycles was periodic imbalances between savings and investment in the economy. While not completely following the "Austrian" theory of the business cycle, Röpke's approach moved along similar lines, arguing that a monetary expansion that kept the market rate of interest below the level that could maintain a balance between savings and investment would feed investment projects and cause misdirections of labor and resources into production processes in excess of the savings available to sustain them in the long run.

Röpke's particular contribution to the analysis of the business cycle was his theory of what he called the "secondary depression." When the boom ended, an economic downturn was inevitable, with the investment excesses of the upturn having to contract and be readjusted to the realities of available savings and the market-based patterns of supply and demand. But while serving on the German National Commission on Unemployment in 1930–1931, he came to the conclusion that there were negative forces at work at that time far beyond any normal type of post-boom adjustment. The failure of cost prices to promptly adjust downward with the decline of finished-goods prices was causing a dramatic collapse of production and employment. Rising unemployment resulted in declining incomes that then created a new round of falling demands for goods in the economy, that in turn brought about another decrease in production and employment. At the same time, growing unprofitability of industry made businessmen reluctant to undertake new investments, resulting in the accumulation of idle savings in the financial markets. Such a sequence of events generated a cumulative contraction in the economy that kept feeding on itself.

Röpke concluded that this secondary depression served no healthy purpose, and the downward spiral of a cumulative contraction

in production and employment could only be broken by government-induced credit expansion and public-works projects. Once the government introduced a spending floor below which the economy would no longer go, the market would naturally begin a normal and healthy upturn that would bring the economy back toward a proper balance.[8]

In 1933, when Röpke published in English an article explaining the findings of the German Commission on Unemployment, John Maynard Keynes expressed to Röpke his "great satisfaction" that German economists were reaching the same conclusions as he had, namely, that government needed to take an active role in steering the economy. But Röpke had no sympathy for Keynes's belief that the market was inherently unstable and permanently in need of government management of "aggregate demand." In Röpke's view the Great Depression represented a "rare occurrence" of an "exceptional combination of circumstances" that required "a deliberate policy of additional 'effective demand' into the economic system." But, Röpke continued, Keynes's construction of a "general theory of employment" based on the exceptional circumstances of the early 1930s was a "counsel of despair" and an extremely dangerous one, because it created a rationale for continuous government tinkering and a strong inflationary bias harmful to the stability of the market economy in the long run.[9] Indeed, Röpke became a leading critic of Keynesian economics after World War II.[10]

The Crisis of Western Civilization

But the central issue that absorbed almost all of Röpke's intellectual and literary efforts in the 1930s and 1940s was what he considered the crisis of Western civilization, the most stark and terrible symptom of which was the rise of totalitarian collectivism as represented by Soviet communism, Italian fascism, and German National Socialism. He devoted all his efforts to opposing and challenging this horrible trend in a series of important and highly influential books. In 1937 he published *Economics of the Free Society*, a treatise on economic principles that not only explained and defended the market economy, but also strongly criticized the ideas of socialism and interventionism.[11] This was followed in 1942 by *International Economic Disintegration*, in which he detailed the disastrous consequences that collectivist economics produced by destroying the international division of labor through trade restrictions, exchange controls, government planning, domestic interventions, and policies of national self-sufficiency.[12]

But the heart of Röpke's critique of the decay of Western civilization and the path for its renewal was in a trilogy published during the war: *The Social Crisis of Our Time*, *Civitas Humana* (later re-issued as *The Moral Foundations of Civil Society*), and *International Order*.[13] This was followed at the end of the war by *The Solution of the German Problem* (1945).[14] And a further reformulation of his conception of a properly ordered and balanced society was offered in *A Humane Economy: The Social Framework of the Free Market* (1958).[15]

The achievements of the eighteenth century, in Röpke's view, were the use of reason for a balanced understanding of both the natural and social world; the awakening of an insight into the possibilities of a free, spontaneous order of market relationships; a conception of man that looked at him in proportionate human terms; and a sense of humanity in appreciating and wanting to improve the human condition. Out of these insights came the physical and biological achievements of modern science and medicine; a free-market order that both liberated man from the status and caste society of the past and dramatically improved his standard of living; and the liberal, democratic ideal in which the individual possessed rights to life, liberty, and property, and in which peace and tolerant political pluralism replaced imperial violence and political absolutism.

But as Röpke saw it, many of these achievements and successes had been twisted in the nineteenth century. The use of reason had become "unreasonable," as there emerged a hyper-rationalism that claimed to have the power to discover the secrets for social engineering. The triumphs of the natural sciences in mastering the physical world had fostered a

"cult of the colossal," in which there was a worship of the things of the material world and the desire for the creation of objects bigger than human life. The grand accomplishments of the market economy had not only freed man from his previous social restraints, but cut him loose from all the societal moorings of family, community, and the harmonies of local life, and in its place reduced man to a proletarianized "mass" in an anonymous, impersonal urban existence. And the ideal of democratic pluralism had been undermined and reduced, increasingly, into an arena of special-interest political plunder.

"Termite State"

The loss of traditional human connections, the dehumanization of man in mass society, and the corruption of the political and economic marketplaces, Röpke argued, had created the sociological and psychological conditions for the emergence of and receptivity to the collectivist idea and its promise of a new community of man, a transformation of the human condition, and a better society designed according to a central plan. All these were false promises and hopes. Collectivism, whether of the fascist or communist sort, meant the end of a rational economic order, threatened the loss of freedom and the end to human dignity, and required the reduction of man to the status of an insect in what Röpke often referred to as the socialist "termite state."

Röpke was uncompromising in his insistence that only the market economy was consistent with both freedom and prosperity. Only the market, with its system of private property rights, provided the framework to harness individual incentives and creativeness for the benefit of society. Only the market could generate the competitive process necessary for the formation of prices that could successfully coordinate supply and demand. Only the market gave each individual the freedom to be an end in himself while also serving as a voluntary means to the ends of others through the mechanism of exchange.[16]

Yet in Röpke's view the market by itself was not enough. The humane society required going "beyond supply and demand," to the construction of an institutional order that incorporated the market in a wider social setting. It was in this context that Röpke proposed the distinction between "conformable" and "nonconformable" interventions in the market. Nonconformable interventions went against the natural workings of the market through the introduction of price and production controls, which disrupted the normal coordinative processes of market competition. Conformable interventions influenced the underlying supply and demand conditions, and the institutional arrangements on which those conditions are based, for the purpose of modifying the results that competitive process would generate.

Röpke, for example, believed that: antitrust laws were necessary and desirable as a method of limiting some private industrial concentration; urban development restrictions were needed to limit the growth of city size and foster a retention of rural life; income redistribution was legitimate to narrow significant income inequalities; and moderate and limited welfare "safety net" programs were consistent with a humane society that remained essentially market-oriented. In fairness to Röpke it should be pointed out that in the wake of the Great Depression and the growing appeal of socialist planning, a large number of market-oriented economists at the time accepted a greater degree of interventionism and welfare-statist programs than many free-market economists would consider legitimate nowadays.[17]

But by the 1950s, Röpke began to have serious second thoughts about the welfare state and its tendency to grow beyond the narrow bounds that he considered reasonable.[18] Röpke agreed with his German liberal colleague Alexander Rustow, who in a paper delivered at a Mont Pelerin Society meeting in the 1950s referred to the welfare state as "the other road to serfdom." Röpke feared that the welfare state, in a democratic system open to the pressures of special-interest groups, threatened to grow to monstrous proportions and create an increasing dependency on the paternalistic state. Furthermore, the costs of funding the welfare state and Keynesian "full employment" policies acted as an engine for

worsening inflation as government resorted to the printing press to pay its bills.[19]

Finally, Röpke argued that the growing politicization of economic and social life through an expanding interventionist-welfare state undermined the possibility for a successful international order based on peace, mutual prosperity, and a rational allocation and use of the resources of the world. International order required countries to practice sound policies at home: respect for private property, enforcement of contracts, protection for foreign investments, limited government intervention, and non-inflationary monetary policies. Networks of international trade and investment would then naturally and spontaneously connect the world through private market relationships.[20] For this reason, Röpke was doubtful that European economic and monetary integration could be successfully imposed as long as the member states were unwilling to follow the necessary domestic policies of limited government and open, competitive market capitalism. Tensions and conflicts were inevitable in an age dominated by collectivist and interventionist ideas.[21]

Wilhelm Röpke was more than just an economist. During some of the darkest decades of the twentieth century, he sounded more like an Old Testament prophet warning of the dangers from a loss of our moral compass. Collectivism had few opponents in our century with as much of a sense of ethical purpose. Precisely because he was an economist by training, Röpke understood the indivisibility of personal, political, and economic freedom in a way that many other critics of socialism in its various forms could never articulate. The appreciation of history and the historical context in his analyses only enriched the persuasiveness of his message. The rebirth of the market economy in Germany and in other parts of Europe after 1945 owes a great deal to his intellectual efforts and legacy. □

1. Wilhelm Röpke, "End of an Era?" [1933] in *Against the Tide* (Chicago: Henry Regnery, 1969), pp. 79–98.

2. Wilhelm Röpke, *The Solution of the German Problem* (New York: G. P. Putnam's Sons, 1947), pp. 59–60; and J. Kaufmann, "In Memoriam, Wilhelm Röpke: Humanistic Liberal," *Nieuwe Rotterdamsche Courant,* February 19, 1966.

3. Ludwig von Mises, "Wilhelm Röpke, RIP," *National Review,* March 8, 1966, p. 200; also, F.A. Hayek, "Tribute to Röpke," in Peter G. Klein, ed., *The Collected Works of F. A. Hayek, Vol. 4: The Fortunes of Liberalism* (Chicago: University of Chicago Press, 1992), pp. 195–97.

4. Wilhelm Röpke, "The Economic Necessity of Freedom," *Modern Age,* Summer, 1959, pp. 227–36.

5. Wilhelm Röpke, "Homage to a Master and a Friend," *The Mont Pelerin Quarterly*, October 1961, p. 6.

6. For an account of the German Ordo-liberals and Röpke's contribution to their ideas and policies, see Anthony J. Nicholls, *Freedom with Responsibility: The Social Market Economy in Germany, 1918–1963* (Oxford: Clarendon Press, 1994); for a critical comparison of the Ordo-liberals with the Austrian economists, especially Mises, see my "The Limits of Economic Policy: The Austrian Economists and the German ORDO Liberals," in Richard M. Ebeling, ed., *The Age of Economists: From Adam Smith to Milton Friedman* (Hillsdale, Mich.: Hillsdale College Press, 1999), pp. 145–66.

7. Wilhelm Röpke, *Crises and Cycles* (London: William Hodge Co., 1936).

8. Wilhelm Röpke, "Trends in German Business Cycle Policy," *The Economic Journal*, September 1933, pp. 427–41.

9. Wilhelm Röpke, "Keynes Revisited," *National Review*, March 26, 1963, pp. 239–41.

10. Wilhelm Röpke, "The Economics of Full Employment" [1952], reprinted in Henry Hazlitt, ed., *The Critics of Keynesian Economics* (Princeton: D. Van Nostrand Co., 1960), pp. 362–85.

11. Wilhelm Röpke, *The Economics of the Free Society* (Chicago: Henry Regnery Co., 1963 [1937]).

12. Wilhelm Röpke, *International Economic Disintregration* (Philadelphia: Porcupine Press, 1978 [1942]); also "International Economics in a Changing World," in William E. Rappard, ed., *The World Crisis* (Freeport, N.Y.: Books for Libraries, 1969 [1938]), pp. 275–90; "Fascist Economics," *Economica*, February 1935, pp. 85–100; and "Totalitarian 'Prosperity,' Where Does It End?" *Harper's Magazine*, July 1939, pp. 165–70.

13. Wilhelm Röpke, *The Social Crisis of Our Time* (New Brunswick: N.J.: Transaction Publishers, 1992 [1942]); *The Moral Foundations of Civil Society* (New Brunswick, N.J.: Transaction Publishers, 1996 [1944]); *International Order and Economic Integration* (Dordrecht, Holland: D. Reidel Co., 1959 [1945]).

14. Wilhelm Röpke, *The Solution of the German Problem* (New York: G. P. Putnam's Sons, 1947 [1945]); also "The German Dust-Bowl," *The Review of Politics*, October 1946, pp. 511–27.

15. Wilhelm Röpke, *A Humane Economy: The Social Framework of the Free Market* (Chicago: Henry Regnery, 1960 [1958]).

16. Wilhelm Röpke, "The Problem of Economic Order" [1951], reprinted in Johannes Overbeck, ed., *Two Essays by Wilhelm Röpke* (Lanham, Md.: University Press of America, 1987), pp. 1–45.

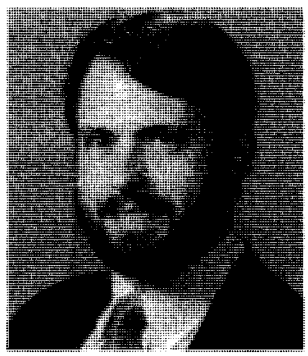
17. Among American market-oriented economists in the 1930s and 1940s who shared some of Röpke 's views on these policy issues were Henry Simon and Jacob Viner at the University of Chicago, and Frank Graham at Princeton University; in Europe the group included F. A. Hayek and Lionel Robbins at the London School of Economics, Walter Eucken and many other market economists in Germany, and Eli Heckscher in Sweden.

18. Wilhlem Röpke, "Is the German Policy the Right One?" [1950] in Wolfgang Stutzel, Christian Watrin, Hans Willgerodt, Karl Hohnmann, eds., *Standard Texts on the Social Market Economy* (New York: Gustav Fischer, 1982), pp. 37–48.

19. Wilhelm Röpke, "Welfare Freedom and Inflation" [1964] in Overbeck, pp. 49–103; also "Repressed Inflation" *Kyklos*, vol. 1, no. 3, 1947, pp. 242–53; "Inflation—Hot and Cold," *National Review*, January 18, 1956, pp. 15–17; and "The Creeping Inflation of Our Times and Values," *Freedom and Union*, September 1961, pp. 12–15.

20. Wilhelm Röpke, "Economic Order and International Law," in *Recueildes Cours*, vol. 86, pt. II, 1954, pp. 202–71.

21. Wilhelm Röpke, "Political Enthusiasm and Economic Sense: Some Comments on European Economic Integration," *Modern Age*, Spring 1958, pp. 170–76; *A World Without a World Monetary Order* (Johannesburg: South African Institute of International Affairs, 1963); "European Economic Integration and Its Problems" *Modern Age*, Summer 1964, pp. 231–44; "European Prosperity and Its Lessons," *South African Journal of Economics*, September 1964, pp. 187–98; and "The Place of the Nation: Beyond the One World," *Modern Age*, Spring 1966, pp. 119–30.



Health Care: Over the Canadian Cliff?

Everyone in Washington recognizes that Medicare is headed over a financial cliff. The growth in spending continues to outpace that of revenues; America's aging population will increase the gap as we enter the next century. Obviously serious reform is a must.

So what does President Bill Clinton propose? A massive taxpayer bailout combined with tighter price controls on existing providers, subsidies for employers who cover retirees, and expanded benefits for program recipients. The GOP Congress, lacking both philosophical principle and political courage, has done little more than mumble that it too desires to reform Medicare. It is the sort of irresponsible behavior that we've come to expect from Washington.

The Clinton package would be dubious enough if the administration's cost estimates could be taken seriously. Alas, federal health-care programs always end up more expensive than predicted. Medicare, Medicaid, renal dialysis coverage, and the short-lived catastrophic health-care initiative all suffered from soaring costs almost immediately.

For instance, within eight years after Medicare's creation, that program's tax rate was running at twice the initial projections; Medicare now spends well over 75 times what it did in its first full year. In fact, at Medicare's inception the House Ways and Means Committee predicted that the hospital insurance (HI) portion would cost $9 billion in 1990, a staggering $58 billion underestimate. HI outlays first exceeded $9 billion in 1974.

The initial costs of Medicare's kidney dialysis program, passed in 1972, were more than twice projected levels. And just eight months after passage of the 1988 Medicare Catastrophic Coverage Act, quickly repealed in response to a firestorm of popular protest, the Congressional Budget Office hiked its five-year cost estimates by upwards of 100 percent. The problem is endemic to third-party payment programs, which naturally inflate demand and thus expenditures.

There's no reason to believe that the administration's proposed pharmaceuticals coverage would be any different. On average, people with insurance use as much as 60 percent more physicians' services and three times as much hospital care as uninsured people. America's staggering health-care cost increases in recent years largely stem from what is essentially cost-plus medicine predicated on third-party payment of most medical expenses.

The inevitable response of future Congresses and presidents to soaring costs would be to impose price controls on prescription drugs, just as on other treatments. However, such past efforts have achieved little.

Congress has steadily tightened its reimbursement policy over the last couple of decades, yet federal outlays for Medicare still jumped from $32 billion in 1980 to an astounding $205 billion this year. The succeeding waves of price controls did, however, reduce services for Medicare recipients. Lim-

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its on drug prices would hinder the development of new pharmaceuticals, as well as restrict patient access to drugs.

Unfortunately, the United States seems to be slowly slipping into the sort of collectivist health care that dots the globe. Whatever the actual intent of a succession of presidents and legislators, their endless interventions—provider payments, business subsidies, polyglot regulations, and price controls—are turning the health market into a government-run system.

That we don't want to go there should be evident from the experience of the highly touted Canadian system. Once promoted by a significant segment of the Democratic party as the answer to America's health-care crisis, it is now suffering rising costs and declining quality.

The most important benefit of single-payer medicine theoretically is its thrift. Yet the only way Canada has been able to constrain spending while offering "free" care has been to explicitly ration medical services. The Vancouver-based Fraser Institute last year estimated that 187,416 people were on surgical waiting lists, up from 172,766 the previous year. Waiting times, too, were up—11.9 weeks to see a specialist after referral by a general practitioner, for instance. It takes another 6.8 weeks to actually receive treatment.

In Toronto "emergency" heart patients are operated on within 48 hours. "Urgent" cases have to wait up to six weeks. Elective patients can sit for four months or more, and year-plus waits are common elsewhere in Canada. One Canadian doctor wrote the *New York Times* to complain that "the risk of dying on the waiting list for cardiac surgery is greater than the actual operative risk."

Equipment that Americans take for granted is rare: Tennessee has more magnetic resonance imagers than does all of Canada. As a result, Canadians with brain tumors have to wait up to a year for an MRI scan. It typically takes three months to receive a CAT scan (though pets with paying owners can be tested within a day!). The United States has three times as many lithotriptors, which smash gall and kidney stones with sound waves, per patient as does Canada. On average, cancer patients wait three times as long as Americans for treatment; they are routinely denied cancer treatment for longer than what their doctors consider to be clinically reasonable.

The problem involves more than high-tech procedures. In Montreal an obstetrician was suspended for exceeding his hospital-imposed quota of deliveries. Delays of months for operations on hands, hernias, cataracts, hip transplants, varicose veins, and tonsils are typical. Patients have to wait even if they are in pain and have limited physical mobility. Yet the Fraser Institute reports that the delays only get worse year after year.

In fact, Canada's arbitrary budget controls caused the province of Ontario to shut entire hospitals during Christmas 1993. Explained Theodore Freedman, president of Toronto's Mount Sinai, which was shuttered for two weeks, "This is not about health care. This is about the deficit." Hospitals have also temporarily dropped specific practices, such as neurosurgery, to save money, and have refused to reopen even for emergency cases.

Ironically, despite these draconian efforts to contain costs, health care isn't really cheaper in Canada. After accounting for differences in population—America has a larger proportion of elderly, poor urban dwellers, and war veterans, all of whom use more health care—and including costs of tax collection, Canada spends roughly the same share of its GDP on health care as the United States. Indeed, in recent years Canada's spending has been rising faster than America's.

The United States faces a stark choice regarding health care: government control or a free market. Medicare's impending collapse should concentrate legislators' minds. Instead of approving the President's counterproductive package of greater government spending and regulation, Congress should emphasize individual responsibility and private choice. □

THE FREEMAN
Ideas On Liberty

My Barbers

by Joseph S. Fulda

When Alex, my Greek barber, retired, I tried several haircutters before settling on a barbershop on West 180th Street on the corner of Broadway, up a bit toward Fort Washington Avenue, in New York. Although Spanish-speaking like all the neighborhood's barbers, the three barbers working at this shop were able to understand my instructions. They did a really fine job, too.

Some years passed, and they grew increasingly disenchanted with the new owner of the store, who wanted them to pay for their own tools of the trade and wouldn't allow them common decencies. So what did they do? Sue? No. File a complaint with a city, state, or federal agency? No. In the best American individualist tradition, they quit to go into business for themselves. To this day the owner of that barbershop has not found success in his replacements. But our heroes pooled their money, bought equipment, and a mere month or two later were in business again—as the competition, located on West 180th Street on the corner of Broadway diagonally across from their old place, a bit down toward Wadsworth Avenue.

They did well in that location, and one of the three eventually retired. The barbershop was located in the first chamber within the building. Through the outer door, one could bypass the barbershop and go behind it. I never knew what went on in that part, as there was neither an exit from the barbershop toward the back nor a window. I was eventually to find out when one day, needing a haircut, I came across the store padlocked with a prominent sign: Closed by order of the New York State Supreme Court—Illegal Gambling site. (In New York, the Supreme Court is the court of first resort for serious cases.)

Of course, I had all the libertarian reactions—but of more immediate interest, I still wanted my hair cut! I went next door to the travel agency to ask what had happened. There in the waiting room's corner was a barber chair with equipment and supplies and one of the two barbers. This resourceful man had persuaded the travel agency to rent him enough work space to do his job. Meanwhile, I learned, the other barber was working at home on Pinehurst Avenue just north of West 180th Street.

Sensing a story, I began to ask questions. The barbers had not known what was going on in the back—and did not care—and hoped the store would soon be allowed to reopen. The authorities did allow them to take possession of their property, after all. (Remember, the state, not the federal government, shut the place down.) The travel agent told me that business was slow and she was more than happy to have the barber defray some of her expenses. The neighborhood, you see, is comprised of numerous immigrants who return frequently to their native countries; travel

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agencies flourish, but there is stiff competition among them for the large market.

Still Partners

I continued to use my barbers, going sometimes to one, sometimes to the other. As a libertarian, I felt a special need not to help the state destroy these men's living—and I recalled that when Alex retired and I started looking for a replacement, I got some fairly unwelcome haircuts in the interim! I learned in discussions with them that my barbers remained partners, splitting their expenses and proceeds. The small space was not designed for comfort, but the haircuts were still up to par. Unfortunately, their hope to reopen their store was not to be realized, as a restraining order was eventually posted on their old place of work.

Undaunted, the two barbers showed their resourcefulness yet again and somehow managed to obtain a store on Broadway between West 180th Street and West 179th Street. The reader can visit them there and attest to the truth of this tale while having his hair cut.

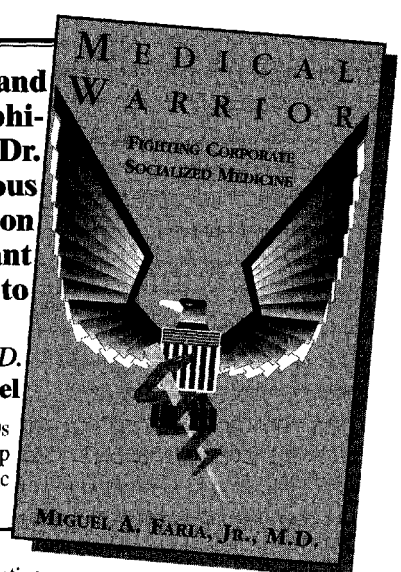
The qualities these barbers showed in the face of market adversity (the change of owners in their original place and the bad working conditions) and government obstacles are not just resourcefulness, ingenuity, and determination. They also benefited from their ability to cooperate—none would have been able to open their second store without the other two and neither of the remaining barbers would have been able to open the third store without the other. I suspect most people would have severed the partnership or acted in a way that would have made maintaining it an insuperable obstacle—and that would have proved their undoing.

These three entrepreneurs and countless others like them across this land are the real, if unsung, heroes of American capitalism. Their stories do not make for captivating biography; they are not the stuff of heroic novels; they are neither titans of industry, nor great innovators, inventors, or investors. But they epitomize the Franklinesque virtues that made America great, and they and others like them are the reason why not everything in this fair land is sold in chains and franchises, as marvelous as those bulwarks of capitalism have admittedly proven themselves. They're the sort of entrepreneurs who provide much more than labor and capital in a felicitous combination; they give the word "independent" a strong, favorable cast. □

"With his masterful grasp of history and his ingenious insight into economics, philosophy, politics, and human nature, Dr. Faria has provided us with an enormous contribution to the recent literature on health care reform, and an important weapon in our life-or-death struggle to preserve private medicine."

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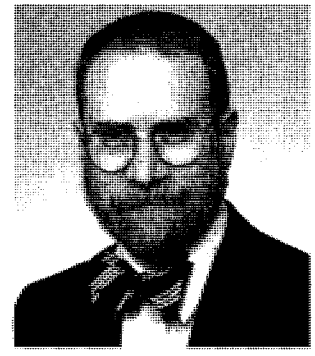
Miguel A. Faria, Jr., M.D. argues that managed care and HMOs are not "free market" alternatives, but rather an unholy partnership of government and corporate interests seeking monopolistic government protection to eliminate competition...





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The Love of Economics

I attended a lecture recently on romantic relationships, and some in the audience became agitated when the speaker invoked economics in his analysis. Beyond the obvious financial issues, many people just did not understand what economics has to do with dating and marriage. This points to an unfortunate feature of many people's understanding of economics.

Economics is not primarily about money and stock markets. Those are topics within economics. Economics is the study of certain implications and consequences of human action; hence the title—*Human Action*—of Ludwig von Mises's magnum opus.

"Human action is purposeful behavior," Mises writes at the start of his treatise. We can identify a long series of facts about human action without doing "research." This is what distinguishes economics from physics. In economics the unit of analysis is the individual, which we know from the inside, so to speak. As human beings we can observe introspectively the features of action. In contrast, when we observe stars or molecules, we are outsiders. We can make repeated observations and experiments to discover the principles and relationships of entities, but we cannot have the same intimate knowledge that we can have about human action.

We can all readily see that when we act, certain things must be true. An action consists in the pursuit of an objective, or end, using means perceived as appropriate to its accomplishment. This has many implications. Acting is choosing. To pursue an end is to choose it from an array of alternatives, including the option of "doing nothing." To embark on a course of action intended to obtain an end is a form of exchange. The actor opts for the intended state of affairs over the future circumstances envisioned in the absence of the action. Implicit in the necessity of choice is the idea of scarcity. All means, beginning with time, are scarce. You can't choose A and non-A at the same time and in the same respect. You can't "have it all."

Opportunity Cost

If action entails choosing one thing rather than another, all action requires giving something up, namely, the most highly valued alternative not pursued. The alternative forgone is the cost of the action, more precisely, the opportunity cost. We can say with certainty that when we act, we value the satisfaction from achievement of the end sought more highly than the satisfaction expected from the highest value forgone. (Anticipated satisfaction can't be measured or subjected to mathematical operations; nor can it be compared person to person.)

Some have criticized this Misesian approach as mere tautology, true by definition. But clearly it is more than that. One's action demonstrates a preference for the chosen objective over anything else one could have aimed at. Hence, Murray Rothbard's term "demonstrated preference." This is not

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Sheldon Richman is editor of The Freeman.

an empty tautology; it is a truth that underlies and makes sense of our observations of the human world. An attempt to refute it is a self-contradiction: the attempt requires action. Thus, these principles of human action has the status of an axiom.

The focus on the individual's selection of goals does not presume egoism or any other ethical category. Nor does it presume that the goal must be money or any other material good. These principles held true for Mother Teresa as well as for John D. Rockefeller. Each chose objectives and suitable (in their judgment) means. Mother Teresa wished to be efficient in ministering to the poor in India, just as Rockefeller wished to be efficient in producing kerosene from crude oil. Their particular ends dictated what "efficiency" meant, but the framework was conceptually the same. Economics is concerned with neither why people choose as they do or nor what they ought to choose. Those matters are left to psychology and ethics.

Marginal Utility

A further implication of human action is the law of diminishing marginal utility. We act to attain values, in effect, according to a scale of descending importance. As we obtain successive units of a good, we devote them to lower priorities. Any one unit is only as important as the lowest priority. For example, I have three cups of water and plan to devote them to these three objectives ranked in descending importance: quenching my thirst, quenching my dog's thirst, watering my rhododendron. If as I begin to drink I accidentally drop the cup, I do not forgo quenching my thirst and devote the remaining cups to the other objectives. Rather, I move the remaining cups up the scale, leaving the least important objective unfulfilled. (Sorry, rhododendron.) In other words, the value to me of any one unit of a good is determined by the value to me of the least important end that good can serve. The utility of the marginal unit (the last one or next one obtained) diminishes as I acquire more.

This all applies to the individual acting in isolation, what Mises calls "autistic exchange." But the principles apply to exchange between individuals too, which preoccupies most of economics. Things get more complicated—money eventually evolves from barter, long structures of production emerge—but the broad outline is the same. Exchange between two people entails some necessary truths. Each party intends to achieve a value through the exchange. Each ranks what he is willing to give up lower than what he will receive. Why exchange otherwise? Each therefore comes out ahead. There's a "surplus" on each side. The same amount of stuff is there; it's only changed hands. Yet each has "more" than he started with. (Either party, being fallible, can err and regret the exchange. But each enters the relationship anticipating gain.)

This is a good time to raise the idea of subjectivism, a concept much misunderstood. The economic meaning of subjectivism differs from its meaning in ethics. In ethics subjectivism means that human beings can arbitrarily determine what is good for them. In economics it means that to understand market phenomena such as prices, the focus must be on subjects—acting beings—not objects. (Thus, there is no conflict on this count between Mises and Ayn Rand.) What we observe in markets grows out of the choices people make about things based on their beliefs and intentions, not out of anything intrinsic to those things. The price of a slow-acting lethal poison might rise as people erroneously come to believe it is nutritious. But the poison will still kill them.

Once economics is seen as focused on human choice, it is no great leap to grasp its relevance to other areas of life not usually thought of in economic terms, such as dating and marriage. This is not to say that economics is all that is relevant, only that the laws of human action apply. □

THE FREEMAN
Ideas On Liberty

Money and Gold in the 1920s and 1930s: An Austrian View

by Joseph T. Salerno

In consecutive issues of *The Freeman*, Richard Timberlake has contributed an interesting trilogy of articles advancing a monetarist critique of the conduct of U.S. monetary policy during the 1920s and 1930s.[1] In the first of these articles, Timberlake disputes the late Murray Rothbard's "Austrian" account of the boom-bust cycle of the 1920s and 1930s. Timberlake contends that Rothbard proceeds on the basis of a "new and unacceptable meaning" for the term "inflation" and a contrived definition of the money supply to "invent" a Fed-orchestrated inflation of the 1920s that, in fact, never occurred. Moreover, Timberlake alleges, Rothbard's account was marred by a "mismeasurement of the central bank's monetary data" as well as by a misunderstanding of the nature and operation of the Fed-controlled pseudo-gold standard by which U.S. dollars were created during this period.

In the two subsequent articles, Timberlake also takes issue, respectively, with the U.S. Treasury's policy of neutralizing gold inflows and the Fed's policy of sharply raising reserve requirements in the mid-1930s, arguing that these complementary policies aborted an incipient economic recovery and brought on the recession of 1937–38. In what follows I will address the weighty charges brought against Rothbard and, in the process, offer an evaluation of the Federal Reserve System's culpability for the economic events of these tragic years that diverges radically from Timberlake's.

Joseph Salerno is a professor of economics in the Lubin School of Business at Pace University.

The Meaning of "Inflation"

Let me begin with Timberlake's contention that Rothbard imputes a meaning to the word "inflation" that is both new and unacceptable. In fact Rothbard's definition of inflation as "the increase in money supply not *consisting in*, i.e., not covered by, an increase in gold," is an old and venerable one. It was the definition that was forged in the theoretical debate between the hard-money British Currency School and the inflationist British Banking School in the mid-nineteenth century. According to the proto-Austrian Currency School, which triumphed in the debate, the gold standard was not sufficient to prevent the booms and busts of the business cycle, which had continued to plague Great Britain despite its restoration of the gold standard in 1821.[2]

Briefly, according to the Currency School, if commercial banks were permitted to issue bank notes via lending or investment operations in excess of the gold deposited with them this would increase the money supply and precipitate an inflationary boom. The resulting increase in domestic money prices and incomes would eventually cause a balance-of-payments deficit financed by an outflow of gold. This external drain of their gold reserves and the impending threat of internal drains due to domestic bank runs would then induce

the banks to sharply restrict their loans and investments, resulting in a severe contraction of their uncovered notes or "fiduciary media" and a decline in the domestic money supply accompanied by economy-wide depression.

To avoid the recurrence of this cycle, the Currency School recommended that all further issues of fiduciary media be rigorously suppressed and that, henceforth, the money supply change strictly in accordance with the inflows and outflows of gold through the nation's balance of payments. The latter provided a natural, noncycle-generating mechanism for distributing the world's money supply strictly in accordance with the international pattern of monetary demands.

Following the triumph of the Currency School doctrine and the implementation of its policy prescription by the Bank of England, its definition of inflation became accepted in the English-speaking world, especially in the United States, where there existed a much more radical and analytically insightful American branch of the School. The term "inflation" was now used strictly to denote an increase in the supply of money that consisted in the creation of currency and bank deposits unbacked by gold. Thus for example, the American financial writer Charles Holt Carroll wrote in 1868 that "The source of inflation, and of the commercial crisis, is in the nature of the system which pretends to lend money, but creates currency by discounting such bills when there is no such money in existence."[3] Even earlier, in 1858, Carroll had written, "Instead of using gold and silver for currency they are merely used as the basis of the greatest possible inflation by the banks," and that "we should prevent any artificial increase of currency to prevent a future . . . catastrophe."[4] So it was the "artificial increase of currency" only—through the creation of unbacked bank notes and deposits—that constituted inflation.

The leading monetary theorist in the United States in the last quarter of the nineteenth century was Francis A. Walker. According to Walker, writing in 1888, "A permanent excess of the circulating money of a country, over that country's distributive share of the money of the commercial world is called inflation."[5]



COURTESY: MASSACHUSETTS INSTITUTE OF TECHNOLOGY

Francis Amasa Walker (1840–1897)

While this version of the definition is applicable to inconvertible paper fiat currency, Walker also believed that inflation was an inherent feature of the issuance of convertible bank notes and deposits that lacked gold backing. In Walker's words, "there resides in bank money, even under the most stringent provisions for convertibility, the capability of local and temporary inflation."[6]

Unfortunately, however, because the writers of the British Currency School, unlike their American cousins, neglected to consider bank deposits as part of the money supply, their policies as adopted in Great Britain failed to prevent inflation and the business cycle. Consequently, and tragically, the School's doctrines and policies fell into profound disrepute by the late nineteenth century, and its definition of inflation was replaced by that of the opposing Banking School, which saw inflation as a state in which the money supply exceeds the needs of trade.

Early American quantity theorists following the proto-monetarist Irving Fisher, in particular, seized upon and adapted this definition to their peculiar analytical perspective. Thus, Edwin Kemmerer wrote in 1920 that, "Although the term inflation in current dis-

cussion is used in a variety of meanings, there is one idea common to most uses of the word, namely, the idea of a supply of circulating media in excess of trade needs."[7] Kemmerer went on to define inflation as a state in which, "at a given price level, a country's circulating media—money and deposit currency—increase relatively to trade needs." From here it was a short step to the currently prevailing definition of inflation as an increase in the price level.[8]

So Rothbard's theory is surely not new and to say that it is "unacceptable" is simply to express one's agreement with the long-entrenched preference among orthodox quantity theorists, including contemporary monetarists, for the Banking School over the Currency School.



Irving Fisher (1867–1947)

Defining Money

Timberlake also challenges Rothbard's statistical definition of the money supply for including savings and loan share capital and life insurance net policy reserves, alleging that Rothbard contrived this definition in order to make the rate of monetary growth appear larger than it actually was during the 1920s. Timberlake argues that the two items in question are not money because "they cannot be spent on ordinary goods and services. To spend them, one needs to cash them in for other money—currency or bank drafts."[9] Let us take these items one at time.

In the case of savings and loan share capital, there are two responses to Timberlake. First, the "share accounts" offered by savings and loan associations are and always have been economically indistinguishable from the savings deposits offered by commercial banks, included in the older (pre-1980) definition of M2 that Timberlake apparently upholds as the appropriate definition of the money supply.[10] In practice depositors could withdraw their savings deposits from commercial banks on demand, because the law that permitted the banks to insist on a waiting period was rarely if ever invoked. Similarly, while savings and loan associations were contractually obligated to "repurchase" their "shares" at par on request of the shareholder, they could legally delay such repurchase for shorter or longer periods depending on their individual bylaws. Nonetheless such delays rarely occurred and "for many years savings and loan associations have made the proud boast 'every withdrawal paid upon demand' or some similar statement."[11]

Moreover, while Timberlake is right that "shareholders" had to trade their share accounts in for currency or bank drafts (at par and on demand) before they could spend them on goods and services, this was equally true of savings depositors at commercial banks. Thus the public has always considered dollars held in savings and loan share accounts or savings accounts as readily spendable as dollars held in commercial bank savings deposits.

Second, Timberlake curiously does not object to Rothbard's inclusion of the savings deposits of mutual savings banks in the money supply, although they also are not included in the M2 definition he favors.[12] What makes Timberlake's position even more puzzling is that mutual savings banks were practically identical in economic function to savings and loan associations and were also technically "mutually" owned by their depositors.[13] So why, then, does Timberlake insist so vehemently on treating the liabilities of

these two institutions differently?

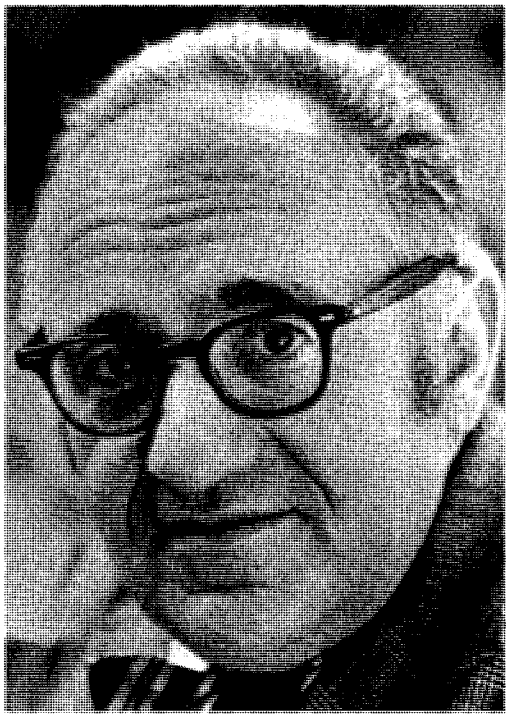
A resolution of this mystery can perhaps be found in the work of Milton Friedman and Anna Schwartz, who excluded the share accounts of savings and loans (and of credit unions) from their definition of the money supply on the grounds that these institutions are technically not banks as defined "in accordance with the definition of banks agreed upon by federal bank supervisory agencies" since "holders of funds in these institutions are for the most part technically shareholders, not depositors." Despite this legal technicality, however, even Friedman and Schwartz were forced to admit that those who place funds with these institutions "clearly . . . may regard such funds as close substitutes for bank deposits, as we define them."[14]

Life Insurance Reserves

This brings us to the issue of the net policy reserves of life insurance companies. Rothbard claimed that the cash surrender values of life insurance companies, that is, the immediately cashable claims possessed by policyholders against life insurance companies, statistically approximated by the companies' net policy reserves, represent a source of currently spendable dollars and should be included in the money supply. Once again the question is not whether insurance companies superficially resemble banks or can be technically classified as such according to some arbitrary regulatory definition. It is whether they essentially function like depository institutions, receiving funds from the public with which to make loans and investments, while contractually promising that such funds are available for withdrawal on demand by the policyholder. In Rothbard's view, the policyholder is economically in precisely the same position as a bank depositor (and thrift institution shareholder) in holding an immediately cashable par-value claim to dollars.

Now admittedly, Rothbard's inclusion of this item in the money supply is controversial, much more so than his inclusion of savings and loan share accounts. However, he was hardly alone in maintaining this position. A number of mainstream writers of money and banking textbooks in the 1960s and 1970s recognized that cashable life insurance reserves possessed some of the characteristics of money. For example, Walter W. Haines characterized insurance companies as "savings institutions" and noted that these savings "can be withdrawn at any time" simply by allowing the policy to lapse, a feature that marks them as a "near-money" on a par with savings accounts.[15] M.L. Burstein maintained that the cash value of a life insurance policy offered "ready convertibility" into cash, was "almost as liquid as a mattressful of currency," and satisfied the "precautionary motive" for holding liquid assets no less than savings and loan accounts and savings bonds.[16] Albert Hart and Peter Kenen included the "net cash values of life insurance" in the broadest class of financial assets possessing the attribute of "moneyness," while Thomas F. Cargill ranked them on a liquidity spectrum immediately below large certificates of deposit, which are included in the current M3 definition of the money supply.[17]

More important, however, even if we grant for the sake of argument that net life insur-



COURTESY: MISES INSTITUTE

Murray Rothbard (1926–1995)

ance reserves should be excluded from the money supply, we find that it makes very little difference to Rothbard's characterization of the 1920s as an inflationary decade. With this item included, the increase in Rothbard's M between mid-1921 and the end of 1928 totaled about 61 percent, yielding an annual rate of monetary inflation of 8.1 percent a year; with this item left out (but savings and loan share accounts included), the money supply increased by about 55 percent over the period or at an annual rate of 7.3 percent.[18] *Mirabile dictu*, by using a definition of the money stock that arbitrarily excludes savings and loan share accounts while including mutual savings bank deposits on the basis of an inexplicable adherence to a legalistic regulatory definition of banks, it turns out that it is Timberlake (and Friedman and Schwartz) who have mismeasured money supply growth during the 1920s.

Flawed Institutions

Timberlake also criticizes Rothbard for "ignorance of the flawed institutional framework within which the gold standard and the central bank generated money" and also of "mismeasurement of the central bank's monetary data."[19] But this is surely a curious charge to level against Rothbard, steeped as he was in Currency School doctrine. In fact, Rothbard was quite cognizant that the U.S. monetary regime of the 1920s and 1930s was not a genuine gold standard in which the supply of money was determined exclusively by market forces, that is, by the balance of payments and the mining of gold, but a hybrid system in which the Fed possessed substantial power to manipulate the money supply by pyramiding paper bank reserves atop its stock of gold reserves. Indeed, Rothbard went much further than Timberlake in rigorously and completely separating those factors affecting the money supply that were subject to Fed control from those that the Fed had no control over.[20]

In analyzing the central bank monetary data, Timberlake starts with the monetary base or "Total Fed," which is equal to currency in circulation plus member bank reserves. From this aggregate he properly subtracts the Fed's legal-tender reserves, mainly the gold stock, whose size depends on balance-of-payments flows and is not under the immediate control of the Fed. What remains is the "net monetary obligations" of the Fed or "Net Fed," which, according to Timberlake, "faithfully indicates the *intent* of Fed policy."[21] From 1921 to 1929, this aggregate declined by 8 percent per year, leading Timberlake to conclude that the intent of Fed policy was decidedly deflationary during this period. The motive for this deflationary policy bias was, Timberlake suggests, to aid Great Britain in re-establishing and maintaining gold convertibility for the pound sterling.

However, as important as it is, the gold stock is not the only factor that lay beyond the Fed's control. For as Rothbard points out, currency in circulation, which improperly remains in Timberlake's Net Fed aggregate, is not controlled by the Fed at all but by the banking public. Any time a depositor withdraws cash from a bank, currency in circulation increases and bank reserves decline, dollar for dollar. Under a fractional-reserve banking system, this loss of reserves causes a multiple contraction of bank deposits that far exceeds the original increase in currency in circulation that induced it and therefore results in a net deflation of the money supply. Conversely, a decline in the amount of currency held by the public causes an overall increase in bank reserves and an overall inflation of the money supply.

This is not all, however—Timberlake also ignores the fact that under the prevailing policy regime the banks themselves could autonomously reduce the amount of bank reserves and thus the quantity of money in existence by deliberately reducing their indebtedness to the Fed. During this period, it was the chosen policy of the Fed to lend liberally and continuously to all banks at an interest, or "discount," rate below the market rate. While the Fed was legally authorized to make such loans to its member banks, it was not mandated to do so. Furthermore, it also retained complete power to set the "discount rate" it charged on these loans. Hence, if it had chosen to, the Fed could have restricted its lending to emergency situations and

charged a penalty rate substantially above the market rate, so as to discourage all but the most seriously troubled banks from applying for loans. In short, it could have almost completely neutralized the inflationary impact of its discounting operations. This "emergency lending" policy had been urged by some prominent officials within the Fed establishment itself.[22]

The fact that the Fed chose instead to pursue a "continuous lending" policy meant that the increase in bank reserves that resulted from the origination of new Fed loans to member banks via the rediscounting of business bills or advances on collateralized bank promissory notes was under the exclusive control of the Fed. But it also meant that the reduction in bank reserves entailed by the net repayment of discounted bills was uncontrolled by the Fed, because it depended solely on the decisions of the banks. Given the Fed's indiscriminate, below-market rate discount policy, the banks were always in a position to maintain or augment their debts to the Fed if they so desired simply by discounting additional bills with the Fed. Thus, as Rothbard concluded, when "Bills Repaid" exceeded "New Bills Discounted," banks were deliberately and autonomously diminishing their level of indebtedness to the Fed and this must be counted as an uncontrolled deflationary influence on bank reserves.

Real Fed Intent

If we follow Rothbard, then, in identifying currency in circulation and the reduction of bank indebtedness to the Fed along with the gold stock as the main "uncontrolled" factors affecting bank reserves, we get a picture of the Fed's intent during the 1920s and early 1930s that is poles apart from the one suggested by Timberlake. Indeed, we find that from the inception of the monetary inflation in mid-1921 to its termination at the end of 1928, "uncontrolled reserves" *decreased* by $1.430 billion while controlled reserves *increased* by $2.217 billion. Since member bank reserves totaled $1.604 billion at the beginning of this period, this means that controlled reserves shot up by 138 percent or 18.4 percent per year during this seven-and-one-half year period, while uncontrolled reserves fell by 89 percent or 11.9 percent per year. Thus Rothbard correctly concluded that the 1920s were an inflationary decade and that it was indeed the intention of the Federal Reserve System that it be so.[23]

The Fed's inflationary intent is perfectly consistent, moreover, with its motive of helping Great Britain re-establish and maintain the pre-war parity between gold and the British pound. While Timberlake properly recognizes this motive underlying Fed policy, he is incorrect in suggesting that it necessitates a deflationary policy on the part of the Fed. In fact, the precise opposite is required. The British pound in the mid-1920s was overvalued vis-à-vis gold and the U.S. dollar, causing British products to appear relatively overpriced in world markets. As a result, Great Britain experienced imports chronically in excess of exports accompanied by persistent balance-of-payments deficits and outflows of gold reserves. Had the Fed deflated the U.S. money supply, thus lowering U.S. prices even more relative to British prices as Timberlake claims was its intention, it would have exacerbated, and not resolved, Great Britain's gold drain. Clearly, then, the Fed's desire to aid Britain in reversing its balance-of-payments deficits and rebuilding its gold stocks called for an inflationary policy intended to pump up U.S. prices, thereby rendering British products relatively cheap and enhancing the demand for them on world markets.[24]

This point about the motive for the Fed's easy-money policy in the 1920s was not only advanced by Rothbard, but by other economists, including monetarists such as Kenneth Weiher. According to Weiher:

> Great Britain was calling for help [in 1924] and Benjamin Strong [president of the New York Fed] heard the call. Expansionary monetary policy in the U. S. would drive prices up and interest rates down in this country, which would tend to send gold flowing toward Great Britain, where prices were lower and interest rates higher. These changes would help America's ally build up its stock of gold. . . . [T]here can

> be no question that the Fed would not have moved when it did were it not for concern over the gold standard and the plight of Great Britain. . . . By 1927, the stagnant British economy needed help from the United States and the rest of Europe. . . . Just as had been the case in 1924, monetary policy was shifted to an expansionary program in an effort to aid Great Britain's struggles to return to the gold standard.[25]

Rothbard's reinterpretation of the monetary data also cuts against Timberlake's claim that the Fed "monetarily starved the country into the worst economic crisis it has ever experienced."[26] On the contrary, the factors controlled by the Fed continued to exercise a highly inflationary impact on bank reserves and the money supply from late 1929 through 1932, as the Fed attempted desperately to ward off the depression precipitated by the termination of the bank credit inflation that it had orchestrated in the 1920s.

The deflation of the money supply, therefore, was caused wholly by factors beyond the control of the Fed. First, there was a loss of confidence in the Fed-dominated phony gold standard among the domestic public and foreign investors. As a result there occurred an increase in currency in circulation and a decline in the Fed's gold stock, both of which caused bank reserves to decline. Second, U.S. banks prudently attempted to save themselves and their depositors by restricting their loans to overcapitalized and failing businesses and instead using these funds to pay down their indebtedness to the Fed, which gave further impetus to the "uncontrolled" reduction of bank reserves. Third, in the second quarter of 1932, the banks also began to increase their liquid reserves beyond the legal minimum. The accumulation of "excess reserves," as they were called, constituted a separate uncontrolled factor that reinforced the deflationary influence of the uncontrolled decline in bank reserves on the money supply.

From the end of December 1929 to the end of December 1931, bank reserves fell from $2.36 billion to $1.96 billion causing RM (for Rothbard's money supply) to drop from $73.52 billion to $68.25 billion or at an annual rate of 3.6 percent. But this monetary deflation was not caused by the Fed, which pumped up controlled reserves by $672 million or at an annual rate of 17 percent during the period, while uncontrolled reserves declined by $1,063 million or by 27 percent per year. During 1932, RM continued to decline, falling to $64.72 billion or by 5.2 percent. But bank reserves increased sharply during the year from $1.96 billion to $2.51 billion, as the Fed furiously inflated controlled reserves. In the last ten months of the year, controlled reserves rose by a staggering $1,165 million, or at an annual rate of 76 percent. Fortunately, this attempted massive inflation of the money supply was undone by the domestic public, foreign investors, and the banks as uncontrolled reserves dwindled by $495 million and banks began to accumulate substantial excess reserves.

The story was much the same in 1933 as a determined inflationary campaign conducted by the Fed in the early part of the year—controlled reserves rose by $785 million in February alone—was defeated by the public and the banks, and RM declined by over $3 billion, or by almost 5 percent.[27]

So once the data have been properly arranged and interpreted, it becomes clear that the Fed does not deserve praise for the bank credit deflation of 1930–1933. This honor goes to private dollar-holders, domestic and foreign, who attempted to reclaim their rightful property from a central bank-manipulated and inflationary financial system masquerading as a gold standard that had repeatedly betrayed their trust.

"Sterilizing" Gold

In two follow-up articles, Timberlake extends his attack on what he considers to be the "deflationary" monetary policies pursued by the Treasury and Fed in the mid-1930s. In particular, he criticizes the Treasury's policy of "neutralizing," or "sterilizing," the effect of the inflow of gold on bank reserves from late 1936 to early 1938 and the Fed's policy of increasing reserve requirements in 1936 and 1937. But neither of these policies caused a contraction of the money supply. They

merely temporarily interrupted a massive monetary inflation caused by the abolition of the gold standard and subsequent devaluation of the dollar engineered by the Roosevelt administration.

It is important to recognize that this influx of gold was not a result of the "uncontrolled" operation of the gold standard, which had been abolished in 1933. Rather, it was the result of the deliberate and steady increase in the price at which gold was purchased by the U.S. Treasury and the Reconstruction Finance Corporation. By January 1934, the price of gold had risen from $20.67 to $35.00 per ounce, or by almost 70 percent, where it was officially pegged by the Gold Reserve Act of 1934. The Treasury was now legally mandated to maintain this devalued exchange rate between gold and the dollar by freely purchasing all the gold offered to it at this price. In effect, then, Treasury gold purchases were now economically identical to inflationary Fed open market purchases, substituting demonetized gold for government securities. Consequently, in response to this unilateral increase in the price of gold above its world price, there occurred a prodigious influx of gold into the United States—a "golden avalanche" it was called at the time—which vastly increased bank reserves. The result was an unprecedented inflation of the money supply (M2) during 1934, 1935, and 1936 at annual rates of 14 percent, 14.8 percent, and 11.4 percent, respectively.[28]

With respect to its influence on the supplies of bank reserves and money, the demonetized gold stock thus had been transformed into a factor "controlled" by monetary—in this case Treasury—policy. Given that the use and ownership of gold money by the public had been legally suppressed, gold was effectively demonetized and its continued purchase by the Treasury was purely a matter of discretionary monetary policy. Accordingly—and contrary to Timberlake's assertion—when during 1937 the Treasury began to finance its purchases of gold in a manner that neutralized their effect on bank reserves, it was not engaging in deflation. The simultaneous sales of government securities to finance these purchases were simply and properly eliminating any extraneous effects of a demonetized asset on the money supply.

Even if gold were permitted to continue in its monetary function, however, Timberlake would still be wrong in criticizing the policy of neutralizing its effect on bank reserves. For under a genuine, Currency School-type gold standard, a country's money supply would increase by exactly the amount of the gold inflow from abroad. This is not inflationary and represents precisely the proper amount by which the money supply should expand, because it is the outcome of the deliberate actions of the country's residents who are decreasing their purchases of foreign imports and increasing their sales of exports in order to satisfy their desires for greater money holdings. This balance-of-payments mechanism is a natural part of the market economy and works continually on all levels—including the region, state, town, and even household—to efficiently adapt money supply to relative changes in money demand.

A problem arises, however, when these benign, money demand-driven gold inflows are used, as they were in the 1920s and early 1930s, as bank reserves to create unbacked notes and deposits. In this case, as F. A. Hayek has so aptly described, international gold flows will regularly cause a serious distortion of the free-market interest rate and investment pattern in the affected countries, leading to a business cycle.[29] The reason is that the needed adjustment in national money supplies upward or downward now entails creating or destroying fiduciary media by expanding or contracting bank loans in defiance of the preferences of the economy's consumers and savers. Thus, a policy of neutralizing the effect of gold flows on bank reserves in the context of a fractional-reserve banking system dominated by a central bank does not constitute a gross violation of the rules of the gold standard; to the contrary, it tends to facilitate the operation of the natural money-supply mechanism that prevails under a genuine gold standard.

Not surprisingly, in the third article of the trilogy, Timberlake also objects to the Fed's policy of raising reserve requirements in 1936 and 1937, which was undertaken to mop up

the massive amounts of excess reserves held by the banking system. Timberlake advances two criticisms against this policy. First, the policy was unnecessary because, even if all the excess reserves that existed on the eve of its implementation were subsequently fully loaned out by the banks, the inflationary potential was relatively minor. Appealing to the Banking School definition of inflation, Timberlake pronounces the 52 percent increase in the money supply that would have resulted as only mildly inflationary because the larger money supply would have exceeded the needs of trade of a fully employed economy by 5.6 percent at 1929 prices, which were about 25 percent higher than prices prevailing in June 1936.[30] In plain language, Timberlake is literally defining away a potential money and price inflation of gargantuan proportions because of its perceived expedience in expanding employment and output and extricating the economy from a depression. But as Timberlake himself admits in a footnote—and as Rothbard and other Austrians have never ceased to argue—what impeded the economy's natural and noninflationary recovery from the depression was the existence of "government programs [that] had actively worked against money price declines for ten years."[31]

Growing Money Supply

In his second criticism, Timberlake contends that the increase in reserve requirements went beyond closing off a potential avenue of recovery for the economy and "turned what had been an ongoing recovery into another cyclical disaster." But if we once again turn to Timberlake's data we find that the money supply (M2) continued to grow, from $43.3 to $45.2 billion or by 4.4 percent, between June 30, 1936, and June 30, 1937, the year in which this policy was implemented. Even if we focus on the last six months of the period, there was hardly a wrenching deflation, as the money supply *increased* at an annual rate of 0.8 percent.[32] Even from Timberlake's monetarist standpoint, then, it is difficult to blame the "recession within a depression" of 1937–1938 on deflationary Fed policy.

Unfortunately Timberlake's strained and narrow emphasis on Fed deflationism as the cause of all the woes of the 1930s causes him to ignore a plausible "Austrian" explanation of the relapse of 1937. As a result of a spurt of union activity due to the Supreme Court's upholding of the National Labor Relations Act of 1935, money wages jumped 13.7 percent in the first three quarters of 1937. This sudden jump in the price of labor far outstripped the rise in output prices and, with labor productivity substantially unchanged, brought about a sharp decline in employment beginning in late 1937.[33] The large upward spurt in excess reserves and the accompanying decrease in the money supply that we observe in Timberlake's data between June 30, 1937, and June 30, 1938, therefore, can be explained as the result, and not the cause, of the recession.[34] As business profits were squeezed by the run-up of labor costs and the economy slipped into recession, banks prudently began to contract their loans and pile up liquid reserves to protect themselves against prospective loan defaults and bank runs. To offset this uncontrolled decline of the money supply, beginning in mid-1938 the Fed (and the Treasury) once again resorted to an inflationary policy, reversing the reserve requirement increase and allowing gold inflows to once again pump up bank reserves. As a result, M2 increased by 5.9 percent, 10.1 percent, and 12.5 percent in 1938, 1939, and 1940, respectively.[35]

Our conclusion, then, is that the Fed's monetary policy, except for very brief periods in 1929 and 1936–1937 when it turned mildly disinflationist, was consistently and unremittingly inflationist in the 1920s and 1930s. This inflationism was the cause of the Great Depression and one of the reasons why it was so protracted. □

1. Richard H. Timberlake, "Money in the 1920s and 1930s," *The Freeman*, April 1999, pp. 37–42; "Gold Policy in the 1930s," *The Freeman*, May 1999, pp. 36–41; and "The Reserve Requirement Debacle of 1935–1938," *The Freeman*, June 1999, pp. 23–29.

2. For a review of this debate, see Murray N. Rothbard, *Classical Economics: An Austrian Perspective on the History of Economic Thought*, Volume II (Brookfield, Vt.: Edward Elgar Publishing Company, 1995), pp. 225–74.

3. Charles Holt Carroll, *Organization of Debt into Currency and Other Papers*, ed. Edward C. Simmons (Princeton: D. Van Nostrand Company, Inc., 1964), p. 333.

4. Ibid., p. 91.

5. Francis A. Walker, *Political Economy* (New York: Henry Holt and Company, 1888), p. 151.

6. Ibid., p. 171.

7. Edwin Walter Kemmerer, *High Prices and Deflation* (Princeton: Princeton University Press, 1920), p. 3.

8. Ibid., p. 4.

9. Timberlake, "Money in the 1920s and 1930s," p. 38. For Rothbard's explanation and defense of his broader definition of the money supply, see Murray N. Rothbard, *America's Great Depression* (Los Angeles: Nash Publishing Corporation, 1972 [1963]), pp. 83–86.

10. I say "apparently," because he states that "No basis exists for a more inclusive money stock than M2" (ibid., p. 42, n. 3). It should be pointed out that, since February 1980, savings accounts of savings and loan associations and credit unions have been included, along with savings deposits of commercial and mutual savings banks in the new M2, an official Fed statistic that is today considered to be the most reliable indicator of movements in the money supply by many economists.

11. John G. Ranlett, *Money and Banking: An Introduction to Analysis and Policy* (New York: John Wiley & Sons, Inc., 1969), p. 251.

12. Paul A. Meyer, *Monetary Economics and Financial Markets* (Homewood, Ill.: Richard D. Irwin, Inc., 1982), pp. 31–32.

13. Walter A. Haines, *Money, Prices, and Policy* (New York: McGraw-Hill Book Company, Inc., 1961), pp. 249–50.

14. Milton Friedman and Anna Jacobson Schwartz, *A Monetary History of the United States, 1867–1960* (Princeton: Princeton University Press, 1963), p. 4, fn. 4. The essential economic—as opposed to the technical legal—identity between commercial bank deposits and all kinds of instantaneously cashable savings accounts held at the various nondepository or thrift institutions was established many years before Friedman and Schwartz wrote, in 1937, in a brilliant but neglected article by Lin Lin ("Are Time Deposits Money?" *American Economic Review*, March 1937, pp. 76–86). This article was not cited by Friedman and Schwartz but greatly influenced Rothbard.

15. Haines, pp. 253–54, 31–32.

16. M. L. Burstein, *Money* (Cambridge, Mass.: Schenkman Publishing Company, Inc., 1963), p. 111.

17. Albert Gaylord Hart and Peter B. Kenen, *Money, Debt, and Economic Activity* (Englewood Cliffs, N.J.: Prentice-Hall, Inc., 1961), pp. 4–6; Thomas F. Cargill, *Money, the Financial System and Monetary Policy* (Englewood Cliffs, N.J.: Prentice-Hall, Inc., 1979), p. 11.

18. I have based this calculation on Rothbard's data. See Rothbard, *America's Great Depression*, p. 88.

19. Timberlake, "Money in the 1920s and 1930s," p. 38.

20. Rothbard, *America's Great Depression*, pp. 94–100.

21. Timberlake, "Money in the 1920s and 1930s," p. 40.

22. On the Fed's discount policy in the 1920s, see Rothbard, *America's Great Depression*, pp. 111–16.

23. For an analysis of the factors involved in the development of the monetary inflation of the 1920s, see ibid., pp. 101–25.

24. On the desire to help Great Britain restore the gold standard at an overvalued gold parity without having to endure the consequences of deflating its economy as an important motive driving the Fed's inflationary monetary policy in the 1920s, see ibid., pp. 131–45.

25. Kenneth Weiher, *America's Search for Economic Stability: Monetary and Fiscal Policy Since 1913* (New York: Twayne Publishers, 1992), pp. 48–49.

26. Timberlake, "Gold Policy in the 1930s," p. 36.

27. On the factors responsible for the monetary deflation of the early 1930s, see Rothbard, *America's Great Depression*, pp. 186–295 passim.

28. Weiher, pp. 75, 79–82.

29. F. A. Hayek, *Monetary Nationalism and International Stability* (New York: Augustus M. Kelley Publishers, 1971 [1937]), pp. 25–32.

30. These figures are calculated from Timberlake's data. See Timberlake, "The Reserve Requirement Debacle," p. 27.

31. Ibid., p. 29, n. 11.

32. Ibid., p. 27.

33. Richard K. Vedder and Lowell E. Gallaway, *Out of Work: Unemployment and Government in Twentieth-Century America* (New York: Holmes and Meier, Publishers, Inc., 1993), pp. 129–36. For a similar explanation of the 1937 slump, see Benjamin M. Anderson, *Economics and the Public Welfare: A Financial and Economic History of the United States, 1914–1946* (Indianapolis: LibertyPress, 1979 [1949]), pp. 432–38.

34. Timberlake, "The Reserve Requirement Debacle," p. 27.

35. Weiher, pp. 75–86.

Classic Satires

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Economics



Comparative Advantage

One of the most powerful and straightforward economic concepts is "comparative advantage." As important and simple as this concept is, however, it seldom seems to inform public discussions of international trade. Almost everyone "knows" that we can't compete with countries that have cheap labor—if we have free trade with such countries either wages will be driven down or many workers will lose their jobs. As Will Rogers once observed, "It's not what people don't know that is the problem, it is what they do know that's not true."

Understanding comparative advantage has the same effect on concerns about free trade as water had on the Wicked Witch of the West. Free trade with other countries (regardless of how much or little their workers are paid) doesn't increase unemployment or lower wages. Indeed, one of the best ways of increasing the wages of U.S. workers is by allowing them to compete with workers (even very low paid workers) in other countries through free trade.

Absolute Versus Comparative Advantage

The most straightforward case for free trade is that countries have different absolute advantages in producing goods. For example, because of differences in soil and climate, the United States is better at producing wheat than Brazil, and Brazil is better at producing coffee than the United States. Obviously both countries are better off when Americans produce wheat and exchange a portion of it for some of the coffee that Brazilians produce.

But does this mean that a country with an absolute advantage in the production of a good should always produce that good rather than import it? No, as the English economist David Ricardo first explained in the early 1800s. A country can have an *absolute* advantage in the production of a good without having a *comparative* advantage. Comparative advantage is what determines whether it pays to produce a good or import it.

Assume that there are only two goods, cars and computers, and one productive resource which is some composite of land, labor, and capital. Assume also that producing 100 cars requires two units of the productive resource (PR) in the United States and four units in Brazil, and producing 1,000 computers requires three units of PR in the United States and four in Brazil.

Thus:

	U.S.	Brazil
100 cars	2	4
1,000 computers	3	4

Americans have an absolute advantage in producing both cars and computers.

It may seem that Americans can realize no gain by trading with Brazilians. Why not produce both cars and computers here? Because

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it *costs* more to produce computers in the United States than in Brazil. All costs are opportunity costs. The cost of producing computers is the cars that *could* have been produced. Using the three units of PR required to produce 1,000 computers in the United States requires sacrificing the production of 150 cars. Using the four units of PR required to produce 1,000 computers in Brazil requires sacrificing only 100 cars.

So even though Americans have an absolute advantage in producing computers, Brazilians have a comparative advantage. Compared to what has to be sacrificed, Brazil produces computers for only two-thirds as much as it costs in the United States. The United States, of course, has a comparative advantage over Brazil in the production of cars. Producing 100 cars here costs 666 computers, while producing 100 cars in Brazil costs 1,000 computers.

Clearly the United States benefits from specializing in cars, which it produces more cheaply than Brazil, and trading with Brazil for some of the computers it produces more cheaply. If, for example, the United States produced both cars and computers it might devote 70 units of PR to car production and 30 units to computer production, yielding 3,500 cars and 10,000 computers. If Brazil produced both products, it might devote 56 units of PR to car production and 24 to computer production, yielding 1,400 cars and 6,000 computers. On the other hand, by specializing in their comparative advantages, the United States can produce 5,000 cars and Brazil can produce 20,000 computers, or a total of 100 additional cars and 4,000 additional computers. The United States could trade 1,450 cars to Brazil for 12,500 computers and have 50 additional cars (3,550) and 2,500 more computers (12,500), while Brazil would have 50 more cars (1,450) and 1,500 more computers (7,500). Trade is productive since it generates more output of both products.

Low Wages Don't Mean Low Cost

Notice that in determining that it is less costly to produce cars in the United States and computers in Brazil, we never mentioned how much U.S. or Brazilian workers are paid. Workers in the United States will be paid more than those in Brazil because they are more productive in our example. So in terms of output, lower wages don't mean lower costs. Indeed, asking whether U.S. or Brazilian workers are less costly ignores the relevant question: less costly doing what? U.S. workers are less costly at producing cars, but Brazilian workers are less costly at producing computers. This is true no matter what U.S. and Brazilian workers are paid.

Moreover, free trade does not cause unemployment in either the United States or Brazil. True, free trade eliminates U.S. jobs in the computer industry and Brazilian jobs in the car industry, but it increases U.S. jobs in the car industry and Brazilian jobs in the computer industry.

Furthermore, the jobs that free trade eliminates are lower-paying jobs than the ones it creates. Without free trade, the United States and Brazil would each employ workers who produce both cars and computers. This means that many workers in each country would be doing jobs in which they do not have a comparative advantage, and therefore in which they are less productive than they could be. With free trade these workers would be directed into more jobs where they are more productive and receive higher pay, since the compensation workers receive ultimately depends on how productive they are.

The concept of comparative advantage is deceptively simple. Tiger Woods surely has the potential of being one of the best caddies in the world. How many people could give you better advice on lining up a putt or selecting a club? He has an absolute advantage. But everyone knows that the opportunity cost to Tiger Woods of becoming a caddie is too high to make that a sensible option. He would be sacrificing the return from being a professional golfer, the activity in which he has a strong comparative advantage. Understanding why Tiger Woods doesn't become a caddie is enough to understand why high-paid U.S. workers benefit when free trade puts them in competition with lower-paid foreign workers. □

THE FREEMAN
Ideas On Liberty

Market Money and Free Banking

by Bettina Bien Greaves

> "If we want to have money, it must be something that cannot be increased with a profit by anybody, whether government or a citizen. The worst failures of money, the worst things done to money were not done by criminals but by governments, which very often ought to be considered, by and large, as ignoramuses but not as criminals."
>
> —LUDWIG VON MISES, speaking at the Foundation for Economic Education, November 8, 1969.

Most people who write about money and banking nowadays from a free-market perspective criticize the Federal Reserve—and rightly so—for contributing to uncertainty by alternating between expansion and contraction. They point to the Fed-induced monetary manipulations that have led to the boom-bust business cycle. They criticize especially the Fed's arbitrary contractions of 1929–1933 and 1936–1938, which resulted in economic downturns and were alleviated only when monetary expansion resumed. They fault the Fed for sitting on its stockpile of gold and for not using it as a basis for further expansion. They object to the Fed's inconsistency, alternating between easy credit one moment and tight credit the next. At the root of their criticism there appears to be a belief, however, that a continual expansion in the quantity of money is not only desirable but also necessary for an economy to prosper.

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As an alternative to national control of the monetary system, these free-market critics of the Fed would prefer private banking. In their view, private banks would be well able to satisfy the market's "need" for currency by issuing bank notes to satisfy the demands of their clientele. Such issues of currency would hold no threat of inflation, they say, for the issues would necessarily be limited by the competition of the issues of other private banks as well as by the obligation of each bank to redeem its notes in real commodity money according to terms agreed upon.

Private banks with the freedom to issue notes are certainly consistent with free-market theory. However, by starting from the premise that the very *purpose* of free banks is to issue currency, it would seem that the advocates of private banks ignore basic economics; they fail to consider, first, what market money is and, second, the basic role of banks in a free market.

Money is not a piece of paper with a dollar sign printed on it; money is basically a *medi-*

um of exchange, something with market value that market participants are willing to accept in exchange. Second, banks are institutions dedicated to handling, safeguarding, lending, and/or managing the funds of depositors, according to agreed-upon terms. Emphasizing the note-issuing aspect of private banking assumes (1) that the paper currency itself is money, (2) that the economy "needs" a certain supply of readily available paper bank notes, and (3) that a less-than-"adequate" amount of currency necessarily leads to economic disaster.

Everyone wants more money—you, I, our friends, families, employers, businessmen. It is not money per se that we want, but purchasing power; we want what money can buy—food, clothing, and shelter, of course, and also automobiles, televisions, computers, medical care, travel, and entertainment. There is practically no end to the wants we can satisfy if we have more money. Government too wants more money to buy things—guns, planes, highways, and the ability to pay its employees; it wants to provide health care, to take care of the poor and the elderly, to clean up pollution, to insure bank deposits, to give humanitarian aid to foreigners, to assist some foreign governments militarily, and so on ad infinitum. There seems to be no limit to the amount of money people would like to have.

Some people carry over into the field of economics the idea that each of us would like more money in his own wallet or bank account. They reason that if everyone would be better off if he had more money, then it should follow that the more money in the whole economy the more prosperous the whole economy would be. Some have even carried this idea to the extreme and have recommended that the government needn't collect taxes at all but may simply print all the paper money it wants, and hand it out to people on the theory that their spending will then bring prosperity. Of course, if this idea were really put into practice, the printed money would soon be so plentiful that it wouldn't be worth anything on the market; it would no longer be serviceable as a medium of exchange, and thus, also, it would no longer be any good as money. Producers would stop producing and there wouldn't be anything to buy—at any price.

Continually Increasing Money

Fortunately economists see through such proposals and do not recommend the unlimited issue of paper money. However, many persons, unfortunately, believe that for an economy to prosper the total quantity of money in the economy must be continually increased.[1] They point to occasional monetary contractions (deflation) in this country and claim that the economy began to pick up only after the Federal Reserve began again to inflate. Deflation, they say, must be avoided at all costs. And most people believe it is the task of government and of the banks to provide the currency, to keep prices relatively stable, and to prevent deflation.

Private banking, according to its advocates, would eliminate violent monetary fluctuations. Private banks of course should be free to issue currency, but their notes would not be legal tender. Their paper notes would represent the medium-of-exchange-commodity on deposit at the bank and would be redeemable by the bank at any time. As such, their notes *could* become the community's money. But their status as money would have to be earned; it would not result from the mere issue of paper currency labeled "money." A private bank's notes would have to compete with readily marketable commodities, as well as with other bank notes, for acceptance as media of exchange. The bank would have to persuade market participants that its notes had value on the market, were generally acceptable to traders, and thus were reliable media of exchange.

The method for introducing the bank's notes into circulation and the interest rate it asked of borrowers would limit the effectiveness of supply and demand in checking under- and over-issue. For instance, a below-market interest rate would invite an increased demand for loans, which the bank could satisfy only by expanding its note issue; an above-market interest rate would discourage loan applications and lead to contraction. However, it is true that the bank's willingness to

redeem on demand all its notes submitted for redemption would prevent any over-issue.

The monetary problem that the advocates of free banking are trying to solve, as described by modern monetary economists, is very complex. But this complexity is not a consequence of the economics of money. Rather it is caused by governmental, not economic, factors—especially the designation of government's notes as legal tender for the payment of debts. The complexity of the monetary situation is the outcome of many regulations and controls. To analyze the problem and the views of today's advocates of free banking, one must review some basic economic principles.

Medium of Exchange

There is really nothing complex about money itself. Money is simply a medium of exchange. Money came out of barter as a result of countless purposive actions of individuals. As the development of specialization and the division of labor expanded to encompass more and more persons, it became difficult and cumbersome to exchange goods for goods, that is, to engage in direct exchange, to barter. If Jones wanted to trade his output for things to consume, he was not always able to locate a would-be trader willing to take his goods and services in exchange for the precise items he wanted. As a result, step by step, Jones and other would-be traders discovered in time that exchanging what they had for a more widely desired commodity would bring them one step closer to a successful exchange.

Traders came to recognize, as the outcome of countless voluntary exchanges, agreements, and contracts, that some particular commodity could serve as a generally useful medium of exchange in their community. Such a readily marketable commodity might be held for a while and then used later when a suitable trading opportunity arose. Thus, over centuries, perhaps millennia, money evolved. No government conceived the idea; it came out of the market. The medium of exchange in any community *must* be something that has market value, purchasing power. If a commodity is easily available and free to everyone, no one will be willing to take it in trade for what he is selling. Such a "free good" will never become a medium of exchange.

The availability of a medium of exchange was a big step forward toward economic progress. The name given to it is "money." Over millennia, many commodities have been used as money—gold, silver, wampum, tobacco, cattle, and more. As a result of voluntary transactions undertaken by countless traders over years, the various commodities used as money were finally narrowed down to practically only one—gold.

Although we now talk about our paper U.S. dollars as if they were money, we should never forget that whatever we use as money must be something people will take in trade. Only its tradability, its acceptability, assures that money is something you and I can exchange for things we want. It should be "something that cannot be increased *with a profit* by anybody, whether government or a citizen," lest that government or citizen take advantage of the situation to increase its quantity until it loses its value as a medium of exchange.

However, we should not dismiss money as unimportant because it is *simply* a medium of exchange. In today's world, almost every interpersonal transaction depends to some extent on a reliable money. It is essential for a viable economy. It facilitates trade, calculation, and production. It enables entrepreneurs operating in a finely specialized division of labor to estimate production costs, calculate potential income, and anticipate future markets. It makes it possible for entrepreneurs to carry out far-ranging and complex financial transactions over long periods of time and across great distances.

Strictly speaking, the government-issued currency in use today, the U.S. dollar, is not money per se. It is a transmogrification of market money foisted on the people by force through the legal-tender laws. It is a derivative of the commodity—gold—that emerged over centuries as the market's medium of exchange. Similarly, privately issued notes would have to earn their reputation as reliable media of exchange to become accepted as money.

Banks and Banking

To understand money, it is important also to analyze banks and their economic beginnings. Banks originated as market custodians for funds entrusted to them by depositors. They soon began to serve as middlemen to help arrange financial transactions for customers. A bank's assets consisted of the funds left with it for safekeeping and money entrusted to it for managing and/or lending. If banks lent funds left with them for safekeeping they did so only at the risk that their depositors, who expected their money to be kept safe and available on demand, might ask for it and find it gone. However, experience taught bankers that all depositors would not ask for all their money at the same time; so a bank could lend a portion of these funds—if it was careful. The bank knew that the rate of interest it asked could influence a person to borrow more or less. If the bank lowered its interest rate, it could expand its currency issue and lend more *for its own profit*. But lending more increased the bank's risk. It always realized that such over-lending might be discovered and it would then have to make up the shortfall from elsewhere or face bankruptcy.

It is argued that expanding credit to lend more money promotes prosperity because it puts money in the hands of businessmen who can use it to good advantage. This argument depends on considering the "seen" and ignoring the "unseen." It ignores the fact that new credit over and above the available supply of savings can be granted only by issuing loans at below-market interest rates. This means expanding credit artificially. Those who benefit from the additional new credit, created *for the profit* of the issuing bank, are helped; they appear on the market ahead of others, bid up prices, and walk off with their credit-financed purchases. Those who do not benefit from the new credit, the savers on whose funds the expansion was based, are hurt. But they are not seen. Not having received any of the new credit, they do not become visible spenders; they are prevented by the beneficiaries of the new credit from using their own money as they wish.

Banks are expected, of course, to lend the money that savers leave with them for that purpose, sharing part of the interest earned with those who furnished the funds. But even in such cases, banks must be cautious. They soon learned from experience that the periods for which loans are made must be coordinated with the dates when the money lent has to be repaid to depositors. In other words, deposits that its customers could claim on demand at any time must always be redeemable from funds on hand. Funds to repay short-term loans must be financed by credits that will be repaid by the end of the short terms specified. And long-term loans may be financed by funds repayable to the bank over longer periods. But those funds too must be back in the bank by the date when they must be repaid to the depositors. For instance, if a bank's short-term loans are backed by long-term mortgages, the bank would be in trouble.

The Role of Government

Much has changed over the centuries since money first evolved on the market and since entrepreneurs first opened banks to serve the needs of persons who engage in money transactions. But the basic economic principles remain the same. To serve as money, a commodity must still possess widespread marketability as a medium of exchange. And to remain in business private banks must still fulfill their obligations.

Governments have become more and more involved with monetary matters. It started when they were called on to settle disputes that arose over contracts. Courts and judges were frequently asked to decide whether the two parties to an agreement had actually complied with the terms agreed upon. Suppose one person agreed to exchange bushels of wheat for money of the realm, and the other agreed to pay a certain amount of money for wheat. When the time came for the farmer to deliver wheat and the buyer to deliver money, one or both parties might object that the other had not complied with the agreement. It was then up to the courts to decide. Was the wheat delivered actually the quantity and quality

specified in the contract? Was the money paid—whether gold, silver, wampum, tobacco, dollars, or pesos—actually "money" as called for in the contract? Only that, and nothing more than that, the courts and judges had to decide.

Government's role in the field of money was soon broadened. From the idea that courts must settle disputes over what was meant by "money" in specific cases, there developed the doctrine that money was whatever the government said it was. Governments took advantage of this situation. They not only decreed what money was but they expanded *for their own profit* the quantity of whatever they decreed to be money. Then they compelled people to accept that money in trade by declaring it to be legal tender for the payment of debts.

Counterfeiters try to piggyback *for their own profit* on a community's money. A government does essentially the same thing. In ancient times, governments clipped or adulterated their coins and then compelled the people to accept them at their previous nominal value. Later, with the invention of the printing press, it became easier to debase the currency. The government could simply declare anything to be money, even a piece of paper. Then government privileged certain banks and protected them from bankruptcy if they printed bank notes *for the profit of the government* over and beyond the gold or silver deposits in their vaults. And the government gave these bank notes legal-tender status. With the establishment of the Federal Reserve system in this country in 1913, the monetary system of legal-tender paper bank notes based on reduced gold and silver backing was formalized. In time the U.S. government itself, through the Federal Reserve, assumed the responsibility for issuing this country's currency. And these paper notes enjoy legal-tender status today.

The redemption in gold or silver of legal tender was at first discouraged and then halted completely. In 1933 it became impossible for citizens to obtain gold for their paper money, and they were eventually prohibited from owning any monetary gold at all. The U.S. government even reneged on its own promises to redeem its bonds and debts in gold. In January 1975, U.S. citizens regained the right to own gold, but they are still compelled to accept the government-issued legal-tender notes.

Throughout all the years since the Federal Reserve Banks opened, the quantity of legal-tender money has continually increased. And the market value, the purchasing power, per unit of this money has continually declined, reflecting the subjective value that individual market participants place on the dollar relative to other goods and services.

Inflation: More Money or Higher Prices?

One reason for confusion over money results from the changed definition of the word "inflation." Originally and traditionally it meant an increase in the quantity of money and/or credit, and it is so defined in *Merriam Webster's Second International Dictionary* (1954).[2] Only in recent decades has the word been widely used to refer to one consequence of a monetary increase: an increase in prices. Granted, this new definition is now widely accepted, but that does not make it correct or expedient. Not only does it leave the language without a term for a monetary increase, but it shifts the blame away from the real culprits to the victims. While the U.S. government and the government-established Federal Reserve are responsible for increasing the quantity of money *for their own profit* and hence for causing prices to rise, it is the victims—businessmen, savers, workers, investors, consumers, and so on—who are blamed for asking or paying higher prices.

Now let us consider the Federal Reserve as "an engine of inflation." Granted, it is difficult to compare the number of dollars in circulation over the years. Statisticians frequently revise their "money stock" estimates, even changing what they include. However, there can be no doubt that there has been a tremendous increase in the number of dollars since 1913 when the Fed was established. There was a Fed-inspired monetary expan-

sion from 1921 to 1929. In 1913, the country's "money stock" (gold, coins, and notes) was estimated at $3.798 billion.[3] On June 30, 1929, at the peak of the stock market boom, this figure had more than doubled to $8.538 billion, representing a substantial inflation. If market prices did not climb to the same extent during those years, as most economists agree they didn't, it is because the effect of the monetary increase on prices was hidden by increased production, due to the initiative, innovation, and productivity of entrepreneurs, creating a downward pressure on prices.

To return to the statistics, the money stock reported on June 30, 1930, dropped slightly from 1929 to $8.306 billion, but by June 1932 it had climbed to $9.004 billion. The Fed's figures show that the country's money has been increased more or less steadily ever since, bounding up especially during war years.[4] By the end of 1998, M2 figures came to $4,288.3 billion. And they continue to climb. If U.S. prices have not risen proportionately, it is due not only to the tremendous initiative, ingenuity, adaptability, and productivity of entrepreneurs but also to the mushrooming demand by foreigners to hold dollars—as their preferred medium of exchange—for their own security and as a hedge against the potential loss in value from inflation of their own country's currencies.

Being unable to trade in gold, and having long since been compelled to accept the U.S. legal-tender dollars in payment of debts, market participants have come to accept them by default as the best available medium of exchange. Having no other realistic alternative, entrepreneurs do their best to calculate their costs and potential markets in terms of dollars. In making business plans, they try to anticipate future fluctuations in the value of the dollar. And as long as the Federal Reserve practices relative restraint, market participants worldwide adjust and adapt fairly successfully. But in the last analysis, the market value of the U.S. paper/credit dollar depends on the judgment of fallible human beings who take into consideration, among other factors the political climate, the interests and *profit* of the U.S. government.

The Effects of Inflation

Supply, demand, and competition for the medium-of-exchange commodity are determined by the subjective values of market participants. This is true whether the medium is gold, a paper substitute for gold, a paper note decreed by government to be legal tender, or a private bank's paper note. Every dollar added to the existing supply of money to which the market has adjusted has at least three inevitable consequences: (1) it confiscates some wealth from anyone who owns dollars; (2) it upsets the calculations of entrepreneurs; and (3) it reduces purchasing power.

New issues of money and/or credit withdraw or extract some value, some purchasing power, from every existing dollar asset, whether in a wallet, savings account, bond, insurance policy, or debt payable in dollars. The value of every person's dollar holdings shrinks even as he sleeps. New issues of money and/or credit upset the calculations entrepreneurs made in dollar terms, distorting production, causing malinvestment, and setting the stage for a boom/bust business cycle. Of course, holders of privately issued currency that does not enjoy legal-tender status are not helpless; they may refuse to accept it if it loses value and turn to some other medium of exchange.

When the quantity of money is increased, the new money is passed from one person to another throughout the economy. But this takes time. Every additional monetary unit created—whether by gold miner, the printing press, credit expansion, or deficit financing (monetization of debt)—goes to some individuals first. It necessarily affects their value judgments, reducing in their minds the marginal utility of each unit of money. Those who receive the new money or new credit first benefit, feel more affluent, spend more freely, and are willing to offer higher prices for goods and services. Their demand for goods and services creates pressures on the market pushing prices upward. The delayed and uneven effect on the market of an inflation helps the early recipients of the new money at the expense of others. Those who do not receive any of the new money until later are hurt; they

must pay the higher prices resulting from the pressure of the increased demands of the early beneficiaries before they get any of the new money themselves.

There have been many times in history when the value of money has dropped drastically because governments have increased the quantity *for their own profit.* One of the most dramatic cases is that of the German mark after World War I. By 1923, the number of German marks was increased by billions, the market value of a single mark fell practically to zero. The marks still enjoyed legal-tender status. However, they were no longer reliable and ceased to serve as money. Creditors engaged in all kinds of subterfuges to avoid being repaid in marks, and debtors tried various tactics to trick their creditors into accepting payment in the depreciated marks.

Many other national currencies have suffered similar fates in recent years—the Bolivian and Argentine pesos, the Russian ruble, the Italian lire, the Thai baht, the Indonesian rupiah, the Hungarian forint, to name a few. Such examples show clearly that there can be too much money.

How Much Is Enough?

Any quantity of money is adequate because prices will adjust. Individual market participants, bidding and competing with one another, will bring the purchasing power parity principle into effect. They will bid more or less for units of money, and more or less for goods and services, depending on their subjective values. The purchasing power per monetary unit will tend to decline as the number of monetary units increases. It will tend to rise as the number of monetary units drops. In the end, the purchasing power per monetary unit will shrink or stretch so that the total available quantity of money, large or small, will suffice to purchase the available goods and services. Thus, any amount of money is enough money, if it is not changed abruptly or arbitrarily and if it is not made legal tender. □

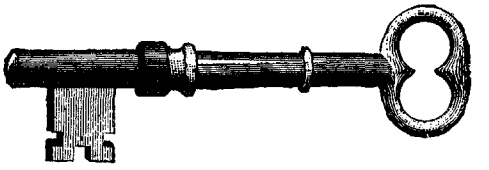
1. This article was sparked by Professor Richard H. Timberlake's three articles in *The Freeman* (April, May, and June 1999).

2. It defines inflation basically as a "Disproportionate and relatively sharp and sudden increase in the quantity of money and credit, or both, relative to the amount of exchange business."

3. Statistics approximate, taken from the monthly *Federal Reserve Bulletins*.

4. The Fed's monetary statisticians apparently took a holiday in 1933 along with the banks. But they returned to the task after the gold stock was revalued from $20.67 to $35.00 per ounce by FDR's *diktat.* The value of the money stock as of December 3, 1933 ($17.470 billion) reflected the increased value of the government's gold holdings. By December 1941, when World War II started, the money stock had increased to $90.435 billion. By the end of the war, it had been expanded to $113.597 billion. In the 1950s, the U.S. gold holdings began to go down as other countries started to withdraw their gold from the United States. However, money stock statistics continued to climb. At the end of the Korean War (1955) it was approximately $133.3 billion. In 1971, Federal Reserve statisticians revised their money stock figures (M2 consisted of currency outside of banks, demand deposits, plus time deposits at commercial banks) and backtracked, calculating M2 in 1964 to have been $273.8 billion. In 1971, Nixon stopped the sale of gold to foreign governments and foreign central banks. He devalued the U.S. dollar in December 1971, to $38 an ounce, and then again in February 1973 to $42.22. In January 1975, the U.S. government resumed selling gold and U.S. citizens regained the right to own gold coins and gold bullion. The price of an ounce of gold zoomed off the charts, indicating the extent to which the effects of inflation, defined as monetary increases, had been suppressed. After the end of the Vietnam War, M2 figures came to $576.5 billion.





CAPITAL LETTERS



Constitutional Question

To the Editor:

Concerning David N. Mayer's article in the July issue of *The Freeman*, yes, "Monica's War" (as broadcaster Paul Harvey labeled it) against Yugoslavia was "immoral," but as to whether it was "unconstitutional" requires clarification.

In Mayer's article, I find no mention of Article VI, paragraph 2, of the U.S. Constitution, which states:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, *any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.* (emphasis added)

This, I presume, was the basis for Mayer's writing that "Some legal scholars have advanced the extraordinary argument that Congress has neither a constitutional obligation nor a right to declare war before the United States joins in a 'police action' sanctioned by either the United Nations or NATO. They argue that U.S. ratification of the U.N. Charter or the North Atlantic Treaty after World War II made us part of a 'new world order' in which member nations can no longer 'make war,' in the classic sense."

Because of paragraph 2, I see nothing extraordinary in the legal argument that the United States is bound by the U.N. Charter and the North Atlantic Treaty. The certain way out of the legal argument and the "new world disorder" is for the U.S. Senate to repeal approval of the U.N. Charter and the North Atlantic Treaty.

—EARL ZARBIN
Phoenix, Arizona

David Mayer replies:

The "Supremacy Clause" of Article VI, paragraph 2, notwithstanding, there is one and only one way in which the U.S. Constitution can be amended, and that is by the procedure stipulated in Article V. Neither the U.N. Charter nor the North Atlantic Treaty can give the U.S. president powers he does not have; the sole source of presidential power is the U.S. Constitution. The Constitution provides that Congress alone has the power to declare war, and that power (to be meaningful) today means the power to decide where and when U.S. military force should be used offensively; the president has only the power of commander-in-chief, which (properly viewed) is the power to determine *how*, not *where*, U.S. military force is used. Constitutionally, then, prior to any U.S. military involvement under either U.N. or NATO auspices, Congress should debate and vote whether or not to commit U.S. troops: under our constitutional system, it is a question to be decided by the legislative, not the executive branch, of the U.S. government. We needn't repeal our ratification of either of these treaties (although there may be other good reasons for doing so) in order to follow the separation of powers mandated by the Constitution.

We will print the most interesting and provocative letters we receive regarding *Freeman* articles and the issues they raise. Brevity is encouraged; longer letters may be edited because of space limitations. Address your letters to: *The Freeman*, FEE, 30 S. Broadway, Irvington-on-Hudson, NY 10533; e-mail: freeman@fee.org; fax: 914-591-8910.

THE FREEMAN
Ideas On Liberty
OCTOBER 1999



Chicago Gun Show

"According to the economic approach, criminals, like everyone else, respond to incentives."

—GARY BECKER[1]

The Chicago boys are at it again. This time the economists at the University of Chicago are making headlines in today's hotly disputed debate about gun control. Milton Friedman set the general standard a generation ago by insisting on rigorous empirical work to support sound (though often unpopular) theory and policy. More recently, Gary Becker extended Chicago-style economic analysis into contemporary social problems such as education, marriage, discrimination, professional sports, and crime.

Now John R. Lott, Jr., until recently the John M. Olin Law and Economics Fellow at Chicago, is making the case that a well-armed citizenry discourages violent crime. Lott analyzed the FBI's massive yearly crime statistics for all 3,054 U.S. counties over 18 years, the largest national surveys on gun ownership, and state police documents on illegal gun use. His surprising conclusions, published in his recent book, *More Guns, Less Crime*:

- States now experiencing the largest drop in crime are also the ones with the fastest-growing rates of gun ownership.
- The Brady five-day waiting period, gun buy-back programs, and background checks have little or no impact on crime reduction.
- States that have recently allowed concealed weapon permits have witnessed significant reductions in violent crime.
- Guns are used on average five times more frequently in self-defense than in committing a crime.[2]

According to Lott, recent legislative efforts to restrict gun ownership may actually keep many law-abiding citizens from protecting themselves from attack. (There's that Law of Unintended Consequences again.)

The Incentive Principle

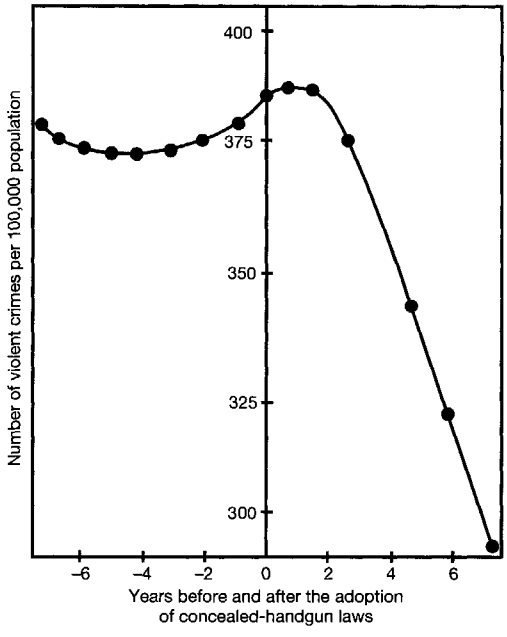
Underlining Lott's findings is a basic economic concept, the law of demand: If the price of a commodity goes up, people use less of it. In the case of criminal activity, if the cost and risk of committing a crime rises, less crime will be committed. This is often referred to as the market's incentive principle.

Gary Becker has showed that increasing the cost of crime through stiffer jail sentences, quicker trials, and higher conviction rates effectively reduces the number of criminals who rob, steal, or rape.[3]

Similarly, Lott argues that state laws per-

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mitting concealed handguns deter crime. "When guns are concealed, criminals are unable to tell whether the victim is armed before striking, which raises the risk to criminals."[4] He produces a variety of statistics and graphs to support his case. For example, the following graph compares the average number of violent crimes in states before and after the adoption of a concealed-handgun law.



The effect of concealed-handgun laws on violent crimes

Source: John R. Lott, *More Guns, Less Crime,* Figure 4.5

Lott's crime figures also remind me of Frederic Bastiat's brilliant essay "What Is Seen and What Is Not Seen." In 1850, this great French journalist wrote, "In the economic sphere,. . . a law produces not only one effect, but a series of effects. Of these effects, the first . . . is seen. The other effects emerge only subsequently; they are not seen."[5]

According to Lott, Bastiat's principle applies in crime statistics. "Many defensive uses [of guns] are never reported to the police."[6] Lott gives two reasons. First, in many cases of self-defense, a handgun is simply brandished, the assailant backs off, and no one is harmed. Second, in states that have stringent gun laws, citizens who use a gun for protection fail to report the incident for fear of being arrested by the police for illegal use of a weapon. Thus, Lott confirms (through extensive surveys) the initial work of Gary Kleck, professor of criminal justice at Florida State University, that guns are used far more frequently in self-defense than in committing crimes. Kleck, by the way, used to have a strong anti-gun bias until he uncovered this revealing statistic.

All this confirms a long-standing constitutional principle: People have the right to own a gun for self-protection. □

1. Gary S. Becker and Guity Nashat Becker, *The Economics of Life* (New York: McGraw-Hill, 1997), p. 143.
2. John R. Lott, Jr., *More Guns, Less Crime* (University of Chicago Press, 1998).
3. Becker and Becker, p. 137.
4. Lott, p. 5.
5. Frederic Bastiat, "What Is Seen and What Is Not Seen," *Selected Essays on Political Economy* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1995 [1850]), p. 1.
6. Lott, p. 5.

Professor Skousen's *Economic Logic* Now Available

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BOOKS

The Great Philanthropists and the Problem of "Donor Intent"

by Martin Morse Wooster

Capital Research Center • 1998 • 198 pages • $15.00

Reviewed by George C. Leef

According to a book titled *The Right Guide* and its companion volume, *The Left Guide*, funding for the various organizations that promote the expansion of government is between three and four times as great as the funding for the organizations that seek to protect freedom, private property, and limited government. The principal reason for this lamentable situation is that several huge foundations that were built on the fortunes of men who were staunch laissez-faire advocates have been turned into cash cows for statist advocacy, among them the Ford, Rockefeller, and MacArthur foundations.

The Great Philanthropists examines the problem of the subversion of the wishes of individuals who create vast wealth and foundations to disburse that wealth after their deaths. The villains of the piece are the "professional" and almost invariably statist foundation managers who think that they know how to use the fortunes amassed by entrepreneurs to refashion society and have no qualms whatsoever about employing the funds in ways the donor would not have approved.

Wooster introduces us, for example, to William H. Allen, one of the earliest of these types, who denounced the "dead hand" of donor intentions and argued that trustees should be free to use foundation money for any purpose they thought worthy 20 years after the donor's death. (In truth, many don't see why they should have to wait 20 minutes.) The philosophy and objectives of "professionals" like Allen usually differ markedly from those of the wealth creators, yet in case after case, they succeeded in taking control of the foundations of the great capitalists. The book explains how it happened.

Consider John D. Rockefeller, creator of Standard Oil. During his lifetime, he made sure that his charitable giving did not promote dependency or waste. But people were constantly hounding him for money, and he was persuaded that he could insulate himself from that hounding by setting up a foundation and letting others handle the giving away of his money; this was "wholesale" rather than "retail" philanthropy. Within one year of the establishment of the Rockefeller Foundation in 1913, Wooster writes, "many foundation trustees and employees were looking for ways to exclude Rockefeller from the foundation's affairs." They would succeed.

Equally harmful was the fact that John D. Rockefeller, Jr., was philosophically much different from his father. Young Rockefeller surrounded himself with advisers who were hostile to capitalism and allowed them to quickly steer the foundation radically away from the desires of the senior Rockefeller. This was a heist worthy of the most audacious bank robbers, yet all done perfectly legally.

In 1919, Rockefeller, Sr., tried to reassert control. He wrote to his attorney explaining what he wished to do to put his foundation back on what he regarded as the right track. The lawyer, however, was aghast at the idea of Rockefeller's controlling his own money and maneuvered to thwart his client's intentions. The foundation continued on its merry statist way, as it does to this day.

The story of the Ford Foundation was similar to Rockefeller's. Henry Ford was a staunch advocate of capitalism. He was virtually the only prominent industrialist who refused to cooperate with the National Recovery Act, thus making himself a target of FDR and his New Dealers.

Confronted with New Deal "share the wealth" legislation that threatened to cost the Ford family control over the business he had built, Ford established the Ford Foundation in 1936. The foundation remained relatively small and unobtrusive until after World War II, but a tremendous infusion of wealth came in following Ford's death in 1947. Henry Ford II, a political moderate, allowed the founda-

tion to fall into the hands of statist philanthropic professionals. Eventually, the younger Ford would resign from the board after being haughtily told by the foundation's president, McGeorge Bundy, that he was just one vote out of 16 and his family lineage meant nothing. On resigning, Ford wrote that "the foundation is a creature of capitalism, a statement that, I'm sure, would be shocking to many professional staff people in the field of philanthropy. It is hard to discern recognition of this fact in anything the foundation does."

Wooster recounts other such disasters, but he also points to several instances where the wishes of the donors have been honored by their foundations, showing that the problem is not insoluble. He identifies several means by which wealthy individuals can ensure that their money is not later turned to purposes of which they would disapprove.

The most important step is simply deciding to buck the trend of giving a free hand to "the professionals." Wooster writes, "The fundamental problem of philanthropy today is not "dead hand" control. It is donors who meekly follow prevailing wisdom and leave their fortunes to professionals who spend the money on causes they like—which are usually not the causes preferred by the donors."

A timely, much-needed book. □

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

The Crisis of Global Capitalism

by George Soros

PublicAffairs • 1998 • 245 pages • $26.00

Reviewed by Brink Lindsey

Reading George Soros on international economic policy is like watching Michael Jordan—at bat. Both experiences reinforce the lesson that excellence in one field of endeavor doesn't necessarily translate into other areas. In Soros's case, success at playing the market does not extend to success at understanding it—or more precisely, the government policies that shape or distort it.

In *The Crisis of Global Capitalism*, Soros rails against what he calls "market fundamentalism," or the belief that "the common interest is best served by allowing everyone to look out for his or her own interests and that attempts to protect the common interest by collective decision making distort the market mechanism." This dogma, he asserts, "has rendered the global capitalist system unsound and unsustainable."

His proposed response to the present peril: "To stabilize and regulate a truly global economy, we need some global system of political decision making. In short, we need a global society to support our global economy." Specifically, Soros recommends the creation of an International Credit Insurance Corporation, which would add up-front guarantees of foreign loans to the IMF's current post hoc mop-ups.

To assert as Soros does that the world today is in the grip of "market fundamentalism" reveals a profoundly distorted view of events. Where are the governments today that toe a strict laissez-faire line? Where even are the opposition parties of any size that do so?

Certainly the world has moved in leaps and bounds toward more market-oriented policies over the past couple of decades, but look who has led the charge—in China, Deng Xiaoping, a committed Communist; in India, P. V. Narasimha Rao, a product of the Congress Party that instituted Soviet-style central planning there; in Argentina, Carlos Menem, a Peronist; in Peru, Alberto Fujimori, an agricultural engineer and ideological cipher; and so on and so on. Yes, there have been reformers who made their case in ideological terms—Ronald Reagan, Margaret Thatcher, Vaclav Klaus—but they have been exceptional. By and large, the worldwide rediscovery of markets has been guided by pragmatism—a rejection of the failed dogma of collectivism in favor of something, anything, that works.

And, of course, the move toward market-oriented policies still has a very long way to go. Although collectivism may have perished as a living ideal, government interventionism remains a huge and distorting presence in the

world economy. Market forces enjoy nothing like the unchallenged ascendancy that Soros claims for them; rather, they must contend with, struggle against, and slip through the loopholes of a massive and overextended public sector.

It is this uneasy coexistence between markets and statism that is the true source of instability in the global economy today. And oddly enough, Soros is not blind to this fact. The author frequently acknowledges how misguided interventionist policies—including unsustainable currency pegs and moral hazard-infected financial systems—led to the recent crises in Asia. Nevertheless, Soros urges, as a response to those crises, the creation of another layer of moral hazard in the form of international credit guarantees. Talk about the triumph of hope over experience!

Soros's hostility to markets stems from his theory of "reflexivity"—which boils down to the common-sense observation that sometimes people act not because of what they think, but because of what they think other people think. In financial markets, this phenomenon can cause herd behavior, which in turn can cause bubbles and panics.

Let's admit that all this is true. But what of it? The question isn't whether markets are perfect; it's whether markets and competition generally and in the long run work better than centralized bureaucratic control. The fact is that markets do sometimes overshoot, but there are limits: bubbles eventually burst, and panics subside. When a market trend begins to look precarious and unsustainable, there are enormous incentives—namely, the prospect of making a killing—to buck that trend and bring it down. George Soros should know: he's made billions that way.

What are the equivalent feedback mechanisms that restrain and reverse the mistakes governments make? Are they as effective and reliable as those of the market? Let's see what Soros himself has to say:

> [M]arkets have a way of correcting their excesses; bull markets are followed by bear markets. Representative democracy seems to be less successful in this respect. It is true that governments and legislatures are regularly replaced by the electorate; that is how the system is designed. But democracy seems incapable of correcting its own excesses.

Well, well. If Soros would only take his own words to heart, he would see that opposition to his interventionist nostrums need not be a matter of dogmatic "fundamentalism." Simple realism is all that's required. Meanwhile, it is the continued recourse to government interference which requires blind faith that somehow, this time, it will succeed. □

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Nixon's Economy: Booms, Busts, Dollars, and Votes

by Allen J. Matusow

University Press of Kansas • 1998 • 324 pages • $35.00

Review by David L. Littmann

Allen Matusow's book is a play-by-play description of Nixon's overwhelming priority—get elected! Not that Nixon was uninterested in the economy. He fully understood the political punishments and rewards that are meted out by rising or falling unemployment and interest rates. Nixon's feel for fiscal and monetary policies probably exceeded that of most, if not all, of his economic advisers, from whom he received a lot of dreadful advice.

But Nixon, the author observes, made economics subservient to politics. Economic policies were simply tools of political expedience. Matusow portrays a President Nixon bored to death and even irritated by economic advice or theories that were not clear catalysts to his political ambition. Conversely, when economic theories, such as the "full employment budget" concept or quotas on Japanese textiles, seemed to further his objectives, he was rapt in attention, participating actively in the ensuing policy debates and critiques.

Nixon's Economy is well organized to take us through the economic turbulence of the

Nixon years. Its chief strength is Matusow's description of the duplicity of Nixon's conduct of economic policy. He reveals the blatant contradictions between the so-called conservative philosophy that one might think would have led Nixon to advocate tax cuts, smaller government budgets, repeal of regulations, removal of trade barriers, and other laissez-faire policies. But no, precisely opposite policies prevailed, culminating in the 1971–74 wage and price controls.

Matusow's commentary on the contradictions between theoretical Republican support for markets versus actual adoption by the administration of socialism is illuminating. Few politicians are long able to resist the temptation to wield governmental power for short-run political advantage. Professed limited-government principles are forgotten or deliberately cast aside when interventionism seems to offer better political rewards. (The author's observations are also relevant to what has befallen the "Republican Revolution" since 1995.)

Sadly, Matusow, professor of history at Rice University, is himself weak on economics. While good at exposing the weaknesses and contradictions in Nixon's economic policies, one sees little indication that he is familiar with serious free-market analysis. Especially as regards monetary policy and the origins of the lethal inflation generated by the Nixon programs of the late '60s and early '70s, the author confuses cause and effect. For example, in chapter three Matusow claims that "the main reason why prices kept rising through 1970 . . . was the big wage increases that workers were demanding and getting." He compounds this confusion in later chapters, suggesting that currency devaluation and oil price hikes are causes of inflation.

Errors like this are not isolated. By chapter six, perhaps in an effort to make the book more readable, the author resorts to normative assertions, using "good" and "bad" with reference to Uncle Sam's manipulation of the dollar vis-à-vis foreign currencies. Later, Matusow falls into the trap of stating that "controls deserved some credit for declining inflation." Yet, he elsewhere credits Milton Friedman's monetarist warning that inflation is always and everywhere a monetary phenomenon.

This unevenness is forgivable for a non-economist. But some shortcomings cannot be excused. The story of the Nixon years would have been a considerably more valuable exposition for future generations of readers and economists had the author included fewer retrospective testimonies from apologists for the Keynesian school, and instead emphasized the disservice of "political economists" and power-hungry advisers, such as Paul Volcker, Arthur Burns, and John Connally. Also, contrary to the author's gratuitous statement that "no one in or out of government [in 1973] foresaw the approach of the [inflation] cataclysm," there were many non-political economists who foresaw and wrote about the futility of controls and catastrophes that awaited economies adopting these bankrupting policies.

Nixon's Economy is worthwhile and germane reading, making clear the important point that the incentives of politicians tend to put them disastrously at odds with sensible economic policies. The author's own lack of economic comprehension, unfortunately, renders the book less valuable than it might otherwise have been. Read the book for its good history and take the author's economic pronouncements with a grain of salt. □

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To Serve and Protect: Privatization and Community in Criminal Justice

by Bruce Benson

New York University Press, Political Economy of the Austrian School Series • 1998 • 416 pages • $37.50

Reviewed by Morgan O. Reynolds

Over the last three decades, the share of GDP consumed by the public sector on crime control has tripled and now exceeds $100 billion annually, or about $1,000 per household. Crime rates have declined in the 1990s, suggesting some benefit from the

expenditure, yet crime stubbornly remains three times higher than 30 years ago, according to FBI statistics. These data imply a substantial decline in the productivity of law-enforcement bureaucracies.

The natural thought of a public choice economist is, "So what else would you expect?" Big government is no more likely to be the answer to crime than to any other problem. Private-sector solutions and market-driven reforms are more likely to work. The root solution for crime is a set of institutions that get incentives right. Custom and law must internalize (privatize) more benefits for crime suppressors and make crime producers pay more of the costs they impose on victims.

Bruce Benson, professor of economics at Florida State University, pursues this logic brilliantly. Benson is a veteran researcher on crime and law, and in this volume he integrates a sprawling literature in a way that changes the whole discussion. The book works on two distinct levels. First, it provides nearly encyclopedic coverage of private techniques in criminal justice that range from medieval Anglo-Saxon days to contracting out of prisons today. Second, and more important, it elevates us to a high philosophical plane by redirecting our attention from social-engineering goals like deterrence and rehabilitation toward a focus on justice and individual rights and responsibilities.

Like education, criminology has long been a field rent by fads. Lacking a real intellectual anchor and populated primarily by sociologists, criminology has for the most part ignored a rights-based perspective. Benson's book fills that void. His premise is that justice for victims should be the goal of our justice system. All else follows from that premise.

Offenses thought of as crimes today, like murder and robbery, were once treated as private torts, with economic compensation as the primary remedy. This private system of justice worked well and could do so again, according to Benson. With the prospect of recovery of damages, the victim had a greater incentive to report a crime, correcting a major failing in our present system where victims only report about 40 percent of crimes to the police. Restitution rights were transferable, thereby promoting efficiency in apprehension and liability.

Our present reliance on the state to protect our property rights and control criminals is very recent, less than two centuries old in most respects. The historical reason for this evolution was that kings took away victims' property rights to restitution, and the path of criminal justice in England then wandered away from individualism toward collectivism. In the tradition of Ronald Coase and Steven Cheung, who debunked the theories that private markets must fail to supply lighthouses or pollinate fruit, Benson's historical research explodes the doctrine that a justice system is a "public good" that only government can provide.

Perhaps Benson's most arresting evidence comes from Japan, which has the lowest crime rate among industrialized nations by far. A primary reason, claims Benson, is that their system is more privatized and victim-oriented than ours. There, the fundamental right is for the victim to be restored to his original condition. In contrast to our culture, in the Japanese culture there is no acceptable excuse for criminal activity. The criminal must bargain for forgiveness with the victim and if the wrongdoer negotiates an acceptable settlement package and shows contrition, public-sector punishment is lenient.

Benson documents the substantial private effort to combat crime in the United States, estimated at $300 billion a year, and therefore larger than the public-sector effort. This will continue to grow rapidly, Benson predicts, if only to compensate for continuing public failure. Our system is also moving toward victims' rights, recently enshrined in many state statutes and constitutions. Benson sees these as largely illusory gains because law-enforcement bureaucracies have co-opted victims' rights organizations. He warns victims' groups that they must forge an independent path in order to transform criminals' "debts to society" into private, transferable debts to individual victims.

Shortcomings in the book are few and usually amount to legitimate differences of judgment or opinion. Benson sometimes fails to use the latest data available, and ignores the

best estimates, say, for the probability of prosecution on arrest. Sometimes he attributes facts like exclusionary rules to the statist nature of the justice system too quickly, ignoring competing hypotheses like rent-seeking by lawyers.

Clearly, the crime solution lies in more individual responsibility and less public responsibility. Benson's daring conclusion—privatize both the demand for and the supply of criminal justice services—leaves us with a wealth of provocative diagnoses and examples for further research. Benson has given us a breakthrough book. □

Morgan Reynolds is professor of economics at Texas A&M University.

Seeing Like a State: How Certain Schemes to Improve the Human Condition Have Failed

by James C. Scott

Yale University Press • 1998 • 445 pages • $35.00

Reviewed by Aaron Steelman

Amazing progress has been made in the twentieth century. The Western world has grown tremendously rich, and many developing countries around the world have "emerged." Today, most people enjoy living conditions that their ancestors could have only dreamed about.

But the twentieth century has also witnessed horrific brutality. Millions have been killed in wars. And an even greater number, perhaps, have been killed by their own governments in the name of "progress." What has been the source of such inhumanity?

In *Seeing Like a State*, Yale political scientist James C. Scott examines "the failure of some of the great utopian social engineering schemes of the twentieth century." He argues that "the most tragic episodes of state-initiated social engineering originate in a pernicious combination of four elements."

First, Scott argues, are "transformative state simplifications," that enable the state to easily track and classify its citizens. This includes the creation of permanent last names, population registers, and the standardization of language.

Second is what Scott calls "high-modernist" ideology. "It is best conceived," he writes, "as a strong, one might even say muscle-bound, version of the self-confidence about scientific and technical progress, the expansion of production, the growing satisfaction of human needs, the mastery of nature (including human nature), and, above all, the rational design of social order commensurate with the scientific understanding of natural laws." National economic planning during World War I excited high-modernist theorists and led them to believe that society actually could be run by enlightened technocrats.

The third element is an "authoritarian state that is willing and able to use the full weight of its coercive power to bring these high-modernist designs into being." Such regimes often gain power during times of war, revolution, depression, and struggle for national liberation.

The last element is a "prostrate civil society that lacks the capacity to resist these plans."

"In sum," Scott writes, "the legibility of a society provides the capacity for large-scale social engineering, high-modernist ideology provides the desire, the authoritarian state provides the determination to act on that desire, and an incapacitated civil society provides the leveled social terrain on which to build." When those four elements are present, the stage is set for the likes of Hitler, Stalin, and Pol Pot—and for the forced villagization of 5 million Tanzanians in the 1970s, a lesser-known tragedy that Scott recounts in a fascinating chapter.

High-modernist ideology, Scott points out, manifests itself in less disastrous ways, too. Consider centrally planned cities. Traditionally, cities have grown naturally to fit the desires and needs of their citizens. The streets of many European and Middle Eastern cities don't fit a grid-like pattern: they sprang up as the population grew and moved. To a resident, everything makes sense. But to a government official who thinks he knows best, it appears chaotic. Surely, a planned city would be much better than one developed seemingly by chance.

Such was the mindset of architect Charles-Edouard Jeanneret, better known as Le Corbusier. He wished to redesign Paris, Buenos Aires, Algiers, and Moscow according to his own plans. He argued, "We must refuse to afford even the slightest concession to what is; to the mess we are in now. There is no solution to be found there." He envisioned a world, Scott writes, in which "door frames, windows, bricks, roof tiles, and even screws would all conform to a uniform code. [Le Corbusier] called for the new standards to be legislated by the League of Nations, which would develop a universal technical language to be compulsorily taught throughout the world."

In the end, Le Corbusier built only one city, a provincial capital in India. Scott notes, however, that he influenced many people, including Brazilian president Juscelino Kubitschek. Kubitschek created the city of Brasilia from scratch and made it the country's capital. Originally, there was one huge public square, but few informal gathering places such as parks, and all its residents were supposed to live in uniform housing projects called "superquadra," which had their own nurseries, schools, stores, and clubs.

The planned city quickly failed; people found life in it undesirable and stifling. Now, most of the population lives in settlements that were never anticipated by Brasilia's planners. High-modernist ideology didn't result in mass slaughter in the case of Brasilia, but it did produce great unhappiness. People didn't want what the planners tried to force on them. The planners weren't able to acquire the "practical knowledge," as Scott calls it, to pull off such a grand scheme. They were ignorant of "the limits . . . of what we are likely to know about complex, functioning order."

This is excellent analysis, but unfortunately, Scott thinks "large-scale capitalism" suffers from similar defects. It "is just as much an agency of homogenization, uniformity, grids, and heroic simplification as the state is . . . . [I]n markets, money talks, not people," he argues. But when I decide to eat breakfast at McDonald's, who is making the decision? I am. I'm using money to buy the meal, but I'm the one doing the talking. In the market, producers cater to the consumers' desires—not the other way around. Scott fails to grasp that point. Nevertheless, *Seeing Like a State* is a brilliant work of remarkable scope. □

Aaron Steelman is a graduate student in the social sciences at the University of Chicago.

Silencing Science

by Steven Milloy and Michael Gough

Cato Institute • 1998 • 68 pages • $8.00 paperback

Reviewed by Kenneth Silber

This slim volume is an ironic how-to guide for heavy-handed regulators, panic-mongering activists, demagogic politicians, venal trial lawyers, dogmatic religionists, and anyone else with an interest in stifling or manipulating science. In breezy style, the authors explain how to impede research and suppress data, using lawsuits, regulation, intimidation, and other methods. They also show how to fill the resulting void with misinformation.

The authors—Milloy is publisher of the Junk Science Home Page (www.junkscience.com); Gough is the former director of science and risk studies at the Cato Institute—draw on numerous examples of science under siege. They present the persecution of Galileo as a cautionary tale (the Inquisition didn't crack down quickly enough to eliminate his influence) and cite the Scopes Monkey Trial as a useful model for interfering with science education. They then launch into more recent anecdotes of obscurantism and obstructionism. Unfortunately (or fortunately, if one remains in the book's ironic mode), there are many ways to silence science.

Outlawing research is one option, the authors explain, pointing to efforts to place a wide-ranging ban on cloning experiments. Alternatively, science can be regulated into the ground, as when the Environmental Protection Agency moved to control pest-resistant plants as if they were pesticides. Government purse strings can be useful in tying up undesired research, such as fetal tissue studies during the Reagan-Bush years. Nor is privately funded science immune to

political attack; one need only stigmatize the research as profit-driven or linked (however tenuously) to Big Tobacco.

Legal harassment works well, too. The authors describe how lawyers representing the alleged victims of silicone breast implants intimidated the Mayo Clinic with onerous demands for medical records. Another form of harassment is to make bogus claims of scientific misconduct; this approach was used by "multiple chemical sensitivity" activists against researchers who raised doubts about that "disease." And don't forget about street protests and celebrity letter-writing campaigns; such techniques helped animal-rights proponents prevent NASA from studying monkeys in orbit.

Even after a research project has been completed, there are various ways to hide or distort the resulting information, the authors point out reassuringly. Careful editing, for instance, allowed a United Nations report to overstate the threat of global warming. Another method is simply not to publish the data; the Energy Department has kept a major radiation study under wraps for years, providing only a brief summary in an obscure bulletin. California's environmental agency went this one better, systematically destroying research documents that did not support the agency's final decisions.

The authors explain how to replace genuine science with various phony substitutes, such as "official science," "consensus science," and "the precautionary principle." The first consists of governmental or other seemingly authoritative pronouncements that happen to be unsupported by evidence, such as a U.S. Senate resolution that women in their 40s should have mammograms. The second involves claiming that there is agreement when in fact there is not, as occurs often in the global-warming debate. The precautionary principle, embraced by environmentalists, means that industrial chemicals and radiation are to be regarded as extremely dangerous, while contrary evidence and uncertainties are swept under the rug.

While *Silencing Science* takes a lighthearted approach, the underlying seriousness of the subject shines through. The suppression of science—whether motivated by politics, ideology, or personal and financial gain—produces bad decision-making, increased risk, and diminished freedom. One comes away from this book with a heightened awareness of danger—a danger not only to scientists but to anyone who depends in any way on their research (everyone, that is, whose participation in modern society exceeds that of, say, the Unabomber).

The book's format does impose certain constraints. The "how-to" approach, while funny, would start to wear thin if the book were to go on much longer; at the same time, the overall subject deserves a more extensive treatment. A somewhat broader picture of the threats to science would take notice of academic postmodernism and New Age mysticism, movements that go unmentioned here. A deeper analysis, rather than merely reporting anecdotes, would delve into the conditions that enable anti-scientific tactics to thrive.

Nevertheless, *Silencing Science* packs a great deal of valuable and thought-provoking material into its slender frame. The book deserves a wide readership. May that readership not include the anti-science types who might actually take its advice. □

Kenneth Silber has written about science and technology for Reason, Insight, the New York Post, *and other publications.*

Staring into Chaos: Explorations in the Decline of Western Civilization

by B. G. Brander

Spence Publishing • 1998 • 418 pages • $29.95

Reviewed by Gleaves Whitney

The right is temperamentally pessimistic. The left is philosophically nihilistic. Both camps have long tended to see the West as culturally decadent, a civilization in decline. So it is odd that, for decades, virtually every major English-language reference work in the social sciences included articles about progress, but not its opposite. It was as though Americans were reluctant to give the imprimatur to decadence and decline as major cat-

egories of thought. One had to look to the French for scholarship on decadence—perhaps because they have had more firsthand experience with it than Americans.

Only in recent years has cultural pessimism received the attention it deserves on this side of the Atlantic. After all, one cannot do serious intellectual history without confronting the pessimism of Nietzsche, Burckhardt, Darwin, and legions of other theorists of decline since the Renaissance. Their works are so numerous as to constitute a veritable type of literature, what I call the "decline-of-the-West" genre.

Because English-language surveys of that genre have been few and far between, it is a pleasure to discover B. G. Brander's most recent book, *Staring into Chaos: Explorations in the Decline of Western Civilization.* Brander is a full-time writer and a former editor for *National Geographic*—not the typical credentials for a student of cultural pessimism. Yet it is precisely because Brander is a layman who has escaped the perils of academic specialization that he is able to read the classic statements of the decline of the West from a fresh perspective.

Brander is clear about his purpose from the outset, and readers should be too. He aims to "distill the insights of more than two-dozen thinkers into this single volume. . . . Where writers contributed whole books on the topic, I offer concise digests of their works." Thus Brander's book, while not categorized as such, functions as a reference work that will give readers a crash course in the decline-of-the-West literature.

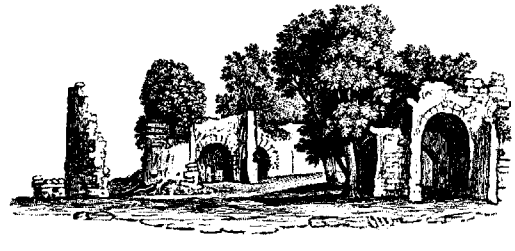
Early chapters introduce notions of cultural decadence and civilizational decline in the thought of Albert Schweitzer, Nikolai Berdyaev, Ernst von Lasaulx, Nikolai Danilevsky, and Henry and Brooks Adams, among others. Brander then trains his sights on three twentieth-century giants of the genre—Oswald Spengler, Arnold Toynbee, and Pitirim Sorokin (to whose memory the book is dedicated). In some 400 pages of text, Brander devotes about 100 pages to each one of these three, ably surveying their works and making them accessible to the educated lay public.

Readers of this magazine will find much of interest in all three, but perhaps most of all Sorokin because of his concern over the fate of freedom and the rule of law. Sorokin, a Harvard sociologist, was already arguing in the 1930s that the West was undergoing one of the greatest transitions in history. Brander encapsulates some of Sorokin's predictions: "Governments will turn increasingly fraudulent and tyrannical. Contracts and covenants will lose binding power and contractual society will collapse. Democracy, capitalism, and [our] free society of free people will be swept away. Freedom will become a mere myth for the majority of people, whom centralized governments will deal with as puppets. Meanwhile, the dominant majority will turn their freedom into unbridled licentiousness." And this: "Private educational institutions will lose autonomy from government control and diminish in favor of public or state-controlled schools." Prescient.

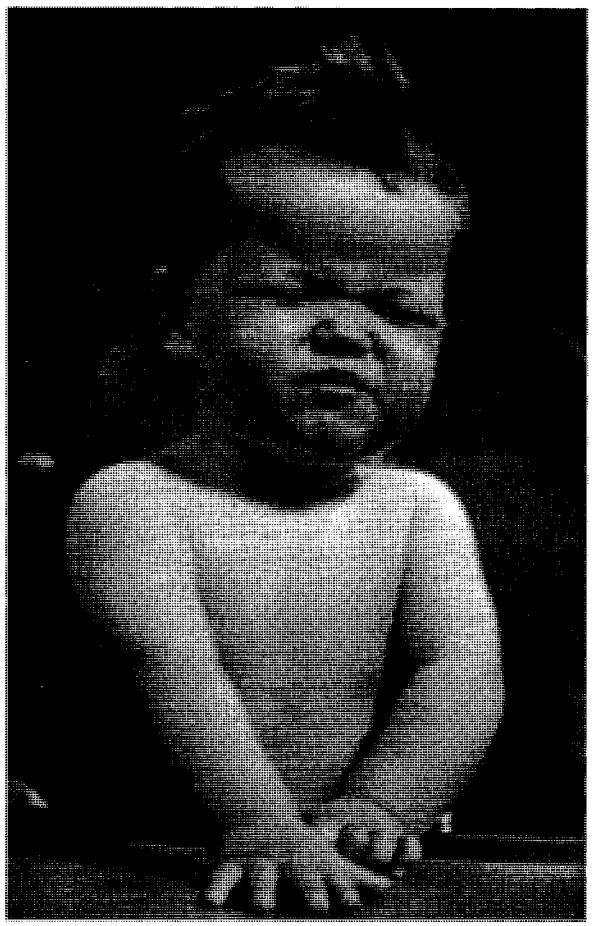
One question that inevitably arises in a survey is why certain thinkers were not included or were given only cameo roles. Christopher Dawson, for example, qualifies as one of the twentieth century's most insightful historians and theorists of decline. Brander, however, cites him only once in the text, and then fleetingly, and lists none of his books in the bibliography. Perhaps this oversight will be addressed in a later edition.

As we approach the millennium, many will seek to understand the signs of the times; many will have premonitions of decline. They would do well to go behind the culture wars of the present day and seek perspective through the provocative historical and social analysis of these giants. In Brander, they will find a competent and congenial guide. □

Gleaves Whitney is chief speechwriter for Michigan Governor John Engler, senior fellow at the Russell Kirk Center for Cultural Renewal, and the senior scholar of the Center for the American Idea.



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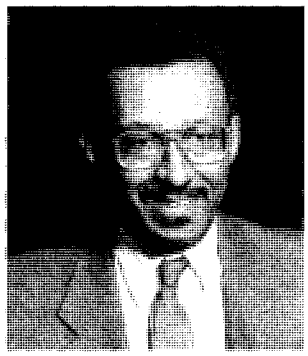
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Conflicting Visions

People generally share common goals. Most of us want: poor people to enjoy higher standards of living, greater traffic safety, fewer wars, greater racial harmony, cleaner air and water, and less crime.

Despite their common goals, more often than not we see people grouped into factions, fighting tooth and nail to promote differing government policies. The policies are often unproductive and have the unintended consequence of sabotaging the goal.

A good example of this conflict is found in the periodic debates over the minimum wage and tariffs. Many people profess concern for the welfare of low-skilled workers. To achieve their goal of helping those workers, one group adamantly demands that Congress legislate higher minimum wages. Another group professing the identical concern is just as adamant in demanding that Congress *not* legislate higher minimum wages. Similarly, one group of advocates for greater employment opportunities might lobby Congress for higher tariffs and stricter quotas on imports. Another group sharing the identical goal will fight against tariffs and quotas and lobby for fewer trade restrictions.

Why do people, who are assumed to be honest, intelligent, selfless, and not motivated by a hidden agenda, arrive at polar-opposite policy proposals as a means to achieve commonly shared goals that may indeed produce polar-opposite results? One possible explanation in the case of unions and companies seeking protection from imports is that they are dishonest and simply promoting their own interests. Their political strategy is to express concern for the unskilled and to lobby for greater employment opportunities simply as a ruse to conceal their true agenda: higher wages, profits, and monopoly wealth.

But there's another answer. They share different visions of how the world works. Consider the effects of different visions by going back to a time prior to Pythagorean and Ptolemaic proofs that the earth was round. Imagine two honest and intelligent people in 1000 B.C. One person's premise is that the earth is flat. Based on that premise, he would argue strenuously that it is not possible to sail west from Greece and reach the Orient. The other person, whose premise is that the world is round, would argue just as strenuously that it is possible to reach the Orient by sailing west from Greece.

Given the premise, the conclusions (one can or cannot reach the Orient by sailing west from Greece) are internally consistent and logical. After all, if the world is flat, one would sail right off the edge and into the abyss before reaching the Orient. On the other hand, if the earth is round, the trip can be safely made. Incidentally, before one condemns the flat-earth vision it should be noted that, while inaccurate, it was nonetheless useful, providing reliable navigation over relatively short distances.

Walter Williams is the John M. Olin Distinguished Professor of Economics and chairman of the economics department at George Mason University in Fairfax, Virginia.

Of course, the flat-earth vision was ultimately laid to rest when people actually circumnavigated the globe. Also, scientific evidence and simple empiricism weighed in to settle the debate. People saw that the shadow of the earth on the moon during eclipses was round, and they also saw that the mast of a ship approaching from the sea is visible before the hull. The incorrect vision about the shape of the earth was demolished by falsifying its premise—not by questioning the internal consistency of the arguments.

Often the underlying premises supporting the conclusions of some arguments are so baseless they are deliberately left unstated. In these cases, they must be teased out by questions such as: for that conclusion to hold, what assumptions are being made about human behavior? Consider the minimum-wage debate. Assuming that both proponents and opponents of higher minimum wages are guided solely by an honest concern for low-wage, low-skilled workers, what is the premise held by those who favor increases in the minimum wage versus that held by opponents? If one's premise (stated or not) is that employers need a certain number of employees to do a particular job, the logic behind increasing the minimum wage as a means to raise incomes of low-skilled workers is internally consistent. The effect of a higher minimum wage would be higher wages for workers and lower profits for employers.

Opponents of higher minimum wages have a different premise. They assume that employers are responsive to changes in labor costs. They believe that there are alternative methods to accomplish a particular task. Employer responses to higher labor costs might include: substitution of capital for labor (automation), employment of self-service techniques (such as self-service gas stations), relocation to a country that has cheaper labor, use of disposable utensils instead of washable ones, fewer theater ushers, and automatic elevators. These and many other substitutes allow employers to economize on labor and produce fewer employment opportunities for low-skilled workers.

The vision that higher mandated wages (that exceed productivity) produce no employment effects also assumes that investors are insensitive to the company's profits and customers are insensitive to higher product prices. Neither is likely. If companies are required to pay higher wages and make no response they will see their profits decline relative to companies that do respond. In turn, investors will see a reduction in their return on equity and will likely move their capital elsewhere.

The company might try to forestall declining profits by attempting to recover higher labor costs by raising product prices. However, consumers are not insensitive to higher prices. They will seek cheaper substitutes, thereby reducing the company's sales. In the wake of higher minimum wages, surviving companies will be those that have found ways to economize on labor.

Zero Elasticity of Response

The premise that employers are not responsive to changes in the cost of labor is what economists call a zero elasticity of response. Put another way, changes in the independent variable (wages) have no effect on the dependent variable (the number of workers hired). There is little evidence that people are insensitive to price changes, whether it be changes in taxes, gas prices, food prices, labor prices, or any other price. The issue is not whether people change their behavior when relative prices rise or fall; it is always how soon and how great the change. Thus with minimum-wage increases it is not an issue of whether firms will economize on labor, it is how much they will economize and who will bear the burden of that economizing.

Thus, it is easy to see how two groups of honest and caring people with the same concern for low-skilled, low-wage workers can advocate opposite policies. They simply have different visions of how the world works. Convincing people how the world really works, in the hopes of promoting better policies, requires examining and debunking false visions and premises—a yeoman's task. □

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Cover portrait of Albert Einstein: CORBIS/Bettmann.

PERSPECTIVE

Who's Who in the School Voucher Movement

Watching the shifting line-ups in the school voucher contest is revealing. The voucher is one of those insidious "reforms" that its advocates herald as an achievable "step in the right direction." The direction varies depending on who's speaking. For some it's improvement of the government's monopoly schools through competition. For others, it's elimination of the government's role in education. That's one problem with the voucher movement: it's a coalition with incompatible objectives.

To date, the coalition has consisted mainly of conservatives, with a significant minority libertarian element. Many other libertarians, however, have warned that the voucher is a Venus flytrap. It looks pretty, but stay away.

It was only a matter of time before someone other than conservatives and libertarians became attracted to vouchers. Considering that key constituents of the Democratic Party, inner-city minority residents, poll in favor of vouchers, it was inevitable that leaders of that party would take an interest.

An editorial in the May/June *New Democrat*, published by the Democratic Leadership Council and Progressive Policy Institute (the "moderate" Democrats with whom Bill Clinton has long been associated), embraced vouchers in a new defense of government schools. These New Democrats are "gloomy" that the public response to vouchers and private scholarships has been so enthusiastic. Recent developments "should be a wake-up call to liberal Democrats who have blocked, watered down, or gummed up reforms such as charter schools and other types of public school choice," the editorial states. Sensing that government schooling is in peril, it recommends that any voucher bill be amended to force private schools to admit all children and "meet or exceed specified performance standards to continue receiving taxpayer funds."

Here's the punch line: "Such an amendment would effectively turn voucher-supported private schools into public charter schools." As the editorial correctly points out, "A public

school is not defined by who 'owns' it, but rather by two features: universal access and accountability to the public for results." The implicit third feature is tax financing.

The New Democrat anticipates that many voucher champions will object. "Fine," it says. "Let's separate the sheep from the goats on education: let's find out who's really interested in improving student achievement and who's interested in simply gutting public education." Education separationists understand that these two goals are not in conflict.

The question for voucherians who favor separation of school and state is: who is more likely to shape the voucher legislation that eventually gets enacted?

I am not the first to predict it, but I foresee a day when the voucher advocates and voucher opponents (excepting the libertarians) switch sides. It won't be long.

* * *

With slightly more than a year to go before the start of the new millennium, it's worthwhile to contemplate how much wealth human beings have created over the last one. Calvin Beisner takes an inventory.

The theory of spontaneous order holds that social cooperation and coordination occur without a central plan and with minimum force. Andrew Morriss has studied a particularly striking example—involving elementary schoolchildren.

Once upon a time American coins honored liberty not political leaders. The country's founders insisted on it. That all changed. Stephan Gohmann teaches a revealing lesson.

The newspapers heralded the finding: Einstein's brain *was* different? What does that mean? Steven Yates gives the gray matter some thought.

The U.S. Constitution contains terms that strike the modern ear as unfamiliar. The specific practices referred to may be passé, but as Wendy McElroy notes, the terms may not be as outmoded as one might think.

For classical liberals, welfare is bad, charity is good. Really? Daniel Oliver points out that it all depends on what the meaning of "charity" is.

The Clinton administration has plans to use the FBI to monitor all traffic on the Internet—for our own protection, of course. Prudent policy or another leech on liberty? Aeon Skoble e-mailed his conclusion.

Freud said that sometimes a cigar is just a cigar. The Food and Drug Administration would have you believe that in light of its alleged effect on health, a cigar is actually a pack of cigarettes. Jacob Sullum scrutinizes the latest call for warning labels.

A quarter century ago many people believed the world's supply of fossil fuels would run out. Considering that a gallon of milk (a "renewable resource") costs more than a gallon of gasoline, that prediction seems flawed. It's even more flawed than you think, says Robert Bradley, Jr.

Once again Big Steel wants help from Washington. How good is its case that foreign steelmakers are "dumping"? And is that a bad thing? Dale DeBoer has the unalloyed truth.

Western Germany, once the post-World War II economic dynamo, today looks like any other European welfare state. Norman Barry identifies the causes of decline.

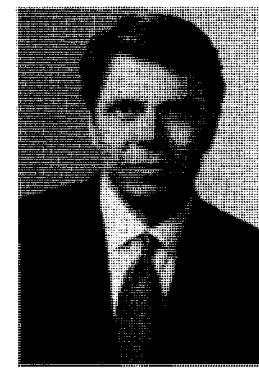
Our columnists offer a smorgasbord of insights: Donald Boudreaux pounces on "predatory pricing." Lawrence Reed examines the connection between the size of state governments and economic success. Doug Bandow analyzes post-Columbine gun policy. Dwight Lee continues his discussion of comparative advantage. Thomas Szasz dissects the metaphor of "mental illness." Mark Skousen relates the story of a private bank in the world's poorest country. Charles Baird takes the pulse of the AFL-CIO. And Roy Cordato, meditating on the claim that the "invisible hand" will be irrelevant in the 21st century, protests: "It Just Ain't So!"

Reviewers this month assay books on a free education market, prospects for a civil society in China, political correctness on campus, the principles of a free society, the automobile, and Ulysses S. Grant.

—SHELDON RICHMAN

Thoughts on Freedom

by Donald J. Boudreaux



Stop Stopping Price Cutting

"There's nothing new under the sun." This aphorism speaks volumes about Uncle Sam's antitrust suit against Microsoft. One of the government's principal accusations in this suit is that Microsoft is a predator—meaning that the attractive deals that Microsoft today offers to consumers cannot be matched by its rivals. When the hapless rivals eventually are bankrupted by Microsoft's pestiferous artifice, Bill Gates and his lieutenants will use the monopoly power they've acquired to raise prices, restrict output, and slow the pace of innovation. The benefits that consumers get from Microsoft's good deals today will be swamped by the costs that consumers endure tomorrow when Microsoft is a monopolist.

This predation theory was endorsed by MIT's Franklin Fisher, the government's chief expert economist in the Microsoft lawsuit. When asked on the witness stand to explain why Microsoft currently charges so little for its Web browser, Fisher testified that "while the [predatory pricing] campaign is going on, consumers are getting a better deal." But beware the future! Fisher affirmed Judge Thomas Penfield Jackson's suspicion that Microsoft is pursuing a strategy of "delayed gratification"—increasing its prospects for future profits by purposely earning unnecessarily lower profits today. (As an aside, I find it curious that many people who insist that Microsoft purposely sacrifices profits today in hopes of earning higher, monopoly profits tomorrow also allege that modern American capitalism compels business leaders to maximize short-run profits at the expense of long-term growth.)

Microsoft isn't the only firm accused today of predatory pricing. The U.S. Department of Transportation accuses major airlines of lowering their fares whenever their markets are entered by upstart carriers. The sole purpose of these fare cuts, the department alleges, is to run the upstarts out of the market so that the major carriers face less competition.

And so it has been for all of antitrust's history. From accusations in the 1880s that Chicago meatpackers charged too little for their beef and pork, through accusations in the 1930s that A&P's low prices unfairly hurt mom-and-pop grocers, to accusations in the 1990s that Wal-Mart predatorily prices downtown retailers into bankruptcy, antitrust has commonly been used to prevent entrepreneurial firms from improving the lot of consumers. Sadly, the current harassment of Microsoft is simply the latest episode in 110 years of this anti-entrepreneur, anti-consumer campaign.

What Is Predation?

Is predation real? Yes—but not in the way that government and many economists believe. In my view, predation occurs only when a firm relies on force or fraud to harm its rivals. For example, if Microsoft dynamites Sun Microsystem's production facilities, that's predation. If Delta Airlines advertises vicious lies about Southwest Airlines' safety record, that's predation. If Barnes & Noble

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Donald J. Boudreaux is president of FEE.

successfully lobbies Congress to ban on-line book selling—thereby bankrupting Amazon.com—that's predation. But it's not predation for a firm to offer consumers better deals. A firm is not a predator if the advantage it wins over its rivals results from voluntary consumer choices.

None of this denies that each firm wants to be a monopolist. But desiring monopoly power is not akin to acquiring monopoly power. A chief justification for free-market competition is that by seeking maximum profit, firms yield benefits—as if by an invisible hand—not only to their owners, but also to their suppliers and consumers. Competition is supposed to encourage firms to compete for consumers. It is supposed to encourage firms to try to "harm" their rivals by offering consumers better deals and, therefore, attracting consumers away from rivals. That's how competition works; that's the only way that competition *can* work.

It is theoretically possible that Acme Corporation today offers deals so attractive to consumers that its rivals soon are bankrupted and, as a result, Acme tomorrow charges monopoly prices. But this possibility hardly justifies government policing against low prices.

First, this possibility is too remote. Not only does the historical record contain scant evidence of predatory pricing, but even successful predators cannot count on their monopoly power lasting. The reason is that any market monopolized by a predatory pricer is one in which the "monopolist" today enjoys excessively high profits *only* because it earlier charged prices that were below its costs. That firm has no special cost or quality advantages. (If the firm did enjoy such advantages, it could have bankrupted its rivals without charging below-cost prices.) Entrepreneurs will surely sweep in rapidly to challenge that firm. Profits in such an industry are low-lying fruit.

Second, there's nothing special about low prices to distinguish them from a million and one other strategies that firms use to attract more business. Anything a firm does to attract more business—cutting prices, improving quality, or more intensely advertising its services—"harms" its rivals. (Again, that's what competition is about!) There's no justification for singling out a firm's low prices as a source of potentially fatal harm to rivals.

Suppose, for example, that Delta Airlines seeks more business not by lowering its fares but instead by investing in safer aircraft (and advertising the improved safety of its fleet). Won't consumers then be more likely than before to fly on Delta? Of course—and a consequence is that United, USAir, AirTran, and other airlines will suffer. If they can't turn to government, Delta's rivals can avoid losing customers only by following its lead by making their airlines more attractive to consumers. These other airlines might cut their fares, or they might also invest in a safer fleet, or they might improve the quality of their in-flight service. They can compete with Delta in countless ways, all of which are to be expected—and applauded—in a market economy. Any airline that doesn't adequately respond to Delta's competitive move to increase the safety of its fleet might well go bankrupt. Indeed, it's remotely possible that Delta's investment in a safer fleet will bankrupt every last one of its rivals, leaving Delta with a monopoly. Surely, though, no one would seriously argue that government regulators ought to have the authority to stop Delta from increasing the safety of its fleet.

When firms cut prices (rather than use other methods) to compete, it is because in those cases price cutting is deemed to be the most effective way to satisfy consumers. In other cases, firms deem other methods to be best. Trusting bureaucrats and judges to second-guess entrepreneurs on how best to please consumers unleashes the possibility of a genuine (and dangerous) form of predation—namely, disgruntled rivals filing predatory pricing suits against entrepreneurial price cutters.

All price cutting should be legal. □

THE FREEMAN
Ideas On Liberty

Invisible Hand Obsolete?

It Just Ain't So!

Allen Murray's *Wall Street Journal* article "Pushing Adam Smith Past the Millennium" (June 21, 1999) purports to discuss the relevancy of Adam Smith's invisible hand for the 21st century. In reality, Murray is not talking about Smith or his invisible-hand metaphor at all. The assumption beneath his conclusion that "Smith's ideas will need some rethinking in the years ahead" is based on a false premise, namely, that Smith's ideas are valid only when markets conform to the world of perfect competition.

The validity of the invisible hand does not depend on market structures or "excludability" in the provision of goods or any of the other "problems" addressed by Murray and associated with perfectly competitive markets. Smith was drawing out the implications of a Lockean world based on "natural liberty." In this world, property is privately owned and freely exchanged. The idea that in pursuing their own interest people will be led as if by an invisible hand to promote the well-being of others is a logical implication of this institutional setting.

In Smith's system of natural liberty, if someone wants to significantly advance his material wealth he must produce things that will advance the well-being of others, and hence society's wealth. If Murray wanted to investigate whether the invisible hand would be an appropriate metaphor for the 21st century, he should have focused on the extent to which private property and freedom of exchange will be secure. Amazingly, this fundamental issue wasn't even raised.

Unrealistic Conditions

Perfect competition is an unrealistic set of conditions which, *when present in all markets simultaneously*, leads to an economy operating with "perfect efficiency"—that is, with all firms producing at the lowest possible cost. These conditions include perfect knowledge by all market participants, many price-taking buyers and sellers, complete homogeneity within product lines, and zero transaction costs. When one or more of these conditions are absent, most contemporary economists argue that markets are "failing." The obscure and otherworldly conditions of perfect competition are used as a benchmark to judge the success of real-world markets.

Murray implicitly takes this benchmark, illegitimately equates it with the invisible hand, and converts the neoclassical theory of market failure into a theory of "invisible hand failure." With no textual reference, Murray characterizes Smith's views with the following three statements: "In Smith's economy, if you consume a good, I cannot"; "In Smith's world [rapidly declining marginal cost] leads to monopoly"; and "In order for Smith's economy to work, sellers must be able to force consumers to become buyers and pay for what they use." This analysis all came about 150 years after Smith wrote and is integral to the world of perfect competition, not the world of *The Wealth of Nations.*

The invisible hand and perfect competition have little to do with each other. This is easily seen in the "problems" that Murray associates with the markets and technologies he expects will dominate the next century. He argues that "The cost to Microsoft of developing Windows software may be huge; but the marginal cost of putting it on one more computer is virtually zero." But this is only a problem within the realm of perfect competition, where efficient pricing requires that firms sell at marginal cost—an illogical result for any real-

world market. Under perfect competition, if marginal cost is zero, a positive price generates "market failure."

But this has nothing to do with the invisible hand. The fact is, unless he uses force, a person selling a product whose marginal cost is zero cannot sell to anyone who doesn't value it more than the price asked. No matter how far above zero the price, the seller—even one as powerful as Bill Gates—cannot make himself better off without making someone else better off. Nothing Murray says negates that fact.

Murray goes on to suggest that this zero-marginal-cost world could lead to monopolies in industries where network effects are important. He states that "in the network economy . . . tens of millions sharing the same e-mail system may have distinct advantage over those who don't. . . . In Smith's world, that leads to monopoly." Murray conflates Smith's world with the world of perfect competition and presents no historical evidence to support his claim. Under Smith's natural liberty, this "monopolist" would still have to make others better off in order to make himself better off. And so long as there were no legal barriers to entry, he would always have to be concerned about innovations and potential competitors.

Murray states that "the danger comes . . . if the pace of innovation slows and temporary monopolies become more permanent." But this is only a danger in the absence of entrepreneurial freedom. The real threat comes from governments that are likely to create barriers to entry with protectionism, franchises, or regulations that allow large firms to operate free of any threat from the outside. This real and historically relevant danger, which was Adam Smith's most important concern, goes completely unrecognized by Murray.

Free-Rider Problem

Finally, Murray frets about "the absence of excludability." His concern? "Digital data are cheap and easy to copy." To the extent that this is true, it may be too costly to exclude non-payers from using software once it is in use. The theory of perfect competition suggests that this will cause the product to be "underproduced."

The "problem" is that the assumption of zero transaction costs is being violated. The costs of excluding free riders are too high. To the extent that these costs make production of the good less profitable, the good will not be produced. But, of course, this is true of transportation costs, labor costs, and all other costs. Outside the world of perfect competition there is no logical reason for placing transaction costs in a separate category. To the extent that the good facing free-rider problems is not produced, resources are freed for other productive endeavors. Resources will flow to where the full costs of production, including transaction costs, are perceived to be less than the potential revenues.

Furthermore, Murray offers no historical evidence to support the underproduction hypothesis. Indeed, his point has been true of software from the beginning, and yet this is one of the fastest growing areas of commerce in the world. To some extent, "non-excludability" has always been present for all kinds of products—radio and television broadcasts, books and magazines, fashions. Indeed, non-excludability to some degree may be the rule rather than the exception. Yet, those preoccupied with perfect competition seem unswayed by the lack of real-world verification of their theory.

The invisible hand may not be an appropriate metaphor for the workings of economies in the next century. But this would be for the same reasons that it has not been an appropriate metaphor for most economies in the twentieth century. Liberty and the invisible hand are corollary. If liberty is treated with the same disdain in the next century as it has been in the present one, then the invisible hand may indeed be a relic of days gone by.

—Roy Cordato
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Material Progress Over the Past Millennium

by E. Calvin Beisner

Reginald Labbe, an English farmer better off than most in his time, died in 1293. His will listed the following possessions:

- one cow and one calf
- two sheep and three lambs
- three hens
- a bushel and a half (about 90 pounds) of wheat
- a seam (about 400 pounds) of barley
- a seam and a half of fodder for cattle
- a seam of mixed grain
- clothing comprising a hood, a tunic, and a tabard (a short, heavy cape of coarse cloth)
- a bolster (a long, narrow pillow or cushion)
- a rug (used as a blanket)
- two sheets
- a tripod or trivet (for cooking food over a fire)[1]

Like most English farmers of the time, he had used tools (probably little more than a hoe and a scythe) belonging to his landlord—which meant, too, that he owned neither land nor dwelling. He had no money. The money value of his estate in his day was figured at 33 shillings 8 pence (1 pound 73 pence), or about $2.75 at today's exchange rate. But of course in his day a shilling bought a great deal more than it does now, after seven centuries of inflation.

What would his possessions have been worth had he died today? Precise calculation is impossible; we don't know the age, weight, or health of his livestock or the quality of his other possessions. But rough estimates put the total value of his livestock today at around $1,000 (assuming that they were smaller and less healthy than typical livestock today), his grain and fodder at around $475 wholesale, his tripod at around $10, and his clothing and bedding at nothing (because they would have been both very worn and of such inferior make that no one today would be willing to use them). The total value of his estate, then, might have been around $1,485 (or £935). For comparison, the average value of farms in the United States today is about $350,000.

When Labbe died, the executor sold off his possessions to pay expenses. He paid a penny sterling (about $8.65 today) for the grave to be dug; twopence ($17.28) for the tolling of the church bell; sixpence ($51.84) for making his will; eightpence ($69.12) for court fees; 46 pence ($397.44) for food for the mourners and pallbearers; and threepence ($25.92) for the clerk who drew up the account for the estate—a total of 66 pence ($570.25), or a little over a third of the value of his estate. (Of course, he was not embalmed and had no hermetically sealed, velvet-lined, stainless steel

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casket to preserve his body for a thousand years.)

If Labbe lived to the average age of people born in the thirteenth century, he was under 30 when he died. More likely, since he had survived infancy and childhood (about half did not), he died in his 30s or 40s. Probably at least one wife had preceded him in death, perhaps in childbirth—one of the most common causes of death for women at the time. Assuming he had fathered eight children in his years of marriage, he would probably have buried four of them in their infancy, perhaps another before its fifth birthday, and another before puberty. If he was fairly typical, then, two of his children survived him.

Slow Population Growth

Such was life, for the moderately better off, in a society in which the death rate was normally so close to the birth rate that population grew at only about 0.17 percent per year, doubling about every 425 years instead of every 42 years, as it would at the world's average growth rate in the 1980s, or every 51 years, as it would at the average rate for the 1990s.[2] Even for the wealthy, life wasn't much more secure. Infant and child mortality rates were little better for the very rich—royalty and nobility—than they were for farmers and peasants, even into the eighteenth century. Britain's Queen Anne (1665–1714) was pregnant 18 times; five of her children survived birth; none survived childhood.

To be more precise, such is a tiny glimpse of life for people throughout most of the past millennium in countries that now are among the richest in the world. There is a good deal more to describe. Most of it is about as dismal by comparison with our experience.

You might have been surprised at the cost of the food served to the mourners and pallbearers at Labbe's funeral—by far the largest cost associated with his death. That is because food was far more expensive in the past, in comparison with labor and practically any manufactured product, than it is today. Agricultural yields were far lower, both per acre and per man-hour of labor.

Eighteenth-century French farming, for instance, produced about 345 pounds of wheat per acre; modern American farmers produce about 6.2 times as much, 2,150 pounds.[3] Early fifteenth-century French farmers produced about 2.75 to 3.7 pounds of wheat per man-hour, and the rate fell by about half over the next two centuries;[4] modern American farmers produce about 857 pounds per man-hour[5]—about 230 to 310 times as much as their French counterparts around 1400 and 460 to 620 times as much as French farmers around 1600. (By the way, this means modern farmers also manage to farm from 37 to 100 times as many acres as their earlier counterparts did. Chalk it up to mechanized equipment.) As the great French historian Fernand Braudel pointed out, life was difficult to live when productivity in wheat fell below 2.2 pounds per man-hour, but for most of the 350 years from 1540 to 1890, productivity was well below that.[6]

Such facts help to explain why earlier generations spent a major part of their incomes just on food (excluding its preparation, pack-



aging, transport, and serving), while we spend far less (under 6 percent of total consumer expenditures in the United States in the 1980s). These developments—along with the advent of glass windowpanes (to admit light and heat but exclude cold and pests) and screens (to admit fresh air and exclude disease-bearing insects); treatment of drinking water and sewage; mechanical refrigeration (to prevent food spoilage and consequent waste and disease); adoption of safer methods of work, travel, and recreation; and the advent of sanitary medical practices, to say nothing of antibiotics and modern surgical techniques—also help to explain why people live about three times as long now.

All this is just one way of looking at changes in human material conditions over the past millennium. Others also are important and instructive.

When Would You Rather Have Lived?

Try a thought experiment. Would you rather live as you do today, with your present income and expenditure patterns, or as royalty lived throughout the last millennium up to the late nineteenth century? It is tempting to pick the life of past royalty. But consider just a few of the things you would have to do without:

- Electricity and all it powers: lights, telephones, radios, televisions, refrigerators, air conditioners, fans, VCRs, X-rays, MRIs, computers, the Internet, high-speed printing presses, and all other industrial automation.
- Internal combustion engines and all that they power: cars, trucks, buses, planes, farm and construction equipment, and most trains and ships.
- Hundreds of synthetic materials like plastic, nylon, orlon, rayon, vinyl, and the thousands of products—from grocery bags and pantyhose to compact disks and artificial body joints and organ parts—made from them.

None of these things were available to anyone, at any price.

No matter how rich you might have been a millennium—or even 150 years—ago, if you'd contracted a bacterial disease, you could not have been treated with antibiotics. If you had wanted to travel from Great Britain to Australia, you could not have done so in less than months, at great discomfort and great risk, not in less than a day and at less risk than driving across London. You could not have enjoyed air conditioning or iced drinks during a hot summer. You could not have talked with anyone by any means other than direct voice. Until the advent of the telegraph in the second quarter of the nineteenth century, you could not have communicated at a distance in writing any faster than you could have traveled; and it was decades later before telegraphic communication was readily available to most cities and towns. You could not have taken or viewed photographs, listened to recorded music, or viewed—let alone made your own!—motion pictures.

Yes, the few rich of the past lived in opulence. (Don't think of castles, most of which were cramped and quite uncomfortable, built for defense rather than comfort.) Think of the great mansions like Blenheim Palace in Oxfordshire, the Château Fontainebleau in France, or even, here in the United States, the Biltmore House in Asheville, North Carolina. Or picture the homes of royalty, like Buckingham Palace or Hampton Court in London, or the Palace of Versailles in France.

But however opulent the surroundings, with their magnificent architecture, gardens, carpets, furniture, china, silver services, and art collections, they were not very comfortable. Heating and especially cooling these mansions were constant problems. They were far less sanitary, and far more smelly, than most lower-class dwellings today. Indeed, the very magnificence of the dwellings of the rich is testimony to the absence, in a pre- or primitive-market culture, of other, more attractive uses of their wealth. A higher proportion of people in advanced countries today can afford to build and furnish great mansions than could in centuries past. But they don't. Why not? Because most of them invest their wealth in productive enterprises or spend it on travel and entertainment instead.

And sanitation? The literary historian James Clifford, after years of note-taking on every reference he could find to sanitation in London, wrote an article that American historian Bernard Bailyn described simply as "horrifying."[7] "A bathroom was a very rare luxury in . . . seventeenth- and eighteenth-century houses. Fleas, lice and bugs conquered London as well as Paris, rich interiors as well as poor," wrote Braudel. "So if we moderns were to enter into an interior of the past, we would very soon feel uncomfortable. However beautiful it might be—and it was often wonderfully so—what seemed like luxury to the people of the past would not be enough for us."[8]

Overland travel even for the rich was by horseback or carriage, and the 450-mile journey from London to Edinburgh, driven by lower-class car owners today in a comfortable seven hours or flown in an hour, required two 18-hour days in a bumpy carriage with neither air conditioning nor heat. For the poor, travel was almost entirely on foot.

Keep the Doctor Away

Medical care? You don't even want to imagine most of it. There were no more effective anesthetics than alcohol and cloves, so when limbs gone gangrenous from infections that would be cured or more likely prevented easily today had to be amputated, patients gritted their teeth and hoped they would pass out from the pain of the crude saws. Germ control? Nonexistent. The germ theory of disease didn't become current until the late eighteenth century, and the use of antiseptics didn't begin until half a century later. Even then, what your doctor didn't know could kill you. The high rate of maternal death in childbirth in early nineteenth-century America is attributable in part to belief in "laudable pus." Doctors believed pus itself was curative, so they would purposely spread it from patient to patient, including to mothers in childbirth.[9] Got a fever? Don't call the doctor; he's likely to bleed you to death trying to cure it. In fact, medicine was so primitive it was a favorite cover for spies; physicians were trusted everywhere, but it took little knowledge to pass for one.[10]

Education was the province of the rich. Few countries before the Reformation had widespread education, and even afterward, schooling was available principally to the rich. A major exception was Scotland after John Knox's followers, convinced that personal knowledge of the Word of God was essential to the maintenance of religious as well as civil liberty, arranged a parish-by-parish system of church-run grammar schools which ensured that practically every child could at least become strongly literate. Scotland's high literacy rate, coupled with its Calvinist ethics of work and saving, were important factors in its making contributions to the Industrial Revolution far out of proportion to its small population. But even there, few were schooled for more than five or six years, and only a tiny percentage attended college, let alone graduated.

Today, by contrast, in the United States, 81 percent of persons 25 years old and over are high school graduates and 23 percent are college graduates, and the growth in availability of education is worldwide. That is a particularly crucial factor in predicting the world's material future, because the creation of wealth depends primarily not on brawn but on brain.

The bottom line? Materially, the world is a far, far better place today than it was not only a millennium ago but even a century ago. Today, every raw material—mineral, plant, and vegetable—is more affordable (which economists will recognize as meaning more abundant), in terms of labor costs, than at any time in the past. Every manufactured product is more affordable than it has ever been. And in producing all this great abundance, we have also reduced health-threatening pollution. Put simply, the world is both a wealthier and a healthier place today than ever.

The most crucial measures of material welfare are mortality rates and life expectancy, since most people value preserving life more than any other material good. A thousand years ago, life expectancy everywhere was under 30 years; today, worldwide, it is over 65 years, and in high-income economies it is over 76 years. The under-five mortality rate has plummeted from about 40 percent every-

where as late as the nineteenth century to under 7 percent worldwide today, and under 1 percent in high-income countries. And improved life expectancy comes not just from declining child mortality but from declining mortality rates at every age of life.

The late economist and statistician Julian Simon, a friend and mentor, produced in 1995 as his last major editing effort a big book, *The State of Humanity*, to show long-term trends in hundreds of material measures of human well-being. Parts cover such categories as life, death, and health; standard of living, productivity, and poverty; natural resources; agriculture, food, land, and water; and pollution and the environment. Want to know long-term trends in slavery, housing quality and affordability, leisure time, energy resources, forest growth, crop and livestock productivity, air and water pollution, disease, murder and suicide, even accident rates? They're all there, in chapters by 60 world-class scholars.

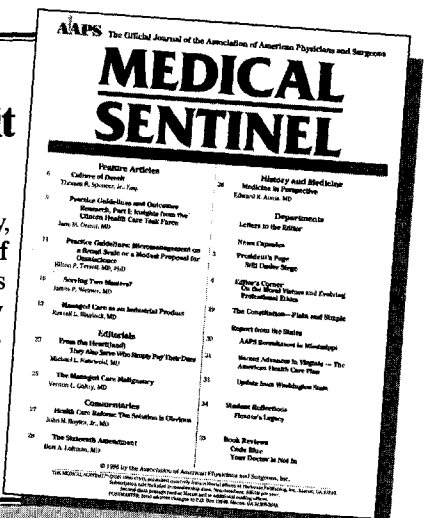
"This is the central assertion of this book," Simon wrote: "Almost every absolute change, and the absolute component of almost every economic and social change or trend, points in a positive direction, as long as we view the matter over a reasonably long period of time. That is, all aspects of material human welfare are improving in the aggregate.[11]

Simon's view has raised eyebrows through the years, but the empirical evidence supports it overwhelmingly. If you're looking for a good way to get a grasp of the material changes we've experienced over the last millennium, *The State of Humanity* would be a great place to start. □

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9. Private communication from Philip T. Newton, M.D.
10. Alan Marshall, *Intelligence and Espionage in the Reign of Charles II, 1660–1685* (Cambridge: Cambridge University Press, 1994).
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THE FREEMAN
Ideas On Liberty

Spontaneous Order on the Playground

by Andrew P. Morriss

I recently observed an intriguing example of the evolution of a private property, market-based spontaneous order at my children's elementary school. A group of fourth and fifth graders created a set of playground rules analogous to those I learned about in my work on spontaneous orders in the nineteenth-century gold rushes throughout the western United States. I was pleased, but not surprised, to find that fourth and fifth graders created a solution to a playground problem based on property rights and markets.

My children attend a Montessori elementary school in Cleveland Heights, Ohio. My older daughter, Kathleen, is in the fifth grade. At this school, as in all Montessori schools, children are grouped in multi-grade classrooms—Kathleen's has fourth and fifth graders together in each of two classrooms. Although the classrooms work separately on most academic subjects, activities like recess are joint. There are thus about 60 children (with four teachers and aides) in the two classes, with a slight preponderance of girls.

The school grounds are not large, although there is a playground plus a large playing field shared with a neighboring Catholic girls' high school. One of the locations that attracts many of the fourth and fifth graders is "the woods," an area of bushes and trees that lies along the border between the school parking lot and playground and the shared athletic field. Here the fourth- and fifth-grade children have created a series of "houses" under various bushes and trees and an economy based on a pinecone currency. I found what my daughter told me about their games fascinating, so I interviewed a large group of her classmates about how they play in the woods.

Establishing Property Rights

On the first day of a school year, children claim their houses by marking off boundaries with various materials (rocks, sticks, logs) that they find in the woods. They then devote considerable effort to improving their houses—adding furniture constructed from materials found in the woods (by common agreement outside materials cannot be brought into the woods). Some create "stores" in which they "sell" materials they create such as "paints" made by pounding plants and rocks into dusts. Others have "hotels" where the homeless (children who come late to the game) can rent rooms until they can negotiate to join an existing house. Additional rooms are added to houses by clearing space under nearby bushes and trees or by purchasing them from neighbors. The rights to a space demarcated in this fashion appear to be widely accepted by both those playing in the woods regularly and the fourth and fifth graders who choose to do something else. (A regular soccer game is a major alternative.)

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Only two groups failed to respect the property rights the children had established. One was a group of three-, four-, and five-year-olds (who have a different recess period) and who, although technically forbidden from playing in the woods, sometimes crashed through the houses in a herd. The second was a group of elementary-age children from another school who sometimes used the adjacent athletic field.

In creating their property rights in this fashion, the children are behaving like the miners who flooded into the American west in 1848–1849 and later years. Like the children at my daughter's school, miners would appear in large numbers in an area of limited physical resources. Like the children, the miners quickly developed simple rules that guaranteed their property rights. Like the rules developed at the school, the miners' rules were respected by latecomers.

Also like the miners (and like most legal systems), the children have developed a concept of adverse possession. Houses left vacant for extended periods (all agreed it was more than one week and less than a month) could be occupied by others, whose title to the property would be recognized by the group. Use of property was thus encouraged. Similarly the miners in the gold rush respected claims left unoccupied for short periods while their owners went for supplies, so long as the claim was marked in some fashion.

Property claims in both systems extended to moveable property. The western miners often left piles of gold ore and valuable supplies in their camps, unguarded out of necessity, while the miners sought more gold. By all accounts, thefts from the unguarded camps were comparatively rare. Similarly, the children leave their stashes of pine cone currency unguarded as well as their collections of materials.

Dispute Resolution

While no children's game would be complete without disputes, this game seems remarkably free of disputes in many respects. In part this is because the clear property rights in their houses give each child a space free from outside interference to play as each wishes. Unlike the commons of a playground, where one group's fantasy game on the jungle gym could be interrupted by another group that insists on its equal right to occupy the space for a game of tag, no group of children can impose on another by disrupting a game in progress. I suspect that one of the major attractions of the woods as a play space stems from the control those property rights provide.

Only one major property rights dispute occurred during the past school year. One child claimed a house occupied by another group of kids. The issue was not decided on a "might makes right" basis. Instead all agreed to choose an uninvolved child as the "judge" and to conduct a court to settle the issue. After the first candidate for judge was rejected as potentially biased, they settled on a child whom several described as the "smartest kid in the class." Each side then found a "lawyer" to present its case, and presented and cross-examined witnesses. After a reportedly dramatic presentation of factual inconsistencies in one side's story, the judge decided for the other side. All accepted the decision—no appeal was lodged with the teachers.

This brings us to another important point. One question always raised about privately based legal systems is the extent to which such systems ultimately depend on external enforcement of the rules they create. There was no such outside authority during the gold rush because the miners were too far from established centers of political authority to appeal to the state. In the rare case that there were nearby military authorities, the tendency of troops to desert to the mines at every opportunity restricted the availability of government force. Surely children in an elementary school, however, could appeal to their teachers to settle disputes.

As part of the Montessori teaching method, the teachers at the school emphasize that the children must solve their own disputes. When I questioned the kids about whether the teachers were available to settle property boundary disputes and the like, they unanimously agreed that the teachers were no help at all. "They just tell us to work it out," one complained. Another agreed that "the teachers just do what they always do, ask us how we'll fig-

ure it out ourselves." Indeed, the children agreed that they did not often seek assistance from the teachers since any major dispute could result in the entire class being told they could not play in the woods for a week while tempers cooled.

Of course, the children are not playing in a state of nature, as the nineteenth-century miners were. The threat of a trip to the principal's office exists for those who attempt to attack others on the playground. Punching another student is not the only way to use violence, however. In my school days the successful school bullies were the masters of applying force in ways unnoticeable to the teachers. One of the things that struck me most about "the woods" was the absence of any evidence of such behavior.

Exchange

In the first gold rushes, miners frequently made rules forbidding sale of claims in an attempt to discourage "speculation." These rules rarely lasted more than a few months as both the new arrivals and original appropriators quickly realized the mutual benefits that trade made possible. Because children often tend to have absolutist ideas about property (at least when it comes to sharing with siblings), I was curious to see how the children dealt with issues surrounding potential exchange of property rights.

Using pine cones as currency, the children developed a cash economy. One could sell goods (items found in the woods), natural resources (kids dug for stones), and labor (owners frequently hired "sweepers" to clean their houses). Alternatively, while pine cones were relatively scarce commodities, they could be directly harvested by investing time in a search. Property rights in houses were freely alienable and changed hands fairly often. Groups of children who played together might break up and some seek new homes; newcomers might join the game or players might decide to switch to soccer and "cash out." Like the gold miners, the children intuitively understood the concept of comparative advantage.

In addition, the overall game rewarded entrepreneurial activity. Children who thought of new uses for the property were able to accumulate significant pine-cone stashes. One group built a "golf course" and charged to play; many others sold particular items and rented rooms.

Interestingly the children resisted destabilizing their currency and society by importing outside pine cones. The Cleveland area has many trees and parks and pine cones are readily available with much less effort than "sweeping" another's house in the woods, yet no one seemed to consider importing pine cones as an alternative source of income. When I walked in areas thick with pine cones with my daughter and her friends, they resisted my suggestion to gather any of the "money" lying on the ground.

Origins

The establishment of houses in the woods is a longstanding game, handed down from class to class. Much as the experienced gold miners known as "old Californians" transmitted miners' law throughout the western United States mineral rushes, the fifth graders hand down the oral tradition of the rules for play in the woods. Thus it is easy to see how the tradition has perpetuated itself.

I should stress, however, that this is not the "Ayn Rand Learning Center" made famous in an episode of the Simpsons. The Montessori system does not include any significant economics content (at least through the fifth grade) and certainly no study of Austrian economics. No U.S. history is taught before the middle school, so the children have not studied the gold rush. Even the fifth graders are barely through ancient civilizations and so unlikely to have devoted much time to studying the developments of markets or trade. Thus they haven't learned market solutions or property rights from a textbook.

They might have learned these lessons at home but these children are also not, as far as I can tell, drawn from libertarian homes that emphasize such things. For example, as a rough proxy of the political climate, in 1996 Bill Clinton overwhelmingly won a straw poll against Bob Dole and Ross Perot in my

daughter's lower elementary class (Harry Browne didn't even make the ballot). Thus they are no more likely than any other group of suburban fourth-grade and fifth-grade kids to have spent much time pondering markets and property rights outside school.

I think there are two explanations for the emergence of a private-property, market-based spontaneous order among my daughter and her classmates. First, the Montessori curriculum puts a heavy emphasis on children learning to solve their own problems. As noted above, the teachers do not intervene to resolve disputes among children other than to restrict the use of force and direct the children toward means of settlement. Appeals to outside authority are thus unavailable except where a child attempts to use force. Since no one controls the game, the children were forced to develop mechanisms that respected the autonomy of the other children and made peaceful interactions possible. Whenever the first fourth and fifth graders hit on such a solution, its advantages would have become immediately apparent.

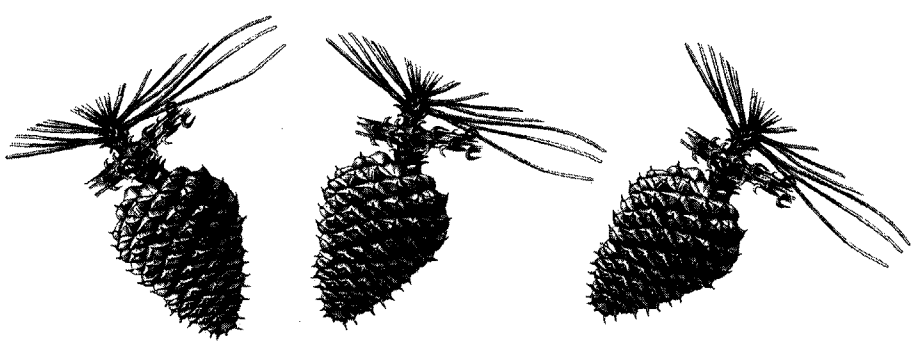
Second, and more important, markets and property rights are natural in a way that authoritarian structures are not. The freedom such solutions provide is just what many children desire (and plenty of adults too!). My daughter and her classmates intuitively know how to facilitate the development of their own spontaneous order that enables them to play the games they want to play while accommodating their classmates' desires to play differently. These children have discovered how to coexist in an environment of diverse interests.

Learning from Kids

There are obviously huge differences between the nineteenth-century American gold rushes and my children's elementary school. Nonetheless the systems of rules and property rights that evolved in both have significant features in common: a reliance on private property rights and market exchange, a limited set of rules facilitating individuals acting in their own interest, and limited resort to outside sources for rule enforcement. It is no accident that these features appear in such a diverse set of social orders. It is precisely because they are so easily generalizable that market-based systems of property rights can accommodate both elementary schoolchildren's games and a gold rush.

The rule of law takes effort to establish, of course. The nineteenth-century miners had to rely on their own resources to set it up. The children can rely on the "night watchman" state provided by the teachers and administration to prevent violence. What is striking is how little intervention was needed to establish peace and good order among both the thousands of mostly single young men who flocked to the gold fields and the fourth and fifth graders described here. It is hard to imagine groups less likely to fall naturally into an orderly society on their own than gold miners and schoolchildren. That they both accomplished it so easily speaks well for our chances to do so on a larger scale.

Many adults could learn quite a bit from the children in my daughter's class. The students found their way to a means of allocating private property rights in a desirable area of the playground that gives each the freedom to play as he or she sees fit without impinging on the rights of others. If more adults imitated such behavior in their lives, we would be much closer to a society of free and responsible individuals. □





States, Economic Freedom, and Wealth Creation

Montesquieu once observed that "Countries are well cultivated, not as they are fertile, but as they are free." The *1999 Index of Economic Freedom*, published by the Heritage Foundation and the *Wall Street Journal*, examined 161 countries and came to the same conclusion: "Countries that have the most economic freedom also tend to have higher rates of long-term economic growth and are more prosperous than those that have less economic freedom." Unequivocally, the numbers show that "countries with the lowest levels of economic freedom also have the lowest standards of living."

One would expect that within a country the same pattern would be evident. Indeed it is, and now we have a comprehensive analysis that proves it: *Economic Freedom in America's 50 States* by economists John Byars, Robert McCormick, and Bruce Yandle. Commissioned by the State Policy Network, an association of some three dozen state-based free-market think tanks, the report argues that "states with relatively more economic freedom enjoy higher rates of growth . . . because individuals in those states are allowed to keep more of their income, and thus the marketplace can more efficiently determine the allocation of resources."

There are profound lessons here for state governments. Their actions and policies *do* make a difference in the material welfare of their citizens. People respond to incentives and disincentives, and they tend to migrate, taking their skills and capital with them, to those locales where those skills and capital are relatively safe from the depredations of high taxes and regulation. Governors and state legislators who want to accumulate power and centralize resources while proclaiming a desire to spur growth are trying to have their cake and eat it too.

Economic Freedom Defined

From the start, the report assumes a definition of "economic freedom" that comports with the ideas of classical-liberal thinkers. The individual is a sovereign entity that the state respects by minimizing its intrusions and providing for a common defense. Economic freedom is expanded when governments limit "encroachments on opportunities for individuals to engage in voluntary exchange." It is contracted when states interfere with voluntary exchange through an array of costly impositions.

Every state provides its own "bundle" of costs and benefits. The tax burden may be low in a state at the same time the regulatory burden is high. A state may have low tax and regulatory burdens that are at least partially offset by a judicial system that encourages frivolous lawsuits or bestows abnormally large damage awards that overcompensate harmed parties and thereby exposes individuals to higher risks of property confiscation and redistribution. A relatively high level of wel-

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fare spending indicates a state is engaged in more income redistribution than others, a violation of economic freedom, and this may offset an otherwise friendly regulatory environment. In any event, the report agglomerates all this information in about as scientific a fashion as is possible.

It assembles data on more than 200 indicators, grouping the resulting measurements under five key categories: fiscal, regulatory, judicial, government size, and welfare spending. Each state is then assigned a rank, from 1 to 50. Idaho turned in the best score as the state with the greatest degree of economic freedom, while New York came in dead last. The five states with the most economic freedom (Idaho, Virginia, Utah, Wyoming, and South Dakota) boasted growth in personal income from 1990 to 1997 that was a spectacular 59 percent higher on average than the five states with the lowest levels of economic freedom (New York, Rhode Island, New Jersey, Massachusetts, and Connecticut).

Just as the human traffic around the world tends to move from the less free to the more free countries, migration patterns within the United States show similar movement. The report confirms that "people are moving into states with high levels of freedom and out of states with low freedom." Birth rates are not markedly different from state to state, so changes in population are heavily influenced by the movement of people. The difference in population growth between the top and bottom of the freedom scale is especially dramatic: Idaho—the freest state—saw its population soar by 16.8 percent from 1990 to 1997, while New York—the least free state—barely held its own with a paltry growth rate of just 0.8 percent.

Per capita personal income in Idaho in 1996 was a low $19,539 when compared to New York's $28,732—a fact which by itself might suggest a conclusion diametrically opposite of the report's general finding. Having lived in Idaho in the mid-1980s, however, I can certify that $19,539 goes a lot further than the same amount of income in a high-cost-of-living state like New York. Indeed, Byars and colleagues show that residents of New York pay twice the state and local taxes than residents of Idaho: $3,858 versus $1,955.

You're also more likely to be working if you live in Idaho rather than in New York. The unemployment rate in Idaho was 3.7 percent below the national average in 1996, while New York's was 15 percent above. In the 1990s, both per capita income and gross state product boomed in Idaho at almost twice the respective rates of New York.

Business Incentives

The strong, positive correlation between economic freedom and economic growth that the report demonstrates has implications for the states in an increasingly controversial area of policy: "incentive" packages designed to lure businesses. Almost every state is now engaged in a tit-for-tat war of selective tax abatements and direct subsidies. For example: To attract a new factory for Ohio and prevent it from locating in neighboring Michigan, Ohio politicians may offer to forgive several years of taxes due and even give the company millions of dollars for job training and infrastructure.

The report does not directly address this form of competition among the states, but its bottom line certainly points in one particular direction. If states want to cultivate growth and prosperity, they should focus on the forest and the trees will take care of themselves. To the extent that these incentives are targeted at a few at the expense of the many, they rearrange wealth and politicize it—which works against an improvement in overall economic freedom. State governments would be better advised to reduce burdens on everyone and foster a policy of "a fair field and no favor." Economic freedom, not political redistribution, is what makes a state—and indeed, a nation—prosper.

Byars, McCormick, and Yandle have done us a favor by proving beyond a shadow of a doubt what we all should have instinctively known. Freedom works, and more of it works even better. □

THE FREEMAN
Ideas On Liberty

The End of Liberty

by Stephan F. Gohmann

Have you checked the coins in your pocket lately? If you see a shiny coin with the image of a man on a galloping horse, be advised that it's not an arcade token but a real U.S. quarter dollar. This new coin is the first of 50 state commemorative quarters to be released over the next decade by the U.S. Mint, which is allowing each state to design the back of the quarter for its own version. The Delaware horseman is Caesar Rodney, a Revolutionary War general who rode all night from Dover to Philadelphia to cast a crucial vote in an effort to assure unanimous support for independence by the 13 original colonies.



The minting of "Caesar" on a U.S. coin symbolizes something that at least some members of the Second Congress worked to avoid. A major disagreement during debate on establishment of the mint was over the image to engrave on coins—a political leader or a symbol of Liberty. Although Liberty won, a cursory check of the coins in your pockets will make it clear that this victory, like others of the founding fathers, was short lived. Not one currently circulating coin bears an image of "Lady Liberty" or anything similar; instead, the images are of politicians.

One contention of those members of Congress who were against the practice of placing a politician's image on a coin was that it would seem emblematic of a monarch. Ironically, with this new Delaware quarter, Americans now have a Caesar on their coins!

Prior to 1909, Americans came into contact with an image of Liberty every time they touched a coin. Since then, that daily association has diminished, and in 1947, when Benjamin Franklin's visage ended the reign of the "Walking Liberty" half dollar, the government eliminated all incidental contact with Liberty. The Liberty half dollar supplanted by Franklin (without his permission), was the last U.S. coin in circulation to be minted with her image. While current coins bear the inscription "Liberty," they no longer contain her image. The sole exceptions are patriotic-seeming coins intended to be sold to collectors, such as silver dollars and gold and platinum coins of higher denominations. It is time to bring Liberty back!

Although many may argue that what appears on our coins is of little importance,

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the image of Liberty gives a daily reminder of what the founders believed when the country began. That Liberty has been replaced on every coin by a politician (with the current exception of the dollar) is an indicator of how the ideology of government leaders has changed. The Second Congress showed reverence for liberty and limited government. Today's coins, with the image of politicians, show reverence for government and its leaders.

A Brief History of Liberty

On December 21, 1791, the Senate had the first reading of "a bill establishing a mint and regulating the coins of the United States." The bill contained a section pertaining to emblems to be placed on the coins. On one side of the coin was to be "an impression or representation of the head of the President of the United States for the time being, with an inscription which shall express the initial first letter of his Christian or first name and his surname at length . . . and upon the reverse . . . shall be the figure or representation of an eagle."[1] Apparently, there were senators who opposed having the President's image on the coin because on the second reading an amendment was proposed. The amendment said that the coin should include an engraving of two hands united surrounded by circles equal to the number of states in the Union at the time of coinage. On the reverse was to be a representation of the female figure of justice holding balanced scales, with the inscription, "To all their due." This amendment was defeated on January 12, 1792, and the bill passed the Senate with its original wording intact.[2]

When the bill reached the House of Representatives, an amendment was put forth to strike the requirement of the President's image in favor of some emblem of Liberty. In support of the motion, Representative John Page said "it had been the practice in Monarchies to exhibit the figures or heads of their kings upon their coins either to hand down in the ignorant ages in which this practice was introduced, a kind of chronological account of their Kings, or to show to whom the coin belonged." He further argued that the money of the United States is "not the money of the President. I am certain it will be more agreeable to the citizens of the United States to see the head of Liberty on their coin than the head of Presidents. However well pleased they might be with the head of the great man now their President, they may have no great reason to be pleased with some of his successors."[3] Page obviously had great foresight.

In rebuttal, Representative Samuel Livermore suggested that the head of the President would make a good emblem of liberty. After debate, the amendment was split in two. The first part striking the words "or representation of the head of the President" passed 26 to 22. The second part calling for an emblem of Liberty passed 42 to 6. The Senate, however, disagreed with this amendment and moved that the House should recede from its position.

When the Senate's response was sent back to the House, Livermore argued in support of the Senate saying that it would flatter the President at no expense to the country. This notion was rebutted by Representative John Francis Mercer, who had been Washington's aide-de-camp. He pointed out that rulers such as Nero and Caligula had also had their images on coins, so it might not necessarily be an honor. Representative Egbert Benson felt uneasy leaving the representation of Liberty up to the judgment of an artist and ridiculed the idea that the people would be enslaved by their president and his image on a coin.

John Page again defended Liberty arguing that "as long as the people were sensible of the blessings of liberty, and had their eyes open to watch encroachments, they would not be enslaved; but if they should ever shut them, or become inattentive to their interests and the true principles of a free Government, they, like other nations, might lose their liberties; that it was the duty of the members of that House to keep the eyes of their constituents open and to watch over their liberties."[4] He argued further that he did not want to treat the president as a monarch and wanted to give few incentives to those who wished to be president. Page feared that certain ambitious individuals would hope to make a name for themselves by becoming president and then having their names handed down through history through their image on coins. Given how

almost every modern president has been conscious of the legacy he would leave, Page again seemed to be unusually insightful.

The question that the House recede from its amendment was defeated 32 to 24. Then the Senate backed down, and the bill passed both houses. Liberty became the emblem for all United States coins.

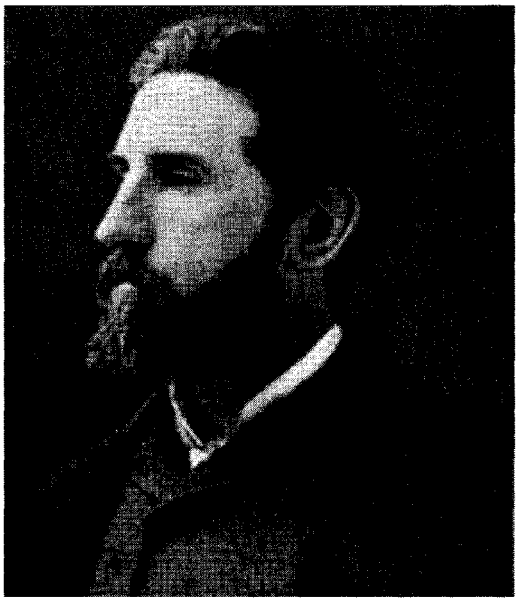
All was well for Liberty on our coins until 1890 when a bill passed Congress foreshadowing the beginning of the end. The Mint had often redesigned coins, but almost always included the figure of Liberty. The 1890 act allowed the director of the Mint, with concurrence from the secretary of the treasury, to redesign any coin as long as it then remained unchanged for at least 25 years. The director had great discretion regarding the emblem of Liberty.

Over the next half of a century, Lady Liberty would disappear from our coins. Liberty was removed first from the penny, and then from the nickel, quarter, dime, and half dollar.

TR and the Coins

One of President Theodore Roosevelt's pet projects was the design of the U.S. coins. Some coins minted during his presidency are thought to feature the most beautiful representations of Liberty. Roosevelt commissioned Augustus Saint-Gaudens to design a coin with Liberty in the classical Greek and Roman design. One of Saint-Gaudens's students, Adolph Weinman, was responsible for creating the Mercury dime, which is an image of Liberty in Mercury's headdress.[5] However in 1909, President Roosevelt wished to issue a coin to commemorate Lincoln's 100th birthday. The Lincoln penny would replace the Indian-head cent. But the image on that penny was not an actual Indian; it was the head of Liberty in Indian headdress. The minting of the Lincoln cent breached the intent of the Second Congress. Liberty was replaced by the image of a president who many would argue usurped constitutional powers held by the people and the states.

The five-cent piece was initially a half dime. Liberty appeared on the silver half dime from its first minting in 1794 until 1873.



Augustus Saint-Gaudens (1848–1907)
Sculptor and designer of classic coins.

The nickel five-cent piece, established by the Act of May 16, 1866, did not initially have a representation of Liberty. It had a shield on one side and a "5" surrounded by 13 stars on the obverse. In 1883, these nickels were replaced by a Liberty-head nickel that was minted until 1913. In that year, Liberty was replaced by the Indian-head or buffalo nickel. Twenty-five years later, the Jefferson nickel replaced the buffalo nickel, again contrary to the intent of the Second Congress.

The Washington quarter was issued in 1932 to commemorate the 200th anniversary of his birth. The standing Liberty quarter had been subject to considerable criticism due in part to the initial design that showed Liberty with one breast exposed. Lady Liberty was replaced with the word "liberty" imprinted next to the image of President Washington, the President whose image Congress explicitly debated against placing on coins.

The dime was first minted in 1796 and contained a representation of Liberty until 1945. The change to the Franklin Roosevelt dime was made by the director of the Mint, Nellie Tayloe Ross, shortly after Roosevelt's death, at the urging of Representative Clyde Doyle. In his letter he said that using Roosevelt's likeness would please the American people and would increase the circulation of the coin.



Half dollar (Kennedy type), 1964: Lady Liberty disappeared from coins in the 1940s.

He favored putting Liberty on the other side, but that did not occur.[6] The wings on Liberty's headdress on the old Mercury dime represented liberty of thought. How ironic that this dime was replaced in 1946 by one bearing the likeness of the great champion of big government.

In 1948 Nellie Tayloe Ross again removed Liberty from a coin. This time the Walking Liberty half dollar was replaced by one with the image of Benjamin Franklin. Fifteen years later, Franklin's image was replaced by that of John F. Kennedy. The Kennedy half dollar had to be legislated since the Franklin had been minted for only 15 years and not the required 25. Weeks after Kennedy's death, President Lyndon Johnson sent a letter to Congress requesting that the half dollar bear the likeness of President Kennedy. Congress wanted to act quickly so that the new 50-cent dies would be ready in time for the new year. Representative William Moorhead of Pennsylvania used the precedent of the coinage of the Roosevelt dime to argue for the immediate change to the Kennedy half dollar. Representative Durward Hall from Missouri opposed the bill, arguing that the House was acting too quickly "under the guise of mass psychological hysteria."[7] Hysteria won out. The bill passed the House 352 to 6 and shortly thereafter passed the Senate.

Liberty has not appeared on a circulating coin for 52 years. Most of the population of the United States was not alive when the last Liberty coin was minted.

So what does this history tell us? Our coins originally were emblematic of liberty. Now they are emblematic of strong centralized government and reverence for its past leaders. One reason we don't have Lady Liberty on our coins may be found in words spoken by John Page during the debate on the mint: "it was the duty of the members of that House to keep the eyes of their constituents open and to watch over their liberties." By removing the image of Liberty from our coins, perhaps federal authorities hoped to reduce any possibility that the American people would realize that their liberties were slipping away. □

1. *Annals of Congress*, Second Congress, Senate, January 1792, p. 71.
2. Ibid.
3. *Annals of Congress*, Second Congress, March 24, 1792, p. 484.
4. Ibid., p. 488.
5. See Ted Schwarz, *Beginner's Guide to Coin Collecting* (Garden City, N.Y.: Doubleday Dolphin Books, 1980).
6. *Congressional Record*, 1945, pp. A2207–2208.
7. *Congressional Record*, 1963, p. 248225.

THE FREEMAN
Ideas On Liberty

Einstein's Brain and the Egalitarian Mind

by Steven Yates

Late last spring a team of neuroscientists based at McMaster University in Ontario, Canada, released the first detailed study of Albert Einstein's brain, which had been preserved since his death in 1955. Einstein was sympathetic to the idea of having his brain studied by scientists after his death.

The team, led by Dr. Sandra F. Witelson, concluded that Einstein's superior mathematical and scientific abilities resulted from certain features of his brain not shared by people of average intelligence. Their results were published in the June 19, 1999, issue of the British medical journal *The Lancet* under the title "The Exceptional Brain of Albert Einstein."

The area of the human brain thought to be the seat of mathematical, visual, and spatial reasoning is known as the inferior parietal region. It is found at ear height in the part of the brain known as the cerebrum. What Witelson and her team found was that Einstein's inferior parietal lobes were 15 percent wider than those of a control group of 91 "normal" brains. In Einstein's brain, a cleft known as the Sylvian fissure diverted from its usual structure. Apparently, the change occurred when Einstein was in his infancy. It did not permit Einstein's brain to develop what is called a sulcus, a groove that normally runs through this part of the brain. The neuroscientists theorized that the absence of this groove may have allowed far more neurons—brain cells that facilitate thinking and communicating—to develop and exchange information. As a result, they reasoned, Einstein developed into the mathematical genius who revolutionized modern physics beginning in 1905 with his paper on special relativity.

Unique Structure

Not all scientists are ready to endorse these findings. Many are cautious because of the superficial similarity between the Witelson study and old studies that tried to correlate brain size or weight with intelligence. Einstein's brain, however, was not exceptional in size or weight. Einstein's intelligence may have resulted from the unique structural property of his parietal lobes. Witelson and her colleagues, it is worth noting, do not consider their results conclusive. They welcome further investigation, recommending electronic imaging of the active brains of today's brilliant physicists and mathematicians to learn if theirs, too, have structural features similar to Einstein's.

It seems possible, though, that a remark Ayn Rand once made will turn out to be right and some people simply do have better brains than others—better in that because of unique structural properties their owners have superior mental capabilities. (See "An Untitled Letter" in Rand's *Philosophy: Who Needs It.*) According to the egalitarian mind, all human

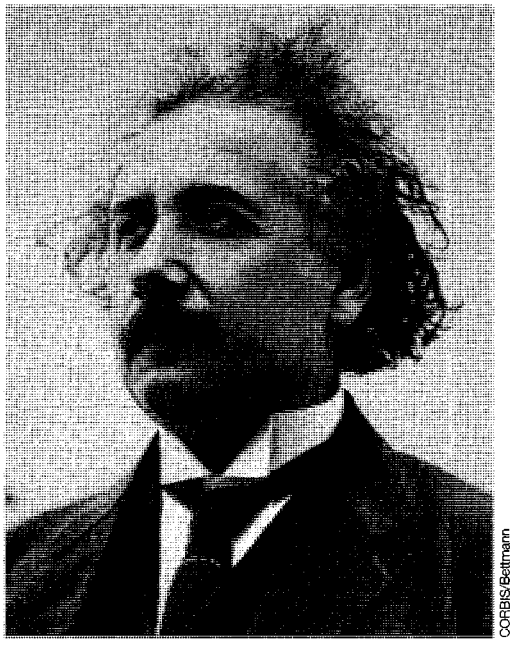
Steven Yates is the author of Civil Wrongs: What Went Wrong with Affirmative Action *(ICS Press, 1994) and numerous articles and reviews.*

beings ought to be social and economic equals, and it is fundamentally unjust for a select few to soar ahead of the pack. The idea of superior intellect, egalitarians have often averred, is just a cover for the exploitation of the many by the few. They tend to sympathize with the idea that intelligence is either a "social construction" or exclusively a product of environment and upbringing. Either one can be changed by the right governmental-educational tinkering.

The rapidly advancing neurosciences may provide decisive refutations of all this. If the Witelson discoveries are right, then one's intellectual capacity is rooted in the structure of one's brain. People's brains are not all the same, and this is a fruit of nature, not a social, political, or educational arrangement.

The point is, left to themselves, a select few—an elite of talent and ability—always soars ahead. This has been true in science, art, political thinking, literature, philosophy, and every other human endeavor of note. There are leaders, and there are followers. If the leaders have structurally better brains, then no kind of government tinkering will change this. All the latter can do is suppress a person's natural inclinations, which is what political systems implemented along egalitarian lines have always done. To see what an egalitarian America would look like, watch the movie *Harrison Bergeron*, based on a Kurt Vonnegut short story. It portrays a society led by "Handicapper Generals" who "equalize" those born with superior brains.

Of course, no one can know in advance who will soar ahead. We aren't in a position to scan children's brains and find out. Not only would such a procedure be vulnerable to abuse, we do not know if it would do any good. We simply don't know enough about the brain to know what to look for. Even if Einstein's unusual parietal lobes explain his superior scientific mind, we do not know what explains excellence in other endeavors. And assuming brain structure to be a factor in superior intelligence, Witelson's team does not claim it to be the only factor. Obviously,



Albert Einstein (1879–1955)

an immediate environment (including especially a strong family unit) that both permits and encourages the exercise of one's mind and independent thought is important too. The plain truth is, beyond these commonsensical judgments, there is a lot we just don't know. The human brain is the most complicated object we have ever studied, and we are not even close to understanding how it generates intelligence.

Our ignorance is why no educational system ought to force students into a single mold, as though they were products on an assembly line. The best educational systems have always been those that allow students maximum freedom to develop at their own pace, having created environments conducive to learning. A free society will encourage education along these lines, and then leave it alone. There is no telling what educational forms might develop, and no way to predict what advances in learning might result.

In the meantime, it might be useful to remember Murray Rothbard's characterization of egalitarianism as a "revolt against nature." □

Is the Constitution Antiquated?

by Wendy McElroy

Article I of the U.S. Constitution addresses the legislative powers that are vested in—held exclusively by—the Congress. One of these powers is the right to "grant Letters of Marque and Reprisal" (Section 8, paragraph 11). Further, Section 10, paragraph 1, of this Article reads:

> No State shall enter into any Treaty, Alliance, or Confederation; grant Letters of Marque and Reprisal; coin Money; emit Bills of Credit; make any Thing but gold and silver Coin a Tender in Payment of Debts; pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts, or grant any Title of Nobility.

Paragraph 1 is an example of what many consider to be antiquated language in the Constitution, particularly with reference to the terms "Letters of Marque and Reprisal" and "Bill of Attainder." Yet many terms considered to be antiquated not only have relevance to our modern day, but they also offer a window into the attitudes and historical events that created the United States. Only by understanding their context is it possible to understand the issues to which the Constitution speaks—then, and now.

Letters of Marque

A letter of marque—or letter of reprisal—is the means by which a government authorizes a civilian to arm a private ship in order to attack and plunder the merchant ships of an enemy nation during war. This is the meaning the term had acquired by the eighteenth century. In earlier use, it referred to the means by which a government righted a private wrong against one of its citizens. For example, if an English trader had his goods stolen in Holland and could not receive satisfaction through the Dutch legal system, the English government might grant him a letter of marque. He was then authorized to seize any Dutch ship to regain the value of the goods stolen from him. By 1700, however, the letter of marque had become an instrument of state by which government could expand its naval power during war.

Private parties who met certain requirements, such as the posting of a security bond, could arm what was called a "private ship of war" and legally plunder enemy merchant ships. Such authorized parties were called privateers by their own government and pirates by the enemy. After being adjudged as "lawful prize" by a court, the seized goods became the property of the privateer. This was his payment. Thus, the government was able to disrupt the commerce of an enemy nation without spending money.

Letters of marque assumed importance in American history as a response to the Prohibitory Act passed by Great Britain in 1775. By this Act, the rebellious colonies were stripped of protection by the English crown. Trade between the colonies and British merchants was forbidden; the seizure and plunder

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of American ships was encouraged. In turn, the Continental Congress issued letters of marque and reprisal that empowered colonial privateers to loot British merchant ships.

The "Instructions to the captains and commanders of private armed vessels which shall have commissions of letters of marque and reprisal," issued by Congress on May 2, 1780, offer a sense of the restrictions placed on privateers. The primary restriction limited attacks to vessels owned by traders of the enemy nation. The private ships of war were "to pay a sacred regard to the rights of neutral powers." The purpose of this restriction was partly to conform with international law and partly to avoid turning neutral nations into hostile ones. The privateer was ordered to "bring such ships . . . to some convenient port" where an Admiralty court could judge whether the plunder was lawful. Privateers were not to "kill or maim,—or, by torture or otherwise, cruelly, inhumanly, and contrary to common practice of civilized nations in war, treat any person or persons surprised in the ship."

On April 16, 1856, most of the major maritime powers signed an international agreement called the Declaration Respecting Maritime Law—more popularly known as the Declaration of Paris—which abolished privateering. The United States declined to sign on the grounds that its navy was so small that letters of marque were required to bolster it during war. Without the letters the United States would be at a disadvantage versus European nations with large standing navies.

During the Spanish-American War (1898), Spain and America—neither of which was a party to the Declaration of Paris—agreed to eschew privateering. It was not until the Hague Conferences at the dawn of the twentieth century, however, that the United States officially renounced the use of letters of marque and reprisal. Thus, the term is antiquated in that it no longer applies to an activity in practice.

Bill of Attainder

The term "Bill of Attainder" occurs not only in Section 10 of Article I (prohibiting the States), but also in Section 9, paragraph 3, "No Bill of Attainder or ex post facto Law shall be passed" (prohibiting the Congress).

In his book *The Supreme Court: How It Was, How It Is*, Chief Justice William H. Rehnquist offers this definition: "A bill of attainder was a legislative act that singled out one or more persons and imposed punishment on them, without benefit of trial" (p. 166). The prohibition against bills of attainder was to prevent anyone from being tried by the legislature rather than by the judiciary. Rehnquist explains that the phrase refers to a "precise legal term which had a meaning under English law at the time the Constitution was adopted."

In English common law, when a person was condemned to death or deemed unfit to live (for example, condemned as an outlaw), he was labeled "attaint"—tainted or corrupted in his blood—and his land was forfeited to the crown. Because the blood was corrupted, a man whose "outlawry" was sufficiently egregious could neither inherit land nor transmit it to his children. Parliament began to use bills of attainder in 1459 to exercise judicial authority. The method became infamous during the reign of the Tudor monarchs—especially Henry VIII—who blatantly used it to punish political dissenters, many of whom could be found legally guilty in no other manner.

Because bills of attainder had been used in colonial America, the framers of the Constitution were well aware of this abuse. Thus, Article II, Section 3, reads, "The Congress shall have power to declare the punishment of treason, but no attainder of treason shall work corruption of blood, or forfeiture except during the life of the person attainted."

Even the exigencies of the Civil War did not entirely remove the American suspicion of bills of attainder. On July 17, 1862, a wartime Congress passed the Confiscation Act directed at citizens of the Confederacy. The intention of the Act was to "suppress insurrection, to punish treason and rebellion, to seize and confiscate the property of rebels." But the term of confiscation was specified to be for the life span of the offender, with his children carrying no taint of blood and thus able to inherit.

Although "bill of attainder" may seem to be as antiquated a term as "letters of marque," some political commentators believe that recent asset-forfeiture laws constitute bills of attainder under another name. These laws allow authorities to seize the property of people who have neither been tried nor convicted of crimes. For example, by power of legislation alone, authorities may confiscate homes, boats, and cars in which drugs are found.

Organizations such as the Institute for Justice believe that such seizure without trial is a violation of constitutional and civil rights. The Bill of Attainder Project (www.isc-durant.com/tom/billofattainder/) is attempting to have the phrase defined in law as "A law or legal device which outlaws people, suspends their civil rights, confiscates their property, punishes or puts people to death without a trial."

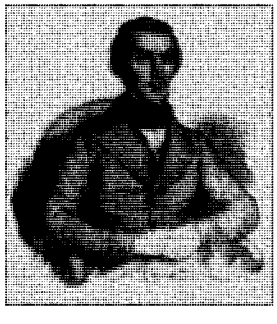
The debate over asset forfeiture raises an intriguing point. Although the specific form of an abuse mentioned in the Constitution may no longer exist, the abuse may have merely assumed another shape.

In sculpting the Constitution—and especially in using certain terms repeatedly—the framers were addressing real political abuses they had witnessed firsthand. Those specific forms of the abuse may no longer exist, but the appetite of some human beings for power and plunder seems to remain unchanged through time. It is necessary to look beyond the quaintness of any specific term and ask, what current legal practice corresponds, in its essence, with one that is prohibited by the Constitution? □

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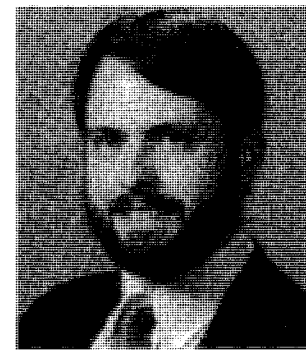


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Emotive Policymaking

We live in an age of paradox. Media saturation following events like the murders at Columbine High School makes it appear that violence surrounds us. Yet the crime rate has been falling and school shootings remain extremely rare. In contrast, the serious violence that pervades some inner-city schools never makes the news.

Moreover, tragedies like Columbine almost always launch a spate of counterproductive policy initiatives—such as gun control. Although inadequate morals rather than inadequate laws led to the Columbine murders, activists, interest groups, and politicians immediately dusted off their old proposals to launch anew.

The temptation to ban firearms is understandable. Anything seems reasonable in an attempt to save even a few people who die by bullet every year. Yet private possession of weapons does not automatically lead to their misuse: heavily armed societies like Israel and Switzerland have only a fraction of our violent crime. America's problem is the willingness to misuse guns, not the availability of guns.

That is evident even from the U.S. experience. Civil libertarian Don Kates points out that the number of firearms almost doubled between 1973 and 1992, while the murder rate fell. The facts, he observes, are "completely inconsistent with the shibboleth that doubling the number of guns, especially hand-guns, would increase homicide rates."

Many Guns

Anyway, it is too late to try to disarm a society where 240 million guns are in private hands. Only the exceedingly law-abiding and extremely docile would give up their weapons. Thus, only totalitarian controls could eliminate private gun ownership. And even police-state measures wouldn't be enough. Otherwise there would be no illicit drug trade today.

Nor is disarmament a reasonable goal. It is easy to belittle the use of firearms for hunting or target-shooting, yet the right to engage in such activities is the bedrock of a free society. Sportsmen rarely misuse their weapons; those who don't should not be punished for the sins of the few who do.

Using guns for self-defense is even more important. There is no more fundamental right, especially in a world in which the police offer only imperfect protection, at best. John R. Lott, Jr., formerly of the University of Chicago, figures that guns are used five times as often to prevent as to commit crimes.

Nor should one desire a world in which only state officials possess weapons. Although a standing army has replaced the militia as America's main defense against foreign foes, the nation's founders rightly distrusted giving government a monopoly on deadly force. Tyranny may seem exceedingly unlikely, but disarming average citizens makes it more

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rather than less likely to occur. That's why the right to bear arms is enshrined in the Bill of Rights.

Of course, Americans should hesitate to respond to even outrageous government abuses with violence. Once loosed, the dogs of revolution cannot be easily controlled. But the government murder (what else can it be called?) of the Branch Davidians at Waco and Randy Weaver's family at Ruby Ridge certainly demonstrates that state authorities cannot be trusted.

Nevertheless, as predictable as the tides, Columbine led to a new campaign to regulate firearms. Proposals included background checks at gun shows, trigger locks, limits on the number of guns that can be purchased, a ban on concealable firearms, and increasing the legal age to buy firearms. Even some past critics of gun controls have flipped in the face of the public relations onslaught.

This sophisticated campaign has been run as if guns were getting easier to buy. To the contrary, argues Lott, "Gun availability has never been as restricted as it is now." As recently as 30 years ago there were few restrictions on gun ownership, even by juveniles. Since then the number of words in federal gun laws has quadrupled, and state and local regulations have mushroomed.

It is hard to find any evidence that this growing body of rules has had any impact on crime. Writes Lott: "Not one academic study has shown that waiting periods and background checks have reduced crime or youth violence." So much for the vaunted Brady law.

There is no reason to believe that the plethora of new proposals would have any better effect. Indeed, none would have stopped the Columbine massacre. As Lott points out, the killers "violated at least 17 state and federal weapons-control laws." A couple more on the books would have made no difference.

But new rules could make crime more likely by disarming potential victims and "citizen cops." Research by Lott suggests that allowing people to carry concealed weapons lowers the violent crime rate. Indeed, private individuals with guns ended two recent school shootings. As noted, there is no evidence that waiting periods lower crime rates. Such restrictions do, however, prevent people from buying guns to protect themselves from imminent danger. Proposals to ban possession of weapons by 18-to-21-year-olds would be equally perverse. The federal government already bars anyone under 21 from buying a gun, but responsible adults between 18 and 21 should not be denied firearms: they are the most likely to be victims of violence. Moreover, John Lott has found that their use of concealed weapons also reduces crime.

In fact, kids who receive weapons from their parents are far less likely than their peers to misuse guns later in life. Interestingly, they are also far less likely to use drugs or otherwise end up delinquent.

Trigger locks would save few lives. A minuscule number of children die in gun accidents, fewer than the number who die in fires they started with lighters, riding their bikes, or even drowning in water buckets. But trigger locks would hinder people from defending themselves in an emergency. (They might also cause some gun owners to be overconfident, and thus less careful about keeping their weapons out of the hands of their kids.) Individual owners can best balance the one risk, if they have small children, against the other, if they live in a dangerous neighborhood.

Licensed dealers already must conduct background checks, including at gun shows. Private individuals need not, but there is no evidence that potential criminals flock to these very public gatherings to consummate illegal deals. Indeed, fewer than 1 percent of convicted felons obtained guns at shows; the Justice Department found that just 2 percent of guns used in crime came from gun shows.

The strongest response to gun crimes is to punish the criminal. Use of a firearm should automatically increase the sentence. Those who knowingly sell guns to criminals or juveniles should be likewise punished.

Legislators should pause before passing any new gun-control measures. Tragedies like Columbine too often trigger policymaking by emotion. In this case, seeking to "just do something" is worse than doing nothing. It is likely to make us all less safe. □

THE FREEMAN
Ideas On Liberty

Let's Not Promote Dependency

by Daniel T. Oliver

Despite the good news that national welfare rolls have declined nearly 40 percent over the last five years and that recent federal and state reforms appear to be at least partly responsible for this decline, the debate over welfare reform is going nowhere.

Welfare-state liberals argue that if government programs are significantly cut (which to date has not happened, as measured by federal welfare appropriations), charity will not be able to make up the difference.[1] Independent Sector, a Washington, D.C.-based coalition of government-funded social-service organizations, believes that "charities cannot come close to filling the gap for proposed cuts in the funding of social programs."[2] Conservatives, on the other hand, argue that charities, churches, neighborhood associations, and other voluntary institutions can assume most if not all responsibilities for the needy now carried out by government.

Yet both arguments overlook an important point: welfare and charity are both forms of dependency. Why would we want to "fill the gap" by replacing one form of dependency—welfare—with another—charity?

Henry Ford, one of the greatest entrepreneurs and philanthropists of this century, once remarked that "the recipients of charity are usually destroyed—for once you give a man something for nothing, you set him trying to get someone else to give him something for nothing."[3] Octavia Hill, a nineteenth-century British landlady and housing reformer who was famous in her day for her work with low-income tenants, similarly criticized what she called "foolish almsgiving": "the lavish and sudden rush of ill-considered gifts . . . is deadly. It is the cause of a steady deterioration of character pitiable to watch."[4]

Both the welfare-state liberal and conservative arguments fail to recognize that in an ideal society, there would be no welfare or charity. Ideally, every adult would be able-bodied and self-supporting. No individual or family would suffer the misfortunes of a house fire or devastating natural disaster. No one would engage in self-destructive behavior such as excessive gambling or drinking.

Obviously, such a world will never exist, but it is the kind of world we should nonetheless strive to approximate, however imperfectly. The question, then, is not how to fill the gap but how to reduce dependency.

What Causes Dependency?

There are really only two reasons why people come to rely on welfare or charity—misfortune and foolishness: people are either victims of circumstances beyond their control, or they willingly engage in self-destructive behaviors. Each of these causes of dependency needs to be examined.

Daniel Oliver (www.smart.net/~doliver/) is a Washington, D.C.-based editor and writer and a research associate at the Capital Research Center (www.capitalresearch.org).

By definition, a misfortune is an event beyond one's control. But in a free society where people are free to exercise their ingenuity, experiment with new technologies, and create better products to serve customers, many misfortunes that have long plagued mankind are lessened if not eliminated altogether.

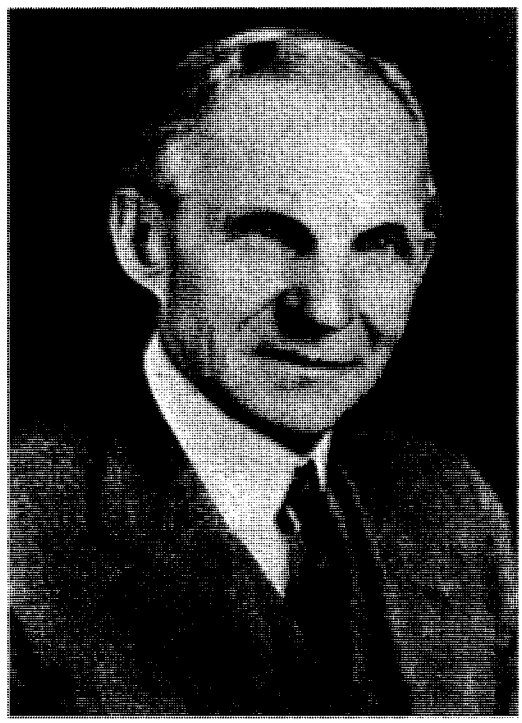
Because of weather radar and satellite images, we can now track and predict the likely course of hurricanes, giving those in their paths time to board up their homes and businesses and move inland to safety. Ships no longer sail into storms and sink, as they did for centuries. Advances in construction have made homes and other buildings more hurricane-proof and earthquake-proof, saving both lives and property.

In this century alone, the life expectancy of Americans has risen nearly 30 years, thanks largely to biomedical research that has discovered cures for scores of diseases that are no longer part of our everyday vocabulary.[5] These diseases once killed husbands and fathers, sometimes leaving their wives and children in poverty. Thus, one way to reduce misfortunes that result in dependency is to ensure that free markets, free inquiry, and entrepreneurship are allowed to work their magic.

The other cause of dependency is self-destructive behavior. When those whose problems are of their own making receive welfare and charity, they are insulated from the natural consequences of their behavior. Rather than suffering the effects of idleness, excessive drinking, and other forms of irresponsibility, recipients are handed a "crutch" (free food and shelter, help with paying utilities) that allows them to persist in their folly. Thus, the "learning experience" that would occur in the absence of welfare or charity—"I have to stop lounging around and find a job," "I have to stop gambling"—is postponed and may never occur.

"Free-Lunch" Charity

Generations ago, most charity workers understood this problem. They knew that "helping" those who were unwilling to help themselves simply allowed self-destructive



Henry Ford (1867–1947)

behavior to continue, and that often the most compassionate course of action was to allow such persons to suffer, perhaps until their suffering became so great that they would be motivated to change. Octavia Hill sometimes had to evict alcoholics and other tenants who refused to work or pay rent, arguing that "the fact of having to move may be a lesson [and] if other landlords did the same, it would certainly stop much evil."[6]

But Hill also understood that charity *could* promote independence if recipients had to give something in return. When her tenants suffered the misfortune of losing a job, she had them clean and repair her many properties in lieu of paying rent. This reinforced the value of work and allowed recipients to keep their dignity until their fortunes improved. Similarly, when Henry Ford in the early 1930s heard that the town of Inkster (a suburb of Detroit) had been particularly hard hit by the Great Depression, he hired its residents to work in his automobile plants and paid others to clean the streets, grow crops, and crush slabs of concrete from demolished buildings for use in paving streets and roads. As he explained, "I do not believe in giving folks

things. I do believe in giving them a chance to make things for themselves."[7]

Unfortunately, too many charities today treat charity as a kind of free lunch. As one literal example, over the last 20 years soup kitchens and other food charities have distributed roughly 10 percent more food each year. Reliance on food charities has increased during both economic upturns and downturns—even though inflation-adjusted food prices have been falling for decades. The main reason for this growing dependency is simple: better-off Americans are donating increasing amounts of food to charities, and since all food has a limited shelf life, it must be quickly distributed.[8]

A recent national study by Second Harvest, the nation's largest network of food banks, found that while nearly 40 percent of food-charity clients are unemployed, only 22 percent of food charities offer employment training and only 9 percent offer actual jobs. Moreover, while 60 percent of clients say they would like information on how to better budget their money (poor budgeting appears to be a major reason for reliance on food charities), only one food charity in five offers budget and credit counseling.[9]

The Task Ahead

Many charities must re-examine their methods to ensure that they are not promoting dependency. Individuals, foundations, and businesses that give to charity must also take a closer look at the organizations they support to ensure that they promote independence. And advocates of a free society must work to eliminate welfare programs. Welfare has promoted dependency in the same way that "bad" charity has and, more fundamentally, it is based on coercion. Welfare is the antithesis of charity and is incompatible with a free society.

Perhaps the most basic rule that could do wonders to improve charity today is, Don't give away anything for free.[10] Welfare rolls have dropped significantly in the last few years as states and the federal government have required recipients to work. It is likely that charity rolls would similarly decline if more charities made demands on recipients to find work, sober up, and the like.

Because misfortune and foolishness will always exist, there will always be a need for charity. But this need is without doubt far less than is commonly believed because bad charity has encouraged many people to become dependent. If all charities begin to follow the example of Henry Ford and Octavia Hill—and give nothing for free—many more Americans will be able to share in the American Dream. □

1. The seeming paradox of declining welfare caseloads and rising welfare expenditures is largely explained by the fact that federal and state governments are spending more per welfare recipient on job training and placement as well as on transportation, day care, and other "workfare" expenses. Heritage Foundation welfare analyst Robert Rector calculates that in 1992, 75 federal welfare programs cost $304 billion. But under recent budget agreements, they will cost $538 billion by 2002. Major reasons for the increase include expanded health-care coverage for low-income children, higher Supplemental Security Income, food stamp, and Medicaid benefits, and new workfare grants. "Welfare Fares Well in Budget," *Investor's Business Daily*, May 21, 1997.

2. "Statement by Sara E. Melendez," Independent Sector Web site, www.indepsec.org.

3. Henry Ford with Samuel Crowther, *Today and Tomorrow* (Cambridge, Mass.: Productivity Press, 1930), p. 179.

4. Quoted in Robert Whelan, ed., *Octavia Hill and the Social Housing Debate: Essays and Lectures by Octavia Hill* (London: Institute of Economic Affairs, 1998), pp. 93, 116.

5. Americans for Medical Progress (Alexandria, Va.), 1991 annual report, pp. 1, 2, and American Council on Science and Health (New York, N.Y.), "America's Health: A Century of Progress."

6. Quoted in Whelan, p. 118.

7. See Martin Morse Wooster, *The Great Philanthropists and the Problem of "Donor Intent"* (Washington, D.C.: Capital Research Center, 1998), p. 20.

8. Robert Lerner and Althea Nagai, "Feeding the Hungry: Should Food Charities Fear Welfare Reform," *Alternatives in Philanthropy* (Washington, D.C.: Capital Research Center, January 1998).

9. Second Harvest, *Hunger 1997: The Faces & Facts* (Chicago: VanAmburg Group, Inc., 1998).

10. In *Overcoming Welfare: Expecting More from the Poor and from Ourselves* (New York: Basic Books, 1998), James L. Payne examines this rule at length. See also Marvin Olasky, *The Tragedy of American Compassion* (Washington, D.C.: Regnery, 1992), for an examination of this and other rules for effectively helping the needy.

THE FREEMAN
Ideas On Liberty

Big Brother Wants to Read Your E-mail

by Aeon J. Skoble

Some people concerned about privacy violations on the Internet object that many Web site operators collect and use information about visitors for demographic research and, yes, advertising. Although "anonymizer" services are available, the simplest way to preserve one's privacy from such operators is simply to refrain from visiting their sites. After all, no one forces you to buy books and CDs online. If you want anonymity, go to a store and pay cash.

A more serious and unavoidable matter is the government's newest scheme for invading everyone's online privacy. In late July, the Clinton administration unveiled a new plan to use the FBI to monitor all Internet traffic, both on military and nonmilitary networks, under the guise of protecting the nation from terrorists who might use the Net for nefarious purposes. According to a draft of the plan, a sophisticated monitoring system would be put in place to constantly track all computer activity, looking for "suspicious patterns." This would help keep tabs on the activities of the usual suspects: drug traffickers, child molesters, and terrorists.

Of course, while that sounds like a reasonable precaution, the potential for abuse is both grave and apparent. The government could monitor political dissidents as easily as it could monitor actual criminals. Any system that enables the authorities to track anyone enables them to track everyone. All electronic commerce and banking, all Web visits, and all e-mail communication would be potentially available for surveillance. This would include the retrieval of passwords for remote log-in. The director of the plan, Jeffrey Hunker of the National Security Council, claims he will make an effort to protect privacy rights. It is not unreasonable to wonder if this is actually a real priority for him.

Two Threats

There are two distinct threats to individual liberties here. First, with this powerful surveillance tool, government's snooping power would grow astronomically. Unlike with wiretaps, Big Brother wouldn't even need a court order to check up on anyone it wanted to investigate. Second, besides government abuse, we would have to worry about the tool being used by others who could illicitly get access to the information either through bribery or hacking.

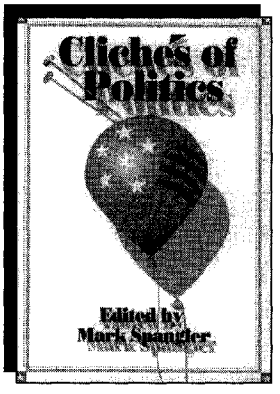
Predictably, the government claims that it is not interested in eavesdropping, but only searching for patterns that might indicate illegal activity. But what does that mean? You can get support for pretty much anything if you invoke the specter of child molesters or drug dealers or terrorists. But when the authorities have the power to track child porn, they have the power to track anything. It's a very short step to their reading our mail, investigating our medical records, and tracking commercial

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and financial transactions. Of course, their answer to concerns of this sort is that if you are not doing anything illegal, you have nothing to worry about. But this is wrongheaded for two reasons.

First, they are the ones who decide what is illegal. Right now, dealing in heroin is illegal. It wasn't that long ago that beer was illegal also. It is well within the realm of the possible that they might decide that e-mail about libertarianism is illegal. After all, in the government's eyes, anyone writing angry messages about Waco might be the next Tim McVeigh.

Second, the very notion that only criminals should be worried about surveillance is contrary to the spirit of the Bill of Rights and the presumption of innocence. Why even bother with search warrants? If you have nothing to hide, you shouldn't object to the police looking around. That is the attitude of oppressive regimes everywhere, but should not be the guiding principle of law enforcement in a free society. We have the right to be secure in our persons, houses, papers, and effects against unreasonable searches. This surely includes our e-mail messages and Web activity. This new plan is a dangerous threat to individual liberty and should not be taken lightly, nor dismissed as hacker paranoia. This affects nearly all of us now. □



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THE FREEMAN
Ideas On Liberty

Just a Cigar

by Jacob Sullum

In July the Federal Trade Commission recommended that Congress require warning labels on cigars. One of the warnings suggested by the FTC nicely illustrates the artful evasiveness of public health officials who seek to shape people's behavior rather than inform them: "Cigars are not a safe alternative to cigarettes."

By denying a claim that no one has made, this admonition avoids the question of just how risky cigars are. Public health officials who are alarmed by the recent increase in cigar consumption prefer to avoid that question, because the evidence clearly shows that the typical cigar smoker faces hazards far less serious than the typical cigarette smoker does. In their campaign to scare people away from cigars, tobacco's opponents have deliberately obfuscated that point, with consequences that can be seen in press coverage of this issue.

Two years ago, the *New York Times* claimed that cigars pose "higher risks" than cigarettes. Last year it reported that "smoking cigars can be just as deadly as smoking cigarettes." In June it said "the disease risks are not as high as they are for cigarette smokers because cigar smokers usually do not inhale the smoke."

Are cigars getting safer? No, but reporters may be getting smarter. Once easily misled by the scare tactics of public health officials and anti-smoking activists, the mainstream press is starting to acknowledge something that medical studies have been finding for decades: Although cigars are not a *safe* alternative to cigarettes, they are a *safer* alternative.

This fact was clear from the data compiled by the National Cancer Institute (NCI) in its 1998 monograph on cigars. Overall, the NCI reported, daily cigar smokers get oral and esophageal cancers almost as often as cigarette smokers. But they face much lower risks of lung cancer, coronary heart disease, and chronic obstructive lung disease—the three main smoking-related causes of death. The upshot can be seen in mortality figures. In a 1985 American Cancer Society study cited by the NCI, men who smoked a cigar or two a day were only 2 percent more likely to die during a 12-year period than nonsmokers, a difference that was not statistically significant. By contrast, the mortality rate was 69 percent higher for men who smoked a pack of cigarettes a day.

The only really bad news for cigar smokers in the NCI report applied to a small minority. The NCI emphasized that the risk from cigars increases with the frequency of smoking and the degree of inhalation. Cigar smokers who inhale deeply face measurably higher risks of heart disease and emphysema (though still not as high as those faced by cigarette smokers), and the risk of lung cancer for a five-cigar-a-day smoker who inhales approaches the risk for a pack-a-day cigarette smoker. That sort of cigar smoker is quite unusual, however. "As

Jacob Sullum is a syndicated columnist, a senior editor at Reason, *and the author of* For Your Own Good: The Anti-Smoking Crusade and the Tyranny of Public Health *(The Free Press).*

many as three-quarters of cigar smokers smoke only occasionally," the NCI noted, and "the majority of cigar smokers do not inhale." Since the available data apply only to people who smoke at least one cigar a day, "the health risks of occasional cigar smokers . . . are not known."

No Measurable Risk

In other words, there is no evidence that smoking cigars in moderation—with moderation defined by the way most cigar smokers actually behave—poses a measurable health risk. But this point was lost on most reporters. Indeed, many news organizations erroneously reported that the NCI had debunked the "myth" that cigars are safer than cigarettes. The headline in the *San Francisco Chronicle* read, "Cancer Institute's Warning on Cigars: Just As Bad As Cigarettes." An Associated Press story said the NCI report was "intended to equate dangers posed by the two products." The article began, "Smoking cigars can be just as deadly as smoking cigarettes." This is like saying that riding a bicycle "can be just as deadly" as riding a motorcycle. It's true in the sense that both activities can result in fatal accidents. But that does not mean they are equally dangerous.

Still, it's easy to see how journalists got the wrong impression. Calling the increase in cigar smoking since 1993 "disturbing" and "alarming," the NCI report downplayed the differences between cigars and cigarettes. "Cigars are not safe alternatives to cigarettes," said NCI Director Richard Klausner. The issue, of course, was not whether smoking cigars is completely risk-free but whether, on average, it is less risky than smoking cigarettes—something no reasonable person could deny after looking at the evidence.

Before the NCI report came out, reporters were primed to expect that it would show cigars are as dangerous as cigarettes, if not more so. Consider how Michael Eriksen, director of the Office on Smoking and Health at the U.S. Centers for Disease Control and Prevention, described the hazards of cigars in a May 1997 *New York Times* story: "Tobacco is tobacco is tobacco." In February 1998, the NCI's Donald Shopland told *USA Today*, "You're smoking a whole pack of cigarettes" when you smoke a cigar. That same month, the addiction specialist Jack Henningfield, who contributed to the NCI report, told *The Wall Street Journal* "it will help explode some of the myths about cigars," including the idea "that they are relatively safe." Around the time the monograph came out, the California Department of Health Services started running a TV spot likening one cigar to *70* cigarettes.

The press may be starting to see through such misleading comparisons. The clear difference in risk between cigars and cigarettes was confirmed once again in a study published by *The New England Journal of Medicine* in June. But this time, reporters paid closer attention.

In the study, researchers led by Carlos Iribarren, an epidemiologist with the Kaiser Permanente Medical Care Program in California, tracked about 18,000 men—1,546 cigar smokers and 16,228 nonsmokers—from 1971 through 1995. Overall, the cigar smokers were about twice as likely to develop cancers of the mouth, throat, and lungs; 45 percent more likely to develop chronic obstructive lung disease; and 27 percent more likely to develop coronary heart disease.

As Iribarren and his colleagues noted, these risks are modest compared to those seen in cigarette smokers. Depending upon the study, cigarette smokers are four to 12 times as likely as nonsmokers to develop mouth and throat cancers; eight to 24 times as likely to develop lung cancer; nine to 25 times as likely to develop chronic obstructive lung disease; and 1.5 to three times as likely to develop coronary heart disease.

Furthermore, smoking-related diseases were concentrated among the heaviest cigar smokers in the Kaiser Permanente study. For those smoking fewer than five cigars a day—76 percent of the sample—only the difference in heart disease risk (20 percent) was statistically significant. Iribarren et al. did not ask the subjects about inhalation, which has been linked to higher risks in other studies, and they did not consider men who smoke a few cigars a month—the typical pattern, according to the NCI report—as a separate category.

More Accurate Coverage

Given the news media's track record in this area, I expected reporters to hype the hazards found by the Kaiser Permanente study and ignore the differences between cigars and cigarettes. But for the most part, the coverage was much more accurate and responsible (though less conspicuous) than the stories that followed the NCI report, probably because the researchers themselves made it clear that cigars are not nearly so hazardous as cigarettes.

The Associated Press, whose story was picked up by several major newspapers, put the hazards of cigars in perspective, noting that "the risks aren't as high as they are for cigarette smokers." The *Washington Post*, which only last year said it was "probably a misconception" that "cigars are healthier than cigarettes because smoke is not inhaled to the same degree," this time correctly cited that factor as the most likely explanation for the comparatively low risks found among cigar smokers.

My favorite story ran in *The Hartford Courant* under the appropriately reassuring headline, "Cigars' Dangers Relatively Low/ Moderate Users Face Only Slightly More Health Risks Than Nonsmokers." The article quoted a local cardiologist who said: "If someone tells me they're smoking one cigar a day, it would be hard for me to jump up and down and say you're killing yourself and be intellectually honest. You are increasing your risk a little bit."

Some reporters still don't get it. "New findings give more weight to warnings that cigars can be at least as hazardous as cigarettes," United Press International declared. If UPI's science correspondent often leaps to such conclusions, she might do well in the long jump, but not in reading comprehension.

Unlike the UPI reporter, FTC Chairman Robert Pitofsky, who wants Congress to ban broadcast ads for cigars as well as require warning labels, seems to have taken a second, more careful look at last year's NCI report. In an April 1998 comment to the *Washington Post*, he misinterpreted the monograph as saying that "regular cigar smoking is roughly as dangerous as cigarette smoking." By contrast, when the FTC issued its recommendations in July 1999, he said, "We now know, based on the findings of the National Cancer Institute, that cigars, like other tobacco products, pose serious health risks."

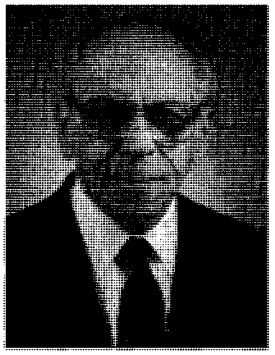
The significance of Pitofsky's backpedaling did not register with everyone. According to the lead of an AP story on the FTC's recommendations, "Federal regulators say they want to correct misperceptions that cigars are less dangerous than cigarettes."

To be fair, it's not surprising that reporters continue to make such mistakes, since public health officials are still pushing the false equation between cigars and cigarettes. Surgeon General David Satcher says the absence of federal warning labels (almost all cigars already carry California health warnings) "implies cigars are different and don't carry the same risk." They are, and they don't. □

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Is Mental Illness a Disease?

"You can know the name of a bird in all the languages of the world, but when you're finished, you'll know absolutely nothing whatever about the bird. . . . So let's look at the bird and see what it's *doing*—that's what counts. I learned very early the difference between knowing the name of something and knowing something."

—RICHARD FEYNMAN

Tipper Gore says that "One of the most widely believed and most damaging myths is that mental illness is not a physical disease. Nothing could be further from the truth." Similarly, the National Alliance for the Mentally Ill (NAMI), the most influential mental health lobby in the nation, states: "Mental diseases are brain disorders." Are these assertions true? And if they are, what are their logical and practical implications?

I say that "mental illnesses" are not diseases, despite the fact that medical and legal authorities call them "diseases," that they are treated with drugs, that those receiving these drugs are called "patients," and that the professionals treating them are called "physicians." Why do I say this? Because the established scientific criterion for disease is a derangement in the structure or function of *cells, tissues, and organs*—a criterion mental illnesses fail to meet, as they can be neither detected nor diagnosed by examining cells, tissues, or organs.

Rather, mental illnesses are identified by certain behaviors, and what concerns Mrs. Gore, NAMI, and others is not the theoretical question of what counts as a disease, but the practical problems posed by these *behaviors*. In fact, whether a person who has a disease feels well or ill, accepts or denies that he is ill, consults a doctor or not, benefits from or is harmed by drugs are all issues important to the *practice of medicine* but not to the *definition of disease*. Likewise, whether a person obeys or breaks the law is irrelevant to the definition of disease. Disease is a physical concept and verifiable phenomenon. Accordingly, gastroenterologists study the abnormal states of the digestive system—not gluttony. Urologists study the abnormal states of the genito-urinary system—not prostitution. Neurologists study the abnormal states of the brain and nervous system—not murder or suicide.

What do psychiatrists study? Do they, as Nancy Andreasen, professor of psychiatry at the University of Iowa, puts it, study "the brain rather than the mind, . . . molecules and chemical transmitters rather than drives and fantasies"? Or do they, as Shakespeare put it, study the persons who suffer "the slings and arrows of outrageous fortune"? This is the

Thomas Szasz, M.D., is the author of The Myth of Mental Illness. *He wishes to thank Alice Michtom, M.D., for help in the preparation of this column.*

crucial distinction masked by equating brain with mind. If "mental illness" means brain disease, then it is not a disease of the mind and psychiatry would be absorbed into neurology and disappear. But this is patently not the case. Psychiatrists regularly occupy themselves with personal conduct of social interest, such as homosexuality, aggression, racism, suicide, and murder.

Expanding "Disease"

It is an elementary principle of logic that one cannot prove a negative. One cannot prove the nonexistence of mental illnesses, just as one cannot prove the nonexistence of ghosts. One can only point out that a belief in mental illness as a disease of the brain is a negation of the distinction between persons as social beings and bodies as physical objects, in the same way that a belief in ghosts is the negation of the distinction between life as activity and death as the cessation of it. What happens when we negate the distinction between social beings and physical objects is that the concept of disease ceases to be limited to the dysfunction of cells, tissues, and organs and is expanded to include "dysfunctional" conduct, especially behavior people in authority find troublesome.

Interestingly, the pioneers of psychiatry understood this distinction, accepted that the scientific concept of disease was restricted to the malfunction of the body, and acknowledged that the term "mental illness" was a figure of speech. In 1845, the Viennese psychiatrist Ernst von Feuchtersleben (1806–1849) wrote: "The maladies of the spirit (*Geist*) . . . can be called diseases of the mind only *per analogiam.* They come not within the jurisdiction of the physician, but that of the teacher or clergyman, who again are called physicians of the mind only *per analogiam.*" And in his classic, *Lectures on Clinical Psychiatry* (1901), Emil Kraepelin (1856–1926) —who created the first modern classification of mental diseases—acknowledged: "It is true that, in the strictest terms, we cannot speak of the mind as becoming diseased." In short, a sick mind, like a sick economy, is a metaphor.

Mind Is Not Brain

Treating the metaphor as the thing itself—the metaphorization of disease, in our case—has led to the confusion of production with product, person with body, and mind with brain. Note that unlike the term "brain," the term "mind" implies agency, intentionality, and motivation. Accordingly, *behavior per se* that may result in disease is often categorized as a mental disease, but is never categorized as a medical disease. For example, excessive drinking is considered a mental disease, not a gastrointestinal disease—though cirrhosis of the liver is. A competent speaker of English may thus assert that schizophrenia has caused a person to kill an innocent bystander and excuse him of his deed, but he would never say that diabetes has either caused such lawless behavior or excuses it. Herein lies one of the most important philosophical-political consequences of the concept of mental illness: it removes, with one fell swoop, motivation from action, encompasses it within illness, and thus destroys the very possibility of separating disease from non-disease, since it offers the possibility that any intentionality or motivation is a potential "disease."

In 1924, the great Eugen Bleuler (1857–1939), the inventor of schizophrenia, declared: "Those who simulate insanity with some cleverness are nearly all psychopaths and some are actually insane." The idea that pretending to be ill is, itself, an illness became socially acceptable during World War II and has since become psychiatric dogma. Kurt Eissler (1908–1999), a world-famous psychoanalyst and psychiatrist, framed the doctrine thus: "It can be rightly claimed that malingering is *always the sign of a disease.*"

Behavior is not—and cannot be—a disease, except in psychiatry. Controlling behavior, with or without a person's consent is not—and cannot be—a treatment, except in psychiatry. And faking illness is not—and cannot be—an illness, except in psychiatry.

Paradoxically, the intellectual bankruptcy of the idea of mental illness is the pillar on which modern psychiatry—and the therapeutic state—rest. *Credo quia absurdum est.* □

THE FREEMAN
Ideas On Liberty

The Growing Abundance of Fossil Fuels

by Robert L. Bradley, Jr.

Only two decades ago nearly all academics, businessmen, oilmen, and policymakers agreed that the age of energy scarcity was upon us and that the depletion of fossil fuels was imminent. While some observers still cling to that view today, the intellectual tide has turned against doom and gloom on the energy front. Nearly all resource economists believe that fossil fuels will remain affordable in any reasonably foreseeable future.

Indeed, these fuels have become more abundant even in the face of record consumption. World oil reserves today are more than 15 times greater than they were when record keeping began in 1948; world gas reserves are almost four times greater than they were 30 years ago; world coal reserves have risen 75 percent in the last 20 years. Proven world reserves of oil, gas, and coal are officially estimated to be 45, 63, and 230 years of current consumption, respectively. Probable resources of oil, gas, and coal are officially forecast to be 114, 200, and 1,884 years of present usage, respectively.

Moreover, an array of unconventional fossil-fuel sources promises that, when crude oil, natural gas, and coal become scarcer (hence, more expensive) in the future, other fossil fuels may still be the best substitutes before synthetic substitutes come into play.

Orimulsion

The most promising unconventional fossil fuel today is orimulsion, a tarlike substance that can be burned to make electricity or refined into petroleum. Orimulsion became the "fourth fossil fuel" in the mid-1980s when technological improvements made Venezuela's reserves commercially exploitable. Venezuela's reserve equivalent of 1.2 trillion barrels of oil exceeds the world's known reserves of crude oil, and other countries' more modest supplies of the natural bitumen add to the total.

With economic and environmental (post-scrubbing) characteristics superior to those of fuel oil and coal when used for electricity generation, orimulsion is an attractive conversion opportunity for facilities located near waterways with convenient access to Venezuelan shipping. While political opposition (in Florida, in particular) has slowed the introduction of orimulsion in the United States, it has already penetrated markets in Denmark and Lithuania and, to a lesser extent, Germany and Italy. India could soon join that list. Marketing issues aside, this here-and-now fuel source represents an abundant backstop fuel at worst and a significant extension of the petroleum age at best.

Robert Bradley, Jr., is president of the Institute for Energy Research in Houston, Texas, and an adjunct scholar of the Cato Institute. This is part of a longer analysis, "The Increasing Sustainability of Conventional Energy," published by the Cato Institute and available at www.cato.org/pubs/pas/pa341es.html.

Synthetics and More

The significance of orimulsion for the electricity-generation market may be matched by technological breakthroughs commercializing the conversion of natural gas to synthetic-oil products. For remote gas fields, gas-to-liquids processing can replace the more expensive alternative of liquefaction. In mature markets with air quality concerns, such as in California, natural gas could become a key feedstock from which to distill the cleanest reformulated gasoline and reformulated diesel fuel yet.

A half dozen competing technologies have been developed, several by oil majors that are committing substantial investments relative to government support. The widespread adaptation of gas-to-oil technologies could commercialize up to 40 percent of the world's natural gas fields that hitherto have been uneconomic.

In addition to orimulsion and synthesized natural gas, tar sand, shale oil, and various replenishable crops also have great promise, however uneconomic they now are, given today's technology and best practices.

Michael Lynch of the Massachusetts Institute of Technology estimates that more than six trillion barrels of potentially recoverable conventional oil and another 15 trillion barrels of unconventional oil (excluding coal liquefaction) are identifiable today, an estimate that moves the day of reckoning for petroleum centuries into the future.

The gas resource base is similarly loaded with potential substitutions. Advances in coalbed methane and tight-sands gas technology show immediate potential, and synthetic substitutes from oil crops have long-run promise. If crude oil and natural gas are retired from the economic playing field, fossil fuels boast a strong bench of clean and abundant alternatives. Even the cautious Energy Information Administration of the U.S. Department of Energy concedes that "as technology brings the cost of producing an unconventional barrel of oil closer to that of a conventional barrel, it becomes reasonable to view oil as a viable energy source well into the twenty-second century."[1]

Today's reserve and resource estimates should be considered a minimum, not a maximum. By the end of the forecast period, reserves could be the same or higher depending on technological developments, capital availability, public policies, and commodity price levels.

Technological advances continue to substantially improve finding rates and individual well productivity. Offshore drilling was once confined to fields several hundred feet below the ocean, for instance, but it now reaches depths of several thousand feet. Designs are being considered for drilling beyond 12,000 feet.

Predictably, advances in production technology are driving down the cost of finding oil. In the early 1980s finding-costs for new crude oil reserves averaged between $11.50 and $12.50 per barrel in the United States and most areas of the world. In the mid-1990s they had fallen to around $7 per barrel despite 40 percent inflation in the interim. In the United States alone, finding-costs dropped 40 percent between 1992 and 1996. That is perhaps the best indicator that oil is growing more abundant, not scarcer.

Finally, the amount of energy needed to produce a unit of economic goods or services has been declining more or less steadily. New technologies and incremental gains in production and consumption efficiency make the services performed by energy cheaper even if the original resource has grown more (or less) expensive in its own right.

Understanding Abundance

How is the increasing abundance of fossil fuels squared with the obviously finite nature of those resources?

"To explain the price of oil, we must discard all assumptions of a fixed stock and an inevitable long-run rise and rule out nothing a priori," says M. A. Adelman of MIT. "Whether scarcity has been or is increasing is a question of fact. Development cost and reserve values are both measures of long-run scarcity. So is reserve value, which is driven by future revenues."[2]

Natural-resource economists have been

unable to find a "depletion signal" in the data. A comprehensive search in 1984 by two economists at Resources for the Future found "gaps among theory, methodology, and data" that prevented a clear delineation between depletion and the "noise" of technological change, regulatory change, and entrepreneurial expectations.[3]

A more recent search for the depletion signal by Richard O'Neill and colleagues concluded: "Care must be taken to avoid the seductiveness of conventional wisdom and wishful thinking. While the theory of exhaustible resources is seductive, the empirical evidence would be more like the bible story of the loaves and fishes. What matters is not exhaustible resource theories (true but practically dull) but getting supply to market (logistics) without disruption (geopolitics). While it is easy to see how political events may disrupt supply, it is hard to contrive an overall resource depletion effect on prices."[4]

The facts, however, are explainable. Says Adelman: "What we observe is the net result of two contrary forces: diminishing returns, as the industry moves from larger to smaller deposits and from better to poorer quality, versus increasing knowledge of science and technology generally, and of local government structures. So far, knowledge has won."[5]

Human ingenuity and financial wherewithal, two key ingredients in the supply brew, are not finite but expansive. The most binding resource constraint on fossil fuels is the "petrotechnicals" needed to locate and extract the energy. Congruent with Julian Simon's theory that the most scarce resource is human capital, wages in the energy industry can be expected to increase over time, while real prices for energy can be expected to fall under market conditions. Under political conditions such as those that existed during the 1970s, however, the record of energy prices can be quite different.

There is no reason to believe that energy per se (as opposed to particular energy sources) will grow less abundant (more expensive) in our lifetimes or for future generations. "Energy," as Paul Ballonoff has concluded, "is simply another technological product whose economics are subject to the ordinary market effects of supply and demand."[6]

Thus, a negative externality cannot be assigned to today's fossil-fuel consumption to account for intergenerational "depletion." A better case can be made that a positive intergenerational externality is created, since today's base of knowledge and application subsidizes tomorrow's resource base and consumption.

The implication for business decision-making and public-policy analysis is that "depletable" is not an operative concept for the world oil market, as it might be for an individual well, field, or geographical section. Like the economists' concept of "perfect competition," the concept of a nonrenewable resource is a heuristic, pedagogical device—an ideal type—not a principle that entrepreneurs can turn into profits and government officials can parlay into enlightened intervention. The time horizon is too short, and technological and economic change is too uncertain, discontinuous, and open-ended. □

1. Energy Information Administration, "International Energy Outlook 1998," pp. 3, 38.

2. M. A. Adelman, *The Genie Out of the Bottle: World Oil Since 1970* (Cambridge, Mass.: MIT Press, 1995), p. 22.

3. Douglas Bohi and Michael Toman, *Analyzing Nonrenewable Resource Supply* (Washington, D.C.: Resources for the Future, 1984), p. 139.

4. Richard O'Neill et al., "Shibboleths, Loaves and Fishes: Some Updated Musings on Future Oil and Natural Gas Markets," U.S. Federal Energy Regulatory Commission, Office of Economic Policy, discussion paper, December 31, 1996, p. 22.

5. M. A. Adelman, "Trends in the Price and Supply of Oil," in *The State of Humanity*, ed. Julian Simon (Cambridge, Mass.: Blackwell Publishers, 1995), p. 292.

6. Paul Ballonoff, *Energy: Ending the Never-Ending Crisis* (Washington, D.C.: Cato Institute, 1997), p. 21.

Economics



Comparative Advantage Continued

The concept of comparative advantage, which I began discussing last month, is a straightforward application of opportunity cost and is almost embarrassingly simple. Certainly people have no trouble understanding and recognizing the importance of this concept in their own personal lives. For example, if you were the best brain surgeon in town and also the best at shining shoes, you would not try to be both a brain surgeon and a shoe shiner. Compared to other shoe shiners, you would be at a tremendous disadvantage shining shoes because of the value of your time performing brain surgery.

People are very good at finding and pursuing their comparative advantages. This doesn't mean that people are always good at what they do. We have all seen people working at jobs they can't do well. It could be, of course, that they have made a mistake and will quickly move on to something they do better. But that clumsy waiter who keeps spilling hot soup on his customers may have a comparative advantage at being a waiter. He could be even worse at everything else. So just as you can be really good at something without having a comparative advantage in it, you can have a comparative advantage at something you don't do very well.

While people seem to understand comparative advantage when making personal choices, they often put this understanding on hold when accepting arguments against international trade. For example, last month I explained why the widely accepted argument that countries with low-paid workers will be able to outcompete us in all goods is wrong. I shall now consider a related, and widely accepted, argument against free trade, and explain the fallacy it contains by modifying the example in last month's column.

Being the Best May Not Be Good Enough

A common complaint by domestic producers is that foreign firms that suddenly begin outcompeting them must be selling below cost. They can often support their case by pointing out that the foreign firms were previously uncompetitive and have not improved their efficiency one bit. So how can these firms possibly be competitive now? It may seem strange that firms unable to compete earlier are suddenly able to without becoming more productive. But it is not strange at all. Foreign firms don't have to become more productive to acquire a comparative advantage over domestic firms.

Consider the table on the next page, which contains last month's example (ignore the number in parentheses for now). Americans have a comparative advantage only in car production even though they are absolutely more productive than Brazilians at producing both cars and computers. The opportunity cost of producing 100 cars is 666 computers in the

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United States and 1,000 computers in Brazil. But the other side of this coin is that Americans have a comparative *dis*advantage in producing computers, which means Brazilians have a comparative advantage in computer production. While it costs 150 cars to produce 1,000 computers in the United States, it costs only 100 cars in Brazil.

So, as explained last month, both countries are better off when Americans specialize in cars, Brazilians specialize in computers, and they trade with each other. Free trade moves resources into each country's comparative advantage, thereby increasing total output.

But assume that an entrepreneur develops a better way of manufacturing computers in the United States: it now requires only 1.5 units of productive resources to produce 1,000 computers. U.S. car manufacturers are just as productive absolutely as before, and no productivity improvements are made in Brazil. But now, the comparative advantage in the United States has shifted to computers, with the absolute advantage in cars becoming a comparative disadvantage. It now costs 1,333 computers to produce 100 cars in the United States as opposed to only 1,000 in Brazil. Under free trade U.S. computer manufacturers are able to outcompete car manufacturers for resources as consumers in both countries find it cheaper to buy computers from the United States and cars from Brazil. Both countries are now better off than before, since trade allows the benefit from more efficient computer production to be fully realized.

	U.S.	Brazil
100 cars	2 units of resources	4
1,000 computers	3 (1.5)	4

True, U.S. unemployment may increase temporarily, as workers in the declining car industry move to jobs in the expanding computer industry. And U.S. car manufacturing will lose money, an unmistakable incentive to move resources to more productive uses. So expect U.S. car manufacturers and their labor unions to complain that the competition putting them out of business cannot possibly be fair because they are still two times more productive than Brazilian car manufacturers. Obviously the Brazilians must be selling below cost—dumping cars in America. But Brazil does not have to sell cars below cost to outcompete U.S. car producers. Americans may be twice as productive manufacturing cars than Brazilians, but it is now 2.66 times more productive manufacturing computers. So the opportunity cost of producing cars in Brazil has become lower than in the United States. There is no legitimate complaint about Brazilian competition. In fact, the real competition is not coming from Brazil at all, but from other Americans. Brazil has done nothing new in our example. The competition facing U.S. car producers is coming from the more productive opportunity the U.S. computer industry is offering workers and resource owners. Car producers simply cannot afford to pay workers (and resource owners) enough to cover their increased opportunity cost given their comparative advantage in producing computers.

Self-Serving Claims

We can now see the self-serving silliness in the claim by industries having to lay off workers because of foreign imports that free trade will cause massive unemployment. If this were true, the opportunity cost of workers would be reduced by trade and they could be profitably re-employed at low cost by the declining industry. The problem declining industries have with free trade is that trade increases employment opportunities, not that it diminishes them.

Our discussion of international trade has ignored many real-world complexities. For example, we observe countries producing and importing the same product, as opposed to our example where countries import only what they don't produce. To explain how both producing and importing the same product is consistent with pursuing one's comparative advantage we will have to examine the concept of marginalism, which will be done in a subsequent column. But our discussion goes a long way to dispel common myths about the dangers of free trade. □

THE FREEMAN
Ideas On Liberty

Fist of Steel

by Dale R. DeBoer

Last year was bad for U.S. steel producers. Imports jumped to historic highs, and domestic prices fell. Corporate steel profits collapsed, and almost six percent of steelworkers lost their jobs. Crying foul, steel producers appealed for relief under U.S. international trade laws. The Clinton administration initiated an anti-dumping investigation against several countries, including Japan, Brazil, South Korea, and Russia. Early in 1999 Congress went further by pushing for quotas on steel imports. Together these efforts appear to be reducing the threat to U.S. steel interests: imports are falling. But at what cost to the U.S. economy as a whole?

The influx of steel imports into the United States is largely an outgrowth of the global economic turmoil of 1998. To understand this, consider the position of two fictional steel producers—Steel Amalgam in the United States and Mitsu Steel in Japan. In the early months of 1998 both plan their steel production, expecting a price of $100 per unit in the United States and 12,900 yen per unit in Japan. At the going exchange rate of 129 yen per dollar the price in both countries is comparable. Both producers begin making steel, incurring costs of $95 per unit here and 12,255 yen per unit in Japan ($95 per unit times 129 yen per dollar).

Unfortunately, demand for steel in Japan begins to decline because of its recession. Falling real output in Japan drives down the demand for steel. As the demand falls (following the logic of supply and demand) the price of steel in Japan begins to fall (by 5 to 7 percent at the wholesale level). At the same time the exchange rate between the Japanese yen and the U.S. dollar begins to change—increasing to 140 yen per dollar. All this makes it much more attractive to Mitsu Steel to sell its product here, where it can earn 14,000 yen per unit of steel ($100 per unit times 140 yen per dollar) rather than 11,977 to 12,255 yen per unit in Japan (reflecting the fall in prices there). So Mitsu Steel increases its sales to the United States, leading to the situation described above. Steel Amalgam sees the price here fall because of the increased supply from abroad—cutting profits. This forces Steel Amalgam to cut back on its current production, leading to layoffs.

Essentially this is what happened in 1998. Since the turmoil of 1998 involved many large steel-producing countries, the loss imposed on U.S. steel interests was large. Therefore, U.S. steel producers sought the protection offered by the trade laws.

Anti-Dumping Laws

Under U.S. law, dumping occurs (1) when a product is sold in the U.S. market at a lower price than in the producing country's market or (2) when a product is sold in the U.S. market at a price lower than the cost of production. For relief to be granted, one of these con-

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ditions must hold and it must be shown that harm resulted from the dumping. From the example, it should be clear how both types of dumping occurred. The yen price of steel here is 14,000 versus 12,000 in Japan. Further, Mitsu Steel incurred costs of 12,255 yen in producing the steel. At the time of production, this was equivalent to 95 dollars. When it sold the steel the sales price in Japan had fallen to 87 dollars (12,255 yen divided by 140 yen per dollar), leaving the dollar sales price less than the dollar cost of production. This satisfies the definition of dumping. Additionally, "harm" was done to the United States. The expansion of imports pushed steel prices down, damaging the profit position of U.S. steel firms and the employment of U.S. steelworkers. So the behavior of the foreign producers is legally actionable under American law.

Notice that the harm to the U.S. firms and workers is the same harm caused by any import—the only distinction in this case is that the influx of imports was sudden, because of rapidly changing conditions in foreign markets. The Japanese export of automobiles to the United States reduces sales of U.S. automobiles, caps the price that can be charged by U.S. automakers, and lowers employment in the U.S. automobile industry.

Should we therefore conclude that all imports harm the United States? Of course not; this discussion leaves out one important element: the benefit to the purchaser of an import. The benefits to the purchaser include getting an item at a lower price, being exposed to greater variety, and because of lower prices, being able to purchase more items. In the case of steel, the beneficiaries are U.S. firms that use steel to make other products (cars, for example) and their consumers.

The benefits of imports most likely do not end with the consumers, however. Competition from abroad spurs a competitive response from U.S. producers, who must become more efficient if they wish to maintain their market position. If they fail to respond, they go out of business. This is the harsh reality of a market economy. It is also a key to its great productivity.

Advocates of anti-dumping laws have a ready rejoinder. Regular imports are acceptable and do offer the advantages enumerated. But products that are dumped are different because dumping is predatory! Predatory behavior is directed at eliminating competition. By doing so, a producer gains an opportunity to earn long-term monopoly profits. Reality does not lend support to this claim. As every first-year student of economics knows, monopoly power and profits arise only if a barrier to entry into the market exists. Since viable steel firms currently operate in the United States, no barrier exists. Even if these firms close, their factories and tools will still exist. The workers currently employed by these firms will still possess their skills. Even if domestic production ends, the firm could easily reopen once a foreign firm began exercising its monopoly power. The only force that would prevent a reopening of a domestic firm is perpetual dumping. If the predation never ended, some other country would be permanently using its domestic resources to give the United States steel cheaper than it can be domestically produced. Rather than complaining we should be offering them thanks for the gift!

Two More Tries

The defense of anti-dumping laws does not end with claims of predatory behavior. A common plea invokes special circumstances, for example, that the industry affected is either an infant or senescent industry. An infant industry is said to be one that has not developed to where it can withstand the full rigors of international competition. If exposed to the wind of foreign competition it will die like a sapling exposed to a hurricane. A senescent industry is one currently in decline and saddled with old capital and dated technology. Like its infant relative, it cannot stand up to the forces of competition. Dumping would presumably drive it out of business.

A claim that the affected industry is either infant or senescent is prone to a common weakness. If an industry is not capable of competing in the international arena, granting the industry protection does not guarantee its survival or growth. An industry or a firm is not a biological entity that will grow and strengthen if provided proper nutrients and

shelter. Rather an industry needs an inducement to improve.

In the absence of competitive pressure firms face no need to improve and are as likely to stagnate in their current noncompetitive position as to evolve into more efficient producers. This logic is more binding on a senescent industry than it is on an infant industry. A senescent industry has fallen from a competitive position to a noncompetitive position. This indicates that the industry does not possess the requisite competitive instinct demanded by a market economy. Justifying protection for such an industry requires making a heroic assumption that given protection the firms in the industry will change their past inefficient behavior. If a firm has not responded to competitive pressure in the past, it seems unlikely that it will become competitive in the absence of competition. Therefore, this line of reasoning likely only codifies the protection of inherently poor producers.

Another special circumstance used to justify anti-dumping protection is that the affected industry is a "strategic" industry. A strategic industry produces a product critical to the long-term health of the economy or society. For instance, the production of weapons of national defense is often considered strategic production. In times of conflict the continued existence of the nation could be threatened if the United States relied on importation of weaponry. This would be a very strong argument but for three concerns. First, how is an item with strategic value to be identified? The Japanese have relied on this argument for protection of their domestic agricultural industry ("We don't want to rely on imported grains during times of war!"). Through creative argument nearly anything can be turned into a product with strategic value ("We must protect television production because during times of war we will need the ability to produce screens for weapon-imaging systems!"). Before legitimating this argument, one must be careful to determine that the item in question has significant strategic importance.

Second, the strategic-interest argument only has force if domestic production is completely eliminated. This has not occurred with any industry for which a clearly defined strategic interest exists. Third, the industries where anti-dumping actions are most commonly taken (for example, textiles) clearly do not have significant strategic value.

It's Not Just Us

Anti-dumping laws in the United States appear to be a backdoor effort to gain protection for industries that do not like the effects of global competition. It is natural that they do not like this competition; they must work harder to make a profit and maintain market share. But the gains to everyone else are great. The excuse of dumping to promote protectionism attempts to justify disreputable policies. This is true not just for the United States but for foreign countries as well, though the United States, with 294 anti-dumping orders in force, followed by the European Union with 135, is the greatest exploiter of this justification. By disguising U.S. protectionism behind the veil of anti-dumping, America deprives itself of the short-term gains of foreign products and long-term gains of greater efficiency. □

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THE FREEMAN
Ideas On Liberty

Germany and the "Third Way"

by Norman Barry

At least two things exercise political and economic commentators on Europe: the meaning and policy significance of the "third way" and the current malaise in the German economy. There is close connection between these two issues, though it is not quite the one that modern statists have in mind. But it is easy to show that the relative decline of the German economic "miracle" is directly linked to its adoption of economic and social policies that are recommended for a future social democratic Europe.

Advocates of the third way in the United States and the United Kingdom have similar, although watered down, things in mind. The European Union is itself suffering from the false promise of the latest modest anti-capitalist medicine. Yet the German experience provides an almost laboratory experiment of the errors of "capitalism with a human face," the "social market economy," "social democracy," or any other version of the third way. It is not enough to condemn the third way's political economy merely because President Clinton supports it. There are much better intellectual reasons for rejecting this currently fashionable doctrine.

No Miracle

For most of the postwar period (West) Germany, outside of Switzerland, was the most successful economy in Europe. Her recovery from the ruins of war was truly spectacular. The tragic irony is that just as countries in the rest of Europe ignored the reasons for this success so they will misunderstand the explanation of her current travails. For her early economic record was the result of the deliberate, almost planned, adoption of a free-market economy, which was completely against the trend of the times. There was no *Wirtschaftswunder* (economic miracle), only the rigorous implementation of well-tested economic policies based on sound theory. Germany's problems today stem from the retreat from this over a 30-year period.

Germany is celebrating the 50th anniversary of the founding of the Republic but the real event to commemorate is the radical free-market economic program introduced by its postwar economics minister, and later chancellor, Ludwig Erhard, in 1948. At the time, the agony of Germany's postwar attempted adjustment to economic reality was exacerbated by the continuation of a ruinous system of wartime planning under the Allied Control Commission. Interventionists though the advisers to West Germany were, they all agreed that there had to be currency reform; the Reichsmark was worthless and little used for whatever exchange actually took place. But Erhard, chief official of the Administration for Economic Affairs for the British and American Occupation Zones, managed, by a superb piece of political chicanery, to engineer a wholesale reduction of price controls under the noses of his Keynesian advisers. An early

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critic was John Kenneth Galbraith, who began his long career of highly profitable private punditry and catastrophic public economic error in postwar Germany. He wrote an influential article that promised misery and poverty if Erhard's policy were to be continued. He was, of course, engaged in writing his book on the theory of price control at the time.

But Erhard pressed on with his economic liberalization. There was probably not a majority in favor of it, and a majority was only narrowly achieved in the elections of 1949, after the policy's prophylactic effects were visible to all but the most blinkered of central planners.

Liberalization was not popular with the political elites. Erhard was never very close to the Christian Democrats, many of whom remained wedded to a form of interventionism and control derived from Roman Catholic social teaching, and the Socialists remained formally Marxist until 1959. Still, the reasons for Germany's success were too obvious to ignore (though Britain remained oblivious to them until 1979), and the country was quickly won round. The Catholics managed to combine the market with religion, and the Socialists became, albeit for a short time, even more pro-capitalist than some of the Christian Democrats. A prominent Social Democrat member of the coalition governments in the 1960s and 1970s, Karl Schiller, actually resigned over a free-market issue. The Social Democratic party has now slipped back to its old socialist ways, and these have been reinforced by the usual contemporary fads, notably environmentalism (the present government is a coalition of Social Democrats and Greens), anti-Americanism, and careful and diluted, but not completely rejected, anti-capitalism.

Seeds of Decline

The seeds of German decline were planted long ago. The intellectual error was by no means confined to the Social Democrats. All major political movements have been infected with the virus of the third way, with its illusion that there is a morally appealing midway point between capitalism and socialism and that we can indulge our social consciences with welfarism and heavy economic regulation without seriously corroding the market society. It is highly successful capitalist societies that are peculiarly vulnerable to these illusions; they have little resonance in Poland or the Czech Republic.

Their origins in Germany date back to the foundation of the Erhard system. There were two interconnected social visions that governed political and economic life in postwar West Germany: the idea of Ordo-liberalism—that is, the peculiarly German version of classical liberalism—and *die Soziale Marktwirtschaft* (social market economy). The values, policies, and personnel of the two intellectual movements overlapped. All German market theorists had some doubts about unregulated capitalism. Most particularly they thought there was a tendency for free contract to produce, quite spontaneously, a non-contract society through the emergence of monopolies and cartels. The German skeptics were encouraged by their own experience; the German economy had been badly cartelized in the early decades of the twentieth century (which ultimately enabled Hitler to run a "non-socialist" command economy). The Ordo-liberals thought that mistaken legal decisions had produced this outcome. In their *Wirtschaftsordnungspolitik*, the legal and political order of a free economy, the state was given the responsibility of preserving, artificially, the foundational rules of a market society, though they ought to have realized that free international trade is the most effective guarantor of a noncartelized economy. The Germans were very much influenced by American antitrust law.

Both "liberal" movements believed in some state welfare but it was much more pronounced in social market theory than in Ordo-liberalism. Alfred Müller-Armack, a member of Erhard's government, coined the deadly phrase "social market economy," and he actually believed in a new concept of the person—neither capitalist man nor socialist man—who would emerge from a properly and ethically organized market society. Erhard himself probably regarded the social market economy as a morally convenient mask behind which

he could advance his genuine market reforms. But at least the German liberals thought that welfare policies should be *marktkonform*, that is, consistent with an efficient exchange system; they should not encourage the emergence of a dependency culture.

However, as the German system developed, it was the "social" element that began to predominate over the "market," and throughout the 1960s the country began to resemble a Scandinavian welfare state, to which its liberal theorists had originally been vehemently opposed. Many reforms were quite debilitating. Unemployment pay was, and is, close to the wage paid for work; sick leave is very generous; and more or less free education can last almost forever. And, as any traveler will tell you, most shops are closed on Saturday afternoon. Given the reduced attractions of work (and German nonwage labor costs are the highest in the world) is it any wonder that German unemployment is 11.5 percent? The original Bismarckian state pension scheme was foolishly extended and its unfunded foundations, in combination with a declining birth rate, promise to present the country with a horrific problem in about 20 years. Government spending, which was kept below 30 percent of GDP under Erhard, is now above 50 percent.

Social Consensus

One reason for West Germany's original success was its social consensus. There was none of the confrontational attitude between capital and labor that so disfigured Britain before Margaret Thatcher. Once trade unions had accepted the market system, they were anxious to cooperate in what became a common enterprise. But this benign industrial culture had its downside. It produced a certain insularity and a hostility to the takeover mechanism: nothing much should change, and nobody should lose his or her job. Fearing the concentration of industry, the Ordo-liberals themselves gave this attitude some intellectual justification. They and the postwar government set up a cartel office, which sedulously sought out any innovator who might get a fraction more than the permitted market share.

German companies have never been concerned about delivering shareholder value. Indeed, they have traditionally financed their investment by bank debt, giving the lie to American business ethicists who worry about the immorality of corporate raiders loading up American corporations with junk-bond debt. Those ethicists looked to Europe as an example of probity, but as it turned out, the "greed-driven" Anglo-Saxon model of corporate governance proved highly flexible and innovative.

What nobody realized in Europe was that the predator breaks up companies, spins off unwanted parts, fires layers of redundant managers, and produces leaner and fitter enterprises. Such restructuring has been the foundation of America's economic success since the 1980s. But in Germany's much-vaunted consensus, the raider is subject to opprobrium and ostracism, especially if he is a foreigner. With banks (which, unlike those in the United States, hold substantial equity stakes in German companies), trade unions, and local interests forming invincible coalitions against change, German managers are secure, as they were in 1997 when Krupp tried a reverse takeover of Thyssen in order to rationalize the steel industry. The stakeholder groups got together and turned a hostile bid into a tame merger, with guarantees of no unemployment. Even Italy seems to be ahead in adopting Anglo-Saxon methods of industrial reorganization. The computer company Olivetti has just completed a spectacular $60 billion takeover of Telecom Italia against a formidable array of stakeholders. The takeover strategy, and motivation to maximize shareholder value, is now spreading to Europe. But Germany is far behind.

Fear of Inflation

Of the classical-liberal principles that undoubtedly inspired West Germany in the early postwar period, only a belief in sound money survived the onslaught of social democracy. Of course, Germany's experience of runaway inflation in the 1920s made the country sociologically equipped to cope with the occasional pains of monetary rigor.

Keynesian demand-management policies were eschewed from the early days, for excellent microeconomic reasons. An independent central bank, the Bundesbank, resisted all political pressures to relax what was basically Chicago-style monetarism ("just watch the monetary aggregates").

But by the 1960s macroeconomics became fashionable, and successive governments became obsessed with tinkering with the aggregates; committees were set up and suggestions made by "wise men" for improving overall performance. But the Bundesbank retained its virtue (and the people their pride in the German mark) right up to reunification, when Helmut Kohl's government compelled the Bundesbank, for overtly political reasons, to sanction a catastrophic one-to-one currency swap, the East German mark for the Deutsche mark. The former was pretty much worthless, and this arrangement, plus the granting of partial West German welfare "rights" to the former East, undoubtedly made the union of the two countries more difficult than it need have been.

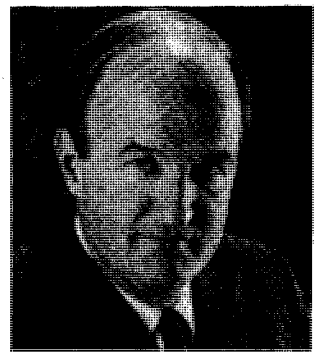
German monetary chastity clearly could not survive the seductive lure of reunification. The next question on the macroeconomic agenda is whether the Euro, the new currency for the continent, will provide a satisfactory surrogate for the beloved mark. The Bundesbank had established a reputation for incorruptibility precisely because of its proven probity: prior to reunification no politician could compete with it in the public's estimation. One of the first things the controversial leftist Social Democrat Oskar Lafontaine did in his brief period as minister of finance in the new Social Democratic government was to put pressure on the European Central Bank to relax its Bundesbank-type monetary rigor. That failed, but one wonders how that institution will survive a coalition of Spanish, Italian, French, and other politicians demanding inflationary employment policies.

With excessive social welfare and a sclerotic industrial economy, Germany is no longer the powerhouse it once was. An early Ordo-liberal, Wilhelm Röpke, once said that "like pure democracy, undiluted capitalism is intolerable." He was a pioneer of the idea of the third way, but even he would be distressed at what has happened to his country.* Perhaps the major problem with Ordo-liberalism was its neglect of public choice. Its adherents really did believe that once people had experienced the joys of the social market they would have less reason to rely on the familiar human motivations and on the historically validated legal and market constraints. Social-market theorists had an "elevated" view of human nature: When politicians and public officials were imbued with a sense of community and reinforced by the glue of solidarity, no one need worry about things like antisocial rent-seeking; moral hazard would not be a problem for enlightened people in a generous welfare system; and managers of industrial corporations would be disciplined without stockholder pressure and the threat of raiders.

But the more astute German commentators learned early on that there is no feasible third way. All economic proposals that run counter to the laws of economics are eventually defeated by these inexorable processes; they may be a little slower to operate than those of physics, but they are just as compelling. Germany has breached just about every one of them in the last 30 years. As Vaclav Klaus, the former Czech premier, put it: "the third way is the third world." □

*_Editor's note_: See Richard Ebeling, "Wilhelm Röpke: A Centenary Appreciation," _The Freeman_, October 1999.

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Ideas On Liberty
NOVEMBER 1999



A Private-Sector Solution to Poverty

"The able bodied poor don't want or need charity. . . .
All they need is financial capital."
—MUHAMMAD YUNUS

For years free-market economists have protested the waste and abuse of foreign aid programs, International Monetary Fund loans, and World Bank projects.[1] P.T. Bauer has been in the forefront as a dissenter against government development programs. For the past 50 years, he has argued forcefully that government assistance in developing nations only retards economic growth.[2]

But if IMF lending, foreign aid, and the World Bank are abolished, what should be done to alleviate poverty? Bauer and other classical liberals advocate reducing trade barriers; increasing foreign investment; establishing property rights, the rule of law, and a stable monetary policy; and encouraging free markets and limited government domestically.

Private-Sector Micro Lending

Yet market advocates have been surprisingly silent on a burgeoning private-sector success story known as "micro lending," the lending of extremely small amounts of money to self-employed entrepreneurs in the Third World by independent banks and institutions. The most famous of these micro-lenders is the Grameen Bank, founded by Muhammad Yunus in Bangladesh, the world's poorest country, in 1983. Yunus is an economics professor at Chittagong University in Bangladesh.

When I say "small loans," I mean minuscule. The Grameen Bank lends only $30 to $200 per borrower. Applicants don't have to read or write to qualify. No collateral or credit check is required. Amazingly, the Grameen Bank has made these micro loans to millions of poverty-stricken people in Bangladesh, $2.5 billion so far. These loans are not interest-free. The Grameen Bank is a for-profit private-sector self-help bank that charges 18 percent interest rates. The default rate? Less than 2 percent. This remarkable record is due to the requirement that borrowers must join small support groups. If anyone in the group defaults, no one else can borrow more.

The bank lends to entrepreneurs, overwhelmingly female, who need only a few dollars to buy supplies and tools. Borrowers might be makers of bamboo chairs, sellers of goat's milk, or drivers of rickshaws. By avoiding the outrageous rates charged by other moneylenders (often 20 percent a month), these people are finally able to break the cycle of poverty. Their small businesses grow, and some use

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their profits to build new homes or repair existing ones (often using a $300 Grameen house loan). Thousands of Grameen borrowers now own land, homes, and even cell phones. And they are no longer starving. Yunus has plans to issue private stock and eventually go public with his antipoverty program.

His bank has been so successful that other micro-lending institutions have sprung up throughout the world. The concept has gained credence everywhere, to the point that even the World Bank and other government agencies have gotten into the million-dollar microloans business.

Saying No to the World Bank

But Yunus won't have anything to do with the World Bank. In his new autobiography, *Banker to the Poor* (highly recommended), Yunus decries the World Bank: "We at the Grameen Bank have never wanted or accepted World Bank funding because we do not like the way the bank conducts business." Nor does he much like foreign aid: "Most rich nations use their foreign aid budgets mainly to employ their own people and to sell their own goods, with poverty reduction as an afterthought. . . . Aid-funding projects create massive bureaucracies, which quickly become corrupt and inefficient, incurring huge losses. . . . Aid money still goes to expand government spending, often acting against the interests of the market economy. . . . Foreign aid becomes a kind of charity for the powerful while the poor get poorer."[3] Peter Bauer couldn't have said it better.

From Marxism to Marketism

Yunus's statements are all the more amazing given that he grew up under the influence of Marxist economics. But after getting a Ph.D. in economics at Vanderbilt University he saw firsthand "how the market [in the United States] liberates the individual" and rejected socialism. "I do believe in the power of the global free-market economy and in using capitalist tools. . . . I also believe that providing unemployment benefits is not the best way to address poverty." Believing that "all human beings are potential entrepreneurs," Yunus is convinced that poverty can be eradicated by lending poor people the capital they need to engage in profitable businesses, not by giving them a government handout or engaging in population control.

His former Marxist colleagues call it a capitalist conspiracy. "What you are really doing," a communist professor told him, "is giving little bits of opium to the poor people. . . . Their revolutionary zeal cools down. Therefore, Grameen is the enemy of the revolution."[4] Precisely. □

1. The latest examples are Paul Craig Roberts and Karen LaFollette Araujo, *The Capitalist Revolution in Latin America* (New York: Oxford University Press, 1997) and James A. Dorn, Steve H. Hanke, and Alan A. Walters, eds., *The Revolution in Development Economics* (Washington, D.C.: Cato Institute, 1998).

2. See P. T. Bauer, *The Development Frontier* (Cambridge, Mass.: Harvard University Press, 1991), *Equality, the Third World and Economic Delusion* (Cambridge, Mass.: Harvard University Press, 1981), and *Dissent on Development* (Cambridge, Mass.: Harvard University Press, 1976).

3. Muhammad Yunus, *Banker for the Poor* (New York: PublicAffairs, 1999), pp. 145–46.

4. Ibid., pp. 203–205.

Professor Skousen's *Economic Logic* Now Available

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The first volume of Mark Skousen's breakthrough college textbook, *Economic Logic*, has just been published. This "micro" text covers supply and demand, monopoly vs. competition, entrepreneurship, wages, capital and interest, and the financial markets. *Economic Logic* is a no-compromise free-market college textbook, with a hands-on approach (it begins with a profit-and-loss income statement). Special price: $21.95 each. Send your order to: FEE, or call (800) 452-3518. Instructors should e-mail requests to mskousen@aol.com for a review copy.

BOOKS

Market Education: The Unknown History

by Andrew J. Coulson

Transaction Publishers and the Social Philosophy and Policy Center • 1999 • 430 pages • $54.95 cloth; $24.95 paperback

Reviewed by George C. Leef

The most pernicious of all the widely held modern beliefs is that education must be provided by the state. "Education is an entitlement!" say nearly all politicians and members of the vast education establishment. Few challenge that assertion. The *inseparability* of school and state is almost as much a given as the separation of church and state.

In this book Andrew Coulson takes dead aim at that belief. Coulson, senior research associate at the Social Philosophy and Policy Center, is a computer software engineer who developed a strong interest in educational history and policy. *Market Education: The Unknown History* is the product of his research. It's a strong case for letting the free market work in education.

Coulson's historical overview of educational history is extremely beneficial. Government education is so widely assumed to be the only possibility that many will be surprised to learn there have been places and times when government kept out entirely. The author's contrast between Athens and Sparta in ancient Greece is illustrative.

In Athens, Coulson writes, "with the exception of two years of military training, the state played no role in schooling." That, of course, did not mean an uneducated populace. Just as Athenians managed to feed, clothe, and house themselves without any government action, so did they educate themselves. Parents paid monthly tuition for the education of their children at whichever of the numerous private schools they preferred. Schools could survive only by offering educational services parents found sufficiently valuable to pay for. Education was not an "entitlement," and wasn't "equal," but Coulson states that even the poorest families were consumers in the education market.

Education was not static in Athens. "Each step in the evolution of Athenian society was matched by a corresponding change or expansion in the offerings of educators," Coulson writes. No government planning agency existed to decide what subjects must be taught and who was permitted to teach them. The result of this laissez-faire approach was a civilization that far surpassed any other in the ancient world. Athens was the intellectual center of the Mediterranean, a wellspring of genius in science, mathematics, philosophy, literature, and more. All those brilliant thinkers working in a culture that esteemed learning—and not a government school to be found!

In contrast, Sparta established a government education monopoly to ensure the preservation of the collectivist/militarist philosophy of Lycurgus and later rulers. Children were regarded as property of the state, which used its education monopoly to breed obedient, warlike people ready to sacrifice themselves for the imagined glory of the state. Intellectual and artistic achievements of the Spartans? Virtually none, Coulson remarks, "apart from being a beacon to those advocating totalitarian systems of education."

The author's investigation into the history of education, both market-driven and state-dominated, proceeds on through Rome, the Middle Ages, the Islamic world (which initially followed the Athenian approach, with similarly magnificent results), and eventually to the last several centuries in England, France, Germany, and the United States. He uniformly finds that beneficial consequences have flowed from educational liberty and less desirable if not downright disastrous consequences from state control.

The largest part of the book is Coulson's examination of the American educational experience, and a fascinating study it is. We learn of the struggle of black parents in Boston in the mid-1800s to escape from segregated public schools, only to lose in a court decision that would become a precedent for the Supreme Court's infamous "separate but

equal" doctrine. We learn of the early advocates of "public education," such as James G. Carter, who argued that we should emulate Sparta's educational model. We learn of the various failed educational fads that our education "experts" have embraced with terrible results for the human guinea pigs subjected to them. After reading Coulson's lengthy exposition, it is impossible to avoid the conclusion that abandoning the education marketplace in favor of government schooling is one of our greatest national blunders.

The last part of the book turns to the many proposals for education reform that are on the loose. Coulson is not very enthusiastic about any of the nostrums such as charter schools, vouchers, and private management. He does, however, praise the idea of privately funded scholarships to enable children to escape from the clutches of the public school system.

Sometimes Coulson drops his scholarly tone in favor of hyperbole, and sometimes he makes important assertions without apparent support. The lapses in the book, however, are microscopic compared to its powerful research and argumentation. If restoration of the free market in education is a matter of importance to you—and it should be—this is a book you don't want to be without. □

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

China in the New Millennium: Market Reforms and Social Development

edited by James A. Dorn

Cato Institute • 1998 • 416 pages • $24.95 cloth; $15.95 paperback

Reviewed by Steven W. Mosher

In June 1997 the Cato Institute sponsored an academic conference in Shanghai, along with Fudan University's Center for American Studies. The government signed off on the event and, for the most part, the Chinese participants carefully avoided sensitive political topics. Not so the irrepressible Cato crowd.

James Dorn, Cato's vice president for academic affairs, reminded his listeners that "The continued success of China's journey to prosperity . . . will depend on whether [they] are willing to allow a true market system to develop, in which individuals can hold secure title to their property and are held accountable for their mistakes, or whether China remains a 'socialist market economy.'"

Edward Crane, Cato's president, made the connection with politics explicit. "There are two fundamental ways to order society: Voluntarily, through the private interaction of individuals, associations, religious organizations, businesses, and so on . . . or coercively, through state mandates . . . because it is in the nature of man to be free . . . society is better off—not just economically but spiritually—when politics plays as small a role as possible in societal affairs."

The Chinese participants (who did not have the advantage of holding either American citizenship or outbound plane tickets) were mostly silent. Professor Zhou Dun Ren stood alone among those who pointed out the connection between economic and political freedom, suggesting that China needed more of both. "The pointer on the roadmap of the 21st century is for China to go down the road of a true market economy. The more developed China is economically, following the free-market model, the more freedom and democracy will advance." Perhaps it is not surprising that Professor Zhou is the *former* deputy director of the Center for American Studies. In China, libertarian sentiments do not go unpunished.

The conference proceedings, published here, offer abundant evidence that China's steps away from rigid central planning and toward the free market have generated spectacular economic growth over the past 20 years. Per capita income has increased fourfold; exports have skyrocketed. Hundreds of millions of Chinese have been lifted out of dire poverty.

At the same time, China's increased material prosperity has had no discernible effect on the political system, which remains a self-perpetuating one-party dictatorship. Despite participant Mao Yushi's claim that "China's economic reforms and opening to the outside

world have advanced both material progress and civil society," evidence of the latter remains scanty.

Kate Xiao Zhou argues that women in rural China have experienced a revolutionary change in their lives as their participation in the market has increased their personal autonomy and freedom. In "Market Development and the Rural Women's Revolution in Contemporary China," she writes that rural women by the millions "have participated in the development of markets, the rise of rural industry, and migration."

China's economic changes have weakened social controls for women, but it has gained them nothing in terms of political rights from the state. And the weakening of the mediating institutions of family and village, as the one-child policy demonstrates, may in some ways render women even more vulnerable to state exploitation. Zhou regrets that this "contemporary rural women's revolution," as she calls it, "has no organization, no leader, and no ideology," but it could hardly be otherwise. If it did, the Party would see it as a threat. It would be either co-opted or crushed, as the China Democracy Party was recently crushed.

Minxin Pei, assistant professor of politics at Princeton University, draws a connection between the economic liberalization and the thousands of semi-official associations that have sprung up over the past 15 years. Pei sees these associations, which include groups of private entrepreneurs, consumers, and village and township enterprises, as a nascent civil society. This may be too optimistic a reading. Many of these organizations represent pre-existing Party and government organizations (the village and township organizations, for instance), and all are required to register their membership and goals with the government. Moreover, a recent government edict forbids the formation of new groups.

What is one to make of this increasing gap between China's material prosperity and the retro behavior of the Chinese Communist Party? Crane suggests that China is "at a crossroads, and that it must choose between political society and civil society—that is, between coercion and freedom as society's organizing principle." I believe that China's leaders *have* chosen—long ago—to organize on the principle of coercion. And there is no evidence I can see that they are wavering in this choice. Indeed, they seem convinced that a continuation of the present "socialist market economy" is their road to national power and personal wealth.

For all the talk about China's "nascent civil society," the People's Republic is at present governed by a single class. This kleptocracy uses its power—combined with the strength of Chinese family ties—to engage in a massive accumulation of wealth. Non-relatives—the vast majority of the Chinese people—can expect to be cheated.

Cato is to be congratulated for going to China and sounding a libertarian call to arms. The conference volume that resulted is worth reading. But there is no force in China today capable of taking the field against the vast Communist kleptocracy. □

Steven Mosher is the president of the Population Research Institute and the author of the forthcoming Hegemon: China's Plan to Dominate Asia and the World.

The Shadow University: The Betrayal of Liberty on America's Campuses

by Alan Charles Kors and Harvey A. Silverglate

The Free Press • 1998 • 415 pages • $27.50

Reviewed by Daniel Shapiro

Many books have discussed political indoctrination on American campuses, but none is as thorough and damning as this one. Alan Kors, a history professor at the University of Pennsylvania, and Harvey Silverglate, a criminal defense attorney and civil liberties litigator, present overwhelming evidence that the loss of liberty on campuses is far greater than most people realize. Speech codes, which punish students and faculty for offensive or "harassing" speech, are ubiquitous. Due process is the exception rather than the rule: secret judicial proceedings routinely deny accused faculty and students the right to be represented by legal counsel, to confront or

call witnesses, and to have an impartial judge and appeals process. Most chilling of all, "sensitivity training," a.k.a. thought reform, tells students what to believe and labels them as "in denial" or as "oppressors" unless they profess the politically correct orthodoxy about race, gender, and so on.

Most people, even critics of political correctness, are unaware of this system because much of it happens outside the classroom. To see the destruction of liberty on American campuses one must also examine offices of student life, residential advisers, judicial systems, deans, freshmen orientation, and the promulgation of rules and regulations. These aspects of the university are inescapable for students (and increasingly for faculty), and punishment for violating its rules occurs behind closed doors. Hence the book's title: *The Shadow University.*

Kors and Silverglate rip the veil off this system, revealing far more cases than have hitherto been reported. Besides providing compelling narratives of various assaults on liberty, the authors also cogently explain the basic moral and constitutional principles of free speech and academic freedom, due process, and freedom of conscience, which are routinely violated throughout academia. A hallmark of their violation is the double standard: provocative speech (such as "born again bigot," "Uncle Tom") by the politically correct is protected, but those who appear to criticize feminism, affirmative action, or other reigning orthodoxies may be censored and/or re-educated.

I'll sketch only a few of the incredible cases: a (white) student at the University of Pennsylvania calls noisy (black) students "water buffaloes" and is charged with racial harassment; a professor at Dallas Baptist University criticizes feminist arguments, is charged with defamation, and is then fired, along with the dean who defended him; a student at Sarah Lawrence is sentenced to sensitivity training for "homophobia" for laughing at a remark made about a gay student; a Catholic residential adviser at Carnegie Mellon University is fired for refusing to wear a symbol in support of gay and lesbian students; freshmen orientation at Williams College requires everyone to gather in a dark auditorium where insults are hurled at them from all directions; a professor at Cornell University is found guilty of sexual harassment at a hearing that he is forbidden to attend or call witnesses, and where the head of the investigating committee says "we have to make the rules as we go along."

How did this arise? Bad ideology plus careerist administrators, answer the authors. The bad ideology is New Left theorist Herbert Marcuse's argument in his 1965 essay "Repressive Tolerance," that the marketplace of ideas masks repression of "progressive" ideas. To prevent the silencing of these ideas, "reactionary" ideas must be censored. This zero-sum view of freedom is followed by today's defenders of speech codes and other assaults on liberty. (However, the authors give no evidence that today's censors were influenced by Marcuse.) As for administrators, they perform their jobs in hopes of moving on to a more prestigious position, often at a new campus. To move on, their reign must be relatively untroubled, which means they aim to appease groups who can cause trouble: militant feminists, blacks, and gays. Sacrifice of other people's freedom doesn't matter.

I wish the authors had dug deeper on the careerism issue. They remark that colleges and universities have taken on many of the trappings of large corporations, minus the accountability, but they do not discuss whether re-establishing accountability requires that colleges become proprietary institutions.

Kors and Silverglate suggest two strategies for restoring liberty. First, litigate. Court challenges to university oppression frequently succeed. State universities are bound by the First Amendment and the requirements of due process; private universities are contractually bound to keep their promises of free inquiry and procedural fairness. Second, publicize oppression: Universities hate publicity. Publicity can shame the university into change, and/or arouse freedom-minded colleagues to revolt.

This is a great book, and that's not hyperbole. It is not an enjoyable topic, but one indispensable for anyone concerned with liberty in academia. I am in awe of the authors.

It must have taken enormous energy, intellectual focus, and a burning passion for justice to uncover this massive oppression on American campuses. All lovers of liberty are in their debt. □

Daniel Shapiro is an associate professor of philosophy at West Virginia University.

Principles for a Free Society: Reconciling Individual Liberty with the Common Good

by Richard A. Epstein

Perseus Books • 1998 • 372 pages • $30.00

Reviewed by William H. Peterson

Law and economics were once openly tied, as witness the title of John Stuart Mill's 1848 work, *Principles of Political Economy*. Or consider that Ludwig von Mises and F. A. Hayek both held doctorates from the University of Vienna not in economics but in *jurisprudence*.

Economics came into its own as a "pure" science, however, with the establishment of the American Economic Association (AEA) in 1885 and publication of Alfred Marshall's *Principles of Economics* in 1890. Has its independence been for the better? Economics has since become increasingly uncertain, mathematical, and state-oriented. But the relationship between state and society at home and abroad in the stormy twentieth century has been anything but calm and stable. The welfare state has arrived, and liberty retreats far more often than it advances.

As AEA cofounder and first president Richard T. Ely contended, a "new world is coming into existence," and "we must have a new economics to go along with it." The state should no longer be only an umpire, said Ely, but should become an agency "whose positive assistance is one of the indispensable conditions of human progress."

What is the proper role of the state? Was Ely correct in advocating a highly interventionist state? Or is it possible to reconcile laissez faire, private property, individual choice, and minimal government with the common good?

That reconciliation constitutes the broad mission of this book by Professor Richard A. Epstein of the University of Chicago Law School. Epstein is a constitutionalist, one who upholds natural law for its utilitarian value and asks for a return to our limited government roots. He is a meticulous thinker who approaches his job here by analyzing scores of law cases. His philosophy can be seen in his endorsement of this quotation from the *Edinburgh Review* in 1843: "Be assured that freedom of trade, freedom of thought, freedom of speech, and freedom of action, are but modifications of one great fundamental truth, and that all must be maintained or all risked; they stand and fall together."

Epstein believes that private property rights are vital in the quest for the common good and registers his approval of recent Supreme Court decisions that have moved in the direction of greater protection for property owners against the grabbiness of government. For example, in *Dolan v. City of Tigard* (1994), the city had maintained that it had the right to compel Mrs. Florence Dolan, the owner of a plumbing-supply store, to dedicate land for a bicycle path without any compensation. The Supreme Court disagreed, with Chief Justice William Rehnquist writing, "We see no reason why the takings clause of the Fifth Amendment, as much a part of the Bill of Rights as the First Amendment or Fourth Amendment, should be relegated to the status of a poor relation."

Epstein is also skeptical of government regulation that is supposed to improve the working of the market for consumers. He takes a dim view of the antitrust suit against Microsoft, arguing that while it may be beneficial to Microsoft's competitors, it ill-serves the legions of Internet consumers who continue to enjoy the competition and downward drift in prices. Epstein fears that use of state coercion to compel Microsoft to vary its product offerings along government-acceptable (that is, competitor-acceptable) lines mocks true competition and risks stifling the sort of innovations that sparked the Information Revolution in the first place.

On the whole, the book offers a splendid defense of laissez faire, but Epstein's Chicago

School utilitarianism sometimes leads him into questionable positions. He accepts, for example, some "forced exchanges" such as public highways and utilities. In granting the state some right to coerce in selected pragmatic cases, Epstein seems to open windows of opportunity for both inefficiency and political hanky-panky. Debates between Epstein and the Rothbardian free marketers over the advisability of permitting government to make people participate in forced exchanges would be intellectual events to savor.

But do not allow this reservation to deter you from reading *Principles for a Free Society.* Epstein's focus is on the need to preserve and indeed to expand freedom, not on the rare instances where he concludes that government coercion is justified. His strong argument that freedom and the common good can be reconciled is one that we must make again and again. □

William Peterson is adjunct scholar with the Heritage Foundation in Washington and Distinguished Lundy Professor Emeritus of Business Philosophy at Campbell University in North Carolina.

Driving Forces: The Automobile, Its Enemies, and the Politics of Mobility

by James Dunn

Brookings Institution • 1998 • $44.95 cloth; $18.95 paperback

Reviewed by John Semmens

Over the last two generations a battle between the automobile and its enemies has raged in most urban regions. Aligned against the automobile is an elite composed of self-appointed visionaries who believe they have the answer to how urbanized man should live. On the other side we have the masses of common people and the commercial interests that have catered to man's preference for the automobile.

The battle is over. The auto has won. Because it empowers the individual to go where he wants to go when he wants to go, the auto provides a freedom and quality of service that public transit systems cannot match. The author refutes all the key anti-automobile arguments. For example, in response to the claim that General Motors conspired to drive the streetcar out of business, Dunn points out that streetcars went out of business around the globe, not by any nefarious deeds of General Motors, but by the superior performance of the automobile. In Los Angeles the auto was embraced as a means of escape from the "corrupt" streetcar monopoly.

In response to the argument that the Interstate Highway Act and Highway Trust Fund gave autos an unfair advantage, Dunn points out that the federal highway trust fund is self-sustaining from taxes and fees levied on highway users. This stands in contrast to federal aid to transit in which users pay a minor share of the costs. Dunn compares transit's and autos' shares of passenger travel (1 and 99 percent respectively) with their shares of government expenditures (25 and 75 percent). Transit would seem to have the unfair advantage.

In response to the argument that American cities should imitate European cities, Dunn asserts that Europe is imitating America. Despite heavy gasoline taxes, huge subsidies for public transit, and more densely developed urban land use, auto ownership has been growing faster in Europe than in the United States.

Public transit has been declining for very good reasons. Foremost among them is that public transit's attractiveness is inversely correlated to personal income. When people are poor, public transit may be the best transportation they can get. As people prosper, they want to move up to a higher quality of transportation. It is economic growth that dooms public transit to a dwindling share of urban travel. Short of driving the majority of urban populations into poverty, there is no public policy that is likely to revive public transit.

Dunn acknowledges that traffic congestion and air pollution are serious negative byproducts of the automobile. The cure, though, is not to waste billions of dollars on attempts to resuscitate moribund public transit systems in the vain hope that this will provide some relief. Instead, he recommends that public

policy focus on more cost-effective solutions.

He calls his program "Auto Plus." The key is to make auto transportation work more effectively and with fewer negative social impacts. Along those lines, he suggests electronic road pricing, technological fixes for vehicle emissions, and vouchers for the transit dependent. Transit agencies, rather than jealously protecting faltering bus and train monopolies, should become "mobility managers," says Dunn. As such, transit officials would promote rather than suppress competition from "jitney vans." And instead of attempting to hold on to the urban poor as a captive clientele, they would be supportive of ways to help the poor obtain cars.

There is one aspect of Dunn's prescription that may cause some consternation among highway advocates. He recommends ending the "trust fund" concept. In fact, he goes even further by suggesting that higher taxes on cars and trucks could be a productive source of revenue for general government purposes. Let's not turn efficient transportation into a cash cow for federal boondoggles elsewhere.

Whether one agrees with Dunn's prescribed remedies or not, his emphasis on hardheaded realism is a better foundation for policy debate than the notions of those who wish that things were different, that people could be induced to give up their prized mobility, or that the clock could be turned back to a time when life was "simpler." □

John Semmens is an economist with the Laissez Faire Institute in Chandler, Arizona.

President Grant Reconsidered

by Frank J. Scaturro

University Press of America • 1998 • 152 pages
$34.50 cloth; $16.95 paperback

Reviewed by Burton Folsom

In almost all polls of U.S. presidents, Ulysses S. Grant ranks near the bottom. Professor Thomas Bailey of Stanford, in a typical evaluation, writes, "Grant was an ignorant and confused President, and his eight long years in blunderland are generally regarded as a national disgrace."

Frank Scaturro, an attorney with a strong interest in this subject, comes forth in *President Grant Reconsidered* to make the case that Grant was a much better president than historians say. He contends that modern historians have taken their cue on Grant from his intellectual contemporaries, who often despised him because he wouldn't appoint them to office. Henry Adams, for example, wrote that Grant "had no right to exist. He should have been extinct for ages. . . . The progress of evolution from President Washington to President Grant was alone evidence enough to upset Darwin."

Scaturro challenges this hyperbole and argues that Grant's presidency (1869–1877) was a positive one in U.S. history. He sees Grant as a forceful and honest president, who said, "I don't lie myself, and I won't have any one lie for me." He used the veto 93 times—more than any of his predecessors—and supported vigorously the rights of newly freed blacks. Frederick Douglass wrote, "To [Grant] more than to any other man the [N]egro owes his enfranchisement and the Indian a humane policy. In the matter of the protection of the freedman from violence his moral courage surpassed that of his party."

Scaturro argues that the amount of corruption in Grant's administration is greatly overstated. Of Grant's 25 cabinet appointments, only one, Secretary of War William Belknap, left in disgrace. A few others had charges made against them, but none was proven. The spoils system operated under Grant, as it had with previous presidents, but Scaturro observes that Grant introduced improvements in the civil service system. In the case of the New York customs house, the author insists that it operated more honestly under Grant than under previous presidents. Finally, Scaturro maintains that Grant's handling of Reconstruction was competent.

The major arguments that Scaturro makes are useful, but he is a strong partisan and sometimes overstates his case. For example, he says it is unfair to blame Grant for the Whiskey Ring and the Credit Mobilier scandals because they started before he became president. Those are valid points. But then he

wants to give full credit to Grant for resolving the *Alabama* claims with England, when in fact those negotiations also began before Grant became president. (The United States had claimed damages from England caused by Confederate cruisers built and aided by British interests.) England's eventual agreement to pay damages stemmed from the German victory in the Franco-Prussian War—it did not want to risk an alliance between the United States and Germany. Grant's administration had almost nothing to do with it.

Scaturro also omits some points favorable to Grant that should have been included. Grant reduced the national debt during his presidency and ended the federal income tax. He also favored a sound currency. Within two weeks after Grant became president, he signed the Public Credit Act, which pushed the United States to redeem its greenbacks in coin as soon as possible. Five years later, he vetoed an inflationary bill that would have increased the greenback supply by more than 10 percent.

Grant was far from a consistent advocate of limited government. Before he assumed the presidency, as well as afterward, he supported the system of federal subsidies for the Union Pacific and Northern Pacific Railroads. The resulting corruption led to the Credit Mobilier scandal and increased government regulation. Grant also tried to annex Santo Domingo and expand the American empire abroad.

Scaturro's book helps offset the traditional historical bias against Grant. From a classical-liberal standpoint, it exaggerates Grant's achievements, but it is still a useful corrective. In some ways, Grant's low ratings in presidential polls are inevitable, the result of prejudices held by many historians. As historian Ari Hoogenboom once noted, "The historian is usually liberal, more often than not a Democrat. . . . The post-Civil War era stands for all the historian opposes." If Grant had unveiled a huge program of land and income redistribution, he might have won over the historians, but that would have destroyed our heritage of liberty and sent us reeling on a statist course long before the "great" presidents of the twentieth century did so. □

Burton Folsom is historian in residence at the Center for the American Idea in Houston, Texas.

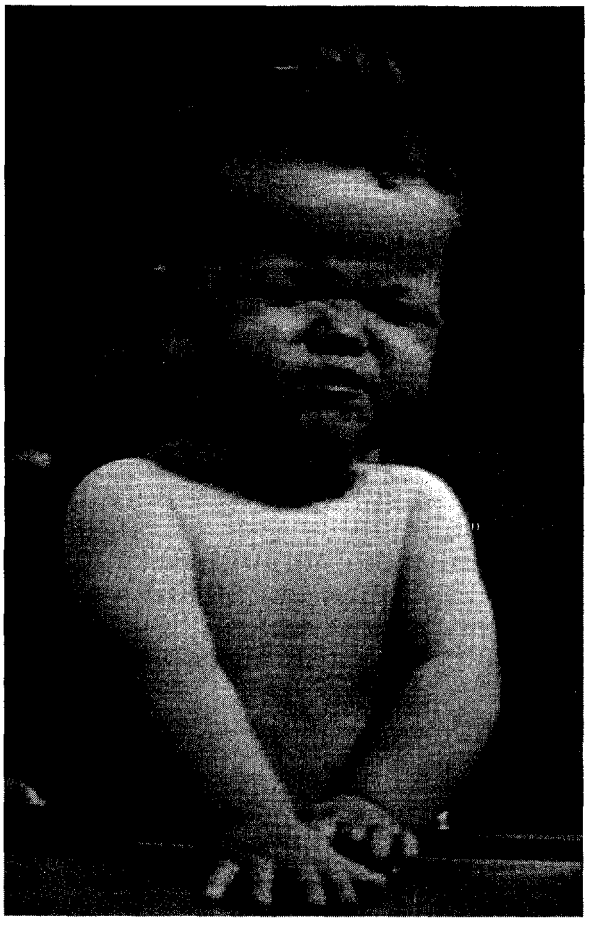
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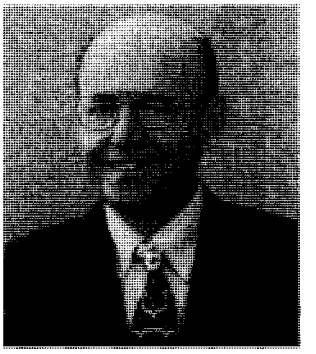
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The AFL-CIO: Renaissance or Irrelevance?

To hear the AFL-CIO tell it, the union movement has reversed its decline and is at the dawn of a renaissance. But among all the puffery, three reported claims are especially suspect: (1) employers routinely harass workers who want to organize; (2) in 1998 the number of union members increased by 101,000; and (3) on average workers represented by unions now make 34 percent more than union-free workers. Perhaps most troubling of all are reports that clergy and civic leaders have announced coalitions with unions to promote improved living standards and a heightened "sense of community."

Worker Harassment

In reality, the decline of the union movement in the private sector continues unabated, and it has nothing to do with employers harassing workers who want to unionize. The principal reason for the unions' plight is that fewer and fewer workers are interested in organizing. In a recent paper for the National Bureau of Economic Research, Henry Farber and Alan Krueger concluded that the demand for unionization among private-sector workers has declined and continues to decline. Workers' bargaining power in employment contracts depends on the quantity and quality of alternative employment alternatives they have. Deregulation and globalization of competition have significantly increased those alternatives in both dimensions. In this environment most workers think the costs of unionization—union-imposed initiation fees, fines, assessments and dues, increased strife between workers and management, lost productivity, and lost working time due to strikes—far outweigh the benefits.

The unions' claim that employers prevent unionization by harassment of workers simply doesn't make sense. First, such practices are already illegal; and second, intense competition for qualified workers prevents employers from mistreating workers. In a 1998 study of the reasons for the continuing decline of unions in the private sector, the Employment Policy Foundation found that only 0.35 percent of the decline could be attributed to managerial opposition activities involving "unfair labor practices" as defined in the National Labor Relations Act. Astute private-sector employers are less likely to harass workers than to try to avoid the burdens of unionization by treating their employees well.

New Members

The 101,000 additional dues payers captured by unions in 1998 were all in the government sector. In 1998 government employee membership increased by 158,000 while private employee membership fell by 57,000. The unions' market share in government employment rose from 37.2 to 37.5 percent, while in the private sector it fell from 9.7 to 9.4 percent. In terms of market share, govern-

Charles Baird is a professor of economics and the director of the Smith Center for Private Enterprise Studies at California State University at Hayward.

ment employment has provided the unions with the only good news they have had since 1953.

This is easy to explain. Government employers don't resist unionization. In fact they encourage it. They and the unions sit on the same side of the bargaining table. Both seek to pick the pockets of taxpayers. The much ballyhooed February 23 win by the Service Employees International Union of the right to represent 74,000 home-care health workers in Los Angeles is a case in point. Those workers are employees of Los Angeles County, and any union-imposed increases in costs will simply be passed forward to the county's hapless taxpayers. In the competitive private sector, union-imposed cost increases cannot be passed forward because customers go elsewhere.

Union Wage Premium

The unions' claim of a 34 percent wage premium over union-free workers is overblown. According to the Bureau of Labor Statistics, in 1998 the median weekly wage paid to union-free private-sector workers was 79.6 percent of that paid to comparable workers who were represented by unions. That figure compares wages only. When total compensation packages are taken into account the union-free to union ratio is 85 percent. Moreover, union representation is not the sole source of the apparent union advantage. The BLS explains that "The difference reflects a variety of influences in addition to coverage by a collective bargaining agreement, including variations in the distributions of union members and nonunion employees by occupation, industry, firm size, or geographic region." In services, union-free wages were 90.1 percent of wages paid to workers represented by unions. In finance, insurance, and real estate the figure was 104.3 percent. Moreover, the ratio of union-free wages to union wages has been steadily increasing. This is another reason for the decline in the demand for unionization.

Statistics will usually overstate the effect of unions on wages. The comparison that should be made is wages paid union-represented workers versus wages those same workers would have received without union representation. Of course that comparison cannot be made. As a second best, wages paid to union-represented workers are compared to wages paid to comparable union-free workers. But this comparison always involves what economists call a spillover effect. Unions are able to get above-market wages for workers they represent only by restricting the supply of workers on those jobs. When the workers who are shut out of those jobs seek employment elsewhere, they spill into the union-free market, depressing wages.

Unions argue that statistics are just as likely to understate their effects on wages because of what they call the threat effect. Employers may raise union-free wages just to avoid unionization—a form of preventive labor relations. However, there is an upper limit to what an employer is willing to pay for labor. That limit, called a demand price, is based on labor productivity and the prices that customers are willing to pay for the goods and services produced with those labor services. In a competitive labor market any margins between demand prices and wages actually paid will be very slim. There will be little room for threat-based wage increases.

Justice?

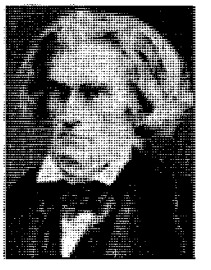
Clergy and civic leaders ought to pause before they sign on to the unions' agenda. Unions cannot raise living standards for anyone except their members. The workers who end up with lower wages because of the spillover effect certainly will not have higher living standards.

Clergy and civic leaders also ought to consider the unions' well-documented history of getting their way through violence and intimidation before they blindly accept the notion that unions foster a "sense of community." Organizations whose survival depends on government-granted rights of coercion rather than their ability to engage others on the basis of voluntary exchange are bereft of merit. They deserve the scorn of everyone who seeks genuine justice for all rather than special privileges for a few. □

THE FREEMAN
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PERSPECTIVE

5,999,999,999 and Counting

Sometime this fall the world's population was estimated to have reached six billion. The U.N. Population Fund, which "knows" precisely how many people there should be in the world, also "knows" precisely what day the world hit six billion: October 12.

In fact, no one knows precisely how many people there are on earth. One would have to have an exaggerated confidence in the record keeping of governments to make such a claim. How reliable are the records—birth and death—of, say, Rwanda?

The Population Fund's perennial campaign to scare us about the number of people is another unfortunate use of taxpayers' money. On its face the number six billion says nothing. In context it says nothing disturbing. The population's rate of increase is slowing markedly. Fertility rates have been falling for decades. According to MSNBC, "Since 1992, the United Nations has had to push back its 6 billion estimate by almost two years."

The Population Fund and its brooding boosters such as Paul Ehrlich and Lester Brown have been predicting disaster from population growth for decades. No set of predictions has been more forcefully falsified. Even Alex Marshall of the Population Fund had to concede that "No one in history thought it would be possible to reach this number with an intact planet; they predicted ecological collapse, famine, and nuclear war, but we are doing rather well and that's an achievement." Marshall is apparently unfamiliar with the work of P. T. Bauer, Julian Simon, and others.

Marshall could not resist adding: "But the other side is that so many people are living in desperate poverty and the population is still growing, mostly in the poorest countries to the poorest families." In fact, people in most places are living longer, healthier lives than ever before. The population grows because the death rate falls.

One of the myths too many of us live by is that people cause poverty. This is worse than wrong. Poverty needs no cause or explanation.

It is wealth that must be explained. And by now we should know the cause of that: people!—more precisely, free and enterprising people living in a regime of private property.

Thus it is interference with private property, not population growth, that should be the cause of concern.

* * *

The countdown to the triggering of the infamous "Y2K bug" nears the zero hour. Whatever happens at midnight on the 31st, there is no gainsaying that people have spent a lot of money to make sure that computers and embedded chips read "00" as "2000" and not "1900." Was it the work of dunderheads that necessitated all the expense, effort, and worry? Or is it only hindsight that permits condemnation of the programmers of decades ago? Bill O. Reitz puts himself in their place.

Ebenezer Scrooge is the Christmastime figure people love to despise. The oddly self-centered man who spent no money on himself is often taken as a foil for anticapitalism. But is Dickens's *A Christmas Carol* really a brief against free markets and for the welfare state? Daniel Oliver goes to the text to examine this question.

The term "states' rights" got a bad reputation because it was identified with slavery and later legally enforced segregation. Yet as Gene Healy argues, if one safeguard of liberty is the fragmentation of political power, then "states' rights," however unfortunate the name and some of its past applications, deserves another look from classical liberals.

Fans of activist government admire America's quiet neighbor to the north for its "enlightened" public policy. In the interest of multiculturalism, Monte Solberg provides a tour of Canada's political milieu.

What happens when the free market displaces central economic planning? James Madison strolls through Prague and samples the fruits of international investment.

Government regulation of business is sometimes mocked for its waste and occasional outright silliness. But the regulatory machine chugs on undaunted. Michael Catanzaro shows the myriad ways that regulation is bad for everyone's prosperity.

By now it's an old saw: no one takes care of someone else's property the way he takes care of his own. George Leef found a supersized illustration of this principle: the North Carolina university system.

Economics is everywhere, even in the choice to go to the movies rather than stay home and read a book. Ninos Malek explores some of the economics of everyday life.

Economically, China was once among the most virulent of communist countries. Over the last 20 years some market reform has taken place. But Christopher Lingle shudders to think of that country's next economic phase: old-fashioned Keynesianism.

People sometimes let their language fool them, as when they attribute features of individuals to groups. Mischief can come from such imprecision, as Tibor Machan demonstrates.

In columns this month, Donald Boudreaux dismantles statist slogans; Lawrence Reed reflects on the difference between government and everything else; Doug Bandow scrutinizes the Korean peninsula; Dwight Lee explains protectionism; Mark Skousen probes Robert Heilbroner's biases; and Russell Roberts wonders if people get the politicians they want. Richard Timberlake reads a newspaper article claiming that the Federal Reserve sets interest rates and protests, "It Just Ain't So!"

Our book reviewers chew over works on the philosophy of individualism, the libertarian-conservative divide, foreign interventionism, the diet gendarme, the New Deal, and the relationship between politics and culture.

—SHELDON RICHMAN

Thoughts on Freedom

by Donald J. Boudreaux



Unfettered Powerful Extremes

Over the years, intelligent and well-meaning opponents of private property and free markets have offered thoughtful and articulate arguments in support of government intervention. None of these arguments have withstood close scrutiny, but at least they were offered in the spirit of honest debate. Such arguments, even though deeply flawed, never infuriate me. Not so with a far-more-common mode of criticizing the market, namely, tossing out slogans. Three of these anti-free-market slogans are particularly galling.

Is Capitalism "Unfettered"?

The first is "unfettered capitalism" (or "unfettered free markets"). Opponents of laissez faire love this one because it so obviously describes an economic system that no reasonable person endorses. So, before I go on, let me declare without qualification: I, too, oppose unfettered capitalism.

The trouble with this slogan is that capitalism, by its very nature—by the fact that it is the product of a system of private property rights—is necessarily constrained. Capitalism is internally and inexorably fettered. To the extent that a society is capitalistic, no one in that society can coercively or fraudulently harm others. Everyone is restrained from violating the equal rights of others.

Consider, for example, Michael Dell, founder of Dell Computers. He earned an impressive fortune by producing affordable computers that consumers voluntarily purchase. Like everyone in a capitalist system, Dell was and remains quite constrained by the rules of private property. Had he produced lousy machines, or had he stubbornly priced his machines so high that too few consumers bought them, he would today be in some less-lucrative line of work. Dell is emphatically fettered by the ability of consumers to spend their money as they see fit, along with the ability of other entrepreneurs to compete with him.

Indeed, central to the economic and ethical case for laissez faire is the recognition that it is the *only* system that provides adequate and appropriate fetters. One of the great benefits of private property and voluntary exchange is that, because no one is compelled to engage in any exchange, all exchanges that do take place are believed by all parties to them to be beneficial.

The ability *not* to exchange—what Boston University law professor Randy Barnett calls "freedom *from* contract"—is an enormously effective fetter protecting the weak from the strong.[1] And only under laissez faire is everyone's freedom *from* contract (along with the freedom *to* contract) consistently respected.

Does Capitalism Favor "The Powerful"?

Reflecting on freedom from contract allows us to dismantle another popular slogan, namely, that "markets favor the powerful over the

Donald J. Boudreaux is president of FEE.

weak." Indeed private property rights eliminate the distinction between "powerful" and "weak." In a market economy, some people are wealthier than others, but no one exercises power over others. Although Bill Gates's wealth is about 600,000 times greater than my own, he has no more power over me than I have over him. If he wants my car, he cannot have it unless I agree to sell it to him. He cannot imprison me, shoot me, or enslave me. He cannot tell me what to eat or drink or with whom I may be intimate. He cannot tell me how to educate my son, or how I may earn a living. It's true that if I want to use Microsoft software I must first buy it from him, but so, too, must he buy from me anything that he wants which I own. We are both free not to contract with the other. It would be perverse to assert that Bill Gates has "power" because he is unusually talented at producing products that please consumers.[2]

A person (or an institution) is powerful only insofar as he can use authorized force to compel others to act against their wills. Only the state has such power. This fact is why the further we move toward laissez faire, the smaller is the scope for the truly powerful—those with political authority—to dominate others. At the laissez-faire limit, all power is eliminated.

Is Laissez Faire "Extreme"?

The third galling slogan is that those of us who consistently champion laissez faire are "extremists." "We must strike a balance between the state and the market," the refrain goes. "Laissez-faire proponents such as Milton Friedman, F. A. Hayek, and Ludwig von Mises are extremists."

Wrong.

The fact is, laissez faire *eliminates* extremes and extremists. That's one of its principal virtues. The greater the scope of the market, the less likely there will be extremes and extremists.

Compare the relationship of one market participant to another with that of the state to its subjects. On the market, farmer Jones can get Ms. Smith's money only by offering her something that she values. Each party to the exchange gains; no one is harmed and no one carries away all of the benefit. If farmer Jones seeks to be an extremist—say, if he asks Ms. Smith to pay $1,000 per bushel of his corn—Ms. Smith walks away. Ms. Smith's freedom not to contract with farmer Jones, along with her freedom to contract with other suppliers, ensures that farmer Jones will abandon his extremist position. Likewise, Ms. Smith cannot be an extremist. She might initially offer farmer Jones a mere one cent for each bushel of his corn, but farmer Jones need not accept. If Ms. Smith wants to buy corn from farmer Jones, she'll raise her offer; she'll abandon her extremist position.

Market prices balance the costs and benefits to all parties of producing and consuming. Extremes are avoided.

Suppose, though, that farmer Jones is so greedy that he isn't content to play by the rules of private property. So he successfully lobbies Uncle Sam for a higher, guaranteed minimum price for corn. The state might achieve this price hike by paying farmer Jones and other corn farmers to reduce their production, and by prohibiting upstart corn farmers from entering the market. Now we've got true extremism. Not only does the state stand ready, ultimately, to kill anyone who insists on doing nothing more heinous than selling corn at prices lower than the dictated minimum, but farmer Jones need no longer bargain with Ms. Smith. If Ms. Smith isn't content to pay the state-enforced minimum price, too bad for her. She remains free not to buy the corn (except insofar as her taxes are used to subsidize corn farmers!), but she may not now bargain with other farmers for a lower price. Government intervention favors corn farmers with a disproportionate—we might say "extreme"—advantage.

Beware of slogans. They are verbal camouflage for weak arguments. □

1. For a more elaborate explanation, see Barnett's impressive and important book *The Structure of Liberty* (New York: Oxford University Press, 1998).

2. The popular belief that Microsoft's current large market share is due to monopolistic practices, network effects, or inefficient "lock-in" has been convincingly exploded in the fact-laden book by Stan J. Liebowitz and Stephen E. Margolis, *Winners, Losers, and Microsoft* (Oakland, Calif.: The Independent Institute, 1999).

THE FREEMAN
Ideas On Liberty

The Fed Sets Interest Rates?

It Just Ain't So!

Newspaper headlines across the country on July 1 provided some bad news for consumers: "Fed moves to raise interest rates." Associated Press writer Martin Crutsinger explained:

"The Federal Reserve raised interest rates for the first time in two years . . . nudging borrowing costs higher for millions of American consumers and businesses. . . . At the conclusion of two days of closed-door discussions, Fed policy-makers said they were increasing the target for the federal funds rate, the interest [rate] that banks charge each other on overnight loans, from 4.75 to 5 percent. The Fed said in a statement that it felt the need to be 'especially alert to the emergence, or potential emergence, of inflationary forces that could undermine economic growth.'"

"When the economy is growing at a rate the Fed believes is too fast," Crutsinger advised his readers, "it raises interest rates to slow spending on big-ticket items such as homes, autos and appliances."

How It Works

Every householder and businessman can relate to an interest rate. They see it as contributing to the cost of the monthly mortgage payment and the payment owed the bank for a business loan. So everyone has some idea that the Fed occasionally cranks up its interest-rate machine, which it keeps in a crypt in the basement of the Federal Reserve Bank of New York, to raise or lower rates. But how does that infernal machine work? Who follows the blueprint, manipulates the levers, and chants the rites to implement an interest-rate change? Let's peek into the basement of the bank and see what goes on there.

I do not have Superman's X-ray vision, but I am certain beyond any doubt that neither the Fed Bank of New York nor any other Fed institution has an interest-rate machine. Nevertheless, the popular belief, as emphasized by the newspaper headline "Fed moves to raise interest rates," must have some foundation in fact. So in what sense did the Fed "raise rates"?

What the Federal Reserve does have is a powerful moneymaking machine that operates through the offices of its New York bank. In activating this machine to raise rates, the Fed's decision-making board, the Federal Reserve Open-Market Committee (FOMC), issues a directive to the bank's account manager to sell more or buy fewer government securities in New York's financial market. This time the directive was to buy fewer. Since the Fed is a major player in the government securities market, when it buys fewer securities it causes the price to fall and their interest rate to increase.

Unlike anyone else who buys something in markets, a Federal Reserve purchase is not made with old money but with brand-new money. *The Fed creates the means of payment.* If the seller of the securities wants cash, the Fed uses its authority to print new Federal Reserve notes. If the seller wants a check, the Fed account manager has the authority to issue one that becomes new bank reserves when deposited. Since the Fed creates new currency and bank reserves to purchase government securities, the securities are perforce *monetized.* They are no longer outstanding debt, but by the alchemy of central banking have been converted into money. Likewise, when the FOMC sells securities or buys fewer than it had been buying, as in this case, the quantity of money in the economy is reduced or its rate of increase is slowed.

The action on July 1 called for the account manager to buy fewer securities until the Fed funds rate rose from 4.75 to 5 percent. "Fed

funds" are the loans banks make to each other for a 24-hour period. Some banks need extra reserves, others have excess reserves. The Fed funds market resolves these asymmetries. Since Fed funds are an important segment of the reserves commercial banks need to carry on their lending and investing business, any central bank action that constrains reserves raises that particular interest rate.

Monopoly Power Over Money

The answer to the question posed above, therefore, is: the FOMC can raise this one short-term interest rate—the Fed funds rate—for a few days. Its means for doing so, however, is its monopoly power to increase or decrease the economy's stock of money, not any device that directly alters market interest rates.

Let's see what happened to other interest rates.

The Federal Reserve Bank of St. Louis publishes weekly a newsletter, *U.S. Financial Data*, which furnishes week-by-week accounts of the U.S. economy's monetary and financial data over the most recent 15 months. According to the July 22 issue, the Fed funds rate duly recorded an uptick on July 1 following the FOMC's action. Most other rates, however, did not follow suit. Corporate AAA bond rates hit a low point in January 1999, rose 100 basis points (1 percent) to June 25, and *fell* 20 basis points in the weeks after the Fed "raised rates." Tax-free municipal bonds, which show little interest-rate movement, had risen slightly since October 1998. After the July rate "hike," their rates too showed a slight decline. Rates for 30-day commercial paper, loans made by nonfinancial companies, were flat for the first six months of this year, rose slightly in June until the rate "hike," then showed a downtick. Thirty-year Treasury rates hit a low spot in October 1998 and rose constantly (about 100 basis points) until the rate "hike." After that, they too declined.

The AP report included charts of interest rates on mortgages and Treasury bonds that showed significant increases in rates since the autumn of 1998. So how could the AP claim that the "Fed raised interest rates" on July 1, when most rates had been rising since the previous October and several rates fell after the rate "hike"? Their report was not an example of valid news but of "economically correct" journalism.

Traditional economics properly teaches that many complex market forces—countless investment and savings decisions not dependent on monetary factors—are essential in determining interest rates. The Fed funds rate that Fed policy can influence through its monopoly over the quantity of money is inconsequential in shaping most short-term and long-term rates in capital markets, unless that moneymaking power subsequently promotes a pervasive price inflation.

Federal Reserve policy is responsible for the quantity of money—cash and bank deposits—that all households and business firms have in their possession at any moment. Furthermore, all severe price inflations and contractions (such as the one from 1929 to 1933) result from excesses or deficiencies of central bank money. All of which means that the Fed's current role in "fighting inflation" amounts to nothing more than undoing things it should not have done in the first place.

By controlling the basic stock of money in the U.S. economy, Fed policy determines the general level of prices. And for a fleeting moment through its control over the money stock, the Fed may influence a few short-term interest rates. But the media claim that the "Fed moves to raise [or lower] interest rates"? It just ain't so. □

—RICHARD H. TIMBERLAKE
Contributing Editor

THE FREEMAN
Ideas On Liberty

Why Y2K?

by Bill O. Reitz

We are fast approaching that fateful day, January 1, 2000. Whether the much-debated Y2K problem will come in with a bang or merely a whimper, only time will tell. But it is interesting to ask why we are in this situation today.

In a recent issue of *The Freeman*, Mark Skousen blamed the problem—which stems from storing dates with only two digits for the year—on a "classic . . . shortsighted blunder" based on "stupidity and incompetence."[1] I must take issue with his characterization. Managers, engineers, and even economists live in a world of imperfect information: we all do the best we can, given the information at hand. I believe that anyone who had to make the decision at that time would have invariably come to a similar conclusion. To call this an "error" is one thing; to blame it on shortsightedness, stupidity, and incompetence is quite another.

Certain important factors are missing from many analyses of Y2K, including the time value of money, the expected probability of a particular outcome, and the uncertainty about projections far into the future. These elements played such an important part in the Y2K decision, and its eventual impact, that they must be discussed further.

In the mid-1950s, computing power was far more expensive than it is today. Programmers of the time, and the managers they worked for, would have been accused of the height of arrogance had they claimed that the software they wrote would still be in use nearly half a century later, or that any decision they made would have any effect so far into the future. Most programmers expected that the life of their products would be a few years—ten at most—and that by the 1960s new software would be written to run on newer, better machines. Even the most arrogant among them would probably not have estimated more than a 1 percent chance that anything they did then would matter to anyone in the year 2000. In hindsight we know that it was the decision these programmers made about how to store data, and not the programs themselves, that would create the legacy known as the Y2K bug.

Moore's Law

If there is anything that is truly responsible for the Y2K predicament, it is Moore's Law, or more properly, the engine of human progress that Moore's Law describes. Gordon Moore, chairman emeritus of Intel Corporation, first observed the rapid improvement in computing power in 1965. At the time, he thought that power doubled every 12 months, but with better information he found 18 months to be more accurate.

The programmers of the original software did not have the benefit of Moore's data to draw on. Even if they had, they most likely would have thought there was a limit to how

Bill O. Reitz is a pen name for a west-coast electronics executive.

far computing power could expand—a wall, as it is called. (Moore himself has been recently quoted as saying that there is a wall.[2])

The implication of Moore's Law is that the cost of a megabyte of computer main memory (now a dollar or two) would have been a few billion dollars in the mid-1950s. Actually, the cost was closer to a few million, because the performance (which for memory is measured as access speed, or the number of times per second you can read or write a piece of data) was thousands of times slower. Because of the incredibly high cost of computers and their limited capabilities, even the most optimistic estimates of the time placed the total world market at a few hundred units. In hindsight we now know that this estimate was off by a factor of about a million. If it were not for this progress, the impact of the Y2K problem would be felt only by a few of the world's largest corporations and government agencies, and its cost would have been far less significant.

Even if these people had thought their decisions might have consequences so far into the future, they would have had to discount the expected value of such a future expense by the time value of money—a factor of around 100 at a discount rate of 10 percent. If we say that the total cost of fixing the Y2K bug is $1 trillion, we see that the expected present value to those programmers and managers would have been $100! Even this improbable result would have been weighed against the present and very real cost of including the extra digits in the databases of the time.[3]

Whether anyone actually went through such an analysis we will probably never know. But if they had, the result was a foregone conclusion—based on the best information available at the time. To conclude that this was entrepreneurial error is simply inappropriate.

In the early days of computers, the central processing unit, or the CPU, used vacuum tubes for logic gates, and memory technology consisted of magnetic "drum" and "core." The engineers and programmers who developed the initial software containing the Y2K bug had probably never heard of three researchers working quietly in a laboratory off the beaten path at AT&T Bell Labs. Walter Brittain, William Shockley, and John Bardeen were developing what would become the transistor. After the first transistors were built, the first practical commercial application would require many years of research and development. One of the early adopters of transistors was Sony Corp., at the time a small, little-known, and struggling Japanese radio manufacturer trying to eke out a profit in the difficult years of rebuilding after World War II. While the big U.S. radio manufacturers were not particularly interested in transistors, Sony realized that they might allow miniaturization and portability. This insight certainly must rank with the greatest advances in the field of electronics, for no matter how clever an innovation is, it is worth nothing until someone uses it for something consumers will buy.

After the transistor was in production, computers also used it. Solid-state memory (as opposed to magnetic core memory) was theoretically possible but neither cost-effective nor size-competitive at that time. Advances in transistor manufacturing made the devices smaller, faster, and cheaper. One of the advances was an imaging process, whereby patterns were placed on the surface of a silicon wafer using photosensitive coatings. This made possible the production of thousands of transistors at once; but more important, it led to the next major advance in electronics.

The Integrated Circuit

An integrated circuit (IC) is a silicon wafer containing the patterns of several transistors, along with a connection pattern hooking them together in a circuit to perform a function.The first IC, built in 1958 by Jack Kilby of Texas Instruments, contained just one transistor and four other components. The first production IC, designed by Robert Noyce (later co-founder, with Gordon Moore, of Intel Corp.), contained eight transistors and eight resistors. The first microprocessor, the Intel 4004 in 1971, used 2,300 transistors. Today's Pentium II has 7.5 million.

Moore's Law applies today primarily to the ever-decreasing scale of the patterns of ICs. The first IC used a "geometry," as it is called, of about 100 microns. This means that the size

of the metal connections making up the transistors and wiring on the chip was about 100 microns wide, which is about 0.004 inch or the width of a human hair. While this sounds small enough, today's leading-edge microprocessors (CPUs) and memory ICs use geometry of 0.25 micron. This is 400 times smaller, but because ICs are basically two-dimensional, you can get 400 squared or 160,000 times as many transistors on the same piece of silicon as you could at 100 microns. The next generation of ICs will have 0.18 micron geometry, nearly doubling capacity yet again.

However, Moore's Law also applied to the cost of computing in the pre-IC days. Just as a wall was hit with one technology (say, vacuum tubes), another came along (the transistor or the IC) to make possible the continuing reduction in cost that has so greatly benefited mankind. Moore's statement that there is a wall in our future is conditioned on limits inherent in the continual reduction in scale of current IC processes. But who is to say that there will not be another technology to come along at that point—or earlier? One obvious possibility is to develop some sort of three-dimensional process for IC manufacture; people are working on this idea today.

Lost Opportunities

You will recall that the true cause of the Y2K bug was not actually the programs developed by the original team of programmers, but rather their decision to store the year with two, not four, characters. Recall also that there have been times when new software has been put into production over the last half century to take advantage of improvements in hardware capability and of software design.

While it is difficult to modify an existing program to use four-digit years, it is relatively simple to design a program that way from the start. New programs, however, had to be compatible with existing databases, which contained thousands or even millions of records representing vast value. It would not only be prohibitively expensive to re-enter these databases, but numerous errors would occur, which would have to be found and fixed, all adding to cost and causing disruption.

However, one issue that is often overlooked in this discussion is that it is relatively simple to write a program for an existing (two-digit) database and append a leading "19" to every date field, thereby converting it to a four-digit database. While these databases may be huge, they are very structured: every record has exactly the same format. The dates are always in the same place, and adding a couple of characters to each record would be relatively easy.

So why didn't this happen? As the '70s, '80s, and then '90s came upon us, the problem was understood by many. The old justification for two-digit years (cost of memory) was no longer valid. Why, other than the natural human tendency to procrastinate, was this simple change not made? Perhaps it was because multiple programs used the same databases and they couldn't all be updated at once. I don't know the answer to this question, but if the Y2K problem turns out to have consequences as dire as some predict, it will be a question that many will wonder about.

If there is any blame to be placed in all of this, surely it does not rest on the shoulders of those who, nearly half a century ago, used their best engineering and management judgment to make what seemed then to be a simple decision. It lies, instead, with the inevitable shortcomings of making decisions based on imperfect information. Let us hope that our descendants will be more generous with us when they examine the effects of our work in the year 2050. □

1. Mark Skousen, "Y2K and Entrepreneurial Error," *The Freeman*, March 1999.

2. Gordon Moore, Intel Developer Forum, September 30, 1997, as quoted by Michael Kanellos, CNETNews.com.

3. The calculation goes like this: $1,000,000,000,000 divided by one million multiplied by 1 percent and divided by 100 equals $100. One million is for the greater number of computers now in use than were expected; 1 percent for the likelihood that the programmers' decisions would affect us today, and 100 for the time value of money at 10 percent.

THE FREEMAN
Ideas On Liberty

Reclassifying a Classic

by Daniel T. Oliver

For a century and a half, *A Christmas Carol* by Charles Dickens (1812–1870) has been read and reread, told and retold, performed and reperformed. Written in 1843, it is the best-known and best-loved Dickens tale. We all know the story. Or do we?

Many people, both fans and critics of Dickens, believe *A Christmas Carol* disparages free enterprise through its portrayal of Ebenezer Scrooge—the "squeezing, wrenching, grasping, scraping, clutching, covetous" miser. Many also think the story, through its depiction of nineteenth-century poverty, was meant to persuade readers to support a welfare state. Yet both these assumptions are mistaken, as a careful reading of the story shows.

Scrooge's character defect is not so much greed as miserliness. He hoards his money *even at the expense of personal comfort.* While many remember the single lump of coal that burns in the cold office of his assistant Bob Cratchit, the fire in Scrooge's own office is described as "very small." Scrooge lives in three sparsely furnished, dingy rooms and has no live-in servants, though he could easily afford them. At one point, Scrooge's nephew Fred remarks that his "wealth is of no use to him. He doesn't do any good with it. He doesn't make himself comfortable with it. He hasn't the satisfaction of thinking—ha, ha, ha!—that he is ever going to benefit us with it."

Dickens gives us no reason to believe that Scrooge has ever been dishonest in his business dealings. He is thrifty, disciplined, and hard-working. What Dickens makes clear is that these virtues are not enough. This becomes apparent when the ghost of Jacob Marley, Scrooge's former business partner, visits him on Christmas Eve. Marley's ghost must forever roam the earth, agonizing over acts of goodwill and kindness that the living Marley left undone: "My spirit never walked beyond our counting house—mark me! in life my spirit never roved beyond the narrow limits of our money-changing hole." Elsewhere the ghost laments, "Why did I walk through crowds of fellow-beings with my eyes turned down, and never raise them to that blessed Star which led the Wise Men to a poor abode. Were there no poor homes to which its light would have conducted *me*?"

That Dickens believes money-making, generosity, and a spirit of goodwill are compatible is evident in the character of Mr. Fezziwig, Scrooge's former employer. Transported back in time by the Ghost of Christmas Past, Scrooge watches the jovial businessman throw a lavish Christmas Eve ball for his employees, relatives, neighbors, and servants. Likewise, during Scrooge's walk home on Christmas Eve, Dickens describes profit-seeking merchants caught up in the spirit of Christmas: "Poulterers and grocers' trades

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became a splendid joke; a glorious pageant, with which it was next to impossible to believe that such dull principles as bargain and sale had anything to do." Elsewhere, he remarks that "the grocer and his [employees] were so frank and fresh that the polished hearts with which they fastened their aprons behind might have been their own, worn outside for general inspection." Dickens even takes evident enjoyment in describing the cornucopia of items that shop owners have placed in their windows to delight passers-by—what some today would deride as the crass commercialism of Christmas: "great, round, pot-bellied baskets of chestnuts," "pears and apples, clustered high in blooming pyramids," "French plums blushed in modest tartness from their highly decorated boxes."

Nowhere in the story does Dickens endorse welfare. Rather, he suggests that charity and hard work in the business world are how best to combat poverty. Early in the story, two gentlemen visit Scrooge's office and ask him to contribute to a fund to buy food and clothing for the poor. Scrooge inquires whether "the Union workhouses" are still in operation. These composed the welfare system of the day, consisting of bleak facilities where the sick, aged, and poor sometimes went to break rocks or fashion rope in exchange for food and shelter. One gentleman replies, "I wish I could say they were not," adding that "many would rather die" than go there, since they cannot "furnish Christian cheer of mind or body." The two gentlemen clearly disparage these government institutions while trying to convince Scrooge, to no avail, that private charity is preferable.

Similarly, there is no suggestion that welfare would help the struggling Cratchit family—although more employment might. When Scrooge and the Ghost of Christmas Present visit the Cratchit household on Christmas Eve, Bob Cratchit mentions a possible business position for his eldest son, Peter, that would supplement the family's income. Again, when Scrooge and the Ghost of Christmas Yet to Come visit the Cratchit family, Cratchit excitedly relates that Scrooge's nephew Fred may help get Peter "a better situation" in business, to which Mrs. Cratchit and one of her daughters excitedly respond.

We all know how the story ends. Scrooge's life is spared, and he resolves to be kind and generous. During a walk on Christmas morning, he encounters the two gentlemen who visited the day before and promises to give a sizable sum to charity. He also encounters beggars. Interestingly, Dickens gives no indication that Scrooge gives to them. Rather, he "questioned" them, perhaps to find out what had brought them to their current state—misfortune or irresponsible conduct—so that appropriate support, whether material or moral, could be given.

After Scrooge's change of heart, he remains a businessman. He is "early at the office" the day after Christmas, where he tells a surprised Bob Cratchit, "I am about to raise your salary!" (Dickens errs here by implying that wages are determined by the renitency of employers' hearts.) He does not become a rabble-rouser for welfare programs. Instead, he takes personal responsibility for assisting the Cratchit family, becomes "a second father" to Tiny Tim, and practices other acts of kindness that Dickens must have hoped his readers would emulate.

In our own age, when the respective roles of business, charity, and welfare are being questioned and debated anew, *A Christmas Carol* offers quite a bit of wisdom. □



Government Education Reinvents Government

Perhaps the most important principle one can ever learn about the nature of government is this: It is different from all other institutions in society because it is the only one that can legally employ force. Unfortunately, it is a principle that has been largely erased from the American memory bank. More than a hundred years of compulsory public education may be largely to blame.

Let's get something straight before we go any further. To note that government rests on the use of force is not some radical anarchist idea. It is the very definition of the institution and its ultimate distinguishing feature. For much of the last half millennium, political scientists of virtually every stripe accepted the notion as fact. No respectable scholar tried to paper it over and pass government off as some kind of voluntary, benevolent society.

America's founders understood this principle well and crafted a regime that never purported to *eliminate* force; they only sought to restrict it to a narrow sphere of life and thereby preserve a large measure of individual liberty. Perhaps George Washington said it best when he purportedly observed, "Government is not reason. It is not eloquence—it is force! Like fire it is a dangerous servant and a fearful master." In other words, even when government does no more than what Washington wanted it to do, and when it does those few things very well as a "servant" of the people, it's still *dangerous* because behind it all is the employment of legalized force.

The Yellow Light

A deeply rooted understanding of this inherent character of government is a pillar of the free society. It's the yellow caution light that prompts wise and peaceful citizens to deliberate long and hard before accepting an expansion of government duties. It creates a healthy skepticism about seductive schemes to supplant private initiative with public action. It discourages attempts to impose a collective conformity at the expense of the individual.

If you are an advocate of the free society today, you surely have noticed an erosion in the understanding of this principle. It may not be an exaggeration to assert that the erosion has been massive and far more deleterious to our liberty and well-being than all but a few ever imagined.

This point struck me hard recently when I read a letter to the editor of a local newspaper. The letter writer was responding to a previously published commentary by a man who had argued that Ernest Hemingway opposed government funding of the arts because he felt that artists should be independent of political influence. She took issue with the commentator on the grounds that Hemingway "did accept money from benefactors." Accepting money freely given by patrons, in the mind of the letter writer, was indistin-

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guishable from accepting money from the government.

Similarly, I have witnessed countless occasions when individuals argued that if government does something and is well intentioned, it couldn't possibly be coercive; or, that if it's "democratic," it's somehow voluntary. The mere fact that politicians are elected validates almost whatever they do as nothing more than consensual acts between altruistic adults. A much more sober and rational view of the limitations of a democratic republic, preferable though it is to any other form of government, is the one that describes it as two wolves and a lamb voting on what to have for lunch.

So it is that we've arrived at the point described by Edgar Freidenberg's 1964 classic, *Coming of Age in America*, where "American high school students viewed the government as a benign institution that one should obey because it was working for the benefit of all the people."[1] How is it possible for such a sad state of intellectual affairs to befall a nation founded on liberty and a rational view of the state? How did it come to be that millions of Americans recoil at the "radical" suggestion that government and legalized force are one and the same?

I can think of no other source of the problem than a century of government ("public") education. When nearly 90 percent of Americans are schooled for 12 formative years by government employees, most of whom earned their teaching degrees at government universities, why should we expect anything other than an obsequious citizenry that views government as the benevolent vicar of what Rousseau called "the general will"?

The history of American public education is replete with statements by professional government school advocates that reek of statism. Judge Archibald Douglas Murphey, founder of the public school system in North Carolina, said that government must educate because "parents know not how to instruct them. . . . The state, in the warmth of her affection and solicitude for their welfare must take charge of those children and place them in school where their minds can be enlightened."[2]

A 1914 bulletin of the U. S. Bureau of Education stated, "The public schools exist primarily for the benefit of the State rather than for the benefit of the individual." And Edward Ross, a prominent sociologist, offered the most chilling description of the role of government in education: "To collect little plastic lumps of human dough from private households and shape them on the social kneading-board."[3]

This outcome was predictable from the earliest days of American public education, and it's no different from anything else the government comes to dominate. He who pays the piper calls the tune. It just isn't in the interests of the government or those who depend on it to sully their own nests with an honest admission that their handiwork is financed and imposed at gunpoint. As education scholar Joel Spring put it 20 years ago, "A teacher, school administrator, or elected official in charge of schools may believe that his personal values represent the general values of the community; worse, he may think that his values should be adopted by the community."[4]

Such explicit statements notwithstanding, it would be hard and perhaps politically counterproductive to argue that today's deficient government school system derives from some grand conspiracy. To explain the appalling ignorance of the American citizenry regarding the essential nature of government, conspiracy theories are not necessary. It's sufficient simply to observe that few employees of the system will rise above immediate self-interest to even recognize, let alone propagate, the notion that government in general and their jobs in particular rest on legalized force.

What difference does all this make? A lot. I can think of no situation more hostile to liberty than a failure of a free people to tell the difference between government and everything else. □

1. Cited in William F. Rickenbacker, ed., *The Twelve-Year Sentence* (San Francisco: Fox & Wilkes, 1999 [1974]), p. 140.

2. Quoted in Murray Rothbard, "Historical Origins," in ibid., p. 11.

3. Quoted in Joel Spring, *The American School, 1642–1985* (New York: Longman, 1986), p. 155.

4. Quoted in Joel Spring, *Educating the Worker-Citizen* (New York: Longman, 1980), p. 14.

THE FREEMAN
Ideas On Liberty

States' Rights Revisited

by Gene Healy

Lamenting the Supreme Court's recent batch of pro-federalism decisions, the *New York Times* termed the Court's newfound affinity for states' rights "Supreme mischief," "deeply disturbing" to right-thinkers everywhere. One expects such talk from dedicated cheerleaders for centralized power. What's more disturbing, however, is the extent to which the *Times*'s perspective has gained credence among advocates of limited government. Modern libertarians, rightly concerned with what the Institute for Justice's Clint Bolick has termed "grassroots tyranny," ridicule and disparage the time-honored doctrine of states' rights.

It's understandable that the under-informed general public associates states' rights with slavery, Jim Crow, Bull Connor's police dogs, and "segregation forever." But classical liberals ought to take a longer view. "States' rights" merely stands for the propositions that (1) the Constitution should be interpreted strictly with regard to the narrow set of enumerated powers granted the federal government; and (2) that the states can nullify or obstruct federal actions that violate the Constitution. As such, the doctrine has a long and honorable pedigree among advocates of limited government. States' rights, in the view of classical liberals like Lord Acton, was no mere excuse for states to violate the rights of their citizens. Rather, the independence of the states in the period before the Civil War served as an effective check on federal aggrandizement. As Acton put it, "Centralization finds a natural barrier in the several State governments."

Modern libertarians tend to have a different perspective, believing that strong federal oversight is indispensable to securing liberty. For example, John McLaughry, head of the libertarian Ethan Allen Institute, says the doctrine of states' rights is little more than "a hoary legacy from the days of human slavery." This view rests on a tendentious version of history, one quite at odds with Lord Acton's, to the effect that in the nineteenth century, state governments were a more serious danger to individual freedom than the federal government. (That perspective is perhaps best encapsulated in Bolick's *Grassroots Tyranny* [1993]. See also the Civil War history offered in "Reviving the Privileges or Immunities Clause" by Kimberly C. Shankman and Roger Pilon; Cato Policy Analysis No. 326, at www.cato.org.)

The true story is more complicated, and, from a libertarian perspective, far more favorable to the states than the federal government. During the nineteenth century, the people, through the agency of their respective states, repeatedly and effectively resisted federal tyranny. A brief historical survey will make that clear. It will also, I hope, suggest some reasons why modern libertarians should rethink their hostility to states' rights.

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The "Reign of Witches" and the Kentucky and Virginia Resolutions

The nation was still in its infancy, and the Bill of Rights not a decade old, when the Federalist party flagrantly violated the First Amendment with the Sedition Act. The Act criminalized uttering or publishing anything of a "false, scandalous, and malicious nature" with the intent to bring the government or its officers "into contempt and disrepute." Anyone found guilty could be fined up to $2,000 and imprisoned for two years. The Federalists promptly put it to use in a crackdown aimed at their political enemies.

One Luther Baldwin was convicted of violating the act for little more than the rough expression of admirable libertarian sentiment. Stumbling into a Newark, New Jersey, saloon, during a parade for President John Adams, Baldwin asked what all the ruckus was. A cannon salute for President Adams, he was told. Baldwin exclaimed that it was all the same to him if the cannon was shot up Adams's rear end. Other convictions were less amusing. David Brown of Dedham, Massachusetts, was sent to jail for 18 months for refusing Supreme Court Justice Samuel Chase's order to name associates who shared Brown's Jeffersonian views. Congressman Matthew Lyon of Vermont, an Irish-born republican radical, was imprisoned for criticizing President Adams's alleged "continual grasp for power." While in jail, Lyons was overwhelmingly re-elected to his seat.

Vice President Thomas Jefferson saw the Federalists' tyrannical rule as a "reign of witches." He and James Madison determined to oppose the Alien and Sedition Acts through the agency of the state governments of Virginia and Kentucky. As historians Stanley Elkins and Eric McKitrick put it in their book *The Age of Federalism*, "the protest was taken up in a formal way by no less a power than the constituted legislatures of two states against an act of the national government." Acting in secret, Jefferson drafted the Kentucky Resolutions, Madison, the Virginia ones. Each articulated the "compact" theory of the Union: that the states are equal partners in the federal union, each with the power to interpret the Constitution and thwart federal abuses thereof.

The Virginia Resolutions warned that "a spirit has in sundry instances, been manifested by the Federal Government . . . to consolidate the States by degrees, into one sovereignty, the obvious tendency and inevitable consequence of which would be, to transform the present republican system of the United States, into an absolute, or at best a mixed monarchy." The states, declared the Resolutions, "have the right and are in duty bound to interpose for arresting the progress of the evil." Jefferson's Kentucky Resolutions urged the other states to join Kentucky "in declaring [the Alien and Sedition] acts void and of no force."

With Jefferson's accession to the presidency, the "reign of witches" passed, as Jefferson ended prosecutions under the Acts. But the compact theory of the Union lived on, to be invoked again in the service of individual rights.

Nullifying the Tariff of Abominations

During the nullification "crisis" of 1828–33, the power of the states was again employed to counter federal abuses. In *For Good and Evil: The Impact of Taxes on the Course of History*, Charles Adams describes the disproportionate burden that the federal tariff imposed on the Southern states: "The South exported about three quarters of its goods and in turn used the money to buy European goods, which carried the high import tax." Most of the revenue was spent on internal improvements and other federal projects in the North.

Understandably, the South chafed at the burdens imposed by the tax system. Some of her most prominent political leaders argued that the Constitution granted no power to tax for the purpose of protecting industry, as opposed to raising revenue. With the tariff of 1828, the "Tariff of Abominations," the battle was joined. The South Carolina legislature denounced the tariff, which brought duties to

their highest pre-Civil War level, as "unconstitutional, oppressive, and unjust."

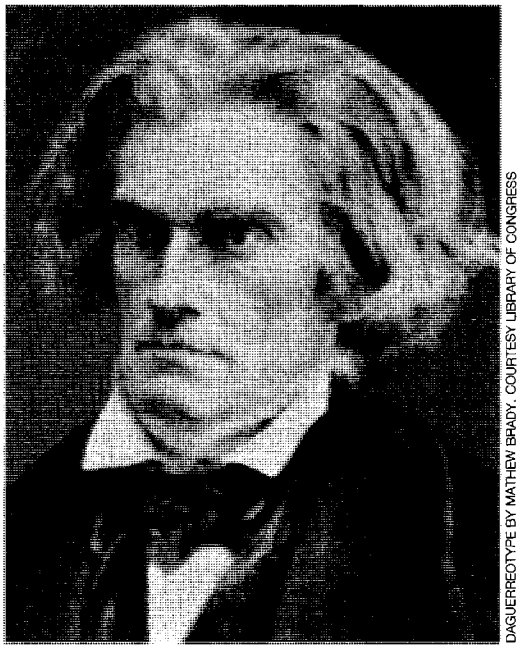
Playing Jefferson's role of 30 years before, Vice President John C. Calhoun secretly wrote South Carolina's Exposition and Protest, in which he outlined the doctrine of nullification. According to Calhoun, state conventions, the same bodies that had ratified the Constitution, could nullify federal legislation that they considered to be in violation of that document. The federal government thereupon could only enforce the law if it secured a new constitutional amendment through the approval of three-fourths of the states.

Calhoun intended the doctrine as a moderate middle position short of the extreme remedy of secession. But soon, a military clash seemed imminent, as President Andrew Jackson denounced nullification and privately swore to hang Calhoun. In the end, though, South Carolina's defiance forced a partial climb-down by the feds. Senator Henry Clay of Kentucky helped usher through a bill securing a 20 percent reduction in the tariff.

Disputes over the unjust federal revenue system would play a central role in bringing about the Civil War (contrary to most contemporary accounts, which emphasize slavery to the exclusion of almost everything else). The centrality of the tariff issue is revealed in Lincoln's First Inaugural, in which he disclaimed any intention to interfere with slavery, but was adamant about collecting federal revenue via the tariff. Republican corporate statism and Northern manufacturing depended on the Union and a high tariff. As a troubled editorialist in the March 18, 1861, *Boston Transcript* put it: "The difference is so great between the tariff of the Union and that of the Confederated States, that the entire Northwest must find it to their advantage to purchase their imported goods at New Orleans rather than at New York. . . . [The government] would be false to all its obligations, if this state of things were not provided against."

Personal Liberty Laws

Ironically, the controversy over fugitive slaves would find Southerners clamoring for a



DAGUERREOTYPE BY MATHEW BRADY. COURTESY LIBRARY OF CONGRESS

John C. Calhoun (1782–1850)

strong federal role and cursing the doctrine of nullification. In his *Battle Cry of Freedom: The Civil War Era*, historian James M. McPherson notes a tension in Southern appeals to states' rights before 1860: "On all issues but one, antebellum southerners stood for state's rights and a weak federal government. The exception was the fugitive slave law of 1850, which gave the national government more power than any other law yet passed by Congress." The South's deviation from principle on this point stemmed in part from economic motives: the federal government's assistance in recovering escaped slaves made the peculiar institution more secure. But those Northerners who opposed slavery fought back with a states'-rights-based resistance to the tyrannical and unjust fugitive slave laws.

The federal Fugitive Slave Law of 1793 authorized slave owners and their agents to cross state lines and recapture fugitive slaves by force, bringing them before local magistrates to prove ownership. Under the law, the deck was stacked against the purported fugitive, who lacked the protection of habeas corpus and jury trial, and had no right to testify in his own behalf. Small wonder, then, that Southern bounty hunters were less than

meticulous in ensuring they'd captured the right person.

Most of the Northern states responded with "personal liberty laws," providing the fugitive with the procedural protections denied him by the federal statute, and in several cases subjecting slave hunters to kidnapping charges. In Vermont, for example, all fugitives were declared free, and anyone who attempted to capture one could be subject to 20 years imprisonment or a fine of $10,000.

Not even the Supreme Court could deter the North from the path of resistance. When the Court overturned a kidnapping conviction under Pennsylvania's personal liberty statute, and voided the statute itself, Pennsylvania merely enacted another. Massachusetts was equally open in its defiance of federal authority. Its legislature passed a law providing that: "No judge of any court of record in this Commonwealth . . . shall take cognizance or grant a certificate in cases that may arise under the third section" of the Fugitive Slave Law of 1793. (Northern defiance of Supreme Court decisions on the slave issue would continue when the Court issued its infamous 1857 opinion in *Dred Scott*. The Maine legislature, for example, was one of several Northern states to declare that *Dred Scott* was "not binding, in law or in conscience, upon the government or citizens of the United States." (Shades of George Wallace!)

To appease an increasingly indignant South, Congress in 1850 passed an even harsher fugitive slave statute. Under that law, proceedings were to be held before (newly created) federal "commissioners," who would only receive half as much for setting the captive free as they would for ruling in favor of his purported owner. All expenses associated with seizing and transporting the captive would be paid by the federal government.

Northern states found the fugitive slave law of 1850 harder to nullify, since it cut state courts out of the process. Still, abolitionists and their "vigilance committees" mounted vigorous resistance to the bounty hunters by force of arms. In 1851, the federal government felt it necessary to make a show of force in response to that resistance. To assist in the recapture of Thomas Sims, a 17-year-old escaped slave working in Boston as a waiter, the feds provided sufficient firepower to ensure that no band of abolitionist vigilantes could free him. When the federal commissioner ruled for Sims's owner, 300 armed federal deputies and soldiers led Sims and his captor from the courthouse to the navy yard, where 250 more federal troops waited to put them on a ship heading South.

Every year, in high school history classes throughout the country, Americans learn a story intended to illustrate the beneficence of the federal government: in 1957, Arkansas governor Orval Faubus vowed to prevent the integration of Little Rock's Central High School; President Eisenhower sent in federal troops to protect black schoolchildren from white Southern mobs. Students might get a more balanced picture of the federal role in race relations if teachers juxtaposed the story of Little Rock's Central High with the story of Thomas Sims.

Libertarian Centralism

The above examples should not be taken to indicate that the states are natural defenders of liberty, organic extensions of the "People" that can be trusted to protect individual rights. Anyone familiar with zoning laws should know better than to embrace such a romantic notion. Instead, this historical survey suggests that the feds are unlikely to be better guardians of individual liberty than the states, and that divided sovereignty can serve as a check against federal oppression.

These examples also undermine the standard account of antebellum federalism, which amounts to public-school history: statist parables designed to make us feel grateful for the presence of our Federal Protector. If the issue were merely historical accuracy, there would be little reason to quibble. But this history is invoked, even by prominent libertarian legal analysts, to justify a particular political program. These scholars, who might be called "libertarian centralists," view the federal government as an indispensable partner in the struggle to protect individual rights. To that end, the libertarian centralists have advanced a number of policy proposals that should give

classical liberals pause—among them: Congress should be free to comprehensively redesign state and municipal codes using the enforcement powers of the Fourteenth Amendment; using the same powers, Congress can legislate directly on matters affecting liberty, with statutes such as the Church Arson Protection Act; and the Supreme Court should depart from constitutional text and engage in moral theorizing when exercising the power of judicial review. Each of these proposals represents a rather dramatic increase in federal authority over the states. The idea that such increased authority will be used to protect liberty rather than to abuse it, represents, like a second marriage, the triumph of hope over experience.

For example, Bolick, in June 7, 1995, testimony before the House Small Business Committee's subcommittee on regulation and paperwork, said that "Congress has the power to enforce the 14th Amendment through appropriate legislation. It should use this power to enact an Economic Liberty Act. The provisions are simple: any federal or state law that restrains entry into a business or occupation must be narrowly tailored to a legitimate public health, safety, or public welfare objective." This appears unobjectionable until one contemplates what that plenary power would mean in the hands of welfare statists.

Another example comes from Roger Pilon, director of the Cato Institute's Center for Constitutional Studies. In a June 18, 1996, *Washington Post* op-ed, Pilon wrote, regarding the federal Church Arson Prevention Act, "There is, however, a proper basis for Congress to act in the case at hand. It is the 14th Amendment. . . . [I]f state measures prove inadequate and there is evidence available to Congress that federal intervention is necessary, there is ample authority under the 14th Amendment for Congress to act."

And in a 1988 *Cornell Law Review* article titled "Reconceiving the Ninth Amendment," Boston University law professor Randy Barnett wrote that "Given that the Fourteenth Amendment extends the protection of constitutional rights to acts of state governments, the Ninth Amendment stands ready to respond to a crabbed construction that limits the scope of this protection to the enumerated rights." Again, although it sounds benign, this view is unjustifiably confident that the federal government won't use the power to enforce unenumerated "positive welfare rights" on the states.

Patrick Henry, arguing against ratification of the Constitution, admonished Virginians to "Guard with jealous attention the public liberty. Suspect every one who approaches that jewel. Unfortunately, nothing will preserve it, but downright force: Whenever you give up that force, you are inevitably ruined." The states did not voluntarily "give up" that force in 1861–65; it was wrested from them by federal aggression. Before the Civil War, individuals were protected from centralized coercion by multiple, divided sovereignties, competing in their interpretations of the national charter, and backing their respective interpretations with force. After that war, individuals were confronted with a powerful unitary state, one that justified its aggression—domestic and foreign—with appeals to "liberty."

Libertarian centralists assure us that we can restore true liberty by gaining influence over that state and making its institutions work for us. The history of American federalism suggests a different solution. If there is a libertarian future, it lies in dividing sovereignty—in nullification and secession: opposing Power with Liberty at every turn; hammering every fault line in an attempt to crack the edifice; dividing and diminishing Power, in the hope that individuals will be better able to overcome it or, failing that, escape it. Any other route is a diversion, and a potentially dangerous one at that. □

THE FREEMAN
Ideas On Liberty

Welcome to Canada

by Monte Solberg

People who are newcomers or visitors to Canada sometimes have trouble understanding how our government works so I have prepared the following short primer.

Taxes are the money forcibly taken from almost every man, woman, and child in Canada by the people in government. These taxes consume about half the average taxpayer's income. The people in government keep a large portion of these taxes for themselves.

Some of the remainder is partially given back to the taxpayer as a kind of allowance. In many ways it's just like the allowance you used to get from your mother when you were a child. The biggest difference is that this mother pays your allowance from the money she has stolen from your piggy bank. As a matter of fact, she also takes her pin money from your piggy bank. Don't ever let your piggy bank run short or mother government will become very angry and abusive. I hope your real mother isn't like mother government.

Some of your tax money is given to other people. When it is given to other people the government often calls it an investment. The recipients of these investments are often millionaires. They become millionaires by being connected to people in government and receiving investments from the government. Sometimes your taxes are given to people who have squandered their opportunities. In Canada this is called social justice.

Monte Solberg is a member of the Canadian Parliament and chief finance critic for the Reform Party.

Canadians are happy to pay taxes because this is how we get free health care. It's good that it's free because sometimes sick people are forced to stay in hospital closets or to wait months for treatment. We wouldn't tolerate this if we actually had to pay for our health care, but because it is free Canadians don't mind, and at least it's not American-style health care. In America no one can afford health insurance, and everyone dies on the street.

Government takes the remainder of the money and gives it to other people who are poor. The poor are people who make less money than the people who aren't poor. However, now that government takes half of people's incomes almost everyone is poor. We do it this way because Canadians are more compassionate than Americans are. Being equally poor helps us eliminate our social deficit.

Canadians go along with this system because bureaucrats and politicians are more responsible with the taxpayers' money than the taxpayers are themselves. If taxpayers were allowed to keep more of their money it would only be wasted on food, shelter, and clothing. Bureaucrats and politicians can be trusted because they are altruistic whereas taxpayers are selfish.

Bureaucrats sometimes invest the taxpayers' money in culture to give us a sense of who we are as a country. Canadians pride ourselves on being tolerant, whereas Americans are intolerant. Sometimes we give hundreds

of millions of dollars away to special-interest groups. These are called partnerships and they enrich the Canadian mosaic.

Imagine how terrible it would be to live in Canada if it weren't for a government that suckles, guides, and watches over us for our entire lives, no matter where we go or what we do, just like a gigantic, doting, dependent, mildly abusive mother (sure, mom has her faults—but who doesn't?).

I trust this short primer will help visitors to my wonderful country understand the progressive nature of our government. Perhaps some visitors can take home valuable lessons on how to treat one another with real compassion. Hello, America, are you listening? □

Classic Satires

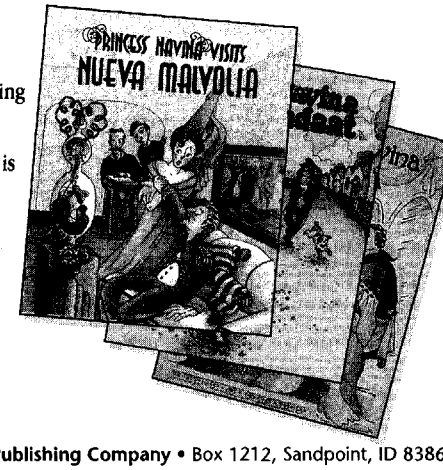
Every age has its witty fable exposing the reigning fallacies, from Jonathan Swift's *Gulliver's Travels* to George Orwell's *Animal Farm.*

In 1990, ***Princess Navina Visits Malvolia*** joined this list. With its captivating diagnosis of modern political woes, it describes a strange land where politicians are duty-bound to cause harm. Hence, they devise policies to provoke social unrest, encourage idleness, and frustrate entrepreneurs.

Since that first volume, political scientist Jim Payne (who writes these tales under the pseudonym Count Nef) has produced two sequels:

– ***Princess Navina Visits Mandaat*** tells of a country where government tries to fix every problem – yet somehow nothing seems to work.

– ***Princess Navina Visits Nueva Malvolia*** (just published) is about a country where politicians are duty-bound to harm people and stay popular in order to win elections. So they follow the "strategy of good intentions," presenting their vexing schemes as compassionate programs to ensure fairness, guarantee jobs, and protect children.



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THE FREEMAN
Ideas On Liberty

Freedom and Foreign Investment

by James Madison

This year, as the Czech people celebrate the tenth anniversary of the end of communism, the capital city of Prague serves as a shining example of what happens when the free market displaces economic planning.

Each morning on the Charles Bridge in the center of the city, more than a dozen vendors wheel out their carts and set up their tiny mobile shops under the 30 statues of saints that line either side of the historic bridge. Along the narrow cobblestone streets extending in all directions from either end of the bridge there are shops with doors wide open and merchants smiling at passersby. Salespeople stand on busy street corners handing out leaflets announcing all the plays, shows, and attractions that are available throughout the city. Tourists abound, always ready to exchange their currency for any number of these goods and services.

Freedom has not only sparked the creativity and ingenuity of the local entrepreneurs, inspiring them to grab their own little corner of the market, but it has brought investments from large foreign corporations as well. Among the more noticeable of these is McDonald's. Prague is home to several McDonald's restaurants including one in Wenceslas Square. The square was the site of the Velvet Revolution that started on November 17, 1989, and led to the resignation of the communist government on December 3. The revolution was dubbed "Velvet" because of its "soft" nature—no one was killed.

The McDonald's Argument

The presence of McDonald's excited me because I have for years used the global proliferation of McDonald's as my premier tool for debating socialists, statists, and others with a general fear of capitalism. I have always known my McDonald's argument was sound, but my visit to Prague provided the opportunity to verify it firsthand.

I start my McDonald's argument by getting my freedom-fearing friends to agree that McDonald's is the perfect example of capitalism run amok. It is, I argue facetiously, a huge American corporation that crowds out the mom-and-pop restaurants by offering low-quality products and paying low wages. Horrible! They quickly agree.

But wait. Mom and pop are doing fine, as are all the dozens of other restaurant owners in Prague. Less than 200 yards from the Wenceslas McDonald's is a hot-dog stand that sold me the greasiest and best-tasting kielbasa dog I have ever had. Less than 50 yards away is another stand where I bought a chocolate-covered cherry ice-cream bar that puts the McDonald's sundae to shame.

Throughout the city, food of every form and fashion can be found. From my favorite greasy hot-dog stand in Wenceslas Square, to my love Linda's favorite restaurant—a French place named U Malířů where the cheapest

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bottle of champagne was nearly $100—it is quite clear that McDonald's is not about to monopolize the food market.

As for quality, the concern of my statist friends falls into two categories: taste and health. Taste is clearly a matter of personal choice. The people standing in line for their Big Macs each time we walked by certainly didn't seem to think that they were being taken advantage of.

As for health, McDonald's doesn't seem much worse than the other options. Judging by the pork with cream gravy and dumplings I've had at U Kamenného mostu on the east bank of the Vltava river, the cheesecake and espresso I had at the newly renovated Kavárna Obecní dům, and the occasional kielbasa dog I had when we were on the run, a Big Mac and fries are hardly worse than the fare offered by the small-scale, domestic entrepreneurs.

Low Wages?

If McDonald's is not flooding the market and the food is not all that bad, then surely there is no excuse for low wages. But what would the employees of McDonald's do if the Czech government outlawed the chain in an attempt to save the employees from their supposedly wretched lot?

Perhaps the displaced employees could open stands on the Charles Bridge. While selling crafts on such a beautiful and historic bridge certainly seems better than making hamburgers on an assembly line, it requires a level of artistic skill that the majority of citizens do not possess. Perhaps they could open one of those cute little shops on the winding cobblestone streets. Being a small business owner is surely desirable, but running a successful business can be difficult and, again, most people do not have the skill to undertake such a venture.

Although it would be wonderful if we could produce an abundant supply of high-paying jobs by simply outlawing all jobs deemed inadequate, the economic reality is that for these workers at this point in their lives, this is their best opportunity.

So if the competition is not destroyed, customers are not deceived, and employees are not worse off, where is the evil? At this point, my friends are mute. Their silence now provides the opportunity to turn the discussion in the opposite direction and show that, rather than causing harm, McDonald's (or any large corporation with high division of labor) actually provides a tremendous benefit to competitors, customers, and employees.

Competitors benefit because a McDonald's employee will not stay there forever. After a few years of ordering cheeseburger wrappers and counting money at night, he will learn the basics of inventory and bookkeeping. Seeing his skills, the competition will hire him away; or he will start his own restaurant and compete against his former employer.

Customers benefit not only in the immediate sense of being served today, but even more so because the McDonald's employee who asks, "Would you like fries with that?" several thousand times will in time learn to read and anticipate the reaction of customers; when he lands the job at U Malířů, he will be able to know when to offer the $200 bottle of champagne and when to suggest the $100 bottle.

Employees benefit because they receive increased pay and higher job security by having acquired the skills that are desired by employers and enjoyed by customers. Were it not for the large amount of easily obtained employment offered by large, labor-divided companies, such workers would have a much harder time finding opportunities to develop valuable skills.

Indeed, it would seem that large international corporations are not so horrible after all. They integrate peacefully with the economy of the countries in which they operate and benefit an array of people in a variety of ways. I have always known this, but after visiting Prague, I am more confident in this belief than ever. □

THE FREEMAN
Ideas On Liberty

The Poverty of Regulation

by Michael J. Catanzaro

Ronald Reagan famously asked voters during the 1980 presidential campaign, "Are you better off than you were four years ago?" A similar test can be applied to government regulation: Has it left us safer and healthier than we would have been without it? Just like the voters in 1980, we can answer that question with a clear and emphatic no.

Regulation, or intervention in the marketplace by government, makes us worse off. Regulation routinely imposes harms that even the most intelligent reformer cannot foresee. Interventionists, as Ludwig von Mises argued in *Critique of Interventionism*, are "seriously deluded regarding the extent of the productivity loss caused by government interventions."[1] We need only scan reams of evidence to see why Mises was right.

According to Cato Institute chairman William A. Niskanen, a former member of President Reagan's Council of Economic Advisers, the total cost of federal regulation is on the order of $500 billion a year. And this figure excludes banking regulation and regulation by state and local governments. Niskanen concludes that the total regulatory burden might be as much as a whopping 10 percent of GDP.

Richard Vedder, an economist at the Center for the Study of American Business, finds that federal regulations cause $1.3 trillion in economic output to be lost each year. This is roughly equivalent to the entire economic output of the mid-Atlantic region, which includes Delaware, the District of Columbia, Maryland, New Jersey, New York, and Pennsylvania.[2] It is often wrongly assumed that state and local governments are wiser or more efficient in enforcing regulations. But they are often just as intrusive and destructive as the federal government. The microcosm of state and local bureaucracies can render businesses helpless before a raft of crippling zoning and environmental laws.

Enforced Inefficiency

When faced with federal, state, and local regulations, businesses must respond—to the detriment of workers and consumers. According to Vedder, businesses are forced to use their resources less efficiently. They operate in a less productive, more costly manner. The result is lower wages, higher prices, or both. In any case, the result is a decrease in the standard of living for workers and consumers.

Mises flatly disproved the notion that regulation and other coercive economic measures make us better off. He argued that "intervention necessarily is illogical and unsuitable, as it can never attain what its champions and authors hope to attain."[3] Take the Occupational Safety and Health Administration (OSHA), which Congress established in 1970. OSHA's mandate was to assure for all workers safe and healthful working conditions "by encouraging employers and employ-

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ees in their efforts to reduce the number of occupational safety and health hazards at their places of employment."

Yet, unsurprisingly, OSHA's 30-year record has been marred by failure. According to a regulatory analysis performed by the Cato Institute, while OSHA supporters cite evidence attesting to the agency's effectiveness, "the vast majority of studies has found no statistically significant reduction in the rate of workplace fatalities or injuries due to OSHA."[4] Interventionists are hard-pressed to maintain that OSHA meets even the minimum criterion for any government program: Does it have any desirable effect on the problem it is supposed to solve?

Worse, OSHA's failure has been bad for business. A 1995 study by the Employment Policy Foundation found that 19 percent of the productivity slowdown in the 1970s was directly attributable to regulations imposed by OSHA and that nearly half of the slowdown in long-term productivity can be explained by rising government regulatory activity.[5] OSHA's poor track record even forced Vice President Al Gore to admit that the agency "doesn't work well enough." Yet despite its failures, OSHA continues to intimidate businesses with the heavy hand of regulation. And it continues to make us worse off. As with almost any form of persistent government meddling, regulation stifles the very forces that drive growth and, hence, prosperity. It becomes the ever-visible hand that swiftly punishes the pursuit of profit, and in turn, those of us who indirectly benefit from it. According to economist Hans Sennholz, government regulation is harmful "because it hampers man's productive efforts where, from the consumers' viewpoint, they are most useful and most valuable."[6]

Blithe Assumption

Interventionists proudly champion greater regulation and control over the economy because they blithely assume the market cannot by itself solve seemingly intractable social and economic problems. It is the state, they grandly proclaim, that most productively and efficiently solves what the market most assuredly cannot.

But meddle as they may, interventionists only succeed in making things worse. Health-care reform offers another telling example of this. Interventionists clamor that the ranks of the uninsured continue to swell because the private insurance market won't cover them. Little do they realize that prices in the health-care economy have been driven up precisely because of government interventions such as Medicare and Medicaid.

Why? Health-care interventionism distorts the price mechanism that allows doctors and patients to negotiate the costs of various treatments. More interventionism inevitably results in an increase in health-care costs, which in turn means fewer people who can afford private health insurance. Interventionists then decide that we need more regulation. This is the vicious circle of regulation. As Mises explained, when regulations make problems worse, more regulations are passed to make up for the harm caused. Interventionists typically capitalize on perceived market failures, and then deceive an unsuspecting public into believing in the inadequacy of the market and pressing for more regulation.

This explains the 69,684-page Federal Register. It is rife with rules and restrictions that alter the way entrepreneurs act in the marketplace. Its mandates are costly, redundant, and ultimately destructive of the market forces that create prosperity for everyone. Yet it continues to grow. But as history has amply shown, it is free markets, not government regulation, that make us better off. Would that the interventionists could learn this most simple of lessons. □

1. Ludwig von Mises, *Critique of Interventionism* (Irvington-on-Hudson: Foundation for Economic Education, 1996 [1977]), p. 14.

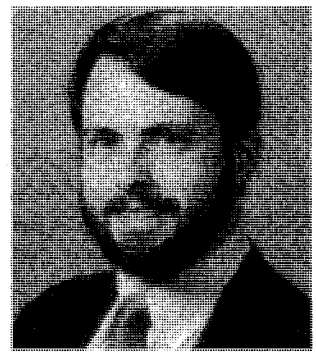
2. Richard K. Vedder, "Federal Regulation's Impact on the Productivity Slowdown: A Trillion-Dollar Drag," Policy Study No. 131, Center for the Study of American Business, July 1996, p. 16.

3. Mises, p. 33.

4. *Cato Handbook for Congress* (Washington, D.C.: Cato Institute, 1999), p. 356.

5. Wayne B. Gray, "The Cost of Regulation: OSHA, EPA and the Productivity Slowdown," *American Economic Review*, December 1987, pp. 998–1006.

6. Hans F. Sennholz, introduction to *Critique of Interventionism*, p. v.



Decoding the North Korean Enigma

Northeast Asia will never be fully secure until the communist dictatorship of North Korea passes from the scene. After threatening to test a new long-range missile, the North says it is willing to negotiate with "the hostile nations" opposing it. But whether it will actually forgo its test launch is anyone's guess.

That the so-called Democratic People's Republic of Korea (DPRK) is able to create so much unease, even in the capital of the world's sole superpower, demonstrates the foolhardiness of America's continued entanglement in essentially peripheral security matters. In the short run, Washington should attempt to ease the Korean peninsula's transition to a new peaceful order. But the United States should simultaneously begin disengaging from the region's unsettling quarrels.

By any normal measure, the DPRK should be irrelevant. Bankrupt, starving, and bereft of allies, North Korea is becoming the least of nations. Barely 20 countries bother to maintain embassies in Pyongyang, the North's capital.

Arrayed against it is an imposing coalition. The Republic of Korea (ROK) possesses an estimated 30 times the GDP and twice the population of the North. Japan is the world's second-ranking economic power with a limited but potent military. The members of the Association of Southeast Asian Nations (ASEAN) states remain aloof from Korean affairs, but all would back the ROK in any crisis.

Russia was once allied with Pyongyang, but is now shipping weapons to Seoul to pay off its debts. China retains modest political ties with North Korea, but has far greater economic links—trade and investment—with the South.

Yet the North continues to drive events in the region. Why? The DPRK retains two advantages. One is a large army, supplemented by missile development and atomic research programs.

There is, however, little behind this seemingly imposing edifice. The North's military capabilities have fallen sharply as its services literally starve: soldiers don't eat and weapons don't get spare parts. The North's nuclear program is only presumed; a recent search of the suspected underground site at Kumchang-ri turned up nothing. North Korea's missiles are few in number and highly inaccurate. In short, the DPRK has done better convincing the world that it possesses weapons of enormous destructive power than actually acquiring them.

The DPRK's second trump is its willingness to play the game of high brinkmanship. Pyongyang regularly engages in dramatically provocative but apparently irrational conduct, brandishing its military mailed fist. The result is usually feverish excitement abroad. For instance, North Korea's latest missile gambit caused House International Relations Committee Chairman Benjamin Gilman to worry

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Doug Bandow, a nationally syndicated columnist, is a senior fellow at the Cato Institute and the author and editor of several books, including Tripwire: Korea and U.S. Foreign Policy in a Changed World.

that one "cannot overstate the danger this development could present to our national security."

Alas, that's what the North wants Gilman to think. Although the new weapon probably could hit Alaska, the United States is more than capable of deterring an attack: Pyongyang would disappear in a radioactive cloud. Moreover, the DPRK already possesses a missile, the Taepo Dong-1, capable of hitting both the South and Japan.

The prospective missile test looks to be just one more attempt to unsettle the DPRK's adversaries. Its probable goal is to shake more cash loose from Seoul, Tokyo, and Washington. Largely ignored by the United States and Japan until it hinted at developing a nuclear weapon, in 1994 the DPRK agreed to freeze its program in exchange for shipments of heavy oil and construction of a nuclear reactor. Stalked by famine, Pyongyang has since pushed, with varying success, for food, investment, and trade.

More Benign Conduct

For all of the perversities and incongruities of North Korean behavior, the regime's conduct remains far more benign than in the past. The DPRK has, for instance, halted its nuclear program, admitted aid workers throughout the country, and hosted South Korean and other foreign businessmen.

Handling a regime that is simultaneously belligerent and opaque is not easy. But having recently completed a full review of U.S. policy toward the North, the administration should reconfigure present policy. Washington should separate its strategy into short- and long-term components.

America's overriding goal should be to maintain peace on the peninsula. Although prior predictions of imminent collapse have proved false, North Korea seems destined for the great dustbin of history. The only question is whether Pyongyang falls in peacefully.

To encourage that end, modest concessions—food aid, diplomatic recognition, foreign trade and investment—are well spent. But Washington should attempt to reverse today's dynamic, under which the North misbehaves in the hope of receiving more benefits.

Although the United States and its allies should accept Pyongyang's offer to discuss the planned missile test, they should not provide an explicit quid pro quo. Instead, they should indicate that a number of benefits will be forthcoming if Pyongyang stops needlessly antagonizing its neighbors.

And they should deliver. In succeeding months the United States should drop additional restrictions on trade, offer diplomatic recognition, and cancel future joint ROK-U.S. military exercises, like the ongoing Ulchi Focus Lens maneuvers. South Korea should expand its so-called sunshine policy. Japan should dangle the possibility of expanded diplomatic and economic ties.

The allies should provide such benefits to the DPRK when it behaves, not when it misbehaves. Should it revert to its policy of disruptive belligerence, all three countries should retaliate quickly but quietly.

That is, they should adopt an official attitude of insouciance—who cares what the North does? However, without public fanfare or threats, which would likely make the North more obdurate, the allied states should slow or suspend positive movement on other issues.

The goal should be to squeeze the North, but not too hard. Again, the objective is to push the DPRK toward a more positive stance without creating either a potentially violent implosion or causing it to strike out.

Although the United States is necessarily involved in the near term, over the long term Washington should seek to disentangle itself from Northeast Asia. It should develop a phased withdrawal program for its troops, and terminate the defense treaty when the pullout is complete. □

THE FREEMAN
Ideas On Liberty

A Lesson in Political Management

by George C. Leef

Suppose you have just learned that the house you live in has leaky water pipes. If not attended to, the damage done by the leaks will compound and the value of the house will decline. Would you spend whatever it took to fix the problem? Or would you go out and buy an expensive new high-definition TV?

That might sound like a silly question, but that's because you are assuming that you own the house. Of course, you would protect its value. The prospect of continuing damage from leaking water would be a strong incentive to repair or replace the pipes. On the other hand, what if the house wasn't your property? The loss in value would not be your loss, and unless the leak threatens your belongings, why bother with it? You might just go out and buy that new TV.

Property rights obviously make a difference. What if there is no real owner with an interest in maintaining the property? That's the case with "public property," which really does not belong to any individual or group. Management of public property depends on the choices of politicians and bureaucrats who stand to gain nothing from making "right" decisions (those that make the best use of it) and to lose nothing from making "wrong" decisions (those that make less than optimal use of it). Political-bureaucratic management predictably leads to neglect of property entrusted to public officials in favor of spending that benefits them more in the currency of politics: influence, power, and prestige.

A recent controversy in North Carolina shows the truth of that theory.

The Campus Crisis

In April 1999 a consultant hired (at great expense) by the board of governors of the University of North Carolina released a report that shocked people. It stated that hundreds of buildings on the 16-campus UNC system were in "deplorable condition." Hundreds of millions of dollars of repair and renovation work was needed "urgently" for dorms, classrooms, laboratories, and libraries. Over a ten-year period, the university system's capital "needs" amounted to $6.9 billion.

Supporters of the university played up the repair and renovation angle, but inspection of the list of proposed spending projects showed that only about half the university's priority "Phase I" spending was to go for repair and renovation of academic buildings. The rest was for land acquisition, various campus enhancements (such as landscaping), non-academic buildings (such as performing-arts centers and athletic facilities), and a large-scale construction program to handle an expected surge in enrollments in the future. The "crisis" in the condition of existing buildings was running interference for a wish list of spending to expand and glorify the university system.

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To pay for the great program to make the UNC system "ready for the next millennium," the consultant proposed multibillion-dollar bond issues by both the state government and by the university system itself. If all that borrowing took place, it would double the state's bonded indebtedness (a point never mentioned by the proponents). To keep the public from rejecting this appropriation of resources by the university system, supporters sought to exempt the bonds from the state's referendum requirement by not having them backed by the full faith and credit of the state. Backers in essence said, "Trust us—you've elected us to make decisions on what is best for the state."

Trying to allay fears that this would be too much debt, politicians and university officials came up with economic arguments that would have any well-taught Economics 101 student laughing derisively. The spending, they said, would "stimulate the economy" and thereby keep the state's economy prosperous. Some people were impolite enough to point out that this is an example of Bastiat's lesson of the "seen and unseen"; left in private hands, the money would "stimulate the economy" in other ways.

Backers also argued that higher education "drove the economy," suggesting that if billions weren't spent as they wanted, somehow North Carolina businesses would be unable to find competent workers. That's a false dilemma. We do not have to choose between workers educated in state universities—there is room for doubt that much education takes place there anyway—and workers who are not educated at all. But bad argumentation is the meat and potatoes of politics.

Skeptics, including me, quickly began to take issue with many aspects of the plan. For one thing, would the expected surge in enrollments actually occur? Distance learning via the Internet is starting to change the market for education, and we have no way of knowing how much it will reduce the demand for the traditional on-campus degree chase. Moreover, college graduates are increasingly having to take what have traditionally been "high school" jobs. As people realize that the market for employees with bachelors' degrees (and masters' and doctorates) is oversaturated—particularly where the degree holder lacks the cognitive skills that are in high demand—fewer people will choose to invest in those degrees. And even if there were an increase in the number of students wanting to enroll, why does that mean that the state university system must expand? There are, after all, private colleges and universities that would be happy to enroll more students.

The Vital Question

The most intriguing question, however, is this: Why had this "crisis" arisen at all? The UNC system receives a large amount of money every year for operations and capital improvements. Its budget has grown significantly in real terms over the last decade. It employs many people knowledgeable about building maintenance. Nevertheless, it was facing a building crisis. The consultant wrote that the overall quality of buildings across the system was "poor."

Buildings deteriorate over a long period. It takes years of neglect before they can be called "deplorable." The conclusion seemed inescapable that the political-bureaucratic managers of the system had failed to adequately maintain the property entrusted to them.

I decided to look back at UNC budgets for the last decade to see what tale they told. If maintenance of existing buildings had been neglected, what kinds of expenditures had been more important to the decision-makers? The documents answered just as I had expected. New construction had been proceeding apace. There was, for example, a new "Convocation Center" at Appalachian State that had cost nearly $30 million; almost $8 million for expansion of East Carolina's football stadium; $2.2 million for a "conference center" at UNC-Asheville and $2.8 million for an even nicer one at UNC-Chapel Hill; $3.5 million for an arboretum at North Carolina State; $16 million for a library expansion at UNC-Charlotte; $5.7 million for a new administration building at UNC-Pembroke; $7.9 million for a physical education facility at Fayetteville State. The list goes on and on.

North Carolina was looking squarely at the age-old problem of political-bureaucratic

management—the lack of incentive for decision-makers to take good care of the property entrusted to them. No financial loss accrues to university officials because they allow buildings to sink to a "deplorable" state. The budget they are given each year isn't their money, so they choose to spend it on items that have little to do with education but increase the nonpecuniary benefits of their positions. Just as big-city politicians tend to neglect mundane things like bridge maintenance so they can spend more on vote-getting programs, public university administrators and their political allies tend to neglect building maintenance in favor of flashy new campus monuments. Eventually the bills must be paid for all the deferred maintenance, but that cost will, of course, fall on the taxpayers—the same taxpayers who have already paid for all the buildings and expenditures that could have been done without altogether.

Missing from the decision-making of government universities is the profit motive. Here's a good way to understand the profit motive: those subject to it stand to gain from being right and lose from being wrong. Actions that make good use of resources are rewarded with profits; actions that make bad use of resources are penalized with losses. In his recent book, *Market Education*, Andrew Coulson makes the point this way:

> [I]n the private sector, the money educators earn or forfeit is their own; in the public sector, it is not. Just as parents are more careful about the kind of schooling provided to their children when they are themselves footing the bill, so too are teachers and principals more attentive in spending that money when they stand personally to gain or lose by their decisions. In competitive markets, then, educators have a clear financial stake in the success of their schools and that success is measured by the number and loyalty of the patrons who are willing to pay for their services.

The profit motive makes the consumer king and those who wish to succeed must strive always to find the best ways of satisfying him. In the profitless world of government education, however, revenues don't come from satisfied customers and that gives decision-makers a free hand to spend money with their own satisfaction in mind. Waste of resources is the inevitable result.

In fact, in government education (as well as other government domains), the misuse of resources can actually be beneficial to the decision-makers. When their waste and folly lead to real or perceived crises, they can plead for more money from the taxpayer to "solve" them. The manifest failure of our government K-12 systems to educate children leads to ceaseless demands for more money, teachers, administrators, equipment, and buildings. All that money does nothing to improve education, but it does benefit teachers, administrators, and the many hangers-on who feed at that trough. In North Carolina, the self-created "campus crisis" has led to proposals that would pour significantly more money into the system and make it easier for the administrators to finance still greater spending in the future. In politics, nothing succeeds like failure. □



THE FREEMAN
Ideas On Liberty

The Force of Economics

by Ninos P. Malek

A long time ago, in a galaxy far, far away . . . there were economists who tried to explain economics in clear terms. Unfortunately, there are only a few in the economics profession who are concerned with making the "dismal science" understandable to the average person. Most "high-powered" economists are more worried about the mathematical elegance. The verbal economist who can actually explain economic events is pushed aside as not being rigorous enough.

What's worse, the average person doesn't care about economics and doesn't understand the power of economic reasoning. What usually comes to mind when hearing the word "economics" is investing, personal finance, or learning how to start a business. However, economics is everywhere whether it's sports, fashion, music, or, yes, the movies! This is a statement that I have repeated several times to my high school economics class (I'm still not sure if they believe me or if they care). My goal as a teacher is to demonstrate to my students, first, that the study of economics is more than just focusing on financial topics and, second, that they have made economic decisions most of their lives.

One decision that most Americans make is to attend a movie or an athletic event. Listening to some people complain about how high movie prices are or that they can't afford to take their family to a 49ers or Sharks game is a bit irritating. Maybe the price is out of the range for some to afford, but the fact is that prices are not too high—the proof of this is that the theater or stadium is sold out. Theaters and professional sports teams would love to charge even more, but they can't because fewer people would attend. And, of course, consumers would love to pay nothing to get entertained, but that won't work either because suppliers would have no incentive to provide the entertainment.

Economic theory dictates that supply and demand determine the prices for goods and services. When demand decreases or supply increases for a product or service, the price, other things being equal, will fall. When demand increases or supply decreases for a product or service, the price will go up—as it should. Any intervention to control prices would be, as the French classical-liberal economist Frederic Bastiat put it, plunder. The problem is that some people think it is their right to take their family to a movie or a hockey game. Consequently, when some are priced out of the market, they protest and call for a legal maximum price, or what economists call a price ceiling. Unfortunately, the result of this ceiling will be a shortage of tickets.

Then there are the people who can afford to pay the ticket price and do purchase it, but still complain about the high price. One of Adam Smith's main insights in *The Wealth of Nations* is that unless both parties in an

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exchange think they will benefit, the transaction will not take place. Therefore, when a person buys a movie or hockey ticket, or anything, it demonstrates that that was the best use of the money compared to all other possible alternatives and, consequently, the benefits of the transaction outweighed the costs. In other words, these people should stop complaining.

A Better Theater

Smith's famous statement, "It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own self-interest," underlies a crucial concept. When the movie theater spends thousands of dollars on bigger screens and sophisticated sound systems, is it because the owner cares about you? Not necessarily. The theater spends this money because it is competing against other forms of entertainment for your dollar. By providing you with a better viewing experience, it benefits as well.

If prices are indeed too high, why do some people still go to the theater rather than wait for movies to hit the video stores? Some might say it's because they do not want to wait. In economics jargon, they have a high time preference. There's probably an additional reason: the feeling people get when sitting in a packed theater. Some feel a sense of connection with others when something inspiring or sad causes them to cry together. When someone does something without considering the costs or benefits to others, we call any side effect of that action an externality. Now I am almost certain that the people around me in the theater are not screaming, yelling, or crying because they are thinking about my enjoyment, or utility. Nevertheless, I still receive a benefit. (Of course, the screaming child or the talker would be an example of a negative externality.)

I recently encountered the power of economics in the movie that could financially surpass *Titanic* and *Gone with the Wind* (in both nominal and real terms): George Lucas's *Star Wars: Episode One, The Phantom Menace*. It begins by stating that there is turmoil in the Galactic Republic because of the taxation of trade routes. The Trade Federation has stopped all trade with the planet Naboo, creating the conflict for the story. In the real world too, governments cause conflicts by infringing on individual freedom and imposing tariffs, quotas, and trade embargoes.

Money also provided a point about economics in *The Phantom Menace*. Money is anything that is generally accepted in trade of goods and services. In the movie our heroes need to replace a defective part on their spaceship when they land on the planet Tatooine. When Qui-Gon Jinn offers a merchant "Republic Credits" for the part, he's told that these credits are worthless. An alternative to money is barter, so Qui-Gon has the ship checked for something tradable. He comes up empty-handed. This leaves no alternative but a risky bet that offers a high payoff. Yet again a simple principle of economics: it takes a high potential return to get someone to take a big risk.

Some of my students thought I was going overboard with my passion for economics when I told them that I wanted to write this article. I hope they'll see what an enlightening tool economics can be even in their leisure time. □

The apple icon identifies articles that are appropriate for teaching students several major subjects—including economics, history, government, philosophy, and current issues.

We also provide sample lesson plans for these articles on our Web site **www.fee.org** and in written form. Professors, teachers, and homeschooling parents need only to visit our Web site or request written lesson plans to take advantage of this unique service.



Other People's Business

Social engineers never tire of conjuring up proofs for their own indispensability. These days those who subscribe to the "let me tell you how to live" ethic are disturbed by the explosion in consumption at all levels of society. So they have some proposals. There is nothing new, of course, in the spectacle of affluent intellectuals' sneering at the common people's enjoyment of wealth. It goes back to the very beginning of capitalism and the consumer society, when the upper crust complained that mass production made it difficult to ascertain to which class any particular person belonged. Later Thorstein Veblen condemned "conspicuous consumption." And in *The Affluent Society*, John Kenneth Galbraith launched his career as a public intellectual by grousing that private consumption was crowding out "public investment," which is a euphemism for political consumption, which in turn is a diplomatic way of saying legalized plunder.

Now Cornell University economist Robert Frank is gaining celebrity, and not insignificant royalties, lamenting the culture of consumption, which he has dubbed "luxury fever."

Frank's jeremiad is a variation of the old "keeping up with the Joneses" theme. He worries that the crass bourgeoisie aims to emulate not the Joneses but the Cabots and Lodges. We in the middle class buy fancy things beyond our means not because we need or even really want them, but rather because we are on a desperate treadmill to obtain the increasingly expensive products that the wealthy have. Thus government needs to save us from ourselves and to stop the rich from being a bad influence on us. If they were forced to buy fewer or less-expensive goods, the consumption standards they set would be more manageable.

Frank's theme is also a variation of the "prisoner's dilemma," which purports to prove that in some circumstances what is good for each may not be good for all. A favorite example is a rock concert. If the people in the front row stand, the rest of the audience will be encouraged to stand. In the end, no one can see any better than when everyone was sitting, but now everyone must be on their feet. That one can't dance while sitting is never taken into account by those who see rock concerts as a kind of market failure. (This doesn't happen at the symphony.)

Frank's own example describes a job applicant who spends a thousand dollars for a suit in order to look sharp at his interview. If the applicant's rivals spend less than a grand, he's in good shape. But when they start springing for thousand-dollar suits, the first poor sap has to spend two thousand dollars. Frank compares this process to an arms race.

This has the distinguishing mark of a typical academic economist's example: it bears scant resemblance to the real world. I daresay few job applicants feel they need to outspend their competition on wardrobe.

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Another Tax

But social engineers never need much to hang their hats on. Once he's identified the "problem," Frank is ready with a solution. The government—it's always the government—should enact a graduated consumption tax, which would be applied to each person's consumed income minus a $7,500 standard deduction. This is intended to reduce frivolous consumption and induce saving. It's all in his book *Luxury Fever: Why Money Fails to Satisfy in an Era of Excess*.

Frank sounds more like an over-reaching psychologist than an economist. We consume more and more, he says, because we easily get used to and dissatisfied with what we have. A house that seemed big when we bought it seems small a few years later. We want more—more not just of what we have but more than others have. He touts a survey which found that a majority of those polled would rather make a lower absolute salary that was more than other people earned than a higher absolute salary that was less than others earned.

Frank also laments that people are driven to buy homes they cannot afford in order to send their children to better schools. That is regrettable. It's also regrettable that Frank doesn't see that governments create this problem by running schools and financing them with property taxes. In a free education market, children wouldn't be assigned to schools by bureaucrats on any basis, including residence.

While we can identify reasons that impel people to buy higher-priced homes than they might otherwise buy (the income-tax deduction for mortgage interest is another reason), Frank is on thin ice when he generalizes. We simply do not know why any particular person buys any particular product. When Frank utters a "tsk tsk" and says "there oughta be a law," I'm reminded of the neighborhood gossip who can't mind his own business. Frank is free to make all the baseless moral judgments he wants about others. He should not be free to call the cops, or the taxman.

But let's grant Frank this: surely in a population of 260 million Americans, some people are buying things in unthinking imitation of someone else. Maybe that is in part why a record 1.4 million Americans went bankrupt last year.

Resist Temptation

What do we do about it? A new tax is surely not a good answer. In a free society, people have a natural right to try keeping up with the Joneses if that's what they want to do; and the rich have a right to spend their incomes as they like. If their consumption tempts moderate-income people to spend unwisely, it is a strange notion of justice that calls for the rich to be punished. Shouldn't grown-ups be expected to resist temptations that do not serve their rational interests? Is it the government's role to shield people from themselves?

Frank and anyone else who suffers insomnia over how other people spend their money could put their time to more productive use by promoting individualism. An individualist is someone who thinks for himself. He is ready to learn from others. But he draws his own conclusions and charts his own course. He doesn't keep up with the Joneses or base his self-worth on whether he makes more money than his neighbors. Can you imagine Howard Roark buying a particular car because it's the kind Ted Turner drives?

In the realm of public policy, individualism is best promoted by radically scaling back the power of government. If from the time a person enters "public" school he learns to regard the government as his master, it is small wonder he never learns to think for himself. People who are free to live and make mistakes will be taught individualism by that most potent teacher: reality.

FEE's founder Leonard Read long counseled that setting an example by personal conduct is many times more powerful than giving a lecture. To the extent Frank has identified an actual problem, he can best address it by practicing individualism. That would be better than lobbying the government to tell other people how to live. □

THE FREEMAN
Ideas On Liberty

China's Flirtation with Keynesian Economics

by Christopher Lingle

China's economy has made enormous progress since modernization began in 1978 under the direction of Deng Xiaoping. However, while no one expects the transition from communism toward market-based economies to be painless, the full truth is much more brutal in that China's economic future may be rather bleak.

After nearly 50 years of experimenting with a failed economic system, China is now flirting with another widely repudiated theory, Keynesian economics. The recent National Peoples' Congress announced plans for a substantially larger budget deficit aimed at stimulating domestic spending to avert an economic slowdown. This attempt to re-inflate China's domestic economy combines numerous interest rate cuts (at least seven since May 1996) and massive public spending on infrastructure that began during 1998.

Attempts to boost overall domestic spending through credit expansion and pump priming are hallmarks of Keynesian policies. It is worth noting that where applied elsewhere in the post-World War II era, these policies eventually contributed to rising misery indexes (unemployment rates plus inflation rates) and rising public-sector debt, and brought "stagflation" into the economic lexicon. In short, although there were some illusory or, at best, temporary benefits, deficit spending and loose monetary policy tended to make matters worse.

Apart from the dubious record of deficit spending, we might inquire whether China's economic illness has been properly diagnosed. While there are warning signs of a dangerous deflationary spiral, the proposed remedies are off base. China's problem with deflation cannot be resolved through Keynesian "reflationary" policies, as they only act as countercyclical measures at best.

China's current price instability is a symptom of other fundamental problems in its domestic economy. To some degree, trying to play in the global economy on its own terms has exposed these faults. But the basic problem is that China faces a glut of manufacturing inventories and insufficient domestic spending. There has been a decline in retail prices since the first quarter of 1999. This is not surprising since China's industrial capacity is estimated to be almost double current demand.

Domestic demand is suffering since workers in state-owned enterprises who have kept their jobs are saving more in light of planned downsizing that must eventually lead to cutting 50 million jobs or more. Although always high, China's marginal saving rate has climbed substantially over the past year to a remarkable 68 percent.

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Declining Exports

Meanwhile, export growth is dwindling. In particular, China has lost ground in some crucial product groups like steel and shipbuilding. Devaluation of the Korean won and Japanese yen has eroded China's comparative advantage in pricing. There are also various signs that foreigners are viewing their presence in China much more critically. In a Japan's Export-Import Bank survey, manufacturing firms with three or more overseas affiliates identified China as the worst on the basis of foreign direct investment performance. Unsurprisingly, statistics offered by China show that investment by Japanese companies declined by 15 percent in 1998, while their total investment declined by 27 percent.

There may be no escape from continued declines in economic growth. Declining exports and incoming foreign investment combined with collapsing domestic consumption is a recipe for a deep downturn. While public-sector budget deficits may delay the process, history proves that governments cannot buy their way out of recession.

In the end, China's economy will face the sharp corrections experienced by other communist countries in transition. Communist economies cannot be reformed without first undergoing a substantial collapse in industrial production. The breakdown may be more or less severe, as can be seen in the different experiences of former Soviet bloc countries. Nonetheless, China's coming collapse is unavoidable owing to imbedded distortions imposed by nearly 50 years of mostly irrational economic policies and political interference. As the internal contradictions of China's "market socialism" unfold, the economy will continue to unravel.

Central planning combined with state ownership of property and the means of production are the principal sources of China's distortions. The worst consequences were temporarily delayed by the impressive growth spurt when some of the worst policies were put aside and personal incentives were permitted to operate.

To a considerable degree, China's experience mirrored the East Asian "miracle" economies in its rapid trajectory. As elsewhere, this high growth phase will wither. Consider the experience of its regional neighbors. As in China, rising costs due to corruption and overspeculation sapped the competitive edge, with domestic economic problems worsened by an overvalued exchange rate. Speculative bubbles led to property developments that far exceed demand, while financial mismanagement contributed to a banking crisis, and so on.

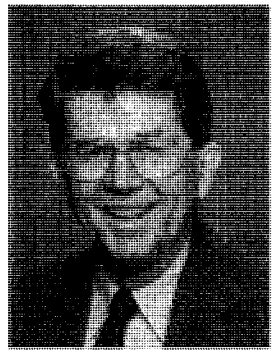
The State Should Retreat

Unfortunately, changing these conditions will not be easy—not least because the economic problems facing Beijing's policymakers are to a considerable degree the outcome of political arrangements. A massive retreat of the state from the Chinese economy is required. Cadres and bureaucrats must have less power.

China's long march to modernizing its key sectors involves many challenges. Transforming a centrally planned economy to a market-based economy is perhaps the most daunting task. This is because the rapid adjustments demanded by, and vigorous competition arising from, globalized markets require supporting institutions that are generally absent in China. Among these are: the rule of law (including independent judges and reliable enforcement mechanisms), modern accounting and financial procedures, public accountability of corporate and political officials, sound money, and a well-integrated national market along with an openness to domestic and international competition.

Leaving earned income in the hands of consumers and investors is a crucial step toward establishing a sustainable basis for economic growth. The key to future growth in the modern global economy is to open up domestic economies to competition while unleashing creative young entrepreneurs who can produce wealth and jobs by starting small and medium-sized enterprises. Printing more money or throwing public funds and credit at the economy will not be able to accomplish this. □

Economics



Politics and Foreign Trade

The case for free trade is overwhelming, both theoretically and empirically. My last two columns developed the theoretical case, which is based on the concepts of opportunity costs and comparative advantage. Even if the people of a country have an absolute advantage in producing everything, they still gain from foreign trade because they cannot have a comparative advantage in producing everything.

Ample empirical evidence backs up the theoretical arguments in favor of free trade. The more that countries permit international trade to direct their productive efforts into their comparative advantages, the more they prosper relative to those that restrict trade. Despite this evidence, almost no country has followed a policy of free trade. With rare, and typically short-lived exceptions, governments reduce economic productivity and their citizens' prosperity by either taxing or imposing quotas on imports. Why? Answering that question is the purpose of this column.

Cooperation vs. Confiscation

Given the advantages of free trade, no government would erect barriers to imports if the political process allowed the same degree of social cooperation as the market process. When trade restrictions are eliminated consumers gain but some workers and investors lose, most temporarily but some permanently. Even those who would lose permanently from eliminating their industry's trade protections would still be better off living in an economy with completely free trade than in one where all domestic industries were protected. Even though individuals may benefit from their industry's protection, they would lose far more as consumers from the protections of everyone else.

Those in an industry subject to intense foreign competition will want government to protect them if they don't have to consider the costs it imposes on others. But protectionism would not occur if an industry had to pay these costs because the burden to consumers is always greater than the benefits to the protected industry.

Unfortunately, when people obtain benefits from government they do not have to pay prices reflecting their costs, as they do for benefits received in the marketplace. The cooperation of the marketplace comes from the market's ability to collect, aggregate, and communicate costs that are widely dispersed over many people so that they are taken into consideration by those responsible for them. In sharp contrast, when the costs from politically provided benefits are dispersed over many people, those costs are likely to be ignored. So government commonly becomes the means by which people can gain private advantage through confiscation rather than through cooperation.

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Weakness of the Many

A trade restriction concentrates benefits on the few in the protected industry at costs that are thinly dispersed over the entire consuming public. With the cost of a trade restriction spread over millions of consumers, few if any will be aware of the little extra they are paying for the protected product. After all, consumers buy hundreds of different products, and a little increase in the price of one product typically has little impact on the well-being of any one of them. Even if a consumer is aware of the extra cost, she will seldom know that it is caused by a trade restriction. And if by some chance she does know the reason for the extra cost, she has little motivation to respond politically. Even if she could eliminate the trade restriction, the effort might cost as much as or more than the restriction. While the total benefit from eliminating the restriction is huge, most of it would go to other consumers whether they took political action or not. But her political action is unlikely to do any good if she acts alone.

Of course, if a large percentage of the consumers act in unison they would surely have a decisive political influence. But because the number of consumers is so large, with each having such a small stake in the outcome, it is almost impossible to organize them for political action. As is often the case, the larger the number of people harmed by a policy, the weaker their political influence.

Power of the Few

On the other hand, because a relative few benefit from a trade restriction, they will be effective in lobbying for it. The benefit to each person will be significant, and each will be aware of both his own gain and the source of that gain. Also, because of the small number of beneficiaries, they are relatively easy to organize for political action. Indeed, they will generally be organized already through industry and occupational associations. So when a trade restriction is being considered, politicians will hear plenty from those favoring the restriction and little if any from those harmed by it. The result is a bias toward providing concentrated benefits and ignoring much larger, but dispersed costs. Therefore, it is often the case that the smaller the number of people benefiting from a policy, the more powerful their political influence in its favor.

With small, organized groups able to capture benefits at the expense of the general public through restrictions on trade (and many other special-interest policies), little social cooperation is achieved through the political process. For that reason, government is a constant threat to the social cooperation that comes from free-market activity.

Considering Some Costs

The costs of trade restrictions are more difficult to identify than indicated above. Consider restrictions on steel imports. Few people buy steel directly. Rather they pay for it indirectly when they buy products made from steel. Also, when an import restriction increases steel prices, employment opportunities are reduced in industries relying on steel as an input. Those who don't get jobs because of a trade restriction will seldom know the reason. It has been estimated that limiting steel imports to 15 percent of the U.S. market would cost American consumers $189,000 a year for each steel job saved, and that for every U.S. steel job saved, over 3.5 U.S. jobs would be destroyed because of higher steel prices.*

If such costs were revealed, rather than concealed, by the political process, we would never reduce our prosperity with trade restrictions. The advantage we all receive from free trade is that it forces industries to consider the full opportunity costs of their productive activity. It's too bad that they aren't required to consider the full cost of their political activity. □

*See Arthur Denzau, "American Steel: Responding to Foreign Competition," Center for the Study of American Business, Washington University, St. Louis, Mo., February 1985.

THE FREEMAN
Ideas On Liberty

The Collectivist Illusion

by Tibor R. Machan

Some fallacies are easy to detect. Consider the fallacy of composition: take a group of human beings and ascribe to it capacities only individuals can have. "Society says," "We decided," "America is violent." Strictly speaking, none of these claims can be true. Society has no mind and mouth with which to say or do anything. Nor are *we* able to decide anything. You, I, and others may decide the same thing. That is the only sense in which we've decided.

Ordinarily when we say such things, it is usually well enough appreciated that we are taking linguistic shortcuts. "America is violent" is supposed to mean only that a significant number of folks in America are willing to deploy violent means to solve problems. Or it refers to the government and not to Americans at all.

Unfortunately, the care necessary to keep this in mind is not always diligently exercised. Karl Marx did not exercise that care when he said humanity is "an organic whole." Strictly speaking, humanity has no convictions, thoughts, memories, imagination, intentions, purposes, or any other attributes of individual human beings.

So what, you say. Why fret?

Changing Standards

The problem is that once you forget that humanity comprises concrete human beings, instead of some big entity, the standards by which we evaluate societies change. After all, it is sometimes necessary to sacrifice a part to save an organic whole. A cancerous organ or gangrenous limb is removed to save the person.

Thus holistic social thinking can have dangerous consequences. Some people's goals, perhaps even their lives, will begin to seem available for sacrifice for the sake of others. Why? Because individuals are not seen as possessing the same rights to life, liberty, and property, but rather are regarded as parts of a whole whose priority is set by public policy.

Why is this kind of thinking even plausible? The reason is that in some contexts groups almost become a single entity. A close-knit acrobatic team, orchestra, or choir nearly exhibits single-mindedness. A jamming jazz ensemble not only works as a single musical unit, but also embarks on the kind of spontaneous innovation that we would usually expect only of individual human beings unencumbered by the necessity of pleasing others. It almost looks as though individuality has disappeared.

Yet it is precisely individuality that makes such cooperation possible. Failure to cooperate is also attributable to individuals, as, for example, when someone fails to understand what is needed to maintain unity. Complex cooperation requires the utmost concentration by the individual participants.

Indeed, there is usually a critical mass

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beyond which groups *in pursuit of a single objective* cannot function well without central direction. A jazz group can jam and produce great music. A swing band cannot—too many people. The same is true with teams, choirs, and other large ensembles. The marketplace, which can comprise the largest number of people, succeeds precisely because there is no central direction and each member is free to pursue his own objectives. A free society has no purpose. Rather, it exists because it enables its members to achieve their own purposes, which they do by using spontaneous institutions to coordinate their activities.

Inspiring Harmony

Witnessing the beauty of harmonized activities aimed at a single purpose can be so inspiring that one might wish to see similar cooperation extended globally. When a modern-day Karl Marx envisions humanity acting like an organic whole, he extrapolates from the musical ensemble, convinced that what is possible for the small group could be, indeed ought to be, realized for the entire species.

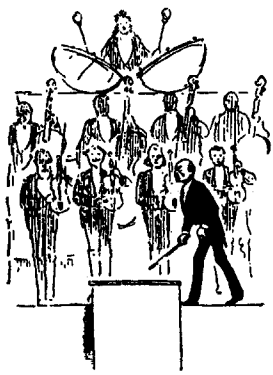
Marx knew that this wasn't possible and never had been. But his vision of its beauty formed a standard of humanity's health and well-being, making it something to be achieved in the future and to be used in judging the present.

The big problem with this vision is that in life any given human being can embrace only so many others, after which the fit will be forced and, indeed, must be coerced. Human beings are essentially individuals geared to moderate social entanglements. Our emotional make-up does not prepare us to be intimate members of a world society, or even of a country, in the sense that we are members of a family. Despite what President Reagan said, America is not a family, nor is Ireland or Iran. Families are sized to permit, with some attention and vigilance, their members to stay close to one another—celebrate birthdays and weddings, attend to the sick, mourn the dead.

If we were the kind of collective beings Marx and other champions of collectivism have imagined us to be, we would have to spread our emotional energies way beyond what they are capable of. We would lose our capacity to love intimately, to care, and to be close. Circles of friends and families are reasonably sized so that one is not always torn between sadness about someone's mishap and joy about someone's good fortune. But if we attempted an intimate relationship with every member of humanity, nothing could be felt toward others because it would be canceled out by opposite feelings every time.

The kind of community that fits human beings can vary a good deal; some people are much more gregarious than others. Thus it must be left to free choice to discover how much intimacy is right and how many communities we can honestly join.

The individual's right to choose freely whether to belong to this, that, or another group is the best moderator of our social capacities. We can overestimate or underestimate what we are capable of in this as in many other regards. But in the long run such things are best left to each of us rather than having visionaries impose an impossible and ultimately destructive social dream. □



CAPITAL LETTERS



Who Wrecked the Trains?

To the Editor:

There is much in Gregory Bresiger's article, "Train Wreck" (*The Freeman*, August 1999), that is factual, but some that is misleading and false.

Yes, at least some railroad leaders after World War II were "lulled" by the strong performance of railroads during the war into "thinking that the good times are back." Yes, most of the railroads' troubles over the years were attributable to (1) wrong-headed government regulation, (2) the tax-financing, subsidization, and government promotion of competitors to the railroads, and (3) the intrusion of labor unions into decision-making that belonged, then as now, in the hands of management. And, yes, government ownership and operation of railroads were prime goals of socialists and communists through much of this century, their relative quiescence today notwithstanding.

But to say, as Mr. Bresiger does, that the troubles of the railroads after the war resulted in "The death of an industry" is manifestly and totally false. Total rail freight volume in 1997 was actually double that of 1944, the peak war year, when railroads carried three-fourths of total traffic in the United States.

True, a very few sizeable railroads, most notably the Rock Island, did "die" and go out of business after the war. Most, however, were acquired by other railroads and continue operating today as part of larger independent systems, thus continuing the same process that has led to the consolidation of railroads throughout history. Still others, mostly smaller railroads, continue as independents even today. Some serve as feeder lines for larger systems, and others perform specialized services, such as for sightseers and train buffs.

Nor is it correct that the "once mighty Pennsylvania . . . was typical of a sick, over-regulated industry." In fact, the Pennsylvania (later Penn Central) was actually atypical within the industry. The troubles that led to its bankruptcy and takeover by the government were directly traceable to the wrong-headed policies of its early management, especially of the railroad's first chairman and CEO Stuart Saunders. Saunders's decision to cave in to union demands as the price for its support of the Penn Central merger was a disaster. The common share price soon after the merger was upward of $80. By the time it was taken over by the government a short while later, the price had plummeted to $2.50.

As for passenger service, the problem "in a word," Mr. Bresiger says, was "politics." Not so. The real problem was, is, and may always be the automobile, which today as for years past handles over 90 percent of total U.S. passenger travel. Only in World War II were railroads a significant factor in the movement of people in the United States, and that was out of necessity.

The proper role for railroads is, always has been, and always will be to move goods. Even in the heyday of passenger service, the movement of people accounted for only slightly more than one-fifth of total railroad revenue. Largely because of the automobile, Amtrak will always be a money loser. Mr. Bresiger's failure to distinguish between the two services, freight and passenger, is at the root of the confusion that pervades his otherwise well-written article.

—CHARLES O. MORGRET
Holmes Beach, Florida

Gregory Bresiger responds:

Mr. Morgret makes a convincing case in criticizing my article. He argues that the poor leadership of the Pennsylvania Railroad in the 1950s hastened its downfall and that the railroad industry is alive and well. I have two points in response. First, the article focused

on passenger service. Clearly, private railroads, including the Pennsylvania, were hampered by regulatory policies that prevented them from raising or dropping fares. They were also hamstrung by ICC accounting standards that were confusing. The Pennsylvania was hurt by regulators during its merger with the New York Central, which took about a decade to complete and included several uneconomic requirements. Finally, Mr. Morgret disputes my argument that politics was a factor in the decline of many railroads and blames instead the automobile. But the automobile—through various subsidies and state-built and state-maintained interstate highways—was the preferred transportation mode of politicians after World War II. The federal and state governments favored the railroads' competitors at every turn. Even the best railroad leadership was hurt by these wrong-headed policies.

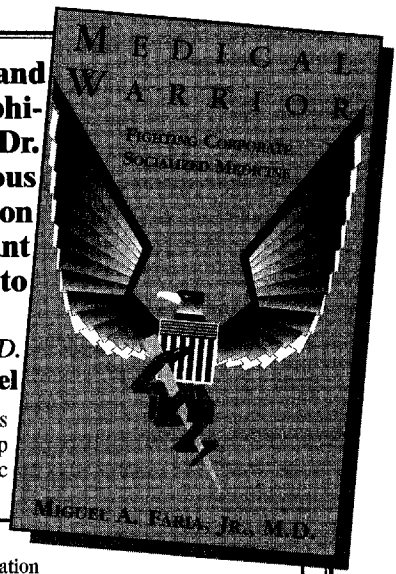
I agree with Mr. Morgret about freight service, which has been far more profitable than passenger service in the United States and which has been making a comeback. But why? Because rates were partly deregulated in the 1980s. □

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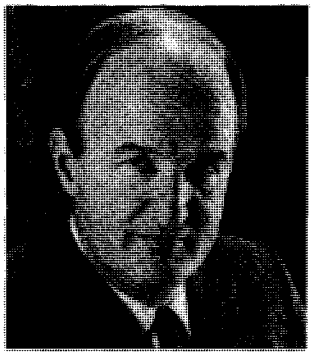
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THE FREEMAN
Ideas On Liberty
DECEMBER 1999



Heilbroner's One-Armed Philosophers

"Without the government, the market as a system would not last two minutes."
—ROBERT HEILBRONER[1]

The May-June issue of *Challenge* magazine highlighted Robert Heilbroner, perhaps the best-selling economics author of all time. This year he published the seventh edition of his celebrated work, *The Worldly Philosophers* (Simon & Schuster, 1999), which has now sold over three million copies.

I am not surprised that *The Worldly Philosophers* has gone through multiple editions since 1953. Heilbroner has written a colorful and entertaining masterpiece. And no one has come up with a better title about the lives and ideas of the great economic thinkers.

Challenge also interviewed the 70-year-old professor. One question they failed to ask, however, is, "Why have you doggedly refused to acknowledge the success of twentieth-century free-market schools of economics?"

Heilbroner's Bias

Yes, it's a sad commentary: Robert Heilbroner, the masterful stylist, suffers from one serious defect—a highly prejudicial, unbalanced view of economics. After revising and updating his book seven times, he still never mentions the Chicago school of Milton Friedman and the Austrian school of Ludwig von Mises and F. A. Hayek (although he does have a chapter on Joseph Schumpeter, the *enfant terrible* of the Austrians).

Heilbroner's resolve is a tragic reminder of the one-sided way economics was taught a generation ago: Give Adam Smith his due, and then spend the rest of the time patronizing Keynes, Marx, Veblen, and the socialists. Meanwhile, the Chicago school, the Austrians, the supply-siders, the public-choice school, and other free-market proponents are poured down an Orwellian memory hole.

Heilbroner's bias reminds me of Stalin's rewriting of history when he would have his enemies' pictures erased from official photographs. In Heilbroner's photograph of the "great economic thinkers," he has erased men like J. B. Say, Carl Menger, Eugen Böhm-Bawerk, Knut Wicksell, Irving Fisher, Frank H. Knight, Henry Simons, Mises, Hayek, Friedman, Robert Lucas, and James Buchanan, among others. Heilbroner writes as if the Nobel Prize in economics hadn't existed for the past 25 years!

Mark Skousen (http://www.mskousen.com; mskousen @aol.com) is an economist at Rollins College, Department of Economics, Winter Park, FL 32789, a Forbes *columnist, and editor of* Forecasts & Strategies. *His textbook,* Economic Logic, *is now available from FEE.*

Both Mark Blaug and James Tobin regard Irving Fisher as the greatest American economist. A year ago, *Time* magazine's editor-in-chief, Norman Pearlstine, named Milton Friedman "economist of the century," ahead of Keynes.[2] Daniel Yergin and Joseph Stanislaw wrote in *The Commanding Heights*: "In the postwar years, Keynes's theory of government management of the economy appeared unassailable. But a half century later, it is Keynes who has been toppled and Hayek, the fierce advocate of free markets, who is preeminent."[3] Yet you wouldn't know anything about Fisher, Friedman, or Hayek after reading *The Worldly Philosophers*.

No one is objecting to Heilbroner's right to favor Keynes over Friedman, but to ignore Friedman (whose name does not even appear in the seventh edition) is a travesty.

Why the Sins of Omission?

All editions of *The Worldly Philosophers* have purposely hid the background of the author, and with good reason. His mentors are Marxists Paul Sweezy at Harvard and Adolph Lowe at the New School for Social Research. No wonder he wrote so sympathetically toward Marx.[4] Heilbroner has been a dedicated "democratic socialist" for most of his life and was for many years the Norman Thomas Professor of Economics at the New School. He is perhaps the only economist in the United States who holds a chair named after a socialist political leader. He has long favored a large public sector and Keynesian deficit spending. He hates the term "free market," adding, "Markets aren't free. They depend on government."[5] He prefers the Marxian term "capitalism."

Several years ago, I met Bob Heilbroner in his New York apartment and asked him why he ignored Friedman and Hayek. He felt that Friedman had not advanced economics beyond Adam Smith, and as for Hayek, he said, "I tried reading Hayek but could never follow him." Yet I give Heilbroner high marks for condemning abstract mathematical modeling in economics as generating "rigor, but, alas, also rigor mortis," and for being the only socialist to publicly give credit to Mises and Hayek for correctly anticipating the collapse of Soviet central planning.[6]

Galbraith and Buchholz: More Balanced Views

Heilbroner could learn a lot from his friend John Kenneth Galbraith. Although Galbraith's title isn't as dramatic, *Economics in Perspective* (Houghton Mifflin, 1987) bends over backwards to be fair to free-market economists. Sure, Galbraith gives full space to his favorite writers (Keynes, Veblen, Marx), but he also devotes major portions of his book to Say's law and the French laissez-faire school, the Austrians' critique of socialism, Fisher's quantity theory of money, and Friedman's monetary counterrevolution to Keynesian economics.

Heilbroner's rewriting of history is one reason more and more instructors are turning to more balanced histories of economic thought such as Todd Buchholz's *New Ideas from Dead Economists* (Penguin, 1989 and revised in 1999). Like Heilbroner, Buchholz has chapters on Smith, Marx, Veblen, and Keynes, but then gives equal time to Alfred Marshall and the marginalist revolution and the twentieth-century counterrevolution of Friedman and Buchanan. Buchholz leaves out the Austrians because, he says, he was never taught anything about Mises or Hayek when he attended Harvard. □

1. Interview with Robert Heilbroner, *Challenge*, May-June 1999, p. 62.

2. *Time*, December 7, 1998, p. 35. However, when *Time* published its "The Century's Greatest Minds" special issue, the editors gave top billing to Keynes. Pearlstine acknowledged a disagreement between him and his editors. "This is not the first time that the editors of *Time* have chosen to disagree with me. . . . I still think Friedman is the economist of the century." (Private correspondence, April 20, 1999.)

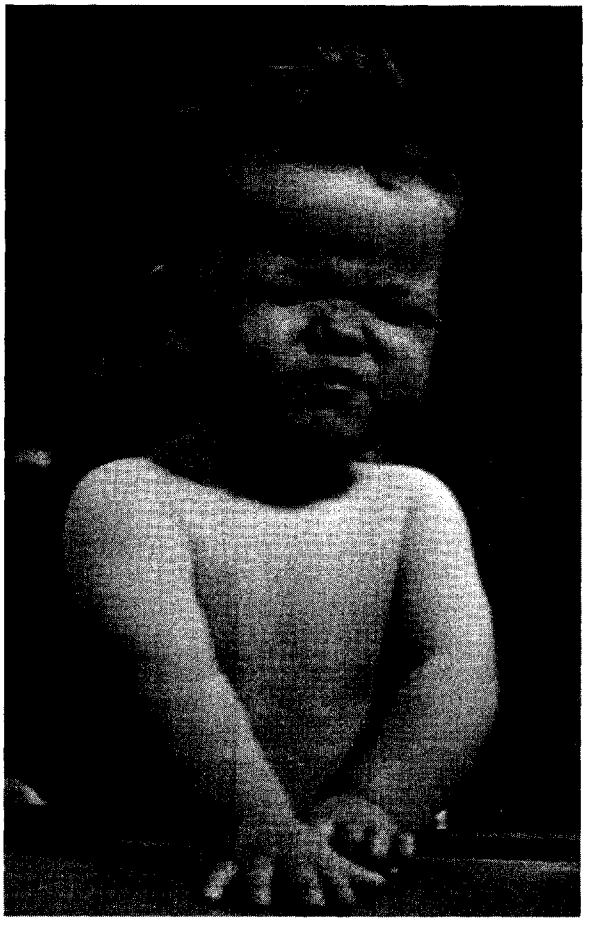
3. Daniel Yergin and Joseph Stanislaw, *The Commanding Heights* (New York: Simon & Schuster, 1998), pp. 14–15.

4. In the 1961 edition I used in college, Heilbroner wrote that Marx was a "devoted husband and father" (p. 124), but after it was revealed that he had an illegitimate son from his housemaid, Heilbroner dropped the approving reference.

5. *Challenge* interview, p. 61.

6. Robert Heilbroner, "The Triumph of Capitalism," *The New Yorker*, January 23, 1989, and "Reflections After Communism," *The New Yorker*, September 10, 1990.

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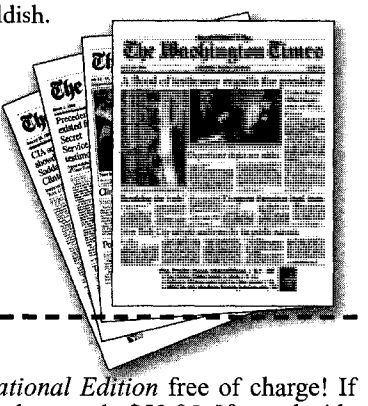


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BOOKS

Individualism in Modern Thought from Adam Smith to Hayek

by Lorenzo Infantino

Routledge • 1998 • 248 pages • $85.00

Reviewed by Andrew I. Cohen

Some social theorists believe that moral, political, and economic order must be imposed according to some central plan. In their view, only constant management can generate and sustain the complex, mutually supportive norms of advanced societies. Another tradition in social thought defends an "open society"—one founded on respect for voluntarism and individual freedom. Thinkers in that tradition believe social order can and should emerge spontaneously.

Lorenzo Infantino, a professor of sociology in Rome, embraces methodological individualism, which understands complicated social phenomena in terms of their simpler components, namely, individual human actions. Infantino presents a wide-ranging survey of central figures in sociology, political economy, and philosophy to compare how individualism and collectivism account for social order.

Two hundred years ago David Hume argued that order does not entail an intelligence that creates it. Admittedly, what Adam Smith calls the "invisible hand," and what F. A. Hayek (following Michael Polanyi) calls a "spontaneous order" may seem planned. It is tempting to misread the complexities of an economy as designed or at least as something design could improve.

Appealing to figures such as Smith, Karl Popper, Ludwig von Mises, and Georg Simmel, Infantino suggests that order must not be imposed. Free actors engage in mutually beneficial exchanges that bureaucrats could not possibly fathom. The reciprocal relationships people voluntarily establish channel self-interest to mutual advantage and promote a prosperous social order.

Social contract thinkers speak of individuals in a "natural condition" who literally construct a social order. Thomas Hobbes, for example, regarded men as having "sprung out of the earth, and suddenly (like mushrooms) come to full maturity, without all kind of engagement to each other." Infantino prefers Smith, Bernard Mandeville, and Popper, all of whom dismissed the idea of a pre-social "pure self." Society is necessary to generate language, moral norms, and an individual's very capacity for self-awareness. Infantino writes, "When man discovers himself, he is already united with others by a social bond; he does not need to create it." Our natural social situation thus militates against social "constructivism."

The norms that emerge in society ought to be privileged, Infantino argues. If norms persist, he writes, "it is because they answer to the needs of the social actors." But one then wonders why government (particularly intrusive government) has emerged and endures. Without appealing to moral values, it is unclear how the norms of liberty and free exchange are better than the norms by and through which government exists and functions. Noting this omission is not necessarily a criticism of Infantino so much as it is a potential problem with any defense of liberal social order.

A significant portion of the text is dedicated to lengthy (albeit useful) citations. It is sometimes unclear, however, how topics among (and even within) chapters cohere in a unified project. Infantino's frequent references to figures and concepts in the social sciences may also seem esoteric to the uninitiated. The general reader may find the book hard going in places.

The book could have drawn stronger links between tyranny and a closed society. Infantino makes some gestures in this direction, but one wishes he had cast a stronger argument to show that constructivism cannot help but produce political and economic malaise. Similarly, the book could have shown more forcefully how spontaneous order and individual freedom go hand in hand. Here, we only see glimpses of the connections.

Lorenzo Infantino has provided a splendid overview of key figures in the social sciences,

how they compare on the issues of political order, and the best way to analyze collective entities. Had he fleshed out the links among his various lines of discussion and done more to clarify the comparisons among thinkers for the reader, the book would have been more useful yet. Still, the author is to be congratulated for his work on this vital topic. □

Andrew Cohen is assistant professor of philosophy at the University of Oklahoma.

Freedom and Virtue:
The Conservative/Libertarian Debate

edited by George W. Carey

Intercollegiate Studies Institute • 1998 • 231 pages • $24.95

Reviewed by Brian Doherty

Libertarians and conservatives seem to want to get along; how else explain this book's existence? It was published by the Intercollegiate Studies Institute, a now-conservative organization founded by libertarian journalist Frank Chodorov as the Intercollegiate Society of Individualists. What happened when Chodorov passed control of his organization to more conservative characters is emblematic of the conservative/libertarian divide that this book explores but fails to bridge: they removed "individualist" from the name, cobbling together a contentless phrase to maintain the initials.

Fear of the unbridled individual is at the root of the conservative/libertarian conflict over freedom and virtue. The conservative fears that people unleashed from the power of the Leviathan state will bring society to rot and ruin; indeed, at least one writer here (Frederick Wilhelmsen) argues that it already has. Libertarians think that, given the corruption of man that conservatives are so prone to emphasize, granting corrupt men power to enforce their vision of virtue is dangerous—and that for various reasons both moral and prudential, violence (the root of all state power) should be used solely to repel or reverse assaults on one's own person or property.

The essays collected here limn some of the difficulties that arise when libertarians and conservatives debate. The debate isn't settled because the combatants don't clarify the two positions or even prove that there is in fact a coherent conservative position. Even the libertarian side seems incoherent, with John Hospers, author of a book called *Libertarianism* and first presidential candidate of the Libertarian Party, having trouble sticking to the basic Millian position that state power oughtn't be used except to prevent harm to others. "Freedom is a great thing," he opines, "but one should not run the danger of destroying oneself in the pursuit of it."

Anthologies raise more issues than a brief review can note; I here concentrate on a couple of themes. The obvious, though unintended, lesson of this book is that there is no coherent conservative position. Some people seem to choose the term for sociological reasons of loose affinity and thus define it to mean whatever they believe. Comparing the views presented here by such supposed conservatives as Richard Weaver and L. Brent Bozell shows that the word means, as Humpty Dumpty said, whatever we want it to mean. Bozell thinks enforcing virtue through violence quite proper; he claims that within the Christian metaphysic he posits as essential to both conservatism and American civilization, "freedom is hardly a blessing; add the ravages of original sin and it is the path to disaster."

Weaver, on the other hand, thinks that "the conservative in his proper character and role is a defender of liberty. He is such because he takes his stand on the real order of things and because he has a very modest estimate of man's ability to change that order through the coercive power of the state. He is prepared to tolerate diversity of life and opinion because he knows that it is right within reason to let each follow the law of its own being." In this, Weaver finds himself embracing the libertarian argument, derived from Scottish enlightenment thinkers and promulgated most thoroughly this century by F. A. Hayek, that man can and does form complex workable orders without government control or management.

One issue that is perhaps even more divisive between libertarians and conservatives comes

up frequently: war and peace. Conservatives tout the importance of an activist U.S. world military to fight off Soviet communism, or now that that is dead, what Robert Nisbet here sees as the "aggressive, imperialist totalitarianisms in the world." The only specific examples he gives are China and Cuba. While none of the libertarians collected here talk about foreign policy, the conservatives clearly are irritated that many libertarians refuse to bow to the exigencies of U.S. world imperialism.

This volume is worthwhile for interesting contributions from both sides, such as M. Stanton Evans's intriguing contention that pre-enlightenment traditions contain more support for limited state power than many moderns customarily suppose and Doug Bandow's argument from an evangelical Christian perspective that, contra Bozell, state power has no useful role to play in the enforcement of Christian morality.

But essays like Russell Kirk's, where he condemns libertarians as "metaphysically mad," and obsesses over his notion that libertarians are disproportionately gay and very unpleasant characters besides, show that however much they may find themselves allied in specific instances against state encroachment, the relationship between libertarians and conservatives is apt to remain one of occasional alliance and persistent mistrust. □

Brian Doherty is the Warren Brookes Fellow at the Competitive Enterprise Institute.

World Disorders: Troubled Peace in the Post-Cold War Era

by Stanley Hoffmann

Rowman & Littlefield • 1998 • 279 pages • $29.95

Reviewed by Ivan Eland

Harvard professor Stanley Hoffmann is an unbridled interventionist. Although he decries any American role as the global policeman, he proposes intervening for so many purposes and under so many circumstances that chevrons begin to form on his shoulders.

Hoffmann rejects the argument that the United States should withdraw from entanglements and international commitments. Although he admits that few threats to American vital interests exist—he makes an exception for the Middle East—he declares that a world of diffuse disorder could rapidly become a dangerous place. He argues that societies and economies are too interdependent for the United States to be sure that what happens in small, poor, weak nations will not affect Americans. He maintains that apathy about what happens in "far away countries of which we know nothing" can lead through contagion—and through the message that passivity sends to troublemakers—to "creeping escalation of disorder and beastliness that will, sooner or later, reach the shores of the complacent, the rich, and the indifferent." In short, Hoffmann endorses the domino theory of instability.

He then goes even further, taking issue with those who say that U.S. foreign policy should be based on interests and not values. Hoffmann asserts that morality is a national interest.

Thus Hoffmann advocates intervention in foreign internal crises when the turmoil threatens regional or international security or when human rights violations become so massive that they cannot be ignored. His broad definition of massive human rights violations includes genocide, mass killings short of genocide, ethnic cleansing, brutal and large-scale repression, mass rape, famines, epidemics, massive breakdowns of law and order, and flights of refugees.

Not only does Hoffmann favor unilateral U.S. intervention under those circumstances, but he advocates the formation of an international military force under United Nations auspices—with member nations pledging earmarked forces for use by the Security Council. The international force would conduct limited police operations against minor troublemakers or deter aggression against threatened states that ask for U.N. troop deployments. He laments that no international taxation exists to support such a force. Given the record of the United Nations in peacekeeping missions, the potential for catastrophic bungling in more ambitious military missions makes this proposal scary.

Our author has an activist military agenda but fails to provide priorities for intervention by a nation that has limited funds and military assets. Even the sole remaining superpower has its limits. More important, although Hoffmann understands that interventions can be difficult, he should realize that in many cases they fail (clan warfare continued after the United States left Somalia, and Haiti is sliding back into dictatorship) and that often outsiders cannot deal with intractable problems that have been around for decades or centuries.

Hoffmann identifies and labels three groups in the American foreign policy community: sheriffs, missionaries, and beacons. The sheriffs want to stop the bad guys of the international community at high noon. The missionaries eschew force and advocate foreign aid and public and private programs to export democracy and market capitalism. In contrast to the other two camps, the beacons merely want the United States to be a showcase of liberty and free enterprise for other nations to emulate. It is unfortunate that this book gives short shrift to the beacons and so extols the costly, dangerous alternatives. □

Ivan Eland is director of defense policy studies at the Cato Institute.

The Food & Drink Police—America's Nannies, Busybodies and Petty Tyrants

by James T. Bennett and Thomas J. DiLorenzo

Transaction • 1999 • 161 pages • $24.95

Reviewed by George C. Leef

Threats to the freedom of Americans to make their own choices and run their own lives are proliferating as fast as mushrooms after a heavy summer rain. Some have already grown to huge, Alice-in-Wonderland proportions (like the IRS), while many others are just sprouting. In the latter category is the threat to our freedom to choose what to consume. Prohibition is gone, but prohibitionists lurk among us. This new book from Bennett and DiLorenzo is about them—America's nannies, busybodies, and petty tyrants, as their subtitle says.

We have always had nags and scolds. In a free society, people are entitled to use their liberty in peaceful ways of their choosing and that includes hectoring other people about their choices. Putting up with them, listening if we desire or ignoring them when we would rather be left alone, is one of freedom's tradeoffs. (In fact, there are probably people who regard *us* as nags and scolds, always telling them not to support Social Security, minimum-wage laws, trade restrictions, and so forth.) The trouble begins when they start turning to the coercive power of the state to impose their desires and values on others. Bennett and DiLorenzo introduce us to a host of individuals and organizations that want to tell you what to eat and drink, and have no compunction about employing the power of the state to make you behave.

One of the chief villains of the book is the Center for Science in the Public Interest (CSPI). The authors paid a visit to the Washington office of CSPI, where "Scarecrows scurried here and there, grimly clutching faxes and fact sheets that no doubt proved or at least asserted with the basso voice of pseudo-scientific surety that whatever you are eating at this very moment *will kill you*." That would not bother me (or the authors) except that the CSPI folks are not content just to warn about overindulging in *crème brûlée*. They scowl at virtually everything tastier than a plate of rice and lentils and want to make certain that you don't push that aside in favor of the *crème brûlée*. "The Center's agenda," write the authors, "is harsh neo-Puritanism. Ban, restrict, end, and regulate are common admonitions in CSPI's publications."

Another malefactor is Jeremy Rifkin, a former left-wing activist turned food nanny. Progress of all kinds worries Rifkin, but progress in food leaves him especially queasy. The bioengineering of food to make plants more beneficial to humans is something that we have been doing on a hit-or-miss basis for thousands of years, but now that science has figured out how to deliberately alter the genetic makeup of a plant to add or subtract just the

right trait, Rifkin and cohorts go berserk. His weapon of choice is the lawsuit. If someone wants to experiment with, say, genetically altered strawberries that are supposed to be more frost-resistant, he can count on Rifkin to seek an injunction on the grounds that some vague federal statute has not been fully complied with. That tactic has slowed progress in food production that would benefit everyone, but poorer people the most. Busybodies don't care much about the consequences of their actions, however.

Freedom of speech is something the food and drink police care about just about as much as they care for a dish of Häagen-Dazs with hot fudge. Because the Supreme Court has ruled that "commercial speech" falls mostly outside the First Amendment, the nannies are constantly running off to the bureaucrats and courts to strike down advertising or labeling that bothers them. Our neoprohibitionists and the regulators at the Bureau of Alcohol, Tobacco and Firearms have conspired, for example, to prohibit the sellers of alcoholic beverages from so much as hinting that there is scientific evidence that moderate amounts of alcohol can be good for people. The authors also relate zany battles over the naming of products, such as Crazy Horse Malt Liquor.

The book is written with a great deal of humor and sarcasm, but make no mistake—Bennett and DiLorenzo are deadly serious in alerting Americans to the growing menace of regulation of our eating choices. They write, "There is much more at stake here than how much tax one will pay on one's twinkies, how many beers one may consume at Pizza Hut after a softball game, or the character of Budweiser ads. What is at issue is how much personal responsibility Americans should assume for their own behavior, and consequently, how much personal freedom they will enjoy."

Precisely. Congratulations to the authors for this splendid counterattack against all those busybodies who want to dictate what you eat and drink. □

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

The Political Economy of the New Deal
by Jim F. Couch and
William F. Shughart II
Edward Elgar • 1998 • xvi + 247 pages • $85.00

Reviewed by Andrew P. Morriss

In this work, Professors Jim Couch (University of North Alabama) and William Shughart (University of Mississippi) employ public-choice theory to provide an insightful look at the New Deal. The authors mix examination of historical evidence and econometric analysis of recently rediscovered data on the spending patterns of New Deal programs to argue that the Roosevelt administration used the massive spending for political purposes. Written in a lively and engaging tone, the book also provides a thorough summary of the extensive literatures on the Depression and the New Deal. Economists will welcome its thorough exploration of the data; noneconomists will appreciate its clear presentation of both the statistical and nonstatistical material.

The first chapter of the book surveys the academic literature on the causes and impact of the Great Depression and the critiques of the New Deal. Concisely summarizing multiple theories about those causes (business cycle, monetary policy, underconsumption, and a range of others), the authors effectively convey the basics of a complex and voluminous literature. Among the most compelling features of this chapter is a chart portraying the growth of the New Deal programs over time. This fascinating diagram makes clear the vast scale of New Deal spending.

The next three chapters offer similarly well-written and thorough descriptions of the New Deal programs. Although primarily summarizing prior work on the New Deal, the authors add a market-oriented critique to the literature survey. For example, they make a point of noting that the Roosevelt administration's approach in the "first New Deal" (1933–1935) was built around an "anti-market ideology" that "placed much hope in the central government's ability to produce favorable results" and attributed the Depres-

sion to the market. Well-chosen examples of New Deal-era political cartoons enliven these chapters. My favorite, titled "The Sower," shows New Dealer Harry Hopkins scattering cash from a sack labeled "WPA" across a map of the South, remarking to Agriculture Secretary Henry Wallace "Shucks Henry, You've never seen a bumper crop! Wait 'til you get a look at this beauty!" In a sense, the remainder of the book is a thorough analysis in support of the message of that cartoon.

Couch and Shughart provide extensive historical evidence to show that New Deal legislation lacked the checks and balances necessary to restrain political use of the programs. For example, they quote Michigan Senator Arthur Vandenberg's comment that the bill establishing the Works Progress Administration (WPA) could be "simplified by merely striking out all the text and substituting two brief sections: Section 1. Congress hereby appropriates $4,880,000,000 to the President of the United States to use as he pleases. Section 2. Anybody who does not like it is fined $1,000. That is approximately the net result of this proposed legislation."

The unique contribution of the book lies in the remaining chapters. Here Couch and Shughart deploy public-choice analysis to understand the spending patterns of the New Deal programs. Relying both on data unearthed in 1969 on New Deal spending across states and additional data the authors discovered in the 1939 *Congressional Record*, Couch and Shughart conclude that "political self-interest was perhaps the most important motive underlying the administration's spending decisions. A state's popular vote for FDR in the 1932 election and its importance to the President's electoral college strategy are consistently [statistically] significant determinants of the amount of federal aid it received."

While the authors build on and challenge earlier empirical work on the New Deal, their analysis is more complete. While space does not permit a complete survey of either the methods or the statistical results here, Couch and Shughart have produced a work that at least ought to shift the burden of persuasion to FDR's defenders.

Although various quibbles are possible with some features of Couch and Shughart's number crunching and their review of prior literature, none is important enough to detract from their overall accomplishment of recasting the New Deal in public-choice terms. From Lyndon Johnson's Great Society to Hillary Rodham Clinton's communing with the ghost of Eleanor Roosevelt, statists have sought to hide in the shadow cast by the "success" of the "Relief, Recovery, and Reform" programs of the New Deal. Revealing the blatantly political nature of those programs is an important step in restoring balance to our political and historical dialogues. □

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Toward the Renewal of Civilization: Political Order and Culture

edited by T. William Boxx and Gary M. Quinlivan

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Reviewed by Fr. Robert A. Sirico

To explore the relationship between politics and culture with an eye toward the "renewal of civilization" is a tall order for one volume. And yet the contributors to this collection do an admirable job of examining many facets of the intersection between political-cultural trends and what most of these authors regard as the decline of civilized standards in arts, letters, behavior, and law, not only in this country but throughout the West. But *Toward the Renewal of Civilization* is no gloom-and-doom tract about the end of the world; indeed, it ends on a wonderfully hopeful note.

This book had special poignancy for me, because I read it after last spring's Littleton, Colorado, high-school shootings. The two young killers had jettisoned civilized norms long before the shooting began, but it appears that adults around the kids were paralyzed

with confusion and fear about how to respond. They tried psychiatrists and drugs and a bit of counseling, but for the most part, the parents, teachers, and school administrators were just biding their time, hoping the kids would straighten out naturally.

Why have such events become almost routine? Hilton Kramer argues that they are a consequence of the institutionalized counterculture that began in the sixties. The intellectual error is rooted in the philosophy of Jean Jacques Rousseau, and specifically the belief that received norms, social customs, institutionalized authorities, and traditional standards of accomplishment and morality are merely artifices designed to inhibit the natural development of the human person. The object, then, is to break free from these supposed artificial restraints, which is precisely what the boys in Littleton imagined themselves doing.

The notion of tyranny is different in each respective vision of what constitutes the natural society. In classical liberalism, tyranny is associated with violence, whether perpetuated by private parties or invasive government. To the Rousseauian, tyranny is bound up with societal expectation, as Claes Ryn points out in his brilliantly argued essay. What's more, he writes, "the longing for Rousseauian liberation often expresses an ominous drive for uninhibited power."

For Ryn, the cultural crisis comes down to a misapplication of the capacity of humans to imagine social improvement. Instead of turning this impulse toward the creation of great art and literature, modern man has turned it toward escapism on one hand and a futile attempt to reconstruct society itself on the other. The result, writes William Allen in his essay, has been that radical challenges to liberal democracy have taken hold in the academy and spilled out into society to create a kind of slow-motion French Revolution against the family and other foundational institutions of the genuinely free society. Elizabeth Fox-Genovese concentrates on that point in her eloquent essay.

The hot-button issues of race and sex are not skirted in these pages, for they too have become bound up with a political tug of war in recent years. With rights given out by the regime to groups according to their lobbying power and their ability to form pressure groups based on shared identity, the politics of race and sex has become a game of spoils in which no one can be said to win. The old racism mutates into a new racism with scarcely a thought given to the possibility that human cooperation and social peace are possible only when the state does not interfere with people's freedom of association.

If the book has a weakness it is that the state is not consistently identified as a leading cause of the continued weakening of essential social institutions. The contributors do not make the mistake of viewing the solution to every social problem as resting with political authority, but that is not the same as identifying the state as the culprit.

They rightly see intellectual and spiritual rejuvenation as the likely font of a cultural renewal—which is the only long-term means of combating the moral nihilism at the heart of the Littleton shootings. The book strongly reinforces the central point of classical liberalism: society manages itself better than any rationalistic intellectuals who grab hold of the reins of power ever have or could. □

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Transforming the Political Marketplace

What we expect from our politicians goes a long way toward determining what kind of politicians we can expect to find in office. Just as suppliers compete by trying to please their customers, politicians compete by trying to please voters. Just as the features of cars tell us something about the preferences of car buyers, the actions of politicians tell us something about the electorate.

In the marketplace for cars, competition insures that the products mirror consumer tastes. Unfortunately, politicians have created barriers to entry that make political competition less vigorous than it might be. And voters do not bear the consequences of their choices with the same immediacy of car consumers. Still, the politicians who survive in office tell us something about ourselves.

We could, for example, expect our politicians to uphold the Constitution and maximize our ability to lead the lives we choose. After all, elected officials at the federal level swear to "support and defend the Constitution of the United States against all enemies, foreign and domestic."

In contrast, we might expect our politicians to see their job as pleasing their constituents regardless of constitutional constraints. And because constituents are a diverse lot, the politician who wants to stay in office focuses on the most influential constituents.

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Frederic Bastiat described the state as "the great fiction by which everyone seeks to live at the expense of everyone else." Everyone may try, but only the politically powerful succeed. When the state is devoted to such efforts, what Bastiat called plunder, a peculiar sort of person succeeds in politics. No, not a thief, but a thief in saint's clothing.

The political marketplace teems with those who sugarcoat redistribution with claims of helping the general public: "We need farm subsidies because the family farm is the backbone of this great nation." A politician who can make that claim with a straight face has a much better chance of being elected than one who says, "I have a lot of friends who are farmers and when elected, I intend to make them rich using your money."

Helping the District

In today's political landscape, however, some politicians dip their hands into the treasury without invoking the legerdemain of the public good. It is not uncommon to read of a member of Congress making the case for his re-election on the grounds that he has successfully steered large amounts of so-called federal dollars into his district.

You would think he might be embarrassed to have taken money from neighboring districts and states merely to enhance, say, the roads of his constituents. But he's actually proud of it. When he is called to task, his supporters have a quick justification: it's his job to help his constituents.

His job? It's his job to use the fiscal process to enrich A at B's expense? I guess that oath of office is just for show. If the Constitution could weep, it would cry us a river.

We once lived in a different world.

We once, at least from time to time, had politicians who understood that the Constitution constrained their ability to spend the people's money. One such man was Grover Cleveland. In his first Inaugural Address, in 1885, he said: "In the discharge of my official duty I shall endeavor to be guided by a just and unstrained construction of the Constitution, a careful observance of the distinction between the powers granted to the Federal Government and those reserved to the States or to the people, and by a cautious appreciation of those functions which by the Constitution and laws have been especially assigned to the executive branch of the Government."

Such language sounds quaint to our ears: a president promising to restrain himself based on higher principle. When push came to shove, Cleveland refused to budge from that principle. In 1887, when a drought hit Texas, a bill arrived on his desk providing funds to buy seeds for struggling Texas farmers. Who could oppose such a worthy cause?

Cleveland vetoed the bill and wrote the House of Representatives that "I can find no warrant for such an appropriation in the Constitution, and I do not believe that the power and the duty of the general government ought to be extended to the relief of individual suffering which is in no manner properly related to the public service or benefit." Cleveland went on to explain to Congress that when the government got into the business of relieving suffering, it discouraged private efforts to fight hardship and hurt our character.

How would the voters of today describe such a veto? Heartless? An example of gridlock? How the world has changed! A reluctance to spend other people's money has become a vice rather than a virtue.

Notice that Cleveland said nothing about the morality of helping the farmers of Texas. He might have felt their cause to be just. But he could not justify federal intervention constitutionally. This narrow perspective reduces the potential for plunder. And one of the purposes of the Constitution is to limit even our honorable desires to alleviate suffering with the public's money. Otherwise, the power of government grows and that of individuals falters.

It is tempting to say that Cleveland's integrity and respect for his oath of office were politically courageous. Perhaps they were. He made plenty of enemies. But he was also popular with the voters. He managed to win the popular vote in three consecutive elections, his two terms book-ending an electoral college defeat. The voters of the late nineteenth century respected the Constitution and honored Grover Cleveland with their support.

If we want politicians who respect the Constitution, those of us who care about it will have to do a better job encouraging our fellow citizens to feel the same way. Then the politicians who will thrive in the political marketplace of the next millennium will be less interested in spending other people's money and more interested in letting us make our own decisions about living life to the fullest.

♦♦♦

FDA Contest

I want to thank all the readers who responded to the contest in my September column asking for your thoughts on a world without the FDA. The contest winners are Karen Kwiatkowski and David Calderwood. Both made a number of interesting points. Karen emphasized how the FDA politicizes the flow of information about the efficacy of drugs while David pointed out how the FDA suppresses information and undermines the nature of the doctor-patient relationship. Karen and David will each receive a $25 gift certificate to use at the FEE bookstore. □

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