LUDWIG VON MISES INSTITUTE

The Free Market

August 1988
Volume VI
Number 8

A Plague From Both Their Houses: The Economic Advisors to Bush & Dukakis

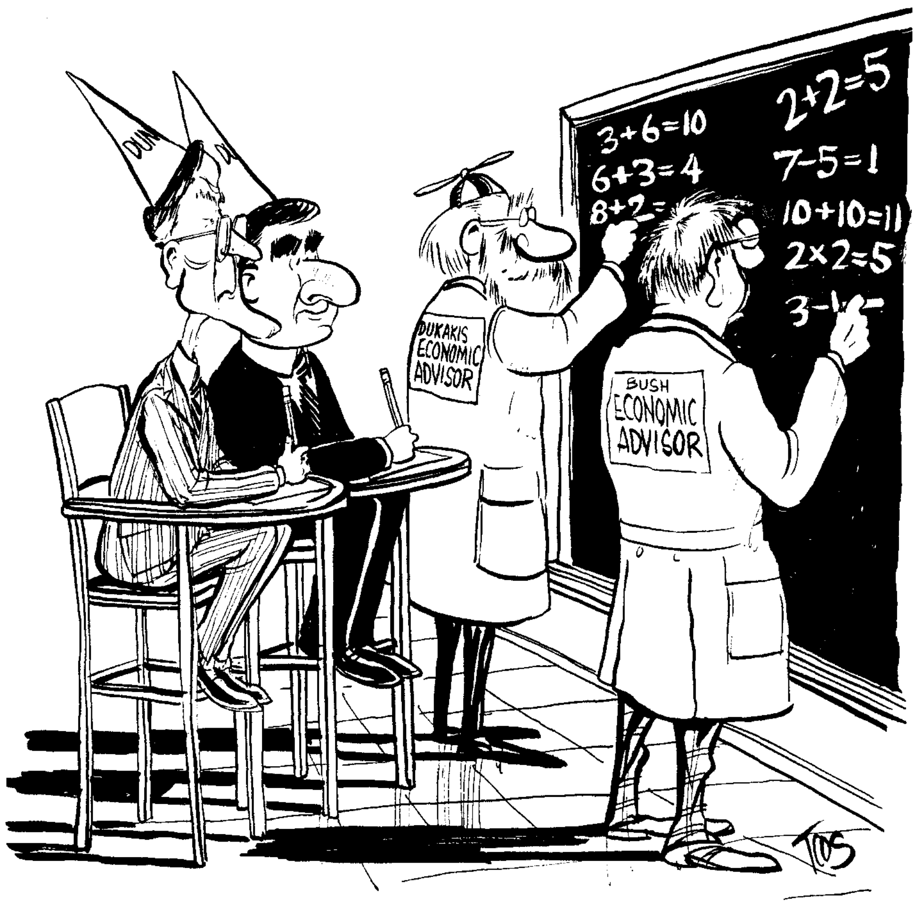
by Lew Rockwell

In primitive societies, witchdoctors legitimized tyrannical government by naming it the mandate of heaven. In return, they got a cut of the earthly loot.

In the U.S., some economists serve the same function. For promoting government intervention as scientific, and advising on the most efficient forms, they receive power, prestige, and money from Washington.

Although these "political economists" differ over candidates and parties, and quibble over small theoretical questions, they are inevitably followers of John Maynard Keynes, the 20th century's most influential justifier of state economic planning.

In the Keynesian tradition, the economic advisors to George Bush and Michael Dukakis share the same intellectual premises, and advocate government power over individuals and businesses, and extensive government intervention in the economy.



Bush's Economists

Michael Boskin

The top economic advisor to the Bush campaign is Professor Michael Boskin of Stanford University. The *Wall Street Journal* (5/23/88) calls him a "mainstream conservative," but that's only within the Keynesian spectrum. As the *New York Times* (6/5/88) notes, Boskin "makes a bow to the late John Maynard Keynes." But it is more than a bow. It is a genuflection.

Keynes believed that at the first sign of a recession, the government should dramatically increase spending...on anything: public works, social welfare, corporate subsidies, the military, etc. It is only important that the spending create a budget deficit, which can then be inflated away through fiat paper money.

But it is government intervention and credit creation that create unemployment and the business cycle in the first place. As the chaos of the 1970s showed—thanks to the policies of Richard "We-are-all-Keynesians-now" Nixon—Keynesian "countercyclical" policies produce unemployment *and* inflation at the same time.

Nevertheless, in *Reagan and the Economy* (Institute for

(Continued on next page)

(Continued from page 1)

Contemporary Studies, 1987), Boskin still advocates ese failed policies:

> Most economists, including myself, oppose an annually balanced budget.... A preferable scheme would be a budget balanced over the business cycle, running deficits in recessions and surpluses in expansionary periods (p. 136).

This is what Franklin D. Roosevelt did in the 1930s when he increased taxes and spending in the midst of a depression. But once the economy recovered, *despite* the New Deal, his successors somehow forgot about running surpluses. And now, with the U.S. economy allegedly in recovery since 1983, Keynesians say deficits don't matter.

The people still worry about it, however, so Boskin proposes to define most of the deficit out of existence with a "capital budget." All the spending that politicians could call "investment" would be counted as increased assets and not as regular spending. Today, for example, when the government spends $100 million on a new office building for welfare bureaucrats, it's considered spending. Boskin would call the building an investment and subtract the 100 million from the deficit.

There is probably no government spending—aside from transfer payments—that some politician couldn't label an investment. So with Boskin's capital budget in place, the government could always run a surplus, no matter how much spending exceeded revenue.

Government spending can never be an investment in the private-sector sense. In fact, government spending is anti-investment. Every penny must be seized from individuals in the private sector who otherwise would have put it to productive use. We can know there is a loss, but not how much, because, as Henry Hazlitt has noted, we can't know what profitable investments *were not made* by entrepeneurs, and what social benefits therefore never resulted.

As Ludwig von Mises showed, bureaucrats—because they operate outside of the price system—have neither the information nor the incentive to invest. Their activities must always lead to a net social loss.

On spending, Boskin calls for a "flexible freeze." Why not an actual freeze? Because, says Boskin, the government should spend *more* in such areas as "education, drug enforcement, and AIDS research." So, while a "flexible freeze" sounds real, it actually means nothing. And if any spending were frozen, Boskin says it should promptly be unfrozen during a downturn "as in 1974-75 or 1981-82" (*New York Times*, 6/5/88). As Keynes said, in downturns "the government must and can replace private demand by public spending" (*The General Theory*, p. 322)

Actually, a recession or a depression is—despite Keynes and Boskin—the very time to *cut* government spending and get Washington out of the way of the market's natural recovery from the Federal Reserve-caused bust.

Boskin's first love, however, is taxes, which he studied at the University of California at Berkeley during its most left-wing period. His PhD dissertation won first prize from the National Tax Association, an organization of federal, state, and local tax collectors dedicated to promoting "revenue enhancement."

All told, Boskin has published two books and twenty-five articles on taxation and right now, he advocates "a broad new federal consumption tax" (*Wall Street Journal*, 5/23/88), which would have a "neutral" effect on the economy (*Reagan*, p. 162).

A recession is—despite Keynes and Boskin—the very time to cut government spending and get Washington out of the way.

But taxes can never be neutral. Taxation transfers resources from producers to non-producers through coercion, which must necessarily disturb market exchange and the structure of production.

Boskin has also written extensively on social security. After two more books and five articles, he concludes that privatization is not the answer. Instead he favors raising benefits and supports the higher taxes engineered by Fed chairman Alan Greenspan when he headed the Reagan social security commission.

Privatization would mean voluntarism, but Boskin advocates "compulsory coverage" because "some individuals...may not save at all or may fail to anticipate or allow for unfavorable contingencies" (*Too Many Promises*, 1986, p. 102). So responsible government must take care of irresponsible individuals.

It's no wonder that liberal Keynesian Lawrence Summers praises Boskin as a "smart, solid guy. He's from the Rockefeller-Feldstein wing of the Republican party" (*Wall*

Street Journal, 5/23/88). Nor that on Boskin's resume, his first character reference is Secretary of State George Schultz, one of America's top corporate statists (and another successful political economist).

"Boskin has hurtled along the fast track of academia that brought other economists to the upper reaches of government, including Arthur Burns," says the *New York Times* (6/5/88). The comparison is apt. Burns, another Republican Keynesian, chaired both Nixon's council of economic advisors and the Federal Reserve, where he helped design and implement Nixon's high inflation and price and wage controls, while claiming to be for sound money and free markets. Burns also delighted in slamming shut the "gold window"—which severed the final tie between the dollar and gold.

Says Boskin, "Public service is important and noble.... I hope to go to Washington for a few years" (*NYT*).

Martin Feldstein

The other senior Bush economist is Professor Martin Feldstein of Harvard, also a Republican Keynesian. Feldstein is also president of the National Bureau of Economic Research, set up more than 70 years ago to encourage statist economic research, and a member of the Trilateral Commission. Founded by David Rockefeller, the commission—to which Bush also belongs—seeks, in its own words, to end the "separation between the political and economic realm" (*Toward a Renovated International System*, 1977). That is, it advocates cartelization of the world economy.

As chairman of the council of economic advisors in the first Reagan administration, Feldstein was the major advocate of higher taxes, and he helped design and push the four Reagan tax increases of those years. Since leaving the administration, he has consistently called for more inflation, higher taxes, and international devaluation of the dollar.

Feldstein, who like Boskin is on the conservative end of Keynesianism, says that sometimes government can make mistakes, but only as "the unintended and unexpected byproducts of well-meaning policies" (*The American Economy in Transition*, p. 3).

But government policies—despite their rhetoric of compassion and humanitarianism—are rarely well-intended. In the name of helping the poor, labor unions and their kept politicians impose minimum wage laws, which then throw people out of work. But this is not an unexpected or unintended consequence; it is precisely what the unions want: to create a labor cartel by reducing job opportunities for marginal workers and therefore cutting competition for their overpaid members.

Federal regulation of business imposes very high costs, often causing small enterprises to shut their doors, or not to open at all. But that is precisely why it is championed by many large firms. Regulation imposes a higher relative burden on the small company than on the corporate giant, and thus also reduces competition.

As another example, the Federal Reserve inflates the money supply precisely because this benefits big banks and the government, no matter what the cost to the rest of us. It claims to be a stabilizing force when it is just the opposite.

Government intervention is almost never undertaken with good intentions. It is imposed because tax eaters—pressure groups or politicians and bureaucrats—have succeeded in using the government to live off the taxpayers.

But Feldstein insists that government intervention is well-meaning because this lets the government and its interests off the hook for all the disasters. It also excuses Feldstein, since he has built his career on providing an intellectual justification for these policies.

> *Government intervention is imposed because tax eaters—pressure groups or politicians and bureaucrats—have succeeded in using the government to live off the taxpayers.*

On May 31, Feldstein and Boskin met with Bush at his summer mansion on the Maine coast. At their urging, Bush called for more Federal Reserve inflation. Not speeding up the printing presses, said the vice president, could "shut down economic growth in this country" (*Washington Post*, 6/1/88). But in the long-run, it is inflation that will do exactly that.

Politicians and their economists never seem to care about the long run. Like Keynes—who was a nihilist at heart—they have very short time horizons. As Keynes quipped, the long run was unimportant; "in the long run we are all dead."

Dukakis's Economists

Robert Reich

George Bush's advisors are conservative Keynesians; Michael Dukakis's are liberal Keynesians. Professor Robert

Reich of Harvard's Kennedy School of Government, for example, advocates an "industrial policy" of "active government" in "partnership" with large corporations (*Minding America's Business*, 1982, p. 331-2).

In this book, Reich calls for centralized direction of business, massive subsidies to favored corporations, more regulation, legal barriers to new entrepreneurs, "a whole range of special tariffs, quotas, loans, and guarantees," and a "knowledgeable" team of government bureaucrats running everything.

All this is in keeping with Keynes, who wrote in 1936 that he wanted "to see the State...taking an ever greater responsibility for directly organizing investment" (*The General Theory*, p. 164).

Reich claims that his plan will "curb market power" and check the size of business. But his policies would deliberately create one huge government-approved cartel, and make it impossible for small businesses to compete, all at high cost to consumers and taxpayers.

Reich wants "government's role in industry...much more open, more explicit, and more strategic" (*The Next American Frontier*, 1983, p. 14), as during World War I, the New Deal, and World War II, when:

> [S]ocial planning...dominated national discourse.... Indeed, large government agencies and large corporations were almost indistinguishable, both to the people who worked within them and to outsiders who dealt with them... (p. 58).

The free market responds to consumers, whereas Reich cares only about big government and big business. It doesn't matter that consumers want home computers, gasoline, or diet sodas. He would take resources away from these areas and devote them to "semi-conductors and fiber optics" (p. 338).

Statists always seem enamored of the latest market-supplied technology (that their policies would have prevented from coming into being). Lenin, for example, loved electrification. So, in the Soviet Union today, there is electricity even in the meanest, farthest outposts of the empire. People may not have decent clothes, food, housing, medical care, or education—let alone appliances that run on electricity—but they have electric current. (Of course, the reliability and quality of the current in the Third World's largest economy is another question.)

Reich wants to subsidize research and development, but the government's sole choice is to stifle them or get out of their way. It is individuals in the market who create new technology. The government, cut off from prices, consumers, and entrepreneurs, cannot know what is best—fiber optics, semi-conductors, diet soda, or anything else.

Only entrepreneurs can forecast the desires of tomorrow's consumers and make sure they are fulfilled efficiently. Reich wants government in charge, siphoning funds to favored big business as in the "Massachusetts miracle," with the entrepreneur's and consumer's only role to obey. Dukakis calls these ideas "thoughtful and well worth thinking about" (*Wall Street Journal*, 5/23/88).

Lawrence H. Summers

Dukakis claims he will balance the budget by increasing the size and power of the Internal Revenue Service. The idea comes from a student of Michael Boskin's, Keynesian Professor Lawrence H. Summers of Harvard, the other top advisor to Dukakis.

Summers comes by his views almost genetically. Both of his parents are Keynesian economists at the University of Pennsylvania, and his uncles include two of the top Keynesians in America, Paul A. Samuelson of MIT and Kenneth J. Arrow of Stanford. Like Boskin, Summers received an award from the National Tax Association for his work. And in addition to studying under Boskin, Summers was also a student and protege of Martin Feldstein, and worked for Feldstein in the Reagan administration.

Along with favoring higher taxes and more "vigorous" collection methods, Summers—like Boskin—wants new consumption taxes.

An enthusiastic taxer, Summers recently edited a two-volume series co-published by the NBER (which Feldstein heads and where Boskin is a senior academic) on *Tax Policy and the Economy* (1987 and 1988), chock-full of essays on how and why to raise taxes.

Along with favoring higher taxes and more "vigorous" collection methods, Summers—like Boskin—wants to impose broad consumption taxes. And he says that economists and policy makers are too concerned about inflation. They should focus on the other side of the Phillips Curve: unemployment.

The Phillips Curve sums up the Keynesian notion that

(Continued on page 5)

(Continued from page 4)

we must have either unemployment or inflation, but cannot have both. The doctrine died after high levels of inflation and unemployment in the 1970s, but Summers still believes in it.

In fact, the Phillips Curve is the reverse of the truth. More inflation brings more unemployment, and sounder money means more jobs. There is no trade-off between the two government-created plagues of monetary debauchment and joblessness. They are visited upon us hand-in-hand.

Summers also calls—with Boskin—for a major government effort to collect more economic statistics, an ominous idea.

Consumers get their information from personal experience, friends, and advertising. Business people need only know about their own markets. But government gathers data about the entire economy to control us.

Unlike consumers and business people, politicians and bureaucrats stand *outside* the market. But to try to run it, they need information about what is going on inside it. Collecting economic statistics imposes huge costs on business, but the government is willing to spare no cost to us, for, as Professor Murray N. Rothbard has noted, "statistics are the eyes and ears of the bureaucrat, the politician, the socialistic reformer."

The Phillips Curve is the reverse of the truth. More inflation brings more unemployment, and sounder money means more jobs.

Brothers Under the Skin

Republican or Democrat, all four of these Keynesians differ only in degree. For example, liberal Keynesians think saving is ridiculous, and want government to discourage it, whereas Boskin thinks that *some* saving is OK.

There are as many varieties of Keynesian economics as there are economists in Washington, D.C. Its doctrines are muddy and open to different interpretations, which is one reason it's so popular: it can be used to justify any interventionist policy, Republican or Democrat.

The Keynesian answer to every economic ill is government stimulation of total demand to increase consumption, investment, and prices. How is this "aggregate demand" to be stimulated? Through government spending and deficits, funded by taxation during booms and inflation during busts.

Before Keynes, most non-socialist economists held to some sort of sound economics. There were no models pretending that the whole of the economy, with millions of individuals and billions of decisions, could be crammed into a group of equations. Economic laws and the logic of human action governed economists' thinking, so most economists advocated a free market.

That ended with the "Keynesian revolution," which gave the first intellectual justification to what politicians wanted to do anyway. All of a sudden, economists—who used to criticize inflation, deficits, and high spending—were applauding these policies.

Not surprisingly, Keynesians of one stripe or another have filled prominent posts in every administration since Herbert Hoover (and his advisors were proto-Keynesians). FDR took all of Keynes's propositions seriously, and sought to centralize investment decisions in Washington and drive prices up through the destruction of wealth (burning crops, killing animals, inflating the money supply, and raising taxes). He also hired the unemployed for unwanted and unnecessary tasks, and cartelized business and banking in the name of promoting a higher level of coordination.

FDR-style Keynesianism is rare today. But the basic themes of Keynesian economics are still with us: that the free market is inherently unstable; that countercyclical fiscal policy is necessary to compensate for this; that investment and consumption are in lock-step, and when one is primed, the other booms; that there is a necessary trade-off between inflation and unemployment; that interest rates are properly manipulated by the central bank, as is the supply of money; that this monetary manipulation can successfully redirect investment; that inflation promotes growth; that consumption is economically superior to savings; and that the free market cannot properly allocate resources. All are exactly wrong, but few—aside from the Austrian school—have ever challenged the fundamental Keynesian assumptions.

Today, most prominent economists reflect the theory's bad policy implications to one degree or another. And that is true of these four economists, who although they may be competitors, are Keynesian brothers under the skin. They also share an ambition to use their undoubted intellectual powers to serve big government and thus advance their careers. As Joseph A. Pechman of the liberal Brookings Institution says: All are "made from the same cloth" (*NYT*, 6/5/88).

Ludwig von Mises discussed such men in *Human Action* (1966 [1949], p. 869):

> The early economists devoted themselves to the study of the problems of economics.... They never conceived of economics as a profession. The development of a profession of economists is an offshoot of interventionism [with] the specialist who is instrumental in designing various measures of government interference.... He is an expert...at hindering the operation of the market economy.
>
> There are thousands and thousands of such professional experts busy in the bureaus of the governments and of the various political parties and pressure groups...and pressure-group periodicals.... The eminent role they play is one of the most characteristic features of our age of interventionism.
>
> There can be no doubt that [this] class of men...includes extremely talented individuals.... But the philosophy that guides their activities narrows their horizon. By virtue of their connection with definite parties and pressure groups, eager to acquire special privileges, they become one-sided. They shut their eyes to the remoter consequences of the policies they are advocating. With them nothing counts but the short-run concerns of the group they are serving. The ultimate aim of their efforts is to make their clients prosper at the expense of other people.

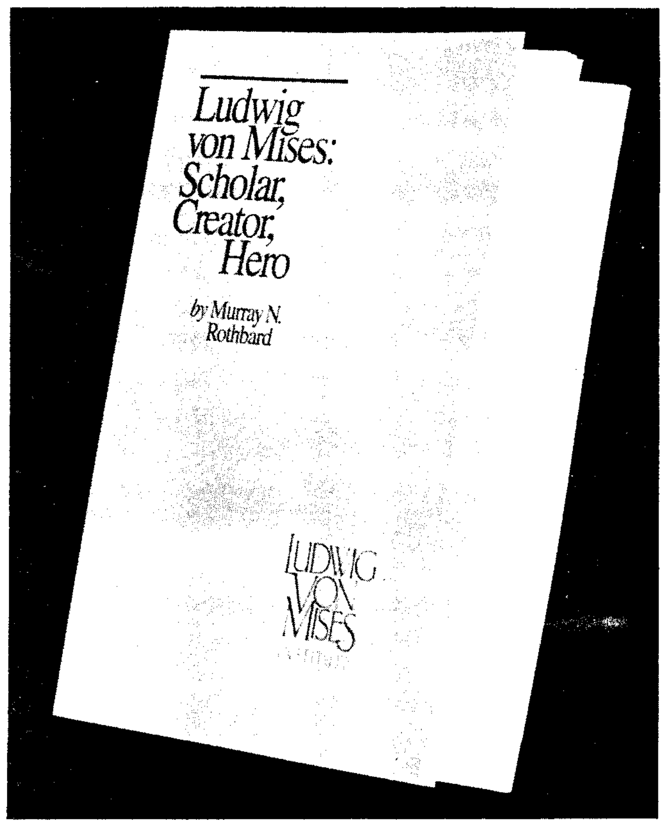
Like witchdoctors, the function of these economists is to give a pseudo-scientific cover to the interventionist policies of their candidate and his backers.

From examining these four men, we can know that big government and its associated special interests cannot lose in 1988. Yes, the subsidies may go to one interest group rather than another, but both sides agree on political control of our economic lives, and on higher taxes and more state planning. No matter who is elected, Keynesianism will be in control.

Not that Boskin and Feldstein, or Reich and Summers, will exercise any real influence. Rather, like the witchdoctor, their function will be to give a pseudo-scientific cover to the interventionist policies of their candidate and his backers. Thus these economists are worth studying for their predictive value, if not for worth of their ideas.

For that, we need economists who share the vision of Ludwig von Mises, and instead of promoting the interests of big government, oppose any interference with the peaceful prosperity of the free market. ■

Rockwell is founder and president of the Ludwig von Mises Institute.



Just published, Murray N. Rothbard's Ludwig von Mises: Scholar, Creator, Hero *is an eloquent and moving tribute to his teacher, and the most definitive book on Mises thus far. It covers Mises's growing up, schooling, intellectual background, career, seminar, influence, and legacy. As Rothbard shows, Mises was not only one of the great minds of this century, he had the courage to defend passionately the cause of liberty in an era of virulent statism. This new book is available for $8.00, which includes U.S. postage and handling.*

Volume VI, Number 8. Editor: Llewellyn H. Rockwell, Jr.; Contributing Editor: Murray N. Rothbard; Institute Publications Editor: Judith F. Thommesen; Managing Editor: Jeffrey A. Tucker; Production Artist: Margaret S. Morris; Publisher: Patricia O. Heckman; Associate Publisher: Norma A. Marchman.