



JE KINDLE-NOTITIES VOOR:

Making Economic Sense

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Thus, deficits are inflationary to the extent that they are financed by the banking system; they are not inflationary to the extent they are underwritten by the public.

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General price changes are determined by two factors: the supply of, and the demand for, money. During 1982–83 the Fed created new money at a very high rate, approximately at 15 percent per annum. Much of this went to finance the expanding deficit. But on the other hand, the severe depression of those two years increased the demand for money (i.e., lowered the desire to spend money on goods) in response to the severe business losses. This temporarily compensating increase in the demand for money does not make deficits any less inflationary. In fact, as recovery proceeds, spending picked up and the demand for money fell, and the spending of the new money accelerated inflation.

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Interest rates fell because of the drop of business borrowing in a recession. “Real” interest rates (interest rates minus the inflation rate) stayed unprecedentedly high, however—partly because most of us expect renewed inflation, partly because of the crowding-out effect. In any case, statistics cannot refute logic; and logic tells us that if savings go into government bonds, there will necessarily be less savings available for productive investment than there would have been, and interest rates will be higher than they would have been without the deficits. If deficits are financed by the public, then this diversion of savings into government projects is direct and palpable. If the deficits are financed by bank inflation, then the diversion is indirect, the crowding-out now taking place by the new money “printed” by the government competing for resources with old money saved by the public.

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Thus, deficits, whichever way you look at them, cause grave economic problems. If they are financed by the banking system, they are inflationary. But even if they are financed by the public, they will still cause severe crowding-out effects, diverting much-needed savings from productive private investment to wasteful government projects. And, furthermore, the greater the deficits the greater the permanent income tax burden on

the American people to pay for the mounting interest payments, a problem aggravated by the high interest rates brought about by inflationary deficits.

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One reason, as many critics have pointed out, raising taxes simply gives the government more money, and so the politicians and bureaucrats are likely to react by raising expenditures still further. Parkinson said it all in his famous “Law”: “Expenditures rise to meet income.” If the government is willing to have, say, a 20 percent deficit, it will handle high revenues by raising spending still more to maintain the same proportion of deficit.

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But even apart from this shrewd judgment in political psychology, why should anyone believe that a tax is better than a higher price? It is true that inflation is a form of taxation, in which the government and other early receivers of new money are able to expropriate the members of the public whose income rises later in the process of inflation. But, at least with inflation, people are still reaping some of the benefits of exchange. If bread rises to \$10 a loaf, this is unfortunate, but at least you can still eat the bread. But if taxes go up, your money is expropriated for the benefit of politicians and bureaucrats, and you are left with no service or benefit. The only result is that the producers’ money is confiscated for the benefit of a bureaucracy that adds insult to injury by using part of that confiscated money to push the public around.

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It is true that if tax rates are 99 percent, and they are cut to 95 percent, tax revenue will go up. But there is no reason to assume such simple connections at any other time. In fact, this relationship works much better for a local excise tax than for a national income tax. A few years ago, the government of the District of Columbia decided to procure some revenue by sharply raising the District’s gasoline tax. But, then, drivers could simply nip over the border to Virginia or Maryland and fill up at a much cheaper price. D.C. gasoline tax revenues fell, and much to the chagrin and confusion of D.C. bureaucrats, they had to repeal the tax. But this is not likely to happen with the income tax. People are not going to stop working or leave the country because of a relatively small tax hike, or do the reverse because of a tax cut. There are some other problems with the Laffer curve. The amount of time it is supposed to take for the Laffer effect to work is never specified. But still more important: Laffer assumes that what all of us want is to maximize tax revenue to the government. If—a big if—we are really at the upper half of the Laffer curve, we should then all want to set tax rates at that “optimum” point. But why? Why should it be the objective of every one of us to maximize government revenue? To push to the maximum, in short, the share of private product that gets siphoned off to the activities of government? I should think we would be more interested in minimizing government revenue by pushing tax rates far, far below whatever the Laffer Optimum might happen to be.

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Wage rates are low in many foreign countries because capital equipment is small and technologically primitive. Unaided by much capital, worker productivity is far lower than in the United States. Wage rates in every country are determined by the productivity of the workers in that country. Hence, high wages in the United States are not a standing threat to American prosperity; they are the result of that prosperity.

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The upshot of chaos theory is not that the real world is chaotic or in principle unpredictable or undetermined, but that in practice much of it is unpredictable. And in particular that mathematical tools such as the calculus, which assumes smooth surfaces and infinitesimally small steps, is deeply flawed in dealing with much of the real world. (Thus, Benoit Mandelbrot's "fractals" indicate that smooth curves are inappropriate and misleading for modeling coastlines or geographic surfaces.)

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Chaos theory is even more challenging when applied to human events such as the workings of the stock market. Here the chaos theorists have directly challenged orthodox neoclassical theory of the stock market, which assumes that the expectations of the market are "rational," that is, are omniscient about the future. If all stock or commodity market prices perfectly discount and incorporate perfect knowledge of the future, then the patterns of stock-market prices must be purely accidental, meaningless, and random ("random walk"), since all the underlying basic knowledge is already known and incorporated into the price.

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The absurdity of believing that the market is omniscient about the future, or that it has perfect knowledge of all "probability distributions" of the future, is matched by the equal folly of assuming that all happenings on the real stock market are "random," that is, that no one stock price is related to any other price, past or future. And yet a crucial fact of human history is that all historical events are interconnected, that cause and effect patterns permeate human events, that very little is homogeneous, and that nothing is random. With

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These are but a few of the subversive implications that chaos science offers for orthodox mathematical economics. For if rational expectations theory violates the real world, then so too does general equilibrium, the use of the calculus in assuming infinitesimally small steps, perfect knowledge, and all the rest of the elaborate neoclassical apparatus. The neoclassicals have for a long while employed their knowledge of math and their use of advanced mathematical techniques as a bludgeon to discredit Austrians; now comes the most advanced mathematical theorists to replicate, unwittingly, some of the searching Austrian critiques of the unreality and distortions of orthodox neoclassical economics. In the current mathematical pecking order, fractals, nonlinear thermodynamics, the Feigenbaum number, and all the rest rank far higher than the old-fashioned techniques of the neo-classicals.

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At first glance, there is some plausibility to this oft-repeated slogan. As Adam Smith pointed out, it is a good thing that we don't rely on the benevolence of the butcher or baker for our daily bread, but rather on their self-interested drive for income and profit. They may intend to achieve a profit, but the efficient production for consumer wants and the advancement of the prosperity of all is the unintended consequence of their actions. But this slogan can be shown to be faulty on further analysis. For example, how do we know what the intentions of

the butcher, the baker, or indeed any businessman, are? We cannot look inside their heads and tell for sure. Suppose, for example, that the butcher and baker, out to maximize their profits, read free-market economics and see that maximizing profit also benefits their fellow-man and society as a whole. As they go about their business, they now intend the consequence of efficient satisfaction of consumer wants as well as their own monetary profit. So if, as some indicate, economic theory only studies unintended consequences of human action, does the learning of some economic theory by businessmen invalidate that theory because now these consequences are consciously intended by the participants on the market?

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Furthermore, the learning of sound economic theory can actually change the actions of businessmen on the market. Many businessmen, influenced by anti-capitalist propaganda, have been consumed by guilt, and may consciously restrict their pursuit of profit in the mistaken idea that they are helping their fellow man. Reading and absorbing sound economic analysis may relieve them of guilt and lead them to seek the maximization of their own profit. In short, now that they are fully cognizant of economics, the intended consequences of their actions will lead to higher profits for themselves as well as greater prosperity for society.

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So what is so great about unintended consequences, and why may no intended consequences be studied as well? And doesn't the accumulation of knowledge in society change consequences from unintended to intended? Not only that: the Misesian discipline of praxeology explicitly states that individual men consciously pursue goals, and choose means to try to attain them. And if men pursue goals, surely it is only common sense to conclude that a good deal of the time they will attain them, in others words they will intend, and attain, the consequences of their actions. Mises's emphasis on conscious choice treats men and women as rational, conscious actors in the market and the world; the other tradition often falls into the trap of treating people as if they were robots or amoebae blindly responding to stimuli.

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There are two ways to advance the message of Austrian economics. One is to fearlessly hold high the banner of Misesian theory to which the wise and honest can repair—a banner which requires calling a spade a spade and pointing out the special interests all too consciously at work behind the government's glittering facade of the "public interest" and the "general welfare." The other path is to seek acceptance and respectability by watering down the Misesian message beyond repair, and carefully avoiding anything remotely "controversial" in your offering. Even to the point of taking the "free" out of "free market." Such a path only entrenches big government.

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Internationally, capital will tend to flow from low-interest- to high-interest-rate countries, raising interest rates in the former and lowering them in the latter. In the days of the international gold standard, the process was simple. Nowadays, under fiat money, the process continues, but results in a series of alleged crises. When governments try to fix exchange rates (as they did from the Louvre agreement of February 1987 until Black Monday), then interest rates cannot fall in the United States without losing capital or savings to foreign countries.

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A central theme of the supply-side school is that a sharp cut in marginal income-tax rates will increase incentives to work and save, and therefore investment and production. That way, few people could take exception. But there are other problems involved. For, at least in the land of the famous Laffer Curve, income tax cuts were treated as the panacea for deficits; drastic cuts would so increase stated revenue as allegedly to yield a balanced budget. Yet there was no evidence whatever for this claim, and indeed, the likelihood is quite the other way. It is true that if income-tax rates were 98 percent and were cut to 90 percent, there would probably be an increase in revenue; but at the far lower tax levels we have been at, there is no warrant for this assumption. In fact, historically, increases in tax rates have been followed by increases in revenue and vice versa. But there is a deeper problem with supply-side than the inflated claims of the Laffer Curve. Common to all supply-siders is nonchalance about total government spending and therefore deficits. The supply-siders do not care that tight government spending takes resources that would have gone into the private sector and diverts them to the public sector.

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They care only about taxes. Indeed, their attitude toward deficits approaches the old Keynesian “we only owe it to ourselves.” Worse than that: the supply-siders want to maintain the current swollen levels of federal spending. As professed “populists,” their basic argument is that the people want the current level of spending and the people should not be denied.

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The Keynesians themselves create the problem by leaving out the price system. The hallmark of crackpot economics is an analysis that somehow leaves out prices, and talks only about such aggregates as income, spending, and employment.

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The Moynihan thesis of the cause of the problem is closer to the mark: the famous insight of three decades ago that the black family was increasingly fatherless, and that therefore such values as respect for person and property were in danger of disappearing. Three decades later, the black family is in far worse shape, and the white family isn't doing too well, either. But even if the Moynihan thesis is part of the problem, what can be done about it? Families cannot be forced together. A

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But the roots of the current medical crisis go back much further than the 1950s and medical insurance. Government intervention into medicine began much earlier, with a watershed in 1910 when the much celebrated Flexner Report changed the face of American medicine. Abraham Flexner, an unemployed former owner of a prep school in Kentucky, and sporting neither a medical degree nor any other advanced degree, was commissioned by the Carnegie Foundation to write a study of American medical education. Flexner's only qualification for this job was to be the brother of the powerful Dr. Simon Flexner, indeed a physician and head

of the Rockefeller Institute for Medical Research. Flexner's report was virtually written in advance by high officials of the American Medical Association, and its advice was quickly taken by every state in the Union.

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The result: every medical school and hospital was subjected to licensing by the state, which would turn the power to appoint licensing boards over to the state AMA. The state was supposed to, and did, put out of business all medical schools that were proprietary and profit-making, that admitted blacks and women, and that did not specialize in orthodox, "allopathic" medicine: particularly homeopaths, who were then a substantial part of the medical profession, and a respectable alternative to orthodox allopathy. Thus through the Flexner Report, the AMA was able to use government to cartelize the medical profession: to push the supply curve drastically to the left (literally half the medical schools in the country were put out of business by post-Flexner state governments), and thereby to raise medical and hospital prices and doctors' incomes.

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In all cases of cartels, the producers are able to replace consumers in their seats of power, and accordingly the medical establishment was now able to put competing therapies (e.g., homeopathy) out of business; to remove disliked competing groups from the supply of physicians (blacks, women, Jews); and to replace proprietary medical schools financed by student fees with university-based schools run by the faculty, and subsidized by foundations and wealthy donors.

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And so, our very real medical crisis has been the product of massive government intervention, state and federal, throughout the century; in particular, an artificial boosting of demand coupled with an artificial restriction of supply. The result has been accelerating high prices and deterioration of patient care. And next, socialized medicine could easily bring us to the vaunted medical status of the Soviet Union: everyone has the right to free medical care, but there is, in effect, no medicine and no care.

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The standard argument against direct democracy goes as follows: direct democracy was fine, and wonderful in colonial town meetings, where every person could familiarize himself with the issues, go to the local town hall, and vote directly on those issues. But alas, and alack!, the country got larger and much too populous for direct voting; for technological reasons, therefore, the voter has had to forego himself going to a meeting and voting on the issues of the day; he necessarily had to entrust his vote to his "representative." Well, technology rolls on, and direct voting has, for a long while, since the age of telephone and television, much less of the computer and emerging "interactive" television, been technologically feasible. Why, then, before Ross Perot, has no one pointed this out and advocated high-tech, electronic democracy? And why, when Perot has pointed this out, do all the elites react in dread and consternation, as if to the face of Medusa, or as vampires react to the cross? Could it be that—for all their prattle about "democracy," for all their ritualistic denunciation of voter "apathy" and call for voter participation—that more participation is precisely what the elites don't want?

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Could it be that what the political class: politicians, bureaucrats, and intellectual and media apologists for the system, really want is more sheep voting merely to ratify the continuance and expansion of the current system, of the Demopublican and Republicrat parties, of phony choices between Tweedledum and Tweedledumber?

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The only possible argument against direct democracy, now that the technological argument is obsolete, is that the public's choices would be wrong. But in that case: it would follow directly that the public shouldn't vote at all, since if the public is not to be allowed to vote on issues that affect their lives, why should they be allowed to vote for the people who will make those very decisions: for the beloved President, the Congress, etc.? Perhaps this logic is the reason that the hysterical opponents of the electronic town hall confine themselves to smear terms; since to make this argument at all would condemn them to scorn and irrelevance.

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Furthermore, making such an argument ignores the vital point: that the decisions of the parasitic bipartisan political class that has run this country for decades have been so abysmal, and recognized to be so abysmal by the public, that almost any change from this miasma and gridlock would be an improvement. Hence—to cite a poll myself—the recent sentiment of 80 percent of the American public that radical change in the system is necessary, and hence the willingness to embrace Ross Perot as agent of such a change.

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The Clinton administration will bring the younger “activist” left-Keynesians to the fore, including the aforesaid Reich, Robert Shapiro of Washington's Progressive Policy Institute, and what might be called the “Wall Street Left,” including the venerable Felix Rohatyn of Lazard Freres, Robert Rubin of Goldman, Sachs, and Roger Altman of the Blackstone Group. We can therefore expect a raft of government measures that will further cripple and distort the market economy. From leftwing groups will come “social” affirmative action-type and environmental regulations that will impose further costs and wreck productivity, particularly of smaller business. Reich and the Wall Street Left will micro-manage the economy into further ailments and disease, while, in the macro-sphere, we can expect higher taxes on the rich in order to “reduce the deficit” while, at the same time, higher government spending will raise the deficit further. We

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The solution, then, is the euphemistically named “population control,” which in essence is the use of government power to encourage, or compel, restrictions on the growth, or on the numbers, of people in existence. Logically, of course, the anti-human-being fanatics (for what is “the population” but an array of humans?) should advocate the murder by government planners of large numbers of existing people, especially in the allegedly overpopulated developing world (or, to use older term, Third World) countries. But something seems to hold them back; perhaps the charge of “racism” that might ensue. Their concentration, then, is on restricting the number of future births.

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In the palmy days of anti-population sentiment, cresting in the ZPG (Zero Population Growth) movement, the call was for an end to all population growth everywhere, including the U.S. Models based on simple extrapolation warned that by some fairly close date in the future, population growth would be such that there would be no room to stand upon the earth.

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This Official View turns out to be dead wrong. In the first place, we must realize the depth of hatred of Americans for what was called “internal taxation” (in contrast to an “external tax” such as a tariff). Internal taxes meant that the hated tax man would be in your face and on your property, searching, examining your records and your life, and looting and destroying. The most hated tax imposed by the British had been the Stamp Tax of 1765, on all internal documents and transactions; if the British had kept this detested tax, the American Revolution would have occurred a decade earlier, and enjoyed far greater support than it eventually received. Americans, furthermore, had inherited hatred of the excise tax from the British opposition; for two centuries, excise taxes in Britain, in particular the hated tax on cider, had provoked riots and demonstrations upholding the slogan, “liberty, property, and no excise!” To the average American, the federal government’s assumption of the power to impose excise taxes did not look very different from the levies of the British crown. The main distortion of the Official View of the Whiskey Rebellion was its alleged confinement to four counties of western Pennsylvania. From recent research, we now know that no one paid the tax on whiskey throughout the American “back-country”; that is, the frontier areas of Maryland, Virginia, North and South Carolina, Georgia, and the entire state of Kentucky. President Washington and Secretary Hamilton chose to make a fuss about Western Pennsylvania precisely because in that region there was cadre of wealthy officials who were willing to collect taxes. Such a cadre did not even exist in the other areas of the American frontier; there was no fuss or violence against tax collectors in Kentucky and the rest of the back-country because there was no one willing to be a tax collector.

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The whiskey tax was particularly hated in the back-country because whiskey production and distilling were widespread; whiskey was not only a home product for most farmers, it was often used as a money, as a medium of exchange for transactions. Furthermore, in keeping with Hamilton’s program, the tax bore more heavily on the smaller distilleries. As a result, many large distilleries supported the tax as a means of crippling their smaller and more numerous competitors. Western Pennsylvania, then, was only the tip of the iceberg. The point is that, in all the other back-country areas, the whiskey tax was never paid. Opposition to the federal excise tax program was one of the causes of the emerging Democrat-Republican Party, and of the Jeffersonian “Revolution” of 1800. Indeed, one of the accomplishments of the first Jefferson term as president was to repeal the entire Federalist excise tax program. In Kentucky, whiskey tax delinquents only paid up when it was clear that the tax itself was going to be repealed. Rather than the whiskey tax rebellion being localized and swiftly put down, the true story turns out to be very different. The entire American back-country was gripped by a non-violent, civil disobedient refusal to pay the hated tax on whiskey. No local juries could be found to convict tax delinquents. The Whiskey Rebellion was actually widespread and successful, for it eventually forced the federal government to repeal the excise tax.

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Except during the War of 1812, the federal government never again dared to impose an internal excise tax, until the North transformed the American Constitution by centralizing the nation during the War Between the States. One of the evil fruits of this war was the permanent federal “sin” tax on liquor and tobacco, to say nothing of the federal income tax, an abomination and a tyranny even more oppressive than an excise. Why didn’t previous historians know about this widespread non-violent rebellion? Because both sides engaged in an “open conspiracy” to cover up the facts. Obviously, the rebels didn’t want to call a lot of attention to their being in a state of illegality.

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Washington, Hamilton, and the Cabinet covered up the extent of the revolution because they didn’t want to advertise the extent of their failure. They knew very well that if they tried to enforce, or send an army into, the rest of the back-country, they would have failed. Kentucky and perhaps the other areas would have seceded from the Union then and there. Both contemporary sides were happy to cover up the truth, and historians fell for the deception. The Whiskey Rebellion, then, considered properly, was a victory for liberty and property rather than for federal taxation. Perhaps this lesson will inspire a later generation of American taxpayers who are so harried and downtrodden as to make the whiskey or stamp taxes of old seem like Paradise.

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More interesting were billionaires Trump and Rockefeller. Speaking from his own lofty financial perch, Donald Trump unctuously declared of Milken’s salary, “you can be happy on a lot less money,” going on to express his “amazement” that his former employers, the Wall Street firm of Drexel Burnham Lambert “would allow someone to benefit that greatly.” Well, it should be easy enough to clear up Mr. Trump’s alleged befuddlement. We would use economic jargon and say that the payment was justified by Mr. Milken’s “marginal value product” to the firm, or simply say that Milken was clearly worth it, otherwise Drexel Burnham would not have happily continued the arrangement from 1975 until this year.

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In fact, Mr. Milken was worth it because he has been an extraordinarily creative financial innovator. During the 1960s, the existing corporate power elite, often running their corporations inefficiently—an elite virtually headed by David Rockefeller—saw their positions threatened by takeover bids, in which outside financial interests bid for stockholder support against their own inept managerial elites.

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The exiting corporate elites turned—as usual—for aid and bailout to the federal government, which obligingly passed the Williams Act (named for the New Jersey Senator who was later sent to jail in the Abscam affair) in 1967. Before the Williams Act, takeover bids could occur quickly and silently, with little hassle. The 1967 Act, however, gravely crippled takeover bids by decreeing that if a financial group amassed more than 5 percent of the stock of a corporation, it would have to stop, publicly announce its intent to arrange a takeover bid, and then

wait for a certain time period before it could proceed on its plans. What Milken did was to resurrect and make flourish the takeover bid concept through the issue of high-yield bonds (the “leveraged buy-out”). The new takeover process enraged the Rockefeller-type corporate elite, and enriched both Mr. Milken and his employers, who had the sound business sense to hire Milken on commission, and to keep the commission going despite the wrath of the Establishment. In the process Drexel Burnham grew from a small, third-tier investment firm to one of the giants of Wall Street.

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The Establishment was bitter for many reasons. The big banks who were tied in with the existing, inefficient corporate elites, found that the upstart takeover groups could make an end run around the banks by floating high-yield bonds on the open market. The competition also proved inconvenient for firms who issue and trade in blue-chip, but low-yield, bonds; these firms soon persuaded their allies in the Establishment media to sneeringly refer to their high-yield competition as “junk” bonds. People like Michael Milken perform a vitally important economic function for the economy and for consumers, in addition to profiting themselves. One would think that economists and writers allegedly in favor of the free market would readily grasp this fact. In this case, such entrepreneurs aid the process of shifting the ownership and control of capital from inefficient to more efficient and productive hands—a process which is great for everyone, except, of course, for the inefficient Old Guard elites whose proclaimed devotion to the free markets does not stop them from using the coercion of the federal government to try to resist or crush their efficient competitors.

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David Rockefeller’s quotation about Milken is remarkably revealing: “Such an extraordinary income inevitably raises questions as to whether there isn’t something unbalanced in the way our financial system is working.” How does Rockefeller have the brass to denounce high incomes? Ludwig von Mises solved the question years ago by pointing out that men of great inherited wealth, men who get their income from capital or capital gains, have favored the progressive income tax, because they don’t want new competitors rising up who make their money on personal wage or salary incomes. People like Rockefeller or Trump are not appalled, quite obviously, at high incomes per se; what appalls them is making money the old-fashioned way, i.e., by high personal wages or salaries. In other words, through labor income.

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And yes, Mr. Rockefeller, this whole Milken affair, in fact, the entire reign of terror that the Department of Justice and the Securities and Exchange Commission have been conducting for the last several years in Wall Street, raises a lot of questions about the workings of our political as well as our financial system. It raises grave questions about the imbalance of political power enjoyed by our existing financial and corporate elites, power that can persuade the coercive arm of the federal government to repress, cripple, and even jail people whose only “crime” is to make money by facilitating the transfer of capital from less to more efficient hands. When creative and productive businessmen are harassed and jailed while rapists, muggers, and murderers go free, there is something very wrong indeed.

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We all know, for example, that “mercantilism,” the economic system of Western Europe from the sixteenth through the eighteenth centuries, was a system of Big Government, of high taxes, large bureaucracy, and massive controls of trade and industry. But what we tend to ignore is that the point of many of these controls was to tax and restrict consumers and most merchants and manufacturers in order to grant monopolies, cartels, and subsidies to favored groups.

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A common form of sale of privilege, especially hated by the public, was “tax farming.” Here, the king would, in effect, “privatize” the collection of taxes by selling, “farming out,” the right to collect taxes in the kingdom for a given number of years. Think about it: how would we like it if, for example, the federal government abandoned the IRS, and sold, or farmed out, the right to collect income taxes for a certain number of years to, say, IBM or General Dynamics? Do we want taxes to be collected with the efficiency of private enterprise? Considering that IBM or General Dynamics would have paid handsomely in advance for the privilege, these firms would have the economic incentive to be ruthless in collecting taxes. Can you imagine how much we would hate these corporations? We then have an idea of how much the general public hated the tax farmers, who did not even enjoy the mystique of sovereignty or kingship in the minds of the masses.

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In our enthusiasms for privatization, by the way, we should stop and think whether we would want certain government functions to be privatized, and conducted efficiently. Would it really have been better, for example, if the Nazis had farmed out Auschwitz or Belsen to Krupp or I.G. Farben?

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Unfortunately, we started catching up to Europe during the Civil War. During that terrible fratricidal conflict, the Lincoln administration, seeing that the Democratic party in Congress was decimated by the secession of the Southern states, seized the opportunity to push the program of statism and Big Government that the Republican Party, and its predecessor, the Whigs, had long cherished.

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For we must realize that the Democratic party, throughout the nineteenth century, was the party of laissez-faire, the party of separation of the government, and especially the federal government, from the economy and from virtually everything else. The Whig-Republican party was the party of the “American System,” of the partnership of government and business. Under cover of the Civil War, then, the Lincoln administration pushed through the following radical economic changes: a high protective tariff on imports; high federal excise taxes on liquor and tobacco (which they regarded as “sin taxes”); massive subsidies to newly established transcontinental railroads, in money per mile of construction and in enormous grants of land—all this fueled by a system of naked corruption; federal income tax; the abolition of the gold standard and the issue of irredeemable fiat money (“greenbacks”) to pay for the war effort; and a quasi-nationalization of the previous relatively free banking system, in the form of the National Banking System established in acts of 1863 and 1864.

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In this way, the system of minimal government, free trade, no excise taxes, a gold standard, and more or less free banking of the 1840s and 1850s was replaced by its opposite. And these changes were largely permanent. The tariffs and excise taxes remained; the orgy of subsidies to uneconomic and overbuilt transcontinental railroads was ended only with their collapse in the Panic of 1873, but the effects lingered on in the secular decline of the railroads during the twentieth century. It took a Supreme Court decision to declare the income tax unconstitutional (later reversed by the 16th Amendment); it took fourteen years after the end of the war to return to the gold standard.

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And we were never able to shed the National Banking System, in which a few “national banks” chartered by the federal government were the only banks permitted to issue notes. All the private, state-chartered banks, had to keep deposits with the national banks permitting them to pyramid inflationary credit on top of those national banks. The national banks kept their reserves in government bonds, which they inflated on top of. The chief architect of this system was Jay Cooke, long-time financial patron of the corrupt career of Republican Ohio politician Salmon P. Chase. When Chase became Secretary of the Treasury under Lincoln, he promptly appointed his patron Cooke monopoly underwriter of all government bonds issued during the war. Cooke, who became a multimillionaire investment banker from this monopoly grant and became dubbed “the Tycoon,” added greatly to his boodle by lobbying for the National Banking Act, which provided a built-in market for his bonds, since the national banks could inflate credit by multiple amounts on top of the bonds.

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The National Banking Act, by design, was a halfway house to central banking, and by the time of the Progressive Era after the turn of the twentieth century, the failings of the system enabled the Establishment to push through the Federal Reserve System as part of the general system of neomercantilism, cartelization, and partnership of government and industry, imposed in that period. The Progressive Era, from 1900 through World War I, reimposed the income tax, federal, state, and local government regulations and cartels, central banking, and finally a totally collectivist “partnership” economy during the war. The stage was set for the statist system we know all too well.

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We should realize that the war against the car did not begin with the discovery of pollution. Hatred of the private automobile has been endemic among left-liberals for decades. It first surfaced in the disproportionate hysteria over what seemed to be a minor esthetic complaint: tailfins on Cadillacs in the 1950s. The amount of ink and energy expended on attacking the horrors of tailfins was prodigious. But it soon emerged that the left-liberal complaint against automobiles had little to do either with tailfins or pollution. What they hate, with a purple passion, is the private car as a deeply individualistic, comfortable, and even luxurious mode of transportation.

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In contrast to the railroad, the automobile liberated Americans from the collectivist tyranny of mass transit: of being forced to rub elbows with a “cross-section of democracy” on bus or train, of being dominated by fixed timetables and fixed terminals. Instead, the private automobile made each individual “King of the Road”; he could ride wherever and whenever he wanted, with no compulsion to clear it with his neighbors or his “community.”

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And furthermore, the driver and car-owner could perform all these miracles in comfort and luxury, in an ambiance far more pleasurable than in jostling his fellow “democrats” for hours at a time.

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Not really. There is no question that the new Thatcher “community charge” was a bold and fascinating experiment. Local government councils, in many cases havens of the left-wing Labour Party, have been engaging in runaway spending in recent years. As in the case of American local governments, basic local revenue in great Britain has been derived from the property tax (“rates” in Britain) which are levied proportionately on the value of property.

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Whereas in the United States, conservative economists tend to hail proportionate taxation (especially on incomes) as ideal and “neutral” to the market, the Thatcherites have apparently understood the fallacy of this position. On the market, people do not pay for goods and services in proportion to their incomes. David Rockefeller does not have to pay \$1,000 for a loaf of bread for which the rest of us pay \$1.50. On the contrary, on the market there is a strong tendency for a good to be priced the same throughout the market; one good, one price. It would be far more neutral to the market, indeed, for everyone to pay, not the same tax in proportion to his income, but the same tax as everyone else, period. Everyone’s tax should therefore be equal. Furthermore, since democracy is based on the concept of one man or woman, one vote, it would seem no more than fitting to have a principle of one man, one tax. Equal voting, equal taxation.

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Unfortunately, the local tax case is characteristic of the Thatcher regime. Thatcherism is all too similar to Reaganism: free-market rhetoric masking statist content. While Thatcher has engaged in some privatization, the percentage of government spending and taxation to GNP has increased over the course of her regime, and monetary inflation has now led to price inflation. Basic discontent, then, has risen, and the increase in local tax levels has come as the vital last straw. It seems to me that a minimum criterion for a regime receiving the accolade of “pro-free-market” would require it to cut total spending, cut overall tax rates, and revenues, and put a stop to its own inflationary creation of money. Even by this surely modest yardstick, no British or American administration in decades has come close to qualifying. _____

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Price deflation on the free market has been a particular victim of deflation-phobia, blamed for depression, contraction in business activity, and unemployment. There are three possible causes for such deflation. In the first place, increased productivity and supply of goods will tend to lower prices on the free market. And this indeed is the general record of the Industrial Revolution in the West since the mid-eighteenth century. But rather than a problem to be dreaded and combatted, falling prices through increased production is a wonderful long-run tendency of untrammelled capitalism. The trend of the Industrial Revolution in the West was falling prices, which spread an increased standard of living to every person; falling costs, which maintained general profitability of business; and stable monetary wage rates—which reflected steadily increasing real wages in terms of purchasing power.

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This is a process to be hailed and welcomed rather than to be stamped out. Unfortunately, the inflationary fiat money world since World War II has made us forget this home truth, and inured us to a dangerously inflationary economic horizon.

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A second cause of price deflation in a free economy is in response to a general desire to “hoard” money which causes people’s stock of cash balances to have higher real value in terms of purchasing power. Even economists who accept the legitimacy of the first type of deflation react with horror to the second, and call for government to print money rapidly to prevent it. But what’s wrong with people desiring higher real cash balances, and why should this desire of consumers on the free market be thwarted while others are satisfied? The market, with its perceptive entrepreneurs and free price system, is precisely geared to allow rapid adjustments to any changes in consumer valuations.

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Any “unemployment” of resources results from a failure of people to adjust to the new conditions, by insisting on excessively high real prices or wage rates. Such failures will be quickly corrected if the market is allowed freedom to adapt—that is, if government and unions do not intervene to delay and cripple the adjustment process.

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A third form of market-driven price deflation stems from a contraction of bank credit during recessions or bank runs. Even economists who accept the first and second types of deflation balk at this one, indicting the process as being monetary and external to the market.

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But they overlook a key point: that contraction of bank credit is always a healthy reaction to previous inflationary bank credit intervention in the market. Contractionary calls upon the banks to redeem their swollen

liabilities in cash is precisely the way in which the market and consumers can reassert control over the banking system and force it to become sound and non-inflationary. A market-driven credit contraction speeds up the recovery process and helps to wash out unsound loans and unsound banks.

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Well, to paraphrase the great philosopher Etienne Gilson on natural law, Austrian cycle theory always survives to bury its enemies. In contrast to conventional wisdom, from Keynesian to monetarist to eclectic, Austrian theory has recently triumphed over its host of detractors in the following ways: 1. The perpetual boom of the '80s. As the 1980s went on, the Conventional Wisdom (CW) trumpeted that recessions were a thing of the dead and unlamented past. Here was a new era, of perpetual prosperity. Wise governmental fiscal and monetary policies, combined with structural changes such as the age of the computer and global capital markets, have made sure that we never have a recession again, that 1981–82 was the Last Recession. I have long asserted that the best “leading indicator” of a recession is when the CW has started proclaiming the end of the business cycle and perpetual prosperity. Sure enough, here we are, and, as Austrians point out, the bigger and the longer the boom, the greater and deeper will tend to be the recession necessary to wash out the distortions and malinvestment of the inflationary boom, brought on by bank credit expansion. 2. The end of inflation. During the great boom of the '80s, the CW also proclaimed that inflation was a thing of the past. It was over, licked. Again: wise government monetary and fiscal policies, coupled with structural economic changes, and “efficient markets,” insured that inflation was finished. And yet, inflation, which never really disappeared, is back in full force, and is even stronger now, in the depths of recession, than it was during most of the boom—a sure sign that not only is inflation still with us, but that it is going to pose a severe and accelerating problem as soon as recovery occurs. 3. (A corollary of one and two.) They forgot about inflationary recession. Inflation has persisted in every post-World War II recession since 1973–74, and indeed really began in the 1957–58 recession, after a couple of years of recovery. Yet everyone—and that means everyone including all wings of Establishment economics, and financial writers and forecasters—forgets all about the new reality of inflationary recession (also called “stagflation”), and writes and talks as if the choice in the coming months is always between inflation or recession.

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4. The average person knows when we're in a recession long before economists do. Establishment economists, mired in their methodology of statistical correlation based on precise dating of cycle peaks and troughs, take a very long time to decide the precise month of the peak—in the current recession, July 1990. It took almost a year after that point before economists deigned to tell us what we already all knew: that we were in a big recession. 5. The average person knows we're in a recession long after the economists have proclaimed “recovery.” Here we have a failing among economists far less excusable than methodological error. For hardly were we told, at long last, that we were in a recession, when the Establishment hastened to tell us that recovery was already under way. In a spectacular mistake, Establishment economists, professionally and politically bedded, as any Administration is, to Pollyanna optimism, hastened to assure us that the recession was over by the beginning of the third quarter of 1991. When

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6. Once a recession has taken hold, the government cannot inflate out of it; government can only delay recovery, not hasten it. This is a vital truth of Austrian economics that has been absorbed by virtually no one. Once a recession is underway, Keynesian-monetarist type stimulation: cheap money, accelerating the money supply, etc., can only make things worse. But look at what has happened to such alleged anti-inflation “hawks” as Alan Greenspan and the Cleveland Fed: as soon as the recession took hold, and even though inflation is now worse than it has been in years, they have all thrown over their alleged anti-inflation principles and have been cutting interest rates like mad, trying rashly and vainly to hype the sick horse with another shot of inflationary stimulus. 7. Tax cuts are good in a recession, or any other time. Students of human folly can only stand in wonder at the Keynesian, one of whose traditional proposals was for tax cuts during recession, suddenly adopting a conservative, monetarist stance. During this recession, Keynesians declare that “yes, well, tax cuts are good in theory (?) but they won’t help us out of recession, because of inevitable lag in the results of fiscal policy.” The complaint is that the cuts will only take effect after a recovery (they hope) has already begun. Well, so what?

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The S & L industry is no free-market industry. It was virtually created, cartelized, and subsidized by the federal government. Formerly the small “building and loan” industry in the 1920s, the thrifts were totally transformed into the government-created and cartelized S & L industry by legislation of the early New Deal. The industry was organized under Federal Home Loan Banks and governed by a Federal Home Loan Board, which cartelized the industry, poured in reserves, and inflated the nation’s money supply by generating subsidized cheap credit and mortgages to the nation’s housing and real-estate industry.

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Greenspan’s real qualification is that he can be trusted never to rock the Establishment’s boat. He has long positioned himself in the very middle of the economic spectrum. He is, like most other long-time Republican economists, a conservative Keynesian, which in these days is almost indistinguishable from the liberal Keynesians in the Democratic camp. In fact, his views are virtually the same as Paul Volcker, also a conservative Keynesian. Which means that he wants moderate deficits and tax increases, and will loudly worry about inflation as he pours on increases in the money supply.

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There is one thing, however, that makes Greenspan unique, and that sets him off from his Establishment buddies. And that is that he is a follower of Ayn Rand, and therefore “philosophically” believes in laissez-faire and even the gold standard. But as the New York Times and other important media hastened to assure us, Alan only believes in laissez-faire “on the high philosophical level.” In practice, in the policies he advocates, he is a centrist like everyone else because he is a “pragmatist.” As an alleged “laissez-faire pragmatist,” at no time in his prominent 20-year career in politics has he ever advocated anything that even remotely smacks of laissez-faire, or even any approach toward it. For Greenspan, laissez-faire is not a lodestar, a standard, and a guide by which to set one’s course; instead, it is simply a curiosity kept in the closet, totally divorced from his concrete policy conclusions. Thus, Greenspan is only in favor of the gold standard if all conditions are right: if the budget

is balanced, trade is free, inflation is licked, everyone has the right philosophy, etc. In the same way, he might say he only favors free trade if all conditions are right: if the budget is balanced, unions are weak, we have a gold standard, the right philosophy, etc. In short, never are one's "high philosophical principles" applied to one's actions. It becomes almost piquant for the Establishment to have this man in its camp.

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Alan is a long-time member of the famed Trilateral Commission, the Rockefeller-dominated pinnacle of the financial-political power elite in this country. And as he assumes his post as head of the Fed, he leaves his honored place on the board of directors of J.P. Morgan & Co. and Morgan Guaranty Trust. Yes, the Establishment has good reason to sleep soundly with Greenspan at our monetary helm. And as icing on the cake, they know that Greenspan's "philosophical" Randianism will undoubtedly fool many free-market advocates into thinking that a champion of their cause now perches high in the seats of power.

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Fluctuating fiat moneys, as the world has discovered, once again since 1971, are unsatisfactory. They cripple the advantages of international money and virtually return the world to barter. They fail to provide the check against inflation by governments and central banks once supplied by the stern necessity of redeeming their monetary issues in gold.

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What the world has failed to grasp is that there is one thing much worse than fluctuating fiat moneys: and that is fiat money where governments try to fix the exchange rates. For, as in the case of any price control, governments will invariably fix their rates either above or below the free-market rate. Whichever route they take, government fixing will create undesirable consequences, will cause unnecessary monetary crises, and, in the long run, will end up in ignominious failure. One crucial point is that government fixing of exchange rates will inevitably set "Gresham's Law" to work: that is, the money artificially undervalued by the government (set at a price too low by the government) will tend to disappear from the market ("a shortage"), while money overvalued by government (price set too high) will tend to pour into circulation and constitute a "surplus."

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So what could be "unfair" about the free-market price? One common protectionist charge is that it is "unfair" for an American firm to compete with, say, a Taiwanese firm which needs to pay only one-half the wages of the American competitor. The U.S. government is called upon to step in and "equalize" the wage rates by imposing an equivalent tariff upon the Taiwanese. But does this mean that consumers can never patronize low-cost firms because it is "unfair" for them to have lower costs than inefficient competitors? This is the same argument that would be used by a New York firm trying to cripple its North Carolina competitor. What the protectionists don't bother to explain is why U.S. wage rates are so much higher than Taiwan. They are not imposed by Providence. Wage rates are high in the U.S. because American employers have bid these rates up. Like all other prices on the market, wage rates are determined by supply and demand, and the increased demand by U.S. employers has bid wages up. What determines this demand? The "marginal productivity" of labor. The

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Thus, the problem faced by American employers is not really with the “cheap labor” in Taiwan, because “expensive labor” in the U.S. is precisely the result of the bidding for scarce labor by U.S. employers. The problem faced by less efficient U.S. textile or auto firms is not so much cheap labor in Taiwan or Japan, but the fact that other U.S. industries are efficient enough to afford it, because they bid wages that high in the first place.

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So, by imposing protective tariffs and quotas to save, bail out, and keep in place less efficient U.S. textile or auto or microchip firms, the protectionists are not only injuring the American consumer. They are also harming efficient U.S. firms and industries, which are prevented from employing resources now locked into incompetent firms, and who could otherwise be able to expand and sell their efficient products at home and abroad.

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But if selling below costs is such a powerful weapon, why isn't it ever pursued by business firms within a country? Our first response to this charge is, once again, to keep our eye on consumers in general and on American consumers in particular. Why should it be a matter of complaint when consumers so clearly benefit? Suppose, for example, that Sony is willing to injure American competitors by selling TV sets to Americans for a penny apiece. Shouldn't we rejoice at such an absurd policy of suffering severe losses by subsidizing us, the American consumers? And shouldn't our response be: “Come on, Sony, subsidize us some more!” As far as consumers are concerned, the more “dumping” that takes place, the better. But what of the poor American TV firms, whose sales will suffer so long as Sony is willing to virtually give their sets away? Well, surely, the sensible policy for RCA, Zenith, etc. would be to hold back production and sales until Sony drives itself into bankruptcy. But suppose that the worst happens, and RCA, Zenith, etc. are themselves driven into bankruptcy by the Sony price war? Well, in that case, we the consumers will still be better off, since the plants of the bankrupt firms, which would still be in existence, would be picked up for a song at auction, and the American buyers at auction would be able to enter the TV business and outcompete Sony because they now enjoy far lower capital costs.

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For decades, indeed, opponents of the free market have claimed that many businesses gained their powerful status on the market by what is called “predatory price-cutting,” that is, by driving their smaller competitors into bankruptcy by selling their goods below cost, and then reaping the reward of their unfair methods by raising their prices and thereby charging “monopoly prices” to the consumers. The claim is that while consumers may gain in the short run by price wars, “dumping,” and selling below costs, they lose in the long run from the alleged monopoly. But, as we have seen, economic theory shows that this would be a mug's game, losing money for the “dumping” firms, and never really achieving a monopoly price. And sure enough, historical investigation has not turned up a single case where predatory pricing, when tried, was successful, and there are actually very few cases where it has even been tried.

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Another charge claims that Japanese or other foreign firms can afford to engage in dumping because their governments are willing to subsidize their losses. But again, we should still welcome such an absurd policy. If the Japanese government is really willing to waste scarce resources subsidizing American purchases of Sony's, so much the better! Their policy would be just as self-defeating as if the losses were private.

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There is yet another problem with the charge of "dumping," even when it is made by economists or other alleged "experts" sitting on impartial tariff commissions and government bureaus. There is no way whatever that outside observers, be they economists, businessmen, or other experts, can decide what some other firm's "costs" may be. "Costs" are not objective entities that can be gauged or measured. Costs are subjective to the businessman himself, and they vary continually, depending on the businessman's time horizon or the stage of production or selling process he happens to be dealing with at any given time.

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If authentic free trade ever looms on the policy horizon, there'll be one sure way to tell. The government/media/big-business complex will oppose it tooth and nail. We'll see a string of op-eds "warning" about the imminent return of the nineteenth century. Media pundits and academics will raise all the old canards against the free market, that it's exploitative and anarchic without government "coordination." The Establishment would react to instituting true free trade about as enthusiastically as it would to repealing the income tax.

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In truth, the bipartisan Establishment's trumpeting of "free trade" since World War II fosters the opposite of genuine freedom of exchange. The Establishment's goals and tactics have been consistently those of free trade's traditional enemy, "mercantilism"—the system imposed by the nation-states of sixteenth to eighteenth century Europe. President Bush's infamous trip to Japan was only one instance: trade policy as a continuing system of maneuverings to try to force other countries to purchase more American exports. Whereas genuine free traders look at free markets and trade, domestic or international, from the point of view of the consumer (that is, all of us), the mercantilist, of the sixteenth century or today, looks at trade from the point of view of the power elite, big business in league with the government.

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Genuine free traders consider exports a means of paying for imports, in the same way that goods in general are produced in order to be sold to consumers. But the mercantilists want to privilege the government business elite at the expense of all consumers, be they domestic or foreign.

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In negotiations with Japan, for example, be they conducted by Reagan or Bush or Clinton, the point is to force Japan to buy more American products, for which the American government will graciously if reluctantly permit

the Japanese to sell their products to American consumers. Imports are the price government pays to get other nations to accept our exports.

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The answer is simple: the market has not been really free. In particular, in South Africa, the major center of world diamond production, there has been no free enterprise in diamond mining. The government long ago nationalized all diamond mines, and anyone who finds a diamond mine on his property discovers that the mine immediately becomes government property. The South African government then licenses mine operators who lease the mines from the government and, it so happened, that lo and behold!, the only licensees turned out to be either DeBeers itself or other firms who were willing to play ball with the DeBeers cartel. In short: the international diamond cartel was only maintained and has only prospered because it was enforced by the South African government. And enforced to the hilt: for there were severe sanctions against any independent miners and merchants who tried to produce “illegal” diamonds, even though they were mined on what used to be private property. The South African government has invested considerable resources in vessels that constantly patrol the coast, firing on and apprehending the supposedly pernicious diamond “smugglers.”

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Back in the pre-Gorbachev era, it was announced that Russia had discovered considerable diamond resources. For a while, there was fear among DeBeers and the cartelists that the Russians would break the international diamond cartel by selling in the open market abroad. Never fear, however. The Soviet government, as a professional monopolist itself, was happy to cut a deal with DeBeers and receive an allocation of their own quota of diamonds to sell to the CSO.

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But now the CSO and DeBeers are in trouble. The problem is not only the recession; the very structure of the cartel is at stake, with the problem centering on the African country of Angola. Not that the communist government (or formerly communist, but now quasicommunist, government) refuses to cooperate with the cartel. It always has. The problem is threefold. First, even though the Angolan civil war is over, the results have left the government powerless to control most of the country. Second, the end of the war has given independent wildcatters access to the Cuango River in northern Angola, a territory rich in diamonds. And third, the African drought has dried up the Cuango along with other rivers, leaving the rich alluvial diamond deposits in the beds and on the banks of the Cuango accessible to the eager prospectors.

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The Rockefeller interest and other Western Big Oil companies have had intimate ties with the absolute royalties of Kuwait and Saudi Arabia ever since the 1930s. During that decade and World War II, King Ibn Saud of Saudi Arabia granted a monopoly concession on all oil under his domain to the Rockefeller-controlled Aramco, while the \$30 million in royalty payments for the concession was paid by the U.S. taxpayer.

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The Rockefeller-influenced U.S. Export-Import Bank obligingly paid another \$25 million to Ibn Saud to construct a pleasure railroad from his main palace, and President Roosevelt made a secret appropriation out of war funds of \$165 million to Aramco for pipeline construction across Saudi Arabia. Furthermore, the U.S. Army was obligingly assigned to build an airfield and military base at Dhahran, near the Aramco Oilfields, after which the multi-million dollar base was turned over, gratis, to Ibn Saud.

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It is true that Aramco was gradually “nationalized” by the Saudi monarchy during the 1970s, but that amounts merely to a shift in the terms of this cozy partnership: over half of Saudi oil is still turned over to the old Aramco consortium as management corporation for sale to the outside world. Plus Rockefeller’s Mobil Oil, in addition to being a key part of Aramco, is engaged in two huge joint ventures with the Saudi government: an oil refinery and a petrochemical complex costing more than \$1 billion each.

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Oil pipelines and refineries have to be constructed, and Standard Oil of California (now Chevron), part of Aramco, brought in its longtime associate, Bechtel, from the beginning in Saudi Arabia to perform construction. The well-connected Bechtel (which has provided cabinet secretaries George Schultz and Casper Weinberger to the federal government) is now busily building Jubail, a new \$20 billion industrial city on the Persian Gulf, as well as several other large projects in Saudi Arabia.

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As for Kuwait, its emir granted a monopoly oil concession to Kuwait Oil Co., a partnership of Gulf Oil and British Petroleum, in the 1930s, and by now Kuwait’s immensely wealthy ruling Sabah family owns a large chunk of British Petroleum, and also keeps enormous and most welcome deposits at Rockefeller-oriented Chase Manhattan and Citibank.

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Iraq, on the other hand, has long been a rogue oil country, in the sense of being outside the Rockefeller-Wall Street ambit. Thus, when the crisis struck on August 2, the big Wall Street banks, including Chase and Citibank, told reporters that they had virtually no loans outstanding, nor deposits owed, to Iraq. Hence, it may well be that Mr. Bush’s war is an oil war all right, but not in the sense of a heroic battle on behalf of cheap oil for the American consumer. George Bush, before he ascended to the vice presidency, was a member of the executive committee of David Rockefeller’s powerful Trilateral Commission. Mr.

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Bush’s own oil exploration company, Zapata, was funded by the Rockefeller family. So this Oil War may instead be a less-than-noble effort on behalf of Rockefeller control of Middle East.