DO WE WANT FREE ENTERPRISE?

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A VOLUNTARY ORGANIZATION

FOREWORD

"WHAT'S THE USE OF TALKING TO OURSELVES? How are you going to reach the masses, those who *need* sound ideas? To whom are you sending material of this sort? Just to businessmen?"

So run the questions when some useful or enlightened statement is distributed among ourselves, that is, among businessmen. Somehow we have come to assume that *we* have a monopoly on economic virtue, that our own thinking is sound, and that it is only others who need enlightenment.

In our get-togethers, meeting in sincere attempts to save our country, we usually aim at the impossible: *How to spread our "wisdom" among the "masses."* Little, if any, thought is given to the one thing we can accomplish: *How to improve ourselves and our own thinking.* The idea that we aren't all-wise, if indeed we are wise at all, seldom strikes us.

Oh, yes, those of us who have succeeded at our enterprises are wise in our specialties. But it does not follow that we are wise in the broad aspects of the economic system in which we operate our enterprises.

The very idea of "educating the masses" is inconsistent with the ideals of freedom and individualism to which we give lip service. Who are "the masses"? Can the term be more appropriately applied to others than to ourselves? We are all *individuals* differing in qualities and abilities. We all share a basic human nature capable of self-development. If this be not true then the ideal of freedom is a fanciful myth.

But this ideal is not fanciful, nor is its economic phase, free competitive enterprise. These *are* attainable. They are attainable if we quit regarding those we would convert as masses or classes. They are attainable if we recognize the individual as the fountainhead of good, of energy, of all that is creative. They are attainable if we acknowledge where attainment must begin: *with ourselves.*

Free competitive enterprise is something we have loudly acclaimed. We have praised it, however, not so much because we have understood it or even because we have wanted to practice it but more because it has seemed to us the antithesis of dreaded socialism. Many of us are not socialists, *knowingly.*

Only now and then, among all of us in America, is there a skilled advocate of free competitive enterprise. Most of us are left speechless in a debate with a socialist, a radical labor leader or any other ardent collectivist. We sputter—we do not explain. We can neither speak our subject well nor do we practice it too well. For in the practical world we have inspired about as many anti-enterprise institutions as have our political opponents.

Not only is confession justified and good for our souls but the meekness it inspires, that is, the teachableness, can save us. For we can learn free competitive enterprise as we have learned our enterprises. We can master the principles of freedom better than our opponents have learned the jargon of their systems, for the principles of freedom are superior!

Early in 1943 the officers and members of the Los Angeles Chamber of Commerce, perceiving these basic reasons for our troubles, *seeing faults in ourselves instead of exclusively in others,* began a program of self-education in free competitive enterprise.

The program was simple. We formed a group of businessmen, big executives and little fellows, whoever was interested. A chairman, to serve as a moderator, was chosen. A member of our staff served as business manager. The group selected a day, most convenient to the majority, to meet once a week at luncheon time. We then selected an economist, a free competitive enterpriser at heart, skilled in his profession, reputed for his courage, his fairness and his broad understanding of business, of government, of labor, of agriculture and of consumer interests. At each session the economist lectured on some phase of free competitive enterprise.

After this first section was under way, after the participants got the spirit of this self-educational venture, there arose a demand for other sections. We put five of them in operation, terminating them in early July to accommodate the absences normal to July and August.

In the fall of 1943 we began these enterprise sections on even a larger scale. We are to continue because there is a demand for continuance on the part of participants and others who have been told of the advantages and of the interest in this type of program.

It is interesting to observe the advantages that have come to us. Our views on many things have been changed and prejudices have been removed. Events and issues of the day take on new meanings. Socialist doctrines and why they won't work are more easily perceived. We have clearer ideas for rebuttal and with clear ideas come words to express our thoughts. We even feel that we are conditioning ourselves for that level of business statesmanship which is to become so essential in the days and years immediately ahead. *We have come to the conclusion that the best contribution we can make to the thinking in our country is to improve our own thinking.*

While this program is edifying to us in Los Angeles its advantages are relatively slight unless there is an acceptance of it elsewhere, in communities both large and small.

We have contended that a program such as ours, modified in some respects to be sure, could be carried on in small as well as in large communities. To give this point a practical demonstration we collaborated with the Olympia, Washington, Chamber of Commerce by offering that organization the services of our Economic Counsel, Dr. V. O. Watts.

In Olympia a group, greatly varied occupationally, agreed to meet every week day at luncheon time for a period of three weeks. The experiment was a greater success than we had expected.

The impressions of the Olympia participants are recorded as the concluding chapter in this issue of THE ECONOMIC SENTINEL.

Outlines of the fourteen lectures delivered in Olympia by Dr. Watts are printed herein not as a pattern to be followed by other economists who may perform similar tasks elsewhere, but rather to share their value and their sturdy philosophy with others, and to portray the general theme at which we are aiming.

Some people have remarked to me that programs such as these are difficult because there is a shortage of able economists, that economists, for the most part, are addicted to the socialistic doctrines. It is true of late that many publicized statements of certain economists have been leftist in tone. Nevertheless, among the nation's several thousand professional economists are a great number of free competitive enterprisers hoping for the day when they may have a hearing.

This is not a thought fathered by a wish. To sample the field we recently wrote a personal letter to some six hundred economists in which we described our experiment and inquired of their interest. We hit an amazing "jack-pot" in the form of encouraging replies. And we only scratched the surface in our exploration.

This type of program is now being nationally sponsored. The United States Chamber of Commerce is giving to it a leadership which a local organization cannot supply. However, we shall continue to provide such cooperation and assistance as we can to all who make inquiry. The publication of these lecture outlines is part of our contribution to what we hope will prove to be a rebirth of the spirit and faith which made America prosperous, strong and free.

Also, we take this means of expressing our gratitude to the Olympia Chamber of Commerce and to its officers: Stanley Starr, its president, and F. W. Mathias, its secretary, for their able and loyal effort in this cooperative enterprise.

—LEONARD E. READ, *General Manager*
Los Angeles Chamber of Commerce

January 15, 1944.

CONTENTS

I. DO WE REALLY WANT FREE ENTERPRISE?

According to a 1942 *Fortune* poll of public opinion, 40 per cent of American business executives believe that socialism would be a good thing for the nation as a whole and another 13 per cent are undecided on the question.

According to the same poll 11 per cent of business executives believe they personally would gain under socialism, 32 per cent believe it would make no difference to them and 8 per cent are undecided. Altogether, 51 per cent of business executives, according to this poll, are not certain but that socialism would be a good thing for them personally.

Friends of Enterprise Are Divided

Said one newspaperman to another, "I'd fall dead if I found a businessman who wasn't in favor of free enterprise." Replied the other, "I'd fall dead if I found a businessman who really wanted it."

1. A city chamber of commerce opposes restrictions which neighboring towns sometimes place on deliveries of merchandise by city merchants and truckers. Yet the same organization is likely to help erect similar barriers against out-of-state or out-of-town enterprise which might compete with its own industries or merchants.

2. Businessmen dislike restrictive policies of farmers and labor unions. Yet many of them say that free competition among themselves would be ruinous. So they lobby for measures to restrict business competition and to legalize price-fixing by government or by their own organizations.

3. Chambers of commerce frequently join the clamor for uneconomic local projects of the State or Federal government on the ground that "Other places are getting theirs; why shouldn't we get ours?" Such "chamber of commerce socialism" leads to increased tax burdens which correspondingly restrict markets and jobs in free enterprise.

4. Many prewar restrictions on business were imposed with the support of certain business interests hoping thereby to win an advantage at the expense of competitors or taxpayers.

   The wage-hour law, for example, was supported by certain New England manufacturers who hoped thereby to restrict competition of southern producers. Other restrictive measures were passed with the help of legislators whose votes were obtained in return for government favors to their business constituents in the form of higher prices for silver or costly public works projects.

5. Farmers denounce trade union efforts to restrict output, reduce hours or limit entry to a particular trade. Yet they themselves vote for crop restriction or prorate schemes, demand restrictions on oleomargarine, and in the name of pest control restrict out-of-state competition.

6. Wage earners denounce business monopolies, and rightly. Yet many of them support certain monopolistic policies of trade unions, not only for themselves in their own occupations but for all workers. Some of these labor practices do as much to restrict output and raise costs of living as any capital monopolies this nation has ever seen.

Recent corrosions of economic liberty in the United States are not due to the efforts of a few communists or fascists. Instead they chiefly come from the fact that so many of us care only about our own liberties and are indifferent or even hostile to possession of similar liberties by others of our fellow citizens. In fact, for a momentary gain in higher prices, higher wage rates or government favors, many of us are willing even to sell our own freedom.

The United States would not last long if the people of New England and the Middle West would not help to repel an invader from the Pacific Coast, or if the people of the Pacific Coast were indifferent to the fate of the Atlantic Coast.

Likewise, freedom from bureaucratic tyranny soon vanishes if no group will fight for any freedom except its own.

To win and preserve freedom of enterprise businessmen must help establish and maintain for their competitors, their customers and their workers, the same liberties that they seek for themselves.

Do We Know What Free Enterprise Means?

Almost everyone seems to favor "freedom," or "free enterprise." Even Hitler said he was for free enterprise—provided it was properly regulated to protect the public interest.

But what is "proper regulation"? Does it include:

1. price maintenance by government or by trade associations?

2. wage-maintenance by government or by the closed shop, closed union, secondary boycott and "hot cargo"?

3. crop restriction, the prorate, and "surplus commodity" purchases?

4. protective tariffs?

5. government deficits and spending to "prime the pump," maintain employment, increase purchasing power, or to serve as the "balance wheel" of the national economy?

6. taxes on undistributed profits, on high incomes or on idle funds in order to force money into circulation?

These and related questions trouble even people who are most vigorous in proclaiming their support of free enterprise. They ask if such "controls" are not necessary to make free enterprise work.

Differences of opinion on such questions do not arise chiefly from differences in patriotism or good intentions, but from differences in knowledge and understanding. Therefore, they cannot be overcome by name-calling, prohibitions on "lobbying" or suppression of "pressure groups."

Instead, the need is for an understanding of what is a good economic system and how it may be built. Except as this understanding grows we shall accomplish little by repeating to ourselves and others, "Free enterprise—it's wonderful!"

Production Comes First

The primary test of an economic system is not the degree of liberty but its efficiency in supplying the needs and wants of its members.

Victory in war and progress in peace depend on production.

1. In wartime the United States has become "the arsenal of democracy," turning out more airplanes, ships and other war supplies than all the rest of the world together. This is because our economic system encouraged the building of greater resources of equipment, skill, managerial ability and cooperative spirit than those of any other nation. Only as other nations develop similar productive efficiency and capacity can they successfully challenge us.

2. In peacetime our high levels of production have brought about

   more sanitary living conditions,
   elimination of child labor,
   abolishment of back-breaking drudgery,
   spread of literacy and enlightenment,
   progress in science and art,
   growth of philanthropy,
   development of kindliness and goodwill.

Progress for the masses can come about only as mass efficiency in production makes available mass supplies of the tools and opportunities necessary for better ways of living.

> Economic statesmanship means promoting "more goods and more services for more people."

Mass unemployment must be abolished if our nation is to be strong in war and prosperous in peace.

Can this not be done without inflation, waste and war?

Class conflict weakens and impoverishes the nation. It grows out of the theory that one class can make real and permanent gains at the expense of another class.

According to a 1943 Gallup poll 51 per cent of American businessmen and 73 per cent of our wage earners believe that election of one political party rather than the other would help business and hurt labor. If business is productive, no policy could help business without helping labor. Do 51 per cent of American businessmen believe they are parasites on labor?

If producers believe they can prosper more by political activity than by increasing their efficiency in production, they will turn from economic competition to politics.

Constructive political activity removes obstacles to useful enterprise so that people may go back to competition in production. Some of these obstacles may be private in origin; others may consist of unnecessary governmental restrictions.

Destructive political activity will aim at using government to restrict production in order to raise prices or to tax one class of producers for the benefit of another class.

A good economic system will develop and harness maximum energy for most efficient use in building a strong and prosperous people.

This implies that a people will take as its symbol, not the pig trough but the workbench, not a bed of ease but a field of opportunity for useful service.

"Pursuit of a Flying Goal"

The end of man is not self-indulgence, but achievement. We live and grow by effort, not by idleness.

Those who make happiness and idle contentment their goals should go to live among the South Sea Islanders. These primitive peoples, by all reports, are as happy as more civilized peoples, and they seem to get that way with much less effort.

Pleasures may help to guide us in certain choices, e.g., in food and drink. Pain helps us to avoid certain physical dangers. But the one who makes mere accumulation of pleasures and avoidance of pain his aim in life is like the traveller who travels only for the purpose of collecting signposts or avoiding rough roads.

Man is highly adaptable. He may find pleasure in many things. Civilized man, who has acquired vast opportunities for self-gratification, must learn to find pleasures in those things which maintain and promote his efficiency. He must learn temperance, balance, self-discipline. Otherwise he loses the efficiency which gives him great opportunity for enjoyment.

The living thread of human evolution is carried by those who learn to find their greatest satisfaction in striving and achieving. No one word or phrase can describe the highest, ultimate goals of human effort. As we progress our vision widens and our goal recedes. We strive for better health, more enlightenment, higher justice, greater kindliness. We acquire new wants and new activities, which in turn give rise to new powers, new opportunities and new ideals.

What kind of an economic system gives opportunity and encouragement to those individuals who make this flying goal their life's purpose? What system gives them opportunity and incentive to unite their efforts with others who possess similar ideals and purposes? Such a system makes a nation prosperous and strong. It is the kind of system we covet for our own country.

Life Is Competitive

War is merely an incident in the ceaseless struggle for survival among individuals and groups. We may hope and work for lasting peace. But will we soon remove the need for military strength to protect cooperative peoples against predatory individuals and bandit nations?

Whether or not war is eliminated, economic competition will remain. In fact, progress in eliminating war will depend on our ability to substitute higher forms of competition for it—as, for example, competition in production and trade. In this development America should lead the way.

The urge of people to multiply and their urge to develop and exercise their various abilities bring about competition for land, resources and markets. In war men try to win these by destroying their competitors. In peace they must win them by advances in arts of production and trade.

H. G. Wells remarks that Utopian reformers have usually ignored the endless variety of men, their endless gradation of quality "over which the hand of selection plays." In planning the society of the future, he says, we must keep in mind the necessity for competition in life "to determine who is to be pushed to the edge and who are to prevail and multiply." He continues,

> "Whatever we do, man will remain a competitive creature, and though moral and intellectual training may enlarge his conception of success and fortify him with refinements and consola-

> tions, no Utopia will ever save him completely from the emotional drama of struggle for exaltations and humiliations, from pride and prostration and shame. Man lives in success and failure just as inevitably as he lives in space and time."

Increasing efficiency is necessary to life and progress, both for individuals and groups.

This does not mean that the future lies with the arrogant, greedy, and grasping. On the contrary, it will fall more and more into the hands of the gentle—the "terrible meek."

"Blessed Are the Meek . . ."

The meek are the cooperative people. They are not conceited or arrogant, but instead are glad to learn. They learn from the words and experience of others. They learn from observing their own experience with men and nature. They adjust their conduct in the light of their knowledge. Thus they become better teammates, or workmates.

They learn to think in terms of long-run goals, e.g.,

1. in terms of their future welfare, as well as temporary gain;
2. in terms of their nation and fellowmen, as well as themselves, their trade, or class;
3. in terms of their children, and their children's children, as well as their own generation.

And these "shall inherit the earth." In fact, they have been doing so for a long time. They still have a long way to go before winning complete possession. But that is only because opportunities for development inherent in man are so great that it takes a long time to realize them. This makes the future a challenge and an opportunity for those who are worthy to carry the torch of human progress.

II. AMERICA'S GREATEST ASSET

Why must the United States guard her borders to keep out people who want to share our prosperity and our opportunities for good living? Certain other nations have to guard their borders to keep their people at home.

With 7 per cent of the world's population and 6 per cent of the land area, the United States possesses

80 per cent of the world's automobiles,
50 per cent of the world's telephones,
33 per cent of the world's railway mileage,
30 per cent of the world's highways,
60 per cent of the world's life insurance policies.

We consumed before the war

75 per cent of the world's silk,
50 per cent of the world's coffee,
60 per cent of the world's rubber.

The American people had 1 radio for every 3 people as against 1 for 90 persons in Russia. New York City used 140 gallons of water per day, per person; Parisians used 47 and Londoners 43.

And no one in his right senses believes that America's 60 richest families owned any large share of our 29,000,000 cars and radios, drank most of the coffee or wore most of the silk.

Why are Americans so prosperous?

Why do we have the world's greatest navy and how do we produce more airplanes than all the rest of the world together?

Other People Work Hard and Skillfully

Is it because of our rich natural resources?

Not entirely. Europe has as great resources as the United States. Yet our levels of production and income are far above those of European nations.

The North American Indians had the same resources as we have today, but they did not build a great civilization.

Do we work harder or more skillfully than other people?

People of many nations work as hard on the average as do we. Some work harder than we do. They show skill and ingenuity in using their equipment. Some of them (e.g., the Swiss, Germans and English) are highly inventive, and all nations have ready access to our scientific and engineering discoveries. Yet no other nation has achieved American levels of production and prosperity.

Bases of National Greatness

1. Freedom of trade

The United States has been one of the world's greatest free trade areas. One language, absence of customs barriers between states and towns, efficiency in transportation and suppression of monopoly and banditry made for free exchange of commodities and services over half a continent.

This permitted more efficient use of our resources through specialization of production in different areas: cotton in the South, wheat and corn in the Middle West, flour in Minneapolis, automobiles in Detroit, movies in California, potatoes in Maine, and oranges in Florida and California.

The people of Massachusetts used to produce their own wheat, flour, iron and many other things which they now buy mainly from other places. They have gained more from specializing in manufacturing, trade, finance, education, art and science than they could have done from trying to protect and preserve all the occupations necessary for self-sufficiency. The rest of the nation has likewise gained from this specialization and trade.

2. Equipment

American workers are better equipped with tools and machinery than workers of any other nation. This makes their average output higher and makes their labor command a higher price than in the case of workers in other nations.

From 1910 to 1930, for example, output per worker rose about 40 per cent in American agriculture and industry largely because of increased mechanization. This increased productivity enabled this nation to fight a costly war, make huge loans and gifts to foreign countries and yet by 1929 to raise the average buying power of our workers to 40 per cent above 1910 levels.

Capital for this mechanization of industry has been supplied by the thrift of those who have saved and invested their money instead of spending it on goods for their personal consumption. Investors made this choice in hope of being free to reap the fruits of their thrift and foresight.

3. Planning, promotion and management

United States leadership has specialized in the task of promoting mass prosperity.

On the other hand, Germany, more than any other nation, massed her national intelligence on military problems and built the world's most efficient army.

In certain other nations the ablest men went into government service or the church and built efficient bureaucracies or churches.

In the United States men of ability were most attracted by the opportunities in private enterprise. Consequently American business and industry have been noted throughout the world for efficiency of management.

4. Individual initiative

American habits of self-reliance kept the duties and costs of government at a minimum.

Taxes were low. Therefore, enterprising and inventive men and women could hope to reap most of the fruits of their efforts. They had corresponding incentive and opportunity for rapid development of industry through reinvested earnings.

Producers were comparatively free from bureaucratic red tape, restriction and delay imposed by government.

Private citizens were not, as in certain other nations, compelled in self-defense to spend a large share of their time and energies in political strife lest some person or party rob them of liberty, life or property. Instead, they could concentrate their energies on producing useful goods and services.

Why Enterprise Must Be Free

Our great industrial system was not built by a few supermen. It was built, instead, by millions of men and women, each trying to do a job better, each learning from others and each building on the work of others.

This was because we tolerated enterprise, pioneering, prospecting, experimentation and speculation more than did other nations.

Freedom from government restriction gave opportunity for initiative.

Class barriers were less important in the United States than in most nations, so that there was a more "open road to talent." Judging each man on his own merit encouraged merit and gave it outlets for usefulness.

The United States was less afflicted than most nations by restrictive private organizations of vested interests, such as cartels and restrictive labor unions. This meant greater opportunity for men and women with new ideas and better methods. (Our anti-trust laws helped in this regard.)

Mass industry requires mass intelligence to operate it as well as to build it.

No human being can make all the decisions necessary for the daily operation of even one automobile factory.

No small group of persons can make all the decisions necessary for running our complicated, modern economy.

Efficient production by modern methods requires continual adjustment of millions of working parts to one another.

The working parts of the American industrial machine include, besides many millions of machines,

60,000,000 workers and
130,000,000 consumers.

Every one of the workers is different from every other and each is constantly changing in abilities and interests. The same is true of consumers.

To maintain a good working adjustment among the working parts of this huge and complicated machine requires more intelligence and enterprise than is possessed by all the "experts" put together.

Each worker must help by searching out the line of work which he can do best and by studying how to do his job well.

Each consumer must help by budgeting his spending to get the most for his money.

Each saver and investor must help by selecting the best place for his savings.

"Were we directed from Washington when to sow and when to reap, we should soon want bread," said Thomas Jefferson.

Only where the masses of workers, consumers and investors are free to choose their jobs, make their own purchases and select their own investments can we get great industry and great prosperity.

Discipline May Increase Freedom

Freedom for enterprise, however, cannot include freedom for doing injury to others. Americans approve suppression of enterprise in peddling narcotics or obscenities. Piracy and slave trading are condemned.

Only when a nation uses its resources productively can it remain prosperous, strong and free. Those who use up their opportunities in wasteful conflict or misdirected effort will not long have freedom.

Sound policy restrains enterprise which clearly injures national efficiency and welfare.

Restraint of uneconomic activity is a result of discipline. Wisely disciplined groups expand at the expense of the undisciplined or poorly disciplined.

Methods for securing discipline necessary for efficiency are:

A. law, which is discipline administered by government;

B. morality, which is self-discipline.

A. Law Is Enforced by Coercion

In civilized societies government has a virtual monopoly of coercive authority, and most government action involves coercion or threat of coercion.

The coercion by government consists in the method by which government obtains funds (taxation), as well as in the exercise of police powers to enforce decrees. Government uses persuasion instead of coercion insofar as it tries to win public support by political speeches, education and propaganda. But even in these cases the costs of the campaigns are often met by taxes, which are coercive.

Because its coercive power over the individual is so great, many people mistakenly regard government as all-powerful. In fact, however, the effectiveness of government control is limited in several ways.

Limited Effectiveness of Coercion

1. Coercion is useful in repressing and restraining undesirable activity, but it is comparatively ineffective in stimulating enterprise. That is because coercion means use of force and fear.

   Fear depresses the higher nerve centers and thought processes. When sufficiently great it paralyzes action.

   At most it induces short-lived bursts of muscular activity. Repeated doses have diminishing effects and eventually produce anger and rebellion.

   Fear is especially ineffective in developing persistence, initiative, inventiveness and ambition. That is why slave labor is too inefficient for operating a highly industrialized society, which requires a high degree of enterprise, ingenuity and responsibility in its members.

2. Continued exercise of coercive authority demoralizes those who wield it.

   It breeds intolerance and arrogance, which make rulers insensitive to the interests and needs of the governed. Trading ideas with subordinates is necessary to wise and efficient leadership. But coercive power provides opportunity and practice in disregarding the opinions and wishes of those subject to this authority.

3. Red-tape, checks and balances, rules of evidence, bills of rights, periodic elections, representative assemblies and other safeguards

on the use of political power slow down government processes. They unfit government to manage competitive enterprises because of the necessity for quick decisions.

Yet these safeguards are necessary for democratic or representative governments. They reduce arbitrary use, or abuse, of government's coercive authority. They help counteract the tendency of coercionists to ignore the interests and sentiments of the people.*

What Government Should Do

1. Suppress violence

   This is the first duty of government. When it is well done producers are protected in the enjoyment of the fruits of their effort. Then private enterprise expands and the people prosper.

2. Repress forms of fraud and vice which are

   a. readily defined and detected;

   b. generally agreed to be undesirable, e.g., peddling narcotics.

   Under this heading comes government's work in setting standards of weights, measurement, sanitation and money. This requires coercion in suppressing competing standards.

   Conversely, governments, especially democratic governments, are ill-suited to deal with forms of fraud or vice which are *not* capable of precise definition, which are *not* easily detected, or which are *not* generally disapproved. Restraint of these types of undesirable conduct constitutes the realm of morality, good taste and reason. (See below.)

3. Manage enterprises requiring some degree of coercion, such as,

   a. operation of lighthouses, building roads and maintaining fire protection, which require coercion in collecting payments;

   b. public education, which requires coercion in financing it and in restricting opportunities for child labor;

   c. conservation measures looking to interests of future generations.

4. Provide for distressed citizens through tax funds that minimum of relief which cannot be provided by relatives, charity or any legitimate form of self help.

   If government-provided relief, however, is not to degenerate into a political tool for suppressing freedom it must be limited to the subsistence level and be administered by expert, nonpolitical agencies.

*In war time, when speed and secrecy are relatively more important, many of the democratic safeguards must be waived. This is especially noticeable in the military forces.

B. Morality Is Self-Discipline

The restraints of morality are self-disciplines. They are the most efficient forms of discipline but the most difficult to achieve.

They are developed by education, persuasion and example.

They help prevent vices or wastes like petty frauds and lying, which government could not detect or could detect only by excessive restraints on useful activities of its citizens.

They permit some degree of variation and selection in better ways of living. For example some dress fashions formerly considered immoral or in bad taste have proved to promote health and comfort. If they had been forbidden by law, as some of our Puritan ancestors might have wished, progress would have been more difficult.

They are necessary for enforcement of law and order.

Businessmen have a vital interest in helping to maintain and raise the nation's standards of morality.

1. The efficiency of labor is affected by standards of industriousness, honesty, sobriety.
2. Availability of capital is affected by standards of thrift.
3. Selling costs are affected by customer standards of honesty and fair dealing.
4. The character of business competition is affected by competitors' standards and by consumers' tastes.
5. National strength and security, which are essential for business, are in large part determined by these standards.

Businessmen may help set standards by

1. personal influence and example,
2. trade association efforts and
3. influence over educational and religious institutions.

Scope of Free Enterprise

Outside the fields where coercion is necessary and beyond the restrictions imposed by moral standards lies the field for free enterprise.

In a progressive society this field is constantly expanding in numberless directions as scientific advances, changing customs and changing tastes open new opportunities for enterprisers.

It is also subject to growing restriction by government and morals as experience shows that certain activities and forms of consumption are detrimental to individual and group efficiency.

For example, fire prevention is no longer left entirely to private enterprise as it once was.

Increasing restrictions of law and morality have been thrown about enterprise in alcoholic liquors.

AMERICA BECAME PROSPEROUS AND STRONG, NOT ONLY BECAUSE HER PEOPLE WERE FREE, BUT BECAUSE THEY USED THEIR FREEDOM WELL.

Disciplined Freedom

Within the field of free enterprise the individual is free to follow the dictates of self-interest as he sees them. This means that each individual is free to use his talents and resources in ways which he considers most advantageous. He may offer them to others on terms which seem satisfactory to him, whether others consider the bargain a good one or not.

Free enterprise is characterized, therefore, by:

1. individual enterprise and individual responsibility;

2. equality of opportunity;

3. competition;

   Competitive enterprise demands *sportsmanship,* which is a high type of moral standard, or self-discipline. The good sport, in business or play, welcomes strenuous competition. He keeps to the rules of the game even when he is losing and in process of being eliminated from the competition.

   The poor sport tries to restrict competition. When losing he tries to alter the rules or he reverts to lower forms of competition, e.g., to fraud or violence. Or he seeks to establish restrictions on winning competitors by monopolistic combinations or by government control.

   Raising standards of sportsmanship in business should be a chief activity of trade associations, schools, chambers of commerce and governments.

   Sometimes, however, these agencies fall under the control of the losers or poor sports, and are used to restrict the enterprise of more efficient producers.

4. free exchange, including:

a. freedom to bargain,
b. prices and rates of pay determined by demand and supply,
c. inequality of rewards for effort,
d. profits: (i) as incentives, (ii) as sources of capital and credit,
e. losses: as means of eliminating the inefficient.

Definition of Free Enterprise

Free enterprise means freedom for every individual to exert his utmost capacity in producing those commodities and services which he thinks other people want. It includes

a. freedom and equal opportunity for every person to choose where he will work and what he will do without asking the permission of any bureaucrat or paying tribute to any organization;
b. rewards determined by voluntary agreements in competitive markets;
c. protection by law and public opinion against predation, fraud and violence;
d. good sportsmanship on the part of participants, who will try to win by superior efficiency and service, not by racketeering, political favoritism, or monopolistic combinations.

Free enterprise is men and women working out their common destiny, not under the lash of coercive authority, but under the discipline of enlightened self-interest and moral responsibility.

III. BUSINESS — MAINSPRING OF FREE INDUSTRY

Money-making by businessmen is as necessary to a free society as vote-getting by politicians.

What Businessmen Are For

Under free enterprise the job of business* is to promote economic cooperation between wage earners, investors and customers. This job has several aspects.

1. Market study

   Businessmen *study* what buyers want and how the right goods may be produced at least cost and in the right proportions.

2. Promotion and investment

   They *persuade* producers to cooperate efficiently by working out agreements for dividing the product.

3. Selling

   They *persuade* customers to buy the products at prices sufficient to meet obligations to producers.

4. Accounting

   They *keep records* of their operations in terms of MONEY, which is the common measure of value and medium of exchange.

Businessmen cannot, like government officials, coerce, or compel, people to do things. Instead, they must rely on persuasion and on offers of money, goods and services in order to win the cooperation of other producers in getting things done.

This is why business enterprise involves so much advertising, bargaining, higgling and haggling.

How else can free people work out the terms and methods of their cooperation?

Socialists, communists, technocrats and other utopians build dream worlds in which people are supposed to cooperate without thought of personal gain, bringing their products to central warehouses and taking away what they need, with none of the bargaining, higgling and selling effort of modern business.

**Business* is here used in the sense in which we say that a successful farmer must be a good "businessman" as well as a good farmer.

In this sense business has to do primarily with money matters, trade and finance. Most of us have a certain amount of business to do in acquiring and spending money. Professional businessmen make their living attending to money matters—merchants, bankers, brokers, accountants, and so on. It is against business in this sense of money-making or "production for profit" that much criticism of free enterprise is directed. (Cf. T. Veblen, *The Theory of Business Enterprise.)*

But money-making business can be done away with only when people are:

A. all-wise and morally perfect, or

B. slaves to custom, or

C. slaves to a master class.

A. No Middlemen in Utopia

If everyone knew just what needed to be done and if everyone always found his greatest joy in doing just the right things, we should need no salesmen or promoters, no bargaining and higgling, no freedom for experimentation and no money measure of value.

1. There would be no need of prices, profits, wages, salaries, rent or interest to induce people to work, save, invest and lend.
2. We should always produce everything we needed in just the right proportions—never too much or too little of anything.
3. No one would ever need to be spurred on to do his best, either by lure of gain or fear of loss.
4. Competition would not be needed to select those best fitted for the more important tasks.

But this would be Utopia, or Heaven, not real life.

Real people need (1) *guidance* and (2) *motivation.*

1. They need indexes and measures of value—money, prices, wages, rent, interest, profits—to tell them:

   a. what consumers want; and
   b. in what proportions they want goods produced.

2. They need every possible incentive, particularly the motive of self-interest, to spur them on to do their best.

   (The usefulness of self-interest as a motive in economic cooperation depends on the kind of self in which one is interested. Creating selves which are better informed concerning (a) what their long-run welfare requires and (b) how to achieve it, is one way of promoting national progress.)

B. Slaves of Custom Give Way to Enterprisers

Certain primitive communities (e.g., Australian Bushmen) use little or no money and carry on little or no trading or business. They are dominated by custom and tradition in their work and by family or tribal communism in distributing the products.

Such people have only a few simple occupations.

Their scale of living is low.

These primitive peoples occupy relatively barren or inaccessible regions not yet demanded by more progressive and powerful neighbors.

C. Coercion Loses Out to Enterprise

Nazis, Fascists, Japanese "Sons of Heaven," Technocrats, Socialists and Communists propose that the masses be subjected to a master party, a master race or a master class.

The "ideal" of these coercionists is variously termed "Totalitarianism," "Collectivism," "Social Security" and "Authoritarianism."

Advantages of Coercion

1. Time and effort may be saved through eliminating all bargaining, higgling and salesmanship.

   This is necessary in military operations because of the importance of speed and secrecy. In peacetime industry this saving is offset by the delays arising from necessary safeguards on the use of coercive authority. (See above, pp. 11-12.)

2. Efficiency may be greater when all decisions are made by patriotic "experts."

   This advantage is more apparent than real, particularly in operating a highly industrialized society. (See above, pp. 9-10.)

Disadvantages of Coercion

1. Experts make mistakes.

   The greater the authority of the experts the more difficult are their tasks and the more costly their mistakes. This limits the efficiency of big business as well as big government.

2. Coercive authority demoralizes leadership.

   Power to compel obedience tends to generate arrogance. It closes the mind to new facts and opinions. It causes men to persevere in their errors and to waste more and more of their energies in combating growing resentment among their subjects. Few men can long resist this tendency.

3. Coercion represses initiative, ambition and enterprise.

   Modern industry requires mass intelligence and mass enterprise to get the economies of mass production. (See above, pp. 9-10.)

Economy of Hope vs. Economy of Fear

Business creates an economy of *hope.* It *lures* producers by offers of trade. For increased output it holds out *rewards* of fame and fortune.

> Business uses prices, profits, wages, interest and rent as traffic lights for coordinating the flow of production with the wants of consumers. It harnesses the ambition of producers, whether it be the ambition to promote personal welfare or family advancement. It makes men work with and for their fellows while they seek to fulfill their own desires. (See pp. 26, 149-153.)

Coercion is useful in repressing uneconomic activities. But as an instrument for inspiring cooperation it can create only an economy of *fear.* It *prods* producers with threats of injury or imprisonment. Which is more effective in getting efficiency, firing squads or profits? History makes plain the answer.

Democratic Governments Are Sensitive

Democracy is rule by the people.* Its strength lies in the opportunity which it provides for stimulating and utilizing the energies and abilities of *all* the people.

A democratic leader is *sensitive,* or *responsive,* to the desires and interests of those he governs. He is their *servant.*

Making government democratic, however, has always been difficult:

1. Government tends to rely on its coercive power.

   Its primary functions have been and are waging war, suppressing violence and fraud, and doing other things requiring a degree of compulsion in administering or financing them. Possessing these powers, government has less incentive to develop the arts of persuasion, which are the methods of democratic leadership.

2. Government is the biggest and most complicated institution in a modern nation.

   The average citizen can keep track only of a few of his government's activities. In case of a representative government he may vote occasionally on certain officers or policies. But altogether he

*Some persons use *democracy* to mean *mob rule,* that is, a government which is merely a rubber stamp for snap judgments of more or less tyrannical majorities.

According to *Webster's New International Dictionary* (second edition, unabridged), however, *democracy* is, "Government by the people; a form of government in which the supreme power is retained by the people and exercised either directly *(absolute,* or *pure, democracy)* or through a system of representation and delegated authority periodically renewed as in a constitutional representative government, or republic . . . SPECIFICALLY, AND COMMONLY IN MODERN USE, A *DEMOCRACY* IS A REPRESENTATIVE GOVERNMENT WHERE THERE IS EQUALITY OF RIGHTS WITHOUT HEREDITARY OR ARBITRARY DIFFERENCES IN RANK OR PRIVILEGE . . ."

Democracies have their defects, but so do other forms of government. Democracies do not last, but neither do other types of government.

May we not agree with Aristotle that all governments in practice are imperfect, but that democracy, as defined by *Webster's,* is usually the least corrupt?

> knows little of what government does and rarely gets a chance to express his opinion on what he does know about government policies. This provides opportunity for government bureaus to override or ignore popular interests and demands.

The ballot, right of petition, right of assemblage and right of free discussion help in making government more sensitive to the wishes of the people. They do not guarantee democracy, but they are useful instruments for promoting more democratic attitudes and policies in government.

When Voting Is Undemocratic

Our government, however, would not be more democratic if the employees in the city hall elected the mayor or if the Federal employees elected the President. It would not be more democratic if the policemen elected the judges and lawmakers, or if the firemen voted each time on whether or not they would answer the fire alarm. A democratic government serves the general citizenry. Its employees are the *servants* of the public, not the *masters*.

Similarly, for employees of a business to elect their managers and determine policies would not necessarily make business and industry more democratic. In practice it has usually made them less democratic by making them less responsive to wishes of consumers for whom the business is operated. Organized producers—farmers, business owners and wage earners—frequently vote to restrict output in order to raise prices for their services. This is no more democratic than for the city hall employees to increase the tax rates for the purpose of raising their salaries.

> However, when any necessary agent of production becomes scarcer and its price rises, those who hire that agent tend to treat it with more consideration. For example, as demand for labor increases employers and customers treat wage earners with more consideration.

Business Is Democratic

Competitive business enterprise is highly democratic because its leaders must rely solely on *persuasion* in promoting cooperation.

> They persuade workers by offers made in terms of wages, hours and working conditions in connection with particular jobs.
>
> They persuade investors by offers made in terms of interest, dividends and security of principal for particular investments.
>
> They persuade suppliers of materials by price offers.
>
> They persuade customers by offers of goods.

Businessmen cannot compel workers to work, investors to lend, or customers to buy under conditions of free, competitive enterprise.

In order to succeed they must offer what other people want. They must be highly sensitive to the desires and even the whims of those whom they serve—workers, investors, suppliers and customers.

For this reason competitive business organizations and other voluntary groups are usually more democratic than government.

Increasing freedom of competition for honest enterprise makes business more democratic by making it more efficient in serving the public.

IV. FREE ENTERPRISE AND FREE PRICES

Mass prosperity and *national greatness* require *mass production.*
Mass production requires *mass enterprise.*
Mass enterprise requires *business democracy.*
Business democracy requires *free exchange.*

Recipe for Revolution

To destroy a nation's prosperity and to overturn its economic and political institutions it is necessary only to create sufficient discontent among producers concerning the terms on which they exchange their services.

This discontent leads to

a. restriction of price competition and

b. inflation of currency and credit.

Restriction of price competition (including wage competition), whether through private organizations or through legislation, leads to:

1. restriction of output, strikes, shutdowns and class warfare;
2. mass unemployment and idle capacity (see below, pp. 94-95, 118-119);
3. popular demands for new government agencies to:

   protect the public against the greed of private monopolies;

   carry out restrictive, price-maintenance schemes on behalf of small producers and unorganized workers; and

   give jobs and relief to the unemployed.

Inflation of the currency or credit to finance a costly program of public works or military preparedness results in:

1. creating a supporting army of party workers and voters for the bureaucracy;
2. enabling government to buy support through judicious location of projects, through purchase of "surplus commodities," and through high-wage policies on public works; and
3. making the banking system and credit structure dependent on continuance of the restrictionist and inflationary policies.

These ingredients are sufficient for a complete political overturn.

> Conflicts between the various producer organizations, logrolling for new government projects, and pressure for new restrictions on competition bring representative institutions and methods into disrepute.
>
> Delays in legal procedures and unpopular decisions bring the courts into disrepute.
>
> Popular clamor grows for a disinterested head of state to protect the public against the greed of private pressure groups and to cut through the delays and red-tape of the bureaucracy.
>
> Mass unemployment, restricted opportunity for able young men, rising taxes and mounting debts create a crisis for which dictatorship seems the only solution.

The United States has tasted this revolution cake. In the spring and summer of 1933 we ate a sizable slice of it and we have continued nibbling at it ever since. Various other nations took much more of it than did we.

But the people of Germany swallowed the whole ugly mess.

Price Maintenance and Revolution in Germany

For two generations, or more, before Hitler's rise to power, price maintenance restrictions on competition had been destroying economic liberty and creating the chronic mass unemployment and discontent which gave the Nazis their opportunity.*

> Associations of producers, called "cartels," under government supervision, fixed prices of commodities. To maintain these prices they fixed quotas of production, limited output and repressed new enterprises which might undercut the vested interests.
>
> Wages were determined for a time by collective bargaining. Costly conflicts between the "irresistible forces" of trade unions and the "immovable bodies" of employers, however, finally led to government wage-fixing through labor courts and compulsory arbitration.
>
> Subsidies, tariffs, quotas, barter agreements, government loans and government commodity purchases controlled foreign trade.
>
> Widespread government ownership of many forms of business, including mines, theaters, pawnshops, meat-shops, warehouses, utilities and the railroads, still further reduced freedom of bargaining and increased price rigidities.
>
> Prices of government services (taxes and license fees) were high and rigid because of deficits on government enterprises and elaborate programs for public works and "social security."

*Cf. Frank Munk, *The Legacy of Nazism*, (Macmillan Co., 1943), Ch. V.

Agriculture was subjugated by government loans, marketing pools to buy "surpluses," cooperative producers' organizations to restrict supply, and government aid in converting grain fields to pasture lands.

A large and costly bureaucracy enforced the economic controls, administered the government enterprises, and sucked dry the sources of new capital.

The legislative bodies were split into numerous factions and blocs representing various conflicting interests, chiefly economic. The resulting log-rolling, class legislation and class conflicts brought representative institutions into public disrepute.

Rigidities of prices and wage rates prevented necessary adjustments between occupations and lines of production. When the worldwide depression of 1930 struck Germany, its producers were unable to make the adjustments of costs and prices necessary for recovery. Production and employment declined while producers quarreled over the terms of trade, that is, over prices and wage rates. This made many Germans ready to welcome the "strong man" who promised to stop the class conflicts and put people to work.

Similar conditions in Italy had prepared the way for Mussolini and his Fascists in 1922.

Scientific Looting

Nazism and Fascism took over industrial systems built by private enterprise and converted them to war purposes.

Totalitarianism, however, has proved less efficient than free enterprise both in peacetime trade and in wartime production.

1. With all her totalitarian trading tricks Germany increased her exports only 8 per cent in the years 1933 to 1938 inclusive, as against a 28 per cent increase in United Kingdom exports, and an 84 per cent increase in United States exports during the same period.

   American blast furnace production per worker in 1937 was 3½ times that of Germany, and in iron and steel products our output per worker was 4 times that of the German workers. In automobile production our advantage was 4 to 1, in radio sets 7 to 1, and in coal production 2 to 1.

2. Initial military successes of Germany were due to the fact that from 1935 to 1939 she spent twice as much on war production as the United Kingdom and France combined.

   At their best the totalitarians never have matched the per capita production of war materials which the United States and England have achieved with far less coercion and regimentation of their peoples.

Nazism and Fascism retained private *ownership,* lengthened hours of labor, stopped strikes and reduced trade union restrictions on employment and output.

They did not, however, restore freedom for private *enterprise.* For cartel and union restrictionism they substituted bureaucratic regimentation, so that producers were even less free than before to offer their goods and services to the highest bidders. Thus these systems reduced still further the opportunities and incentives for individual initiative.

By fostering a war psychology and by inflationary trickery and fraud, the totalitarians increased employment.

But instead of promoting mass thrift and investment they looted the nation for the war machine and its masters. And, instead of restoring economic flexibility and opportunity for private enterprise, they increased the rigidity of the price system and ordained for all producers the bureaucratic goosestep. This ossification of the national economy would have prevented Germany from winning world dominion in peacetime competition. It was useful only for one purpose —the blitzkrieg.

Economic Liberty Depends on Flexible Prices

"Adapt or die" is a law of life which applies to nations as well as to animal species. Progressive peoples must encourage change.

Oxcart and horse-and-buggy industries must give way to railroad, automobile and aircraft industries.

Handworkers must give way to machinists and machine operators. Millions of farm boys and girls must become factory workers, business workers and professional workers in towns and cities.

Contracts must be revised to distribute losses in depressions and gains in booms; methods must be improved to reduce costs; new economies must be effected to maintain or restore credit depleted by errors in investment.

How readily can such changes be made if they require consent of monopolistic organizations of producers or permission of government officials and boards?

If a nation is to have the benefits of mass enterprise, the changes incident to progress must be brought about chiefly by individuals freely making their own bargains and arrangements with one another as to what and how they shall produce and trade.

Wanted: Automatic Traffic Lights

If individuals are to choose their own occupations they must be given signs and signals so that they may know what occupations are most in demand relatively to supply.

They must also be given incentives, or rewards, to persuade them to follow the signals.

Prices for commodities and services provide both signals and incentives.

When demand for a commodity increases relatively to supply, the price rises, profits increase, demand for labor expands, and wages rise in that industry.

This increase in prices, profits and employment draws capital and labor into production of the scarce commodity.

Production increases until the price and income premiums in that industry disappear.

High prices also encourage consumers to economize scarce commodities and search for cheaper substitutes.

A decrease in demand, causing a decline in price, has the opposite effects. It leads to a decrease in output.

Monopoly and government price-fixing destroy freedom of exchange, freedom in production, and freedom in consumption.

Prices can be raised above the competitive level only by restricting the amount offered for sale.

Prices can be kept below the competitive level only by restricting the demand (rationing).

Either form of restriction limits individual opportunity to produce and consume.

Both types of restriction require coercion to make them effective.

Should Costs Determine Prices?

Producers often demand that government prevent prices from falling below "costs."

Wage-earners ask that wages be raised to keep pace with rising living costs.

Distributors ask for laws to enforce a certain markup to cover costs.

Manufacturers demand tariff duties to "equalize" costs as against foreign competitors. (See below, p. 80.)

Professional workers sometimes justify high charges on the ground that they are necessary to cover costs of training.

But first let us ask, "What costs should be used as a basis for price fixing?"

Should we take the costs of the less efficient, high-cost firms, in poor locations, with a small volume of business? In that case we encourage inefficiency.

Or should we take the costs of the more efficient, low-cost firms, with good locations and a large volume of business? In that case we are likely to put out of business certain producers whose efforts are needed to help meet demand.

Should we use as our guide, the costs of the shops catering to the "quality" trade, or those of the less pretentious shops serving the general public.

Only the free workings of demand and supply on price can give a quick and democratic answer to these questions.

Secondly, we must realize that a rise in prices causes a rise in costs.

1. A rise in prices for oranges raises the cost of land suitable for growing them. It raises the value of labor used in picking them. A fall in prices has the opposite effects. Therefore, when producers say their costs are high it may mean that demand has been high and profits good, resulting in a high markup of land values and other costs.

2. Price maintenance frequently stimulates competition in advertising, or "service." This raises costs and leaves producers no better off than before. However, consumers are likely to be worse off. They get less benefit from the advertising and "service" than they would have received from the lower prices which free price competition would have set.

3. Price maintenance which places prices above their competitive level reduces volume of sales and in this way often raises costs so that producers are no better off than before.

4. Raising one man's selling prices raises his customers' costs. This makes necessary an increase in their selling prices and leads to another increase in the first man's costs.

Attempts to guarantee general prosperity by guaranteeing producers a certain markup over costs are as futile as efforts to lift ourselves by the bootstraps.

Yet price cutting is sometimes uneconomic and destructive.

Controlling Cutthroat Competition

1. Discriminatory price cutting for the purpose of establishing a trade monopoly is subject to prosecution under state and federal anti-trust laws, as it should be.*

This does not mean that every producer who cuts prices below costs in order to drive a competitor out of business is guilty of "unfair competition." Sometimes there is room only for one producer in a local market, as, for example, in case of a newspaper in a small town. In that case, when two producers want the same market, "cut-throat competition" is the only way under free enterprise to decide who is to get it.

In case such competition is likely to establish a monopoly in a line vital to the community's prosperity, government may declare the industry a "public utility" and grant a franchise, or permit, to one party or the other. In return for this grant of monopoly the favored producer must submit to government regulation of his charges and methods of operation.

Such grants of monopoly and government intervention, however, should be kept to a minimum and used only as a last resort. They should be confined to "natural monopolies" in the production of services vital to the community's prosperity. That is because every extension of the public utility principle adds to the cost and complexity of government, increases economic rigidities, reduces the adaptability of the national economy, and retards progress in the industry so controlled. In most cases cut-throat competition leading to a small-scale local monopoly is less costly and less obnoxious than the government regulation necessary to prevent it.

On the other hand, cutthroat competition which may be permissible between moderate-sized business rivals should be outlawed when used in a discriminatory way by a widespread and powerful combination or concern. Then discriminatory price cutting becomes a means for establishing monopoly, not merely in a local market, but in a line of commerce or industry. Profits of monopoly in one area may be used to support discriminatory price cutting and establishment of monopoly elsewhere. Such price cutting is forbidden by the anti-trust laws of the United States and few persons wish to see this safeguard of competition removed.

The anti-trust restrictions on price cutting, however, are very different from the effects of the so-called "fair trade" laws and "unfair practices" acts. Instead of preventing growth of monopoly such laws restrict competition and legalize policies precisely similar to those of the monopolistic combinations which the anti-trusts laws are designed to prevent. (See below, pp. 89-95.)

*Price discrimination refers to price differences not accounted for by differences in grade, quality, quantity, production costs, selling costs or transportation costs. Even under this definition not all price discrimination should be a concern of government. Only when price discrimination is creating a monopoly in a given line of trade should it be outlawed.

2. Standards of quality should be enforced by government when such enforcement is necessary to protect health or prevent the grosser forms of fraud.

   Price maintenance, however, does little or nothing to eliminate unsanitary conditions, as, for example, in case of barbers or physicians, or to eliminate fraud, as in the case of drugs. It may even increase fraud by encouraging advertising of nonexistent or insignificant differences in quality. In such cases the fraud or unsanitary conditions should be attacked directly through setting of minimum standards, not through restriction of price competition.

   Furthermore, it should be recognized that raising minimum standards also raises minimum prices and reduces the quantity which consumers can buy. High quality is a fine thing, but of what use is it to the consumer who gets little or none of the goods because of their high prices?

3. Our main reliance for raising standards and reducing fraud must be education of producers and consumers, through schools, trade associations, chambers of commerce, "better business" bureaus and factual advertising by competitors.

   Competition for the patronage of informed consumers will reform or eliminate dishonest producers more quickly and effectively than government regulation. This does not mean that consumers must be educated to appreciate all of the technical details of the products they buy. Often it is enough that buyers and sellers learn to appreciate the value of a seller's reputation for fair dealing.

4. Exchange of information concerning costs and selling prices, together with education in cost accounting, helps to reduce that type of price cutting which sometimes results from ignorance on the part of producers.

   Producers who cut prices below cost because they do not know their own costs are not likely to do any great share of the business in any line because they tend rapidly to eliminate themselves. True, others may come in to take their places, but such producers, because of their inefficiency and inexperience, are a petty annoyance rather than a major business problem. In time of depression they are often blamed for a general decline in price levels which is due to far different causes.

5. In "sweated" lines the only real remedy for low wages is a change in the balance between the demand for and supply of labor.

   Workers employed in so-called "sweatshops" are typically those with little skill who do hand labor or work on simple machines. Often they are illiterate and foreign speaking, possessing only skills which are relatively abundant, e.g., skill in needle work.

Merely closing the sweatshops or passing minimum wage laws sends these workers into other employments even worse paid, or else reduces them to some form of dependency and beggary.

The real remedy lies in educating these wage earners for better paid work or encouraging investment of new capital in the industry to equip the workers with better machinery and to bid up the price of their labor.

6. Every producer must be prepared to meet and win out against a certain amount of "dirty competition" without resorting to similar unfair practices himself.

   The controls needed to prevent all unfair competition would be so costly and restrictive as to stop all enterprise and progress.

7. Organized price maintenance aggravates business depressions.

   Price levels decline during a business depression, but this decline is a *symptom* of declining spending power, not the *cause*. When buyers have less money to spend, a policy of price maintenance merely reduces the number of units of goods and services which people can buy. It therefore aggravates the decline in output and employment, which is the real evil of business depressions. (See below, pp. 94-95, 118-119.)

Protect the Price Cutter

Freedom to cut prices as well as to raise them is necessary to ensure economic efficiency and progress.

1. By cutting prices the more efficient firm grows at the expense of the less efficient. The more progressive firm impels others to adopt the better methods or go out of business. Thus the general public gets cheaper goods and increased buying power.

2. Cutting prices of goods which are relatively abundant brings about contraction in these lines. At the same time it encourages expansion in other lines by:

   a. reducing costs of production for suppliers of the scarcer goods,

   b. giving buyers more money to spend on them.

   Thus it helps preserve or restore such economic balance between various lines of production as provides the maximum quantity of satisfactions from the productive resources available.

3. Price differentials between commodities or services in the same line often or usually are accompanied by differences in quality of goods or extent of services, or both. This permits closer adaptation of commodities and services to the varied wants of consumers.

   For example, there is about as much difference between haircuts as between the various makes of automobiles, and it is just as unreasonable to enforce the same prices in the one case as the other.

4. Price cutting is an economical and efficient method of introducing goods and services of new concerns which cannot give their customers certain satisfactions offered by long-established firms, such as the prestige of well-known labels or assurance of time-honored reputations.

   From the consumers' standpoint this is an advantageous and economical method of promoting a new business.

   From the competitors' standpoint it is no more costly than an effective advertising campaign. However, since price cutting is often less costly than an effective advertising campaign, it enables new enterprises to get started with less initial capital and less promotional expense than would otherwise be necessary.

   Thus it favors smaller business units and promotes competition necessary for preserving free enterprise.

Free exchange and free prices open the door to more efficient methods, to the economies of mass production and to the opportunities of new industrial and commercial frontiers.

When our pioneering forefathers struck out across the seas, into the forests and over the plains and mountains, they accepted whatever their own efforts and Dame Fortune brought them.

They gave up the security and comforts of the stay-at-homes in the hope that someday they or their children might be more free, more secure and more prosperous.

They braved dangers, learned new ways of making a living, and subsisted on a scale far below that now considered minimum for health and decency.

What would have been the history of America had no one been permitted to subject himself to such risks and privations? Suppose parents, labor organizations and governments had said, "No one shall go exploring or prospecting until he can be guaranteed 30, 40, or 50 cents per hour. No homesteader shall work more than 40 hours per week. No one shall plow new land and raise a crop until all producers are guaranteed parity prices."

Would our frontiers have been pushed westward along a 2,500-mile front at an average rate of 10 miles per year for 250 or 300 years? Would we at the same time have been building the world's richest nation and caring for a population increasing by leaps and bounds?

It is not necessary to turn back the clock and subject ourselves to all the hardships and poverty endured by our ancestors.

But if we want liberty for our people to explore life's opportunities and to prospect for better ways of living we must let them succeed or fail as the results of their own bargains and their own efforts.

> Only as producers agree to work together for what they can earn in free competitive markets can a people develop the industry and enterprise which build national prosperity and greatness.
>
> It may be our fond wish that everyone should live in peace and plenty. But it won't be achieved by limiting investment, work and production in order to maintain prices, profits and wage rates.

Economic progress requires freedom for each producer to expand output.

This freedom is of little use, however, unless producers are also free to trade their surpluses.

This means they must be free to arrange and accept terms of exchange, prices and rates of pay, which satisfy those who are making the trades—themselves.

Do we really want such freedom of enterprise and exchange? Or do we prefer some kind of "parity program"?

V. WHAT PRICE PARITY?

In the Agricultural Adjustment Acts of 1933 and 1938, Congress decreed that the United States Government shall establish "parity" prices for farm products and "parity" incomes for farmers.

To this end the Secretary of Agriculture was given power to

control acreage planted and harvested,
establish marketing quotas,
levy processing taxes on farm products,
buy or sell farm products,
regulate and control the commodity exchanges,
issue licenses for buying and selling farm products,
inspect books and operations of farmers,
make loans on farm products,
make cash payments to farmers who obey orders.

Under this authority a steadily growing bureaucracy has spread the tentacles of its control over American agriculture and related industries at a cost of from one to three billion dollars per annum to American taxpayers and consumers.

> The courts have ruled that the Federal Government may fine a man for growing wheat on his own land to feed to his own chickens.
>
> Government purchases and holdings of "surplus" commodities give it control over prices and prosperity for every farmer in the United States and even in foreign nations.
>
> These purchases also affect living costs for every American consumer as well as for many citizens of foreign countries.
>
> Government payments to farmers for *not* producing deprive taxpayers of liberty as consumers, rob other producers of opportunity to produce the goods which these taxpayers otherwise would have bought, and compel consumers to pay for *reducing* the supply of things they may want to buy.
>
> Fines and imprisonment are provided for those who dare to impede the execution of the government's agricultural program.

The corrosion of economic liberty in the United States under this program raises the question, "What price parity for agriculture?"

The Parity Formula

Parity prices are defined by law as prices which will give farm commodities a purchasing power, with respect to articles that farmers buy, equivalent to the purchasing power of such farm commodities in the base period.

"Basic commodities" to be especially benefited by this program are defined by law as cotton, wheat, corn, tobacco and rice.

> This list does not include meats, which yield to farmers nearly as much money as all the so-called "basic" commodities put together.
>
> It does not include dairy products, which yield as much as any three "basic" commodities together.
>
> It does not include poultry, which is as important as tobacco and rice combined.
>
> It does not include fruits or vegetables, which likewise are more important than most of the crops officially declared to be "basic." Remedy of these omissions provides a golden opportunity for further expansion of the parity program.

"Parity" income is that average farm income which has the same relation to non-farm incomes as existed in the base period.

The *base period* for all commodities except tobacco is August 1909 to July 1914. For tobacco the base period is August 1919 to July 1929.

> "Wholesale prices of farm products in the United States were relatively higher in 1909-1914 than in any period of equal length before, at least in a century." (Dr. Joseph S. Davis, Director of the Food Research Institute, Stanford University.)
>
> In the decade 1919-1929 average tobacco prices, however, were double those of 1909-1914 and were far above average prices for any previous decade in our history.

The parity program for agriculture, therefore, assumes that the relation between farming and non-farm occupations at some time in the past was more equitable than it was later. This is a backward-looking theory, but it has been popular with farmers as long as the ideal or "base" period selected was a boom time for farmers.

Farmers Work Harder and Get Less

Why should not government restore boom-time price levels for farm commodities?

> "For generations farmers have worked longer hours under harder conditions than city people. Their opportunities for amusement have been less varied. They have enjoyed less of the latest comforts and luxuries. They have little or no chance to become really wealthy. No one ever becomes a multimillionaire in farming.
>
> "Yet without the farmer we should all starve. In fact, all wealth comes ultimately from the extractive industries, chief of which is farming.

"Farming requires as much intelligence, training and experience as any other occupation. Why should it not be paid accordingly?

"The farmer is the backbone of the nation—economically, politically and morally. Yet the superior attractions and opportunities of city life and work are constantly depleting farm ranks. The very foundations of our nation are threatened by this drift."

These arguments again raise the question, "What are prices for?"

Why should coal sell for one cent per pound while diamonds cost many thousands of dollars per ounce?

Why should any man be paid more than another?

Why should a Babe Ruth get as much as the President of the United States and many times the pay of able and hard-working farmers, carpenters, schoolteachers and so on?

Why should a bit of clever ventriloquism be paid so much more than the same time and energy put into baking bread?

Why should a good farmer be paid more than a poor farmer?

Trumpet Calls for Producers

Differences in prices, salaries, wages, profits and so on, tell producers what things are scarce and what things are abundant relatively to consumer wants. They also encourage producers to increase output of the more desirable goods as compared with the less desirable.

High average prices and high incomes in certain lines relatively to others act as trumpet calls to urge producers into lines where they are most needed.

Relatively low prices and incomes in any line warn producers to improve their products and methods or to look for other employments.

Adjustments to changing conditions of demand and supply are essential in a prosperous and progressive nation. They are essential to national life and growth.

Horse-and-buggy industries must contract or disappear as new lines arise and expand.

How could the United States have met the challenge of Japan and Germany if it had clung to the industries and methods of 1909-1914 while other countries forged ahead?

A free society can make these changes only through the aid of free exchange and a free price system.

Vocational guidance experts and educators may help producers

> find work best suited to their talents. But they cannot tell producers what things are most in need of doing without the aid of a free price system.

In a free economy buyers bid up the prices of goods and services which they want increased *more than others.* It is to the producers of these things that they offer higher rewards.

Progress Increases Demand for Town Labor

As a nation prospers the demand for town workers increases faster than the demand for farm workers.

> In 1790 about 90 per cent of our people were engaged in agriculture. Today, about 20 per cent are so employed.
>
> Yet the natural rate of increase by surplus of births over deaths has been much higher in the country. Had it not been for a continuous and rapid migration of people from the farms over the past several centuries our nation would be almost 100 per cent agricultural.
>
> Towns and cities have been built only by the pull of higher incomes and more attractive conditions offered by urban life and urban occupations.

The disparity between rural and urban living and working conditions is often exaggerated.

1. Comparisons of average money incomes fail to account for the fact that most farmers get part of their livelihood "in kind," including food raised on the farm and housing for which no cash is paid.

2. "Average farm income" also fails to include earnings of farmers from non-farm work.

3. Comparisons of working hours usually fail to mention the time spent in getting to and from work. This is usually greater for urban workers.

4. Farming as an occupation receives a backwash of submarginal workers from the towns and cities. These are persons who cannot meet urban standards of competition and who prefer the meager subsistence which they can produce for themselves on the farm to poor-relief handouts in towns. Many such cases are included in the 50 per cent of farmers who receive only 10 per cent of total farm income.

However, the fact that the balance of migration has been away from the farms for several centuries shows that urban conditions have been more attractive, all things considered.

Causes of this relatively greater increase in demand for urban labor are:

1. As nations prosper their peoples' incomes rise and they spend most of the increase, not on food, but on things produced mainly in towns and cities—manufactured goods, medical and dental services, books, education, travel, etc.

2. As people prosper they demand finer *quality* rather than increased *quantity*, e.g., in textiles and clothing. This calls mainly for increased urban labor applied to a given amount of raw materials.

3. As people prosper they demand more service with commodities —"free" delivery, attractive packaging and wrapping, bright lights and fine showcases in the stores, a chance to "shop around," privileges of exchange and the money back guarantee. These increase costs of "distribution" and raise the demand for urban workers.

4. Factory methods replace home production. Canning, candlemaking, soapmaking, baking, butchering, spinning and weaving used to be done in farm homes. Power-driven machinery now makes it possible to do them in the factories more cheaply and under better working conditions than in the homes.

5. Farm machinery, made in city factories, displaces farm labor. Power, once supplied by human labor and later by animals fed on farm-grown crops, is now supplied by oil and electricity.

   In 1850 the primary power on United States farms was about 6½ million horsepower. In 1930 it was 70 million. In 1916 there were less than 30,000 tractors on United States farms. In 1925 there were over 470,000, in 1930 over 900,000, and in 1940 over 1,500,000. From 1920 to 1930 the replacement of work animals by other sources of farm power released for other uses 30 to 40 million acres of crop land formerly needed to produce feed for horses and mules.

Supply of Farm Labor Outruns Demand

The farm labor supply increases faster than the labor supply in urban occupations because rates of population increase are higher on farms than in towns and cities. This means that the supply of new apprentices is relatively greater for agriculture.

> Until about 1750 A.D. people died faster than babies were born in all European and American cities. Consequently cities could maintain themselves or grow only by drawing people away from the farms.
>
> Even today in the United States, because of higher birth-rates on farms, there must be a net migration of about 150,000 people each year away from the farms into the cities in order to maintain the existing ratio of farmers to urban workers.

> In the next 20 years the labor force of the United States is expected to increase by 14½ million. Of this increase, 7 million will come from farms, 4 million from villages and only 3½ million from cities.* *What would be the results upon our standards of living if the Federal Government enforced a farm-parity policy which would keep the entire 7 million new farm workers in agriculture?*

Improved methods and equipment, furthermore, have increased per capita farm output. Therefore, less farm labor is necessary to produce a given amount of food and other materials.

> In 1800 from 35 to 50 hours of labor were necessary to harvest and thresh an acre of wheat with a yield of 15 bushels. Today, with a binder and stationary thresher, it takes 4 to 5 hours, and with a harvester-thresher combine only 45 minutes.
>
> By 1939 the labor time required to produce a bushel of wheat had been cut 60 per cent from levels of World War I. The cost, including cost of the machinery, had been cut in half. For corn the labor time was cut in half and the production cost by more than 40 per cent during the same period.
>
> "Recent indications are that . . . in agriculture the gains in efficiency have been greater from 1920 to 1930 than in any previous decade."**
>
> A study of a group of Minnesota dairy farms for 1929-1936 showed that the feed required to produce 100 pounds of hogs decreased during those 8 years by 10 per cent. Egg production per hen increased 35 per cent. There were marked improvements in the cropping system. Altogether, the output per worker increased by more than 20 per cent in those 8 years.
>
> Better breeding and culling of cows has increased butterfat production per cow in the United States from 160 pounds in 1920 to 187.5 pounds in 1941.

Because of this increased agricultural efficiency and because of a slowing down in rate of population increase in the United States as a whole, it seems safe to say that a stationary farm population can take care of America's future needs for agricultural products. That is, it can if the enterprise and inventiveness of American farmers are given free play under competitive conditions.

To hold the farm population constant, however, about 350,000 persons must leave the farms each year *over and above* any entry of new labor into farming.***

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*T. J. Woofter, *Land Policy Review*, March-April, 1940.

**H. R. Tolley and A. P. Brodell, "The Role of Machinery in the Development in the United States," *United States Department of Agriculture*, 1934.

***Every year many thousands of families move to the farms. Some of these are ex-farmers who go back to farming after a try at city life. Others are newcomers to farming. Some of the latter, finding that the poets have left out some of the less pleasant facts about farm life, soon return to the cities.

How can this net migration from the farms be brought about in a free society except through the workings of a free price system?

Or do we want bureaucratic agencies to tell us who shall go to work in the cities and who shall stay behind on the farms? As a result of extending price controls we are rapidly approaching such a condition. Do we wish to continue the trend?

The Boom of the '20's

Since 1914 various conditions and policies have aggravated the long-term farm problem:

[a] by slowing down the rate of migration from the farms,

[b] by encouraging over-expansion of credit to farmers, and

[c] by increasing the instability of markets for farm products.

1. From 1910 to 1920 prices for farm products and farm lands rose rapidly due to:

    [a] heavy immigration into American cities from Europe, and

    [b] large food exports to Europe on account of the war.

    This led to over-expansion of agricultural credit, especially in wheat raising, and to an orgy of land speculation. In other words, farmers bought land and equipment "on margin" as millions of persons later bought securities "on margin."

    From 1913 to 1920 the value of farm land per acre rose 70 per cent while total farm mortgage indebtedness rose 90 per cent.

2. Our Federal Government and several state governments did not permit the liquidation of this unsound condition in 1920-1921 to work itself out as stock market speculation was liquidated in 1930-1931. Instead, these governments encouraged and aided farmers to refinance and continue their borrowings at lower rates of interest.

    From 1920 to 1923 farm lands lost half of their 1913-1920 rise, but farm mortgage debt rose another 27 per cent over 1920 levels (52 per cent of the 1913 total), and average interest rates were reduced from approximately 6½ per cent to 5¼ per cent.

3. At the same time the Tariff Act of 1922 was reducing the ability of foreign nations to buy American produce.

4. To offset the threatened reduction in our exports the United States government encouraged extensions of credit to foreign nations far beyond the capacity of these nations to repay the debts in view of our high-tariff policy. This weakened the private credit structure of the United States.

5. During the '20's world markets for many leading raw materials, including certain farm products, were artificially maintained by various price-rigging schemes.

   Typical of these was the price-rigging Stevenson plan for British East Indies rubber. The Canadian wheat pool, the United States Federal Farm Board operations and price-maintenance for copper by United States exporters working under the Webb Act of 1919 were other illustrations. Similar price-rigging was carried on for coffee, silk, tin, sugar, and other commodities.

   In most cases the price-rigging was supported by private or public credit. This enabled the operators to carry on longer but made the collapse more serious when it finally came.

6. Our Federal Government's cheap money policy, facilitated by heavy gold imports, encouraged widespread speculation in American real estate and in corporation securities. It also fostered a rapid expansion of consumer credit.

These policies led to financial breakdown and general depression, beginning in the autumn of 1929.

The Depression of the '30's

The depression of the '30's was prolonged and intensified by further attempts to restrict competition and prevent liquidation of unsound credit positions. (See below, pp. 44-46, 99-102.)

> These policies arose from the theory that the key to recovery lay in maintaining consumer purchasing power. According to this theory both government and business should at all costs maintain or increase payments to individuals through maintaining wage-rates, salaries, dividends, expenditures for plant expansion, public works and public loans.

The result has been continuous and rapid extension of government control over agriculture, labor, business and consumers. Bureaucratic dictation is rapidly replacing voluntary enterprise, with consequent loss of political integrity and economic efficiency.

Dictated Prices Produce a Dictated Economy

This expansion of government control and restriction of private enterprise arose from increasing efforts to "manage" prices, including prices for services (wage rates) and prices for credit (interest rates).

> This attempt at price control began with the protective tariff. (See below, pp. 72-80.)

It got its greatest impetus before 1933 from political exploitation of the Federal Reserve System, first, to finance World War I and secondly, to "stabilize" the general price level.

After 1933 efforts to control prices spread through all sectors of the economy.

Control of prices can only be made effective by control of production or consumption, or both.

When this control of prices is centered in government hands, the control of production and consumption must be put in the same place.

If government is to guarantee "parity" for agriculture it must restrict enterprise, not only for farmers but for all other producers and all consumers. This is part of the price we shall pay for "parity," *but not all.*

As bureaucracy grows political democracy declines. Deliberative bodies and representative bodies cannot manage a "managed economy." Therefore, loss of political liberty is added to the costs of a "parity" program and we get a form of Nazism under another name. *But even this is not all.*

Experience has shown that considerations of political expediency and personal ambitions of the rulers dominate a "managed" economy, not economic considerations. The result is loss of economic efficiency, reduced prosperity and reduced national strength. These are also part of the price of a "parity" program undertaken by government on behalf of farmers, wage-earners, or property-owners.

What then is the total cost of government "parity" programs?

Loss of economic liberty.
Loss of political liberty.
Loss of prosperity.
Loss of national security.

Are we "paying too much for the whistle"?

How to Help the Farmer

Farmers want:

1. buying power, not money,

2. earned income, not handouts.

They can get these things by expanding markets for farm products. This means reducing costs and increasing output in urban occupations by:

1. attacking monopoly and restriction of output in urban employments;
2. encouraging enterprisers to invest profits in ways which expand output and reduce prices of the goods farmers buy;
3. encouraging urban enterprisers to open new jobs for the hundreds of thousands of young men and women who each year should move from rural homes to urban life and work.

An open door to talent in every line—this is the way of progress for the farmer and city worker alike.

VI. KING MIDAS JOINS ROBIN HOOD

King Midas was the man who once had the power to turn everything he touched into gold.

Robin Hood was a popular bandit of medieval England. He justified his hold-ups on two grounds:

a. The vested interests had "done him wrong."

b. He robbed only those who could afford it and he gave much of his plunder to the poor.

What a lot of good deeds Robin Hood might have done if he had lived when King Midas had his golden touch! King Midas could have made good on the instant the losses of those who were robbed by this charming bandit. In that way Robin's hijacking could have gone on forever, along with his benevolences, with no injury to anyone.

Amazingly enough, modern governments do have this "golden touch" and they often do use it to support various legal or illegal rackets.

Governments Have a "Golden Touch"

Governments can make money out of almost anything—copper, lead, glass beads, wood and paper. Such money is often for a while "as good as gold," as far as its buying power is concerned.

> This magic of government's golden touch reaches its highest form in the case of check money, or "deposit currency."

Governments are also notoriously lavish in use of their credit. In fact it is hard to say sometimes whether a modern government is borrowing money or manufacturing it. Certainly a national government can borrow more easily than private persons because it can pay its debts by manufacture of new money, as well as by forced levies (taxes) on its citizens, including those citizens who lent it money.

Having Fun on Easy Money

By manufacturing money and by credit manipulations, a strong government can get great quantities of "easy money."

It can use this easy money to help finance projects which would otherwise be too unpopular with the people.

Ancient monarchs used to "debase" the currency by putting more lead and less gold or silver in the coins. By such means they got more money for their lady friends, finer palaces, bigger armies, and more costly entertainments.

Modern rulers "inflate" the currency or credit for similarly uneconomic uses. Japan and Germany, for example, built their armies and carry on their wars in large part with such easy money.

Our own United States Government has used this easy money in large quantities to help finance its wars, including loans to allies. The question here does not concern the object of the spending but whether most of the money might not better have been obtained by taxation. (See below, pp. 56-66.)

To an increasing degree since 1920 the United States has been using its great monetary and financial powers as an economic marijuana.

In the '20's it used a cheap money policy to offset the evil effects of the 1922 Tariff Act and to avoid agricultural deflation. How this aggravated the problem and led to over-expansion of credit in the real estate and securities markets has already been described. (See above, pp. 39-40.)

The result was the crisis of 1929 and the beginning of a world-wide depression.

Sending Good Money After Bad

Instead of encouraging the liquidation of unsound price and credit positions in 1930, the Federal Government sought to bolster them by still more lavish use of government credit and government controls.

The Federal Farm Board purchases of farm commodities, the Hawley-Smoot Tariff Act of 1930, government spending for public works, government pressure in 1930-1931 for wage maintenance, the raising of railway wages and freight rates in 1931-1932, and the creation of the Reconstruction Finance Corporation—all were aimed at maintaining prices, credit and consumer spending rather than at removing the original causes of the depression.

Private corporations cooperated by maintaining dividend rates in 1930 at 95 per cent and in 1931 at 70 per cent of 1929 levels despite a decline in profits of 83 per cent in 1930 and a huge aggregate loss in 1931.

A few corporations, notably the Ford Company, raised wage rates even while business was declining.

These policies were based on the theory that we could spend our way back to prosperity.

Private enterprise cannot long operate on this theory.

> Despite a sincere desire to maintain prices, wages, dividends, and expenditures for plant expansion, most corporations had to retrench after a few months or a year of experience with the spending theory. This retrenchment was all the more drastic because of the attempts to maintain boomtime dividends, prices, wage rates and investment policies in 1930.*

King Midas to the Rescue

Declining prices came to be regarded as the cause of the depression, and a movement for restricting price competition gained rapid headway during the fall and winter of 1932-1933.

In the spring and summer of 1933 the spending theorists joined forces with the advocates of price-maintenance and took over the United States government—with general popular approval.

> The Agricultural Adjustment Act, the National Industrial Recovery Act, and devaluation of the dollar were designed to maintain or raise prices. These measures were supported by a huge Federal spending program financed by expansion of bank credit.

In 1935 the A.A.A. and the N.I.R.A. were upset by the United States Supreme Court. Business and employment immediately improved.

The advocates of price-fixing, however, still controlled the government. Consequently new price-maintenance measures were devised and were accepted by a reconstructed Supreme Court:

state and local "little N.R.A.'s,"
the Bituminous Coal Act,
resale price-maintenance laws,
the National Labor Relations Act,
milk control laws,
hundreds of new interstate and intercity trade barriers,
minimum wage laws,
the Federal Wage and Hour law,
the Surplus Commodity Corporation,
a new A.A.A.,
the food stamp plan.

To effectuate these controls a host of other measures were adopted to use government's "golden touch" in expanding currency and credit:

abandonment of the gold standard,
a costly public works program,

*There is considerable evidence that the liquidation was completed by the summer of 1932 and that business was ready to resume its upward march. At this point, however, the United States underwent a political interregnum followed by a near-revolution.

numerous government lending agencies,
government guarantees for private loans,
a "soldiers' bonus,"
unemployment insurance and pensions,
subsidies to farmers,
huge purchases of silver at greatly inflated prices,
purchase of "surplus farm commodities."

By inflating currency and credit these measures were intended to raise the rate of consumer buying which the price-maintenance schemes otherwise would have reduced.

Thus the Midas touch of government was used to make good the various Robin Hood raids on consumers' pocketbooks and the public treasury.

But why do consumers and taxpayers tolerate policies which restrict output, reduce the purchasing power of money and raise taxes?

The answer is to be found in the fallacious and fraudulent theories of Robin Hood economics.

Robin Hood Economics

Two-gun Charlie once heard a park-bench "economist" explain how business depressions were brought on by failure of businessmen to pay out enough money to wage-earners and stockholders so that consumers could buy the goods produced. This convinced him that his "work" was a patriotic duty. It helped business as long as he took care to spend the proceeds of the holdups in buying the goods of his victims.

> This made money circulate, increased sales, reduced overhead costs, and increased profits.
>
> Of course it was illegal, but this only made Charlie a martyr when the police caught up with him.

Before we dismiss Charlie's theory as idle rationalization let's compare it with the theories used to defend certain popular policies:

1. "Depressions are caused by over-saving due to the fact that some rich people get more than they can spend and also to the fact that workers are not paid the full product of their labor. Therefore, higher taxes on profits and on large incomes will force money back into circulation and help business."

2. "If city people can be forced to pay higher prices and subsidies for farm products, farmers can buy more of the products of city industries. This will increase business, employment and incomes of city people so that they can buy more of both town and country products."

3. "If we can force employers to pay higher wages, we can buy more of their goods. This will increase sales volume, reduce overhead costs, and increase profits."
4. "If my customers will pay me higher prices, I can pay higher wages, my workers can buy more goods, other businesses will be helped, employment in general will expand, production will increase and everyone will be better off."

In short, holders of these theories say:

> "Pay us more money, so that we can buy more from you. That will make us all more prosperous. If you won't do this voluntarily we shall take steps to force you."

Coercive policies based on this Robin Hood brand of economics are of two general sorts:

1. *Taxing* one class for the benefit of another class.

   This reduces employment and purchasing power in precisely the same way as a spread of banditry.

2. *Restricting output and trade* to raise prices or rates of pay.

   This has the impoverishing effects of an earthquake, fire or flood, each of which likewise reduces output and trade.

Let us consider these policies in detail.

A. Destructive Taxation

The Robin Hood theory of taxation was directly responsible for the 1936-1937 Federal tax on undistributed profits. This tax was based on the notion that business could be made more prosperous by being forced to pay out more of its profits, either as taxes or dividends, in order to put more money into the hands of consumers.

The same theory lies behind schemes like the Townsend old-age pension plan and the Ham and Eggs scheme. These propose to make the nation prosperous by taxing producers for the benefit of non-producing pensioners.

Robin Hood economics also has helped promote a perversion of the ability-to-pay principle in taxation. According to this perversion, tax-paying ability is measured by the *producers'* surpluses instead of by the *consumers'* surpluses. Consequently the United States places its highest tax rates on job-making, enterprise, thrift and efficiency.

> Base rates for taxes on corporation profits are double the base rates for taxes on other forms of income.

The higher the total net profits of a corporation the higher is the rate of taxes it must pay. This means that the more successful job-makers are taxed at higher rates.

In addition, when profits are paid out to the owners as dividends, they are taxed again at the same rate as other forms of personal income.

The more efficient and profitable firms are those which should expand most rapidly. These are the firms which can pay higher wages and sell at lower prices. Yet discriminatory taxation takes from them their chief means for expansion—reinvested profits.

What sort of an automobile industry would we have today if recent tax laws had been in effect 20, 30 or 40 years ago? Could it have grown to anything near its present size? Would it be able to employ hundreds of thousands of workers, producing millions of cars in peacetime and millions of needed war machines in wartime?

Unemployment is one of our chief peacetime problems. This means a surplus of job-*seekers* and a shortage of job-*makers.*

Yet our heaviest tax burdens are placed on job-makers, and the rates are increased in proportion to efficiency in performing this most useful service.

Could the enemies of America devise a more effective method for destroying both our liberty and the industrial basis of our national strength?

Near-confiscatory taxation of upper-bracket personal incomes has thrown another serious obstacle in the path of private enterprise.

Roughly one-third of the venture capital going into development of new business and new jobs formerly came from income-receivers above the $100,000 level. This source of funds for expansion of enterprise is now almost completely destroyed. It has been estimated that, after deduction of taxes, total net income going to these persons and families was reduced 90 per cent between 1929 and 1940, inclusive. In fact, it is doubtful if this class of income receivers is making any net contribution to the capital market after deduction of inheritance and estate taxes.*

Aside from reinvested profits and high incomes the only other significant source of new capital necessary for our national progress and security is the savings of the upper middle classes (income-receivers from $5000 to $100,000).

Dr. Imre de Vegh estimated that net income of these income-receivers, after taxes, was reduced 42 per cent between 1929 and 1940.

*Savings, Investment, and Consumption," by Imre de Vegh, Papers and Proceedings, *American Economic Review,* February, 1943.

These and other restrictions on enterprise help explain the fact that sales of new corporation securities in 1933-1939 remained at 10 to 20 per cent of the average for 1920-1930.

They also help explain why the United States Government had to provide 85 per cent of the new capital for financing the war effort in World War II as against approximately 10 per cent in World War I.

Solicitors for philanthropic enterprises frequently tell the well-to-do prospect that his gift will not cost him much, because he would have to pay most of the money in taxes anyway. A corollary to this argument is equally sound and no less commonly expressed: "Why make further investments or work harder when I must bear all the losses while most of any gains I happen to make will be taken by taxes?"

Thus Robin Hood tax policies kill the business goose which lays the golden eggs of consumer income.

B. Trade Union Restrictionism

According to a popular trade union theory high wage rates are the key to business prosperity and full employment.

> A leading trade union publication attributed prewar unemployment to high taxes which reduced prospects for profits. The same article, however, argued that prospects for business expansion in the near future were "particularly favorable" because hourly wage rates were the highest in history.*
>
> In other words, employers supposedly are made prosperous by what they pay out, not by what they receive in return. This prosperity of the employers in turn gives rise to an increased demand for labor and thereby benefits the community as a whole.
>
> It follows from this theory that measures for raising wage rates promote the general good even though they restrict labor's output of goods and services.
>
> It also follows that measures to raise wage rates for one trade, e.g., coal miners, benefit all other workers, e.g., carpenters who buy the coal.

Supporting this theory is the belief that competition between workers for jobs reduces wages to levels set by the neediest and least efficient. Therefore, it is argued, wage competition must not be permitted between individual workers. Instead, minimum wage rates must be fixed by the average worker's standard of living.

**Monthly Survey of Business*, American Federation of Labor, July-August, 1939.

Restrictionist policies resulting from these theories are:

1. compulsory unionism (closed shops), restriction of apprentices, closed unions, restriction of output, featherbedding, reduced working week and penalty over-time rates;
2. standard rates of pay which ignore differences in skill and efficiency, opposition to piece-work basis for wages, adjustment of wage rates to changes in living costs regardless of changes in labor efficiency;
3. wage maintenance in depression as a "recovery" measure, attempts to set wages according to the ability to pay of the more profitable enterprises and above the ability to pay of marginal employers;
4. government unemployment relief and old age pensions on a more and more liberal scale to help raise wage rates and increase consumer buying power.

These policies raise costs of production, restrict output, reduce the demand for labor, retard economic progress, and endanger national strength and security.

C. Agricultural Restrictionism

According to Robin Hood economics city workers are benefited by paying higher prices for farm products and by paying taxes for subsidies to farmers.

> "City workers are unemployed because the farmer cannot buy the surplus products of the cities. Give the farmer more money and everyone will be more prosperous." So runs the argument.

Supporting this theory are two additional dogmas commonly preached by farm politicians:

1. "Competition among farmers permits the middlemen, who are better organized, to take more than a fair share of the consumer's dollar."

   As an argument for agricultural restrictionism this is no better than the assertion that two wrongs make a right. Where monopoly does exist in marketing of farm products it should be eliminated. In recent years, however, government policy, supported in many cases by farmers, has been a leading factor in promoting monopoly in this field.

2. "In comparison with other types of workers farmers are underpaid on the basis of the amount of hard work required."

   This raises again the question already discussed of whether or not producers should be paid according to the worth of their services as evaluated in competitive markets. (See above, pp. 17, 26, 35.)

These Robin Hood theories are used to support a policy of agricultural restrictionism intended to raise prices and incomes for farmers. These include:

1. restriction of production and sales through spurious soil conservation measures, prorate schemes, interstate trade barriers, marketing agreements and penalty taxes on competing products (e.g., oleomargarine and filled milk);

2. restriction of competition through monopolistic practices of certain farm organizations;

3. government subsidies, crop loans, tariffs and "surplus commodity" purchases.

These policies, whatever the excuse made for them, are means for coercing one class into paying tribute to another class. Their economic effects are the same whether they are legal or illegal, whether they are practiced by the few or the many, and whether they are for the benefit of the poor or the rich.

When illegal they are termed *rackets.* When carried out by government it seems not unreasonable to call them *legalized rackets.*

If prosperity requires maintaining a fixed ratio between farm and non-farm incomes it is hard to explain America's economic progress. During the past centuries the farmers' share of the national income and their relative importance as a market for urban goods was declining from 90 to 95 per cent down to 10 per cent, the approximate figure in recent years. In fact, if maintaining a given ratio of income between different classes is necessary to prosperity it would be a mistake ever to disband armies because armies are important markets for goods.

The theory that one class can be benefited by paying tribute to another class is a cheat and a fraud. City people are benefited by the goods which farmers produce for them, not by the goods farmers take in return.

It is to the interest of urban consumers to pay whatever prices are necessary to induce farmers to supply the desired quantities of farm products under competitive conditions. An honest policy of soil conservation is also in the public interest.

But organized restriction of output to raise prices and tax-supported subsidies to raise incomes are no more to the economic interest of non-farmers than train robberies or bank hold-ups.

Neither are they in the long-run interest of farmers.

D. Business Restrictionism

Business restrictionism is based on the argument that price maintenance promotes general prosperity.

> According to this theory, higher prices enable business owners to pay higher wages, buy more materials, contribute to charities and pay taxes. Thus the business restrictionist promises to make consumers, as well as other businessmen, more prosperous by charging them more for what they buy.

We also find among businessmen the same fear of price competition which exists among trade unionists and farm restrictionists. The notion is widespread that price competition always levels down, causing a depressing spiral of falling prices, falling profits, falling wages, increasing unemployment and declining quality of goods.

Supported by these Robin Hood theories a host of restrictions have been placed on business competition:

> interstate and intercity trade barriers,
> discriminatory taxes on chain stores,
> "little N.R.A." laws for dry cleaners and barbers,
> resale price maintenance laws, (see below, pp. 89-95),
> government fixing of retail milk prices,
> protective tariffs, (see below, pp. 67-88),
> market allocation (usually illegal),
> price maintenance agreements (usually illegal),
> pressure for protective railway rates,
> demand for uneconomic spending by government.

These policies restrict growth of the more efficient firms by restricting opportunity to capture markets from high cost operators through cutting prices. Thus they retard economic progress.

> Increased efficiency reduces costs.
>
> If business owners are strongly organized they may keep for themselves most of the gains from these cost reductions.
>
> If wage earners are well enough organized they may capture most of the gains.
>
> Under competitive conditions, however, the gains are more widely distributed. Business owners gain in proportion to the extent to which they introduce improvements more rapidly than competitors. Workers gain as more efficient firms expand operations and bid for labor against other employers. All classes gain as consumers from the decline in prices. As falling prices in one line release consumer purchasing power, demand increases for products of other lines, including products of new industries and services of new trades.

Competition is a levelling process. In a retrogressive society it levels down, but in a progressive society it levels up.

When enterprise is free, when science is advancing, and when capital is increasing faster than population, competition speeds adoption of improved methods. It expands output per worker, increases the demand for labor, and raises general levels of purchasing power, even while prices of particular goods are being reduced.

Such were the conditions in the Americas for 300 years. To a lesser extent they prevailed in many other nations.

In recent years, however, vested interests have been given increasing protection at the expense of community prosperity and progress. *The world has been faced with a conspiracy of the inefficient.*

The Fallacy of Robin Hood Economics

The conspiracy of the inefficient, however, gets most of its support from well-intentioned producers and consumers who honestly believe that prosperity can be promoted by scarcity policies and price maintenance.

They forget that a man's prosperity does not consist in what he sells or gives away but in what he is able to buy.

Nor does a man's prosperity depend on the amount of money he has or the high prices he charges. Instead it depends on the abundance of commodities and services which he can obtain.

This abundance and high purchasing power depend on high production.

This high production is obtained by specializing on those things we can do best and getting other things by trade. Cheap transportation promotes prosperity by facilitating and inducing such specialization.

High production is also promoted by greater use of tools, machinery and methods which increase output per man hour and free labor and purchasing power for new industries and services.

Attempts to protect any vested interest against competition arising out of trade or labor-saving methods injure all other interests in the community.

For example, protection to a local industry against out-of-state competition may be provided by maintaining freight rates. Such protection is said to benefit the community by providing jobs for workers in the protected industry and profits for the owners.

However, insofar as such protection maintains a higher level of prices than would otherwise prevail it reduces the purchasing power of all other workers and all other business owners. It is equivalent to a sales tax levied on all other producers for the benefit of those who are protected. It thereby reduces wage levels in all other trades and reduces local markets for all other commodities and services.

Thus it reduces the demand for labor in all other trades to the extent that it maintains employment in the protected trade.

In addition it prevents an increase which would be brought about in average income levels through transfer of labor to industries able to sell in competition with the goods of other areas. (See below, pp. 69-70.)

Consumers are not benefited, therefore, by being charged higher prices so that they can be paid more money as wage earners or stockholders.

Employers are not benefited by being forced to pay higher wages so that they may sell more goods.

On the contrary, trade restrictions and output restrictions which are used to raise prices or wage rates above competitive levels reduce prosperity for those who buy the restricted commodity or service.

The further this is carried the greater is the loss.

Occasionally monopolists in a particular line can get greater total net returns by selling a smaller quantity for more than they could have sold a larger supply.

But this means merely that buyers (a) get less of the restricted commodity and (b) reduce their purchases of other goods in order to get the extra money to pay the restrictionists.

It means that producers in other lines lose markets and get less in return for their efforts.

It also increases competition for jobs in the unrestricted lines as workers are barred from the monopolized, or restricted, fields.

Gains to the monopolists, moreover, quickly disappear as other producers adopt similar tactics and raise prices of the goods which the first monopolists buy.

What to Do?

Farm groups refuse to yield their special privileges while industry has its price-maintenance policies and labor has its featherbedding restrictions on output.

Business is not in a good position to talk free markets to wage earners or farmers when it demands restriction of price competition for itself.

Local communities justify their log-rolling for Federal pork on the ground that they are paying for similar government projects elsewhere.

Until each of us becomes conscious of the beam in his own eye there is little hope of removing the mote from the eye of someone else. The fallacies common to all monopolistic restrictions and legalized rackets must be recognized and attacked together. The advantages of free enterprise, competition and increasing productive efficiency must be recognized by leaders in every line.

Logrolling for liberty must replace logrolling for special privilege.

Meanwhile the ease with which government can borrow from the banks, who dare not refuse to lend, provides the means for corrupting Congress and the people, expanding the bureaucracy and financing new experiments in government restriction of enterprise.

We hope to use inflation—the Midas touch—to offset the restrictive effects of Robin Hood restrictionism and yet to escape the usual results of inflation. How?

The answer is more *price control,* this time to keep prices *down* instead of *up.*

Will it do the trick? Will price control enable us to eat our inflation cake yet escape the deflation stomach-ache which usually follows?

VII. CAN PRICE CONTROL STOP INFLATION?

The United States Government is attempting to control prices for commodities and rents through the Office of Price Administration.

Prices of labor's services—wage rates—are controlled through the War Labor Board.

Interest rates are controlled through numerous government lending agencies and through the Federal Reserve System.

Profits, the price of enterprise, are controlled through excess profits taxation, renegotiation of contracts, and cost-plus-fixed-fee contracts.

Can these controls prevent inflation?

What Is "Inflation"?

We speak of:

currency inflation,
gold inflation,
credit inflation,
price inflation.

As commonly used inflation means:

- a decline in the purchasing power of money arising from the fact that the rate of spending runs ahead of the output of goods.

From 1933 to 1939 the United States experienced a considerable amount of credit inflation with little price inflation.

Since the outbreak of war in 1939, however, we have experienced inflation in every sense of the term.

The amount of money in circulation has risen from $7 billions in August 1939 to $20 billions in January 1944.

Bank deposits have risen from $56 billions to $108 billions.

Savings of individuals and unincorporated business are estimated by the United States Department of Commerce statisticians at:

$ 7.5 billions in 1940
13.6 billions in 1941
26.9 billions in 1942
36.0 billions in 1943

These savings compare with savings of less than $10 billions for the best year prior to 1941.

The excess of money put in the hands of consumers over the value of goods put in the merchants' hands for sale is estimated at $3 billions per month for 1943. This is the "inflationary gap" and it promises to widen as the war continues.

When general price controls were established in April 1942, the Administrator of the Office of Price Control said:

> "There can be no effective price control while at the same time there is so large an amount of excess purchasing power."

Yet since that date the rate at which this excess purchasing power is created has doubled.

What has been the result?

Price Controls Do Not Stop Inflation

Official cost-of-living indexes have shown comparative stability since price controls were adopted, especially in the case of specific commodities brought under control.

However, these indexes have become increasingly unreliable as measures of the value of money. They do not make allowances for:

rising prices of real estate and corporation securities,
rising prices of producers' goods,
rising prices in second-hand markets,
"black market" prices,
declining quality of goods,
substitution of high-priced for low-priced lines,
reduction in services to consumers,
increased time and expense of shopping,
linked purchases,
premiums paid by government agencies,
cost of subsidies,
depletion of stocks and shortages of goods,
costs of operating price controls and rationing.

Adopting a new form of currency—ration coupons—also has helped to conceal the decline in purchasing power of money. However, the purchasing power of this new, ration-coupon currency is depreciating as point values for various commodities are raised or as the goods cease to be available.

Results of Inflation

1. Currency inflation encourages waste.

   Government gets the money first and most easily. Therefore, the waste begins with government spending and is most noticeable there.

For example, easy money enables the government to ship war bond posters by air express while vitally needed war supplies wait their turn. It enables government to clutter up the long distance wire services with the most trivial messages, and to take thousands of workers out of essential industries for trivial government employments.

As the easy money seeps down through the national economy it dulls incentive and induces extravagance:

hoarding of labor, materials and machines;
absenteeism, loafing and featherbedding;
costly and unnecessary advertising;
increased consumption of luxuries;
hoarding of commodities by consumers;
increased travel for non-essential purposes.

Easy money also permits the waste of continuing unsound economic policies, such as the penalty rates on hours over 35 or 40 per week.

2. Inflation of currency and credit gives government the means for destroying liberty.

   When money, together with the power that goes with it, is obtained by consent of those giving it, democratic controls and liberties are preserved. "Control of the purse" has been the people's most effective means for controlling government.

   Modern governments, however, are able to get funds merely by printing bonds and turning them over to the banks in return for new checking accounts. In the United States the process requires consent of the legislature,* but this consent is much easier to obtain when no new taxes have to be levied and when part of the funds is used to help key legislators get elected by government-financed favors for their constituents.

3. Inflation intensifies conflict between buyer and seller, employer and employee, borrower and lender. It turns attention from producing and working to organizing and bargaining.

4. Most advertised among the results of inflation are the inequities in distribution created by rapid changes in the purchasing power of money. Certain individuals and classes lose through no fault of their own and others gain through no merit of their own.

   Chief sufferers from price inflation are fixed-income groups: pensioners, interest receivers and certain salaried workers.

   Through rent controls urban real estate owners have been victimized. Through disproportionate taxation of profits, stockholders have gained much less than certain other classes in the current inflation.

*By huge, lump-sum appropriations for vaguely-defined purposes Congress has given up much of its control over finances. In the case of the "Occupation Currency" this control seems entirely lost. (Cf. Walter E. Spahr, "Allied Military Currency," Sanders Printing Co., N. Y., September 1943.)

Farmers and industrial wage earners usually gain by price inflation, except in totalitarian or feudal societies, or at least they lose less than other classes. In the deflation which follows, however, they usually lose more than other classes except enterprisers.

5. Inflation sooner or later ends in deflation.

   The deflation need not last so long as the inflation or bring about a return to pre-inflation levels of prices, currency or credit.

   Nevertheless, deflations are periods of more or less painful readjustment, usually in political as well as in economic matters.

Price Control Aggravates Inflation Evils

1. Price ceilings increase tendencies to waste and inefficiency when money and credit are being inflated.

   a. They encourage wasteful buying and consumption as long as stocks of goods hold out.

   b. Cost-plus contracts—a method of putting a ceiling on profits—create the belief that "Costs don't matter; the only thing that counts is speed in production." This attitude causes indifference to waste of a most serious sort—the waste of lost opportunities to make better use of materials, labor and equipment. Producers try to increase output merely by hiring more labor and machinery instead of trying to use more efficiently what they have.

   c. Red-tape, delays, labor freezes, complicated and conflicting orders, pressure politics, and difficulties of enforcement slow down production, destroy initiative and incentive, and throw new obstacles in the way of producers. No matter how competent the administrators may be they cannot adjust prices with sufficient rapidity and accuracy to keep production flowing smoothly.*

   d. Decisions concerning prices and production come to be determined more and more by political considerations—the number of votes involved—rather than the true merits of the case.

2. Price ceilings and wage controls destroy liberty. They make necessary the development of bureaucratic controls to do the work of the price system and they can be used to reward friends and punish opponents of the government's policies.

*One common criticism of the Office of Price Administration is that it contains too many college professors. But what would have been the problems if the O.P.A. had been turned over to representatives of organized labor, or to representatives of organized business, or to joint committees? Bad appointments could have been made from any trade or profession, no one of which has a monopoly of good or bad judgment. The responsibility for such appointments rests on those who made them, not on the group from which they were selected.

Secondly, it is said that the ceilings should have been applied earlier and more generally. *But frozen prices do not mean frozen costs.* Therefore, regardless of when or how applied, they squeeze producers and check output as costs rise because of declining efficiency of personnel, resort to higher-cost sources of materials (e.g., in mining and agriculture), resort to inferior substitutes, more rapid wearing-out of machinery, longer working hours, and wartime regimentation.

Freezing of wages means that transfers of labor from less essential to more essential jobs are governed by bureaucrats instead of by the changes in wage rates as between occupations.

Bureaucracy becomes a vested interest logrolling for power, buying support with unlimited funds and jealously striking at the roots of free enterprise by discriminatory taxes and by fostering monopolistic restrictions on behalf of its political supporters.

3. Government price control merely transfers the conflict over prices and rates of pay from the economic to the political field without reducing its intensity.

   Fixed prices do not mean fixed costs. Costs change with changes in materials, technique, volume of output, and character of labor force, especially in wartime. Under government price fixing, however, the process of adjusting prices to costs requires constant dickering with government officials, resulting in delay and uncertainty for producers.

   This encourages organization of political pressure groups representing every important economic interest. These war with one another, as well as with various government agencies. Even the government agencies are brought more and more into conflict with one another.

   The result is growing contempt for government, increasing class warfare and spread of evasion.

4. Government price control does not abolish the inequities of inflation. Whether or not it increases them cannot be determined.

   Certainly without rationing it does little or nothing to prevent inequities because commodities go to first comers who may be the least meritorious consumers. It also leads to favoritism by sellers towards customers.

   Even under rationing, great inequities persist. A ration system, for example, may give a day-old infant as much meat and sugar as a hardworking lumberjack. This is the spurious "arithmetical" equality of coercive communism, not the "proportional" equality of freedom and progress.

   Metropolitan New York normally consumes three times as much canned goods as the residents of our Southeastern States. New Englanders use twice as much as the people of the West Central States. Yet all are treated alike by price controls and rationing. This is "proportional" inequality created by a policy of "arithmetical" equality.

   Price controls also have frozen and intensified certain inequities which otherwise would have corrected themselves under the free play of demand and supply. For example, wage rates increased 50 to 100 per cent for some lines during the conversion to a war economy, while wages in other lines no less essential increased little. The premium for industries which had to be greatly expanded was useful in the first months of the war effort. It is detrimental after the industry has attained its growth.

5. Price ceilings promise only to intensify the difficulties of the deflation which always follows inflation of currency and credit such as the United States is now experiencing.

   a. That price controls could prevent the reaction which customarily follows inflation is at best an unproven theory. History records various attempts at price freezing. But as far as we know the price controls always broke down before the currency inflation was brought to an end. This is because price control aggravates the evils of inflation while covering up a chief symptom. Inflation of currency and credit continues as long as price controls seem to be working, and even after they begin to fail the breakdown is attributed to the lack of patriotism or to the greed of the violators rather than to bad government policy.*

   b. Those who expect price controls to hold down prices "until postwar production catches up with consumer demand" forget that this production will itself put enough new money into circulation to buy the increased output. The war-boom "savings" will remain intact, ready to flood the markets at any moment. "TRYING TO 'OUTPRODUCE INFLATION' IS LIKE A MAN'S TRYING TO OUTRUN HIS OWN SHADOW." (William C. Mullendore.)

   c. In the long run price controls are more likely to be an unsettling than a stabilizing influence because they interfere with making of agreements between producers. Consequently they discourage production and intensify shortages.

      On the upswing this creates keener bidding for commodities and increases the demand for inflationary spending to overcome the shortages.

      When the inflationary spending ends and deflation begins, price controls interfere with the making of private agreements (bargains) necessary for rebuilding private enterprise.

      The greatest obstacles to readjustment in a period of deflation are price rigidities. General price controls can only increase these.

      (i) They build up a huge bureaucratic organization with a vested interest in continued "management" of the economy.

      (ii) They create in private enterprise many vested interests in price control, rationing and allocations.

      (iii) Price ceilings to control inflation create precedent for "price floors" to prevent deflation.

*Cf. Horace White, *Money and Banking* (Ginn and Co., 1935), p. 55.

Putting Ice on the Thermostat

Subsidies are being used increasingly as an administrative escape from production problems created by price ceilings.

These subsidies in their turn create new difficulties and promise only to increase the wastes and dangers of inflation.

1. A subsidy always costs taxpayers more than it saves consumers whenever it is applied to all producers or to most producers in a given line.

   It might save consumers more than it costs taxpayers if it were given only to a few producers whose costs were considerably higher than average and who could not reduce those costs in other ways. In practice it is usually too costly or too difficult to ascertain what part of the output is unavoidably high cost.

2. Under inflationary conditions subsidies increase wasteful consumption by reducing prices of consumers' goods to all consumers, rich and poor alike.

   This is especially obvious when subsidies are applied to the more expensive, semi-luxury commodities like coffee, butter and meats.

3. Subsidies increase bureaucratic control which is all the more difficult to throw off when initiated in a time of rising prices and high incomes.

Farm organizations shout "Regimentation!" in protest against subsidies used to keep prices *down*. Scarcely audible, however, are their protests against even greater regimentation in the form of crop restrictions and crop "loans" used to keep prices *up*.

The argument is used that subsidies must be given to farmers in order to escape inflationary demands of wage earners. But will such additions to farm incomes, which are already at an all-time high, make wage earners more contented?

The argument that one unsound policy can only be avoided by another equally unsound represents an abdication of leadership and a betrayal of public trust.

This would soon be recognized if there were general understanding of the fact that the price system is the thermostat of the national economy. To attempt to control inflation by means of price ceilings is like trying to cool a room by putting ice on the thermostat.

What Are Prices For?

Numberless adjustments of production and consumption are necessary every hour of every day for efficient operation of a modern industrial economy.

These adjustments call for numberless decisions by producers and consumers, buyers and sellers.

Under the automatic workings of a free price system each individual records his decisions on all problems and policies as they affect him and as he knows them. As he buys commodities and as he markets his services his actions affect supply and demand, prices and wages.

These prices and wages, in turn, directly or indirectly affect the decisions of employers, investors, farmers, other wage earners and other consumers. Thus, by watching price changes and making adjustments to them, each individual adjusts to the decisions of every other member of the economy without the necessity for knowing or understanding the many factors which entered into the making of those decisions. Such a free price system is essential to efficient operation of the great and complex industrial economy which is necessary to our national survival.

War makes necessary increased government control of the economy for (1) speed, (2) secrecy, (3) unity, and (4) suppression of activity not useful in the war effort.

But, even in wartime, efficiency will be promoted by placing the main burden of coordinating and directing producers' efforts on the automatic workings of the price system.

1. *The number and complexity* of factors which must be taken into account in modern industry far exceed the comprehension of any person or group of persons. The task of making decisions, or planning, must be so decentralized that it is shared by every buyer and every producer, including the humblest wage earner. In no other way can the final result take into account the vast diversity of changing conditions under which millions of producers unite their efforts.

2. *Energy, inventiveness, and enterprise* are greatly stimulated by the prizes offered under a system of free exchange and free prices. Bureaucratic controls make use of certain powerful motives, e.g., personal and group loyalties, or fear of punishment. That is, bureaucrats may get a certain amount done by appeals to love of country or to fear of punishment. But even military forces find it worth while to add economic incentives and personal rewards to the other motives used in maintaining individual efficiency.

Free enterprise (including free exchange, which is essential to free enterprise) can be our greatest asset in war, as well as in peace.

Why Civilians?

Efficiency in the civilian economy requires a civilian type of organization. *"Total wars" are not won merely by putting everyone under military discipline.*

1. The military forces consist of a selected personnel. Therefore it is easier to make rules which call for uniform treatment of individuals. For example, the waste involved in issuing uniform food rations is much less for the military than for the civilian economy.

2. Civilian tasks are too numerous and complex to be organized and conducted along military lines. Perhaps because destruction is simpler than construction, killing men easier than working with them, freedom of enterprise and inspiring individual initiative are relatively more important in civilian life. (However, increasing complexity of military operations, as new and more complicated weapons are devised, is leading toward greater flexibility in military organization and discipline, especially in wartime.)

3. Civilians are responsible for continuing in many respects the peacetime "way of life" which the military forces are fighting to defend. These include schools, churches and habits of family life which are necessary for the continued life and progress of the nation. They include wise planning for postwar reconstruction. Wars are not won unless the victorious nation can resume the essential modes of living which it fought to defend. This maintenance of peacetime activities adds to the complexity of the civilian economy and increases the need for retaining freedom and flexibility incompatible with a militaristic form of organization.

4. Much of the regimentation evident in the military forces actually decreases efficiency, but is needed to maintain secrecy, speed in sudden emergencies, and discipline to prevent panic in battle.

5. The feeling of imminent personal danger plays a much larger part in motivating the soldier than the civilian. In fact, only men in prime physical and mental condition can endure the strain of military life, particularly in the front lines. Even these can endure it only for short periods.

Economics of Siege and Defeat

In case of siege or imminent defeat contrasts between civilian and military life tend to disappear.

Fear of personal injury becomes an important civilian motive.

Many civilian activities which are important for the continued life of the nation must be restricted or discontinued.

Motivating and directing producers become unimportant compared to careful use of supplies already available.

Fortunately the United States is not besieged and is not losing the war. We, therefore, can and should maintain activities and forms of organization which do not show their benefits immediately on the battle line, but which instead may contribute to the war effort and to victory two or three years hence.

1. We should rely more on persuasion than on threats and on economic motives, or self-interest, rather than on fear of punishment or personal injury. These methods and motives may not result in as great temporary spurts of energy as may be obtained from military methods and fear of personal danger. But they do make possible more continuous effort and more intelligent conduct over much longer periods of time.
2. We should retain and encourage activities and institutions which will aid in postwar reconstruction.

Our military forces have a right to expect and demand these as fruits of their military successes.

This is not to argue that government should pay no attention to the price system in wartime.

Sound Price Control in Wartime

1. Taxes should be increased to reduce the inflationary gap sufficiently to prevent rapid price increases in free markets.

   At the present time this increase in tax rates should fall on incomes *below* $15,000 per annum. These incomes make up approximately 99 per cent of total personal incomes after deduction of present taxes and war bond purchases.
2. All restrictions on output or employment which are designed to raise or maintain prices or wage rates should be abolished.
3. Mobility on the part of labor and enterprise on the part of management should be encouraged.
4. Automatic price controls sometimes suffer temporary breakdown, or work badly, because of a sudden increase in demand or decrease in supply due to war conditions. When this happens in the case of an *essential* commodity or service (*not* including such luxuries as coffee, sugar, butter, or meats) temporary price controls, allocations and rationing may properly be instituted until the cause of the failure has been removed.

   At the outbreak of a war, for example, a five-fold increase in demand for some important war material may send prices temporarily far above the level necessary to stimulate the needed production. In that case price controls and rationing may be advisable for the few months necessary to increase output.

Government policy should be, however, not to replace the automatic controls of the free price system, but to facilitate their operation.

Winning the Peace

The war will not be won unless we reestablish the conditions necessary for peacetime prosperity and progress. This means reestablishing freedom of enterprise, including freedom of exchange and a free price system.

The closer we approach the end of the war, therefore, the more imperative it is to begin dismantling the wartime restrictions and burdens on enterprise.

This requires an immediate attack on inflation, mainly by increased taxation and by greater economy in government spending.

Experience indicates that such an attack will not make headway so long as price controls are concealing the more obvious symptoms of inflation.

For this reason, a first step towards winning the peace involves abandonment of the attempt at general price and wage controls.

VIII. AMERICA CAN COMPETE

Should freedom for enterprise stop at our national borders?

Can we compete with the "pauper labor" of Asia—or should we try?

Would freedom for our traders to buy and sell foreign goods in America break down American standards of living?

Why is "free enterprise" good and "free trade" bad? Doesn't the enterprising trader deserve freedom when his enterprise takes him into foreign markets?

American businessmen are divided on these questions. According to a recent *Fortune Magazine* poll 45 per cent of our business executives favor maintaining or increasing present United States tariffs after the war, 55 per cent favor lower tariffs or free trade.

Why Trading Nations Prosper

Prosperity depends on *ABUNDANCE* of goods and services: food, clothing, shelter, schools, hospitals, libraries, scientific laboratories, churches, art galleries, museums, theaters, services of dentists and doctors, radios, automobiles, railroads.

Abundance depends on *HIGH PRODUCTIVITY*. We cannot have high levels of wages and scales of living unless we have high levels of output.

High productivity cannot be obtained without *DIVISION OF LABOR*. This means that people specialize in doing what they can do best. This specialization is necessary to develop skill, to make use of special talents, to stimulate invention of labor-saving machinery and to economize equipment.

But division of labor is impossible without *TRADE*.

Prosperity — abundance — high productivity — division of labor — trade—together these provide the economic basis for *PROGRESS*.

That is why civilization has developed first and furthest along trading routes and at trading centers—along seacoasts and rivers, around good harbors and at junctions of highways and railroads.

Sparkplugs of Civilization

Without trade, and with everyone producing only for his own needs, people are condemned to the poor and brutish life of savages.

> People can produce and enjoy only the barest necessities of life when each family must make its own clothes, shelter, tools and other things as did our early ancestors. Under such conditions there can be no scholars, scientists, artists and doctors. Sickness and death rates are high. People are illiterate and ignorant.
>
> In fact, most Americans would die of cold, hunger and disease in the first year if they ceased to specialize and trade with one another.

Agriculture unaided can produce *subsistence* for a few. But *civilization* requires trade, transportation and a host of service lines, along with specialists in manufacturing, mining, lumbering, fishing and many other occupations. It is service lines, including trade, which will most of all need developing in the future. (See above, p. 37.)

Traders act as sparkplugs of civilization by:

1. searching out more abundant and cheaper sources of supply;
2. finding markets for the more efficient and lower cost producers;
3. extending the use of superior tools and methods of working and living;
4. enabling other producers to increase output by concentrating on their specialties.

Traders Are Producers

Some people say, "Traders are not producers. They only distribute what other workers produce."

But how much production would we have without trade?

> Farmer Brown might have a granary full of grain yet be poor indeed if he could not trade his grain for clothing, fuel and other things. In that case he would soon stop producing so much grain.
>
> Tailor Jones might have a shop full of clothing yet starve to death if he could not trade for food. In that case he would soon stop producing so much clothing.

Work is productive only if the results are useful and valuable to somebody. Traders add to the usefulness and value of things by arranging for producers to exchange their surpluses.

> Waste material dealers, for example, seek out old rags, waste paper and metal scraps which have no value or are a nuisance to their present owners. Then they find others who have a good use for these materials.

All other traders do the same thing. Like fishermen or miners, they create value by taking things from where they have little value to where they have more value.

Production means creating utility and helping to make valuable things more abundant.

Goods may be *processed,* but they are not fully *produced* unless they have reached the final users. They still lack full usefulness and value. Creating such utility—"place utility," "time utility," and "ownership utility"—is the job of the merchant. In doing this job he is as productive as the farmer, manufacturer, miner or lumberman.

An efficient trader may do more than an efficient farmer to create jobs, promote prosperity and increase welfare. A good farmer can add a few thousand dollars of value to the material with which he works. A good trader may add hundreds of thousands of dollars to the nation's annual net income by finding new opportunities (markets) for our latent productive energies.

Annual contributions to the national income by traders and their employees in the United States are usually about 30 per cent greater than the annual contribution of agriculture.

Trade, finance and transportation together produce as much value and income as all manufacturing industries combined.

By arranging trades, or finding markets, the merchant increases the purchasing power of other producers. He gives value to their land, labor and machinery by making the products more salable and valuable. Therefore, he creates credit and helps put it to work in production.

In these ways trade increases the demand for labor.

Trade Raises Wage Levels

The demand for labor consists of wages offered for its services. It does not consist of work to be done.

There is never any limit on the work to be done. Every thinking person knows of more things to do than he could accomplish in several lifetimes. If *work* were all people wanted no one need ever be unemployed. In that case we should all go to the barren places of the earth to live—the North Pole or the Sahara desert.

What wage-earners and other producers really want is *pay* for their work, not merely work itself.

Whatever increases the rewards for labor increases the demand for labor and increases opportunity for employment of the only kind we care much about—*remunerative* employment.

> Unemployment consists, not in lack of work but in lack of pay for what work is to be done.

The rewards offered for labor's services depend on the usefulness, or productivity, of those services.

This productivity, in turn, is increased as all workers and all groups of workers specialize on what they can do best and exchange the products.

> The United States has the world's highest wage levels partly because it has been one of the world's greatest free trade areas.
>
> This came about, however, only because the United States Constitution forbade the states to interfere with interstate commerce. Before the adoption of the Constitution each colony, and after 1776 each state, was erecting more and more tariff barriers against the goods of the others. After the adoption of the Constitution the desire to continue these trade restrictions still existed. The opening of the West, for example, led New England farmers to demand tariffs or subsidies to protect them against cheap wheat from cheap western land. Fortunately for both New England and the West such tariffs were forbidden and subsidies soon became unpopular with consumers and taxpayers.
>
> Without domestic trade the people of Michigan would not have enjoyed many oranges and California would not have had many automobiles.
>
> Without foreign trade, silk stockings and rubber-tired automobiles would not have been part of the "American standard of living."

In other words, trade increases the demand for labor by increasing the rewards for effort. And this is just as true of foreign trade as of domestic trade. Differences in economic conditions and wage levels increase rather than reduce the advantages of international trade.

High Wages No Obstacle to Trade

If high wage rates were an obstacle to trade, high-fee doctors would not hire low-wage gardeners. Similarly, wage differences would prevent Massachusetts from doing business with Florida, California with Alabama, or England with India.

Despite high wages, the United States for a generation has been running a neck-and-neck race with Great Britain (another high-wage nation) for the position of the world's leading exporting nation.

Following are percentages of foreign sales to total output for certain important American producers prior to 1939:

RELATION OF EXPORTS TO TOTAL PRODUCTION

automobiles,	12 to 14 per cent	oranges,	10 to 20 per cent
petroleum products,	15 " 35 " "	lard,	25 " 33 " "
raw cotton,	40 " 60 " "	rye,	20 " 25 " "
canned fish,	40 " 58 " "	rice,	10 " 20 " "
dried fruits,	30 " 50 " "	wheat,	10 " 18 " "
motion pictures,	30 " 40 " "	tobacco,	40 " 50 " "
typewriters,	30 " 40 " "	aircraft,	20 " 35 " "
refined copper,	25 " 35 " "		

These and many other American lines on an export basis have successfully met foreign competition.

And the chief competitors of the United States in foreign trade are the high-wage nations, not the low-wage nations.

Japan was no exception to this rule, for only a minor part of her exports was competitive with ours.

Where labor's output per hour is high, costs may be low despite high wage rates.

Japanese protectionists have said, "How can our flesh-and-blood workers stand up against the competition of American machines and cheap power? We must have tariff protection against the cheap products of American power-driven machinery!"

In many lines, especially in those using power-driven machines, the United States can undersell the world, despite high wage levels. In fact, it is our efficiency in these lines which sets the high standard for American wage rates.

United States wage levels are ten times as high as wage levels in India, China or Japan only because our labor on the average is ten times as productive. And, since our average productivity is higher than the average productivity of any other nation our costs of production are lower in most lines despite our high wage rates.

To keep wages high, however, we must specialize in lines where the productivity of our labor is high and our costs low. We must get by trade the products of industries where the productivity of our labor is low and our costs are high.

For example, if we devote some of our labor to lines where it is only two or three times as productive as Asiatic labor, we thereby drag down the average level of our productivity and reduce the average level of wages. This is because we raise costs for the more efficient lines by forcing them to pay higher prices for their supplies and because we reduce the purchasing power of wages paid in those more efficient lines.

The Discriminatory Tariff

Tariff duties restricting imports may benefit home producers of the restricted articles.

But they do so only at the expense of:

1. exporting industries, which thereby lose foreign markets;
2. processors of the restricted commodities;
3. dealers in the restricted commodities;
4. consumers.

Thus tariffs *discriminate* against various producers and consumers at the same time they give *protection* to a few.

Since those injured are more numerous and important than those benefited, duties of this sort should be called "discriminatory tariffs," instead of "protective tariffs."

1. The following domestic lines gain directly from both imports and exports:

   transportation and communications,
   wholesalers, retailers, brokers,
   hotels, restaurants, bakeries,
   education, dentistry, medicine,
   public utilities,
   construction,
   finance,
   amusements,
   government service.

   Producers in the above service lines make up half of our peacetime working force. They cannot be injured by competition of foreign producers. On the contrary they benefit from foreign trade (1) as consumers, and (2) as suppliers of services to exporters and importers.

2. An overwhelming majority of farmers and manufacturers would benefit from reduction in American trade barriers as well as foreign trade barriers. Among farmers this includes producers of cotton, tobacco, corn, pork products, wheat and fruits. Among manufacturers it includes producers of automobiles, petroleum products, movies, many textile products, rubber products, radios, sewing machines, many chemicals, agricultural machinery, electrical machinery and apparatus, industrial machinery, and a host of other iron and steel products. These producers would benefit from expansion of home and foreign markets as well as from increased purchasing power in terms of foreign goods.

3. Many of our important domestic industries have depended on cheap foreign materials, such as rubber, sisal, jute, furs, cork, wool, silk, linen, hemp, shellac, chromium, nickel, tungsten, manganese, tin, mercury, hides and leather, scientific instruments and crude drugs. Most of these commodities could have been

produced in the United States, or home-produced substitutes could have been found—*but only at higher cost, which would have reduced markets for the finished goods.*

The Businessman's Socialism

When industries in which our labor is relatively less efficient ask for subsidies or tariffs it is not merely because they need protection against the *foreigner*. It is equally due to their need for help against the competition of more efficient *home* industries which are bidding against them for labor, land, machinery and materials.

Why does Mr. X, an American manufacturer, have difficulty meeting the competition of, let us say, English manufacturers in the same line?

"Because he has to pay higher wages than his English competitors," says the protectionist.

But why does Mr. X have to pay these higher wages? Is it not because so many other American employers are offering higher wages than are paid in England?

And who are these high-wage employers?

They are employers in lines where American labor is relatively more efficient. For example, American labor is about twice as productive on the average as English labor, mainly because it is equipped with twice as much power-driven machinery. Therefore, on the average, American employers can afford to pay twice as high wages to our workers as those received by English workers.

This is what makes it hard for Mr. X whose workers are only perhaps fifty per cent more productive than the English workers. His trouble is not due to his inefficiency compared to the foreign producer. It is due to his inefficiency relative to other American producers who bid up the price of American labor. It is against this American competition for labor that Mr. X craves help, as well as against the competition of the foreign producers.

If subsidies and tariffs for relatively less advantageous industries did not injure other home producers no one except the foreigner could object to our tariffs.

But these subsidies and tariffs raise costs and diminish markets for all other home industries which do not need such special help. They drag down the more advantageous industries at the same time they help the less advantageous lines.

This is why they are sometimes termed "the businessman's socialism." They help the less prosperous and less efficient only by dragging down the more prosperous and more efficient.

It is true that hourly wage rates may be raised so high by monopolistic labor practices that they reduce employment and wage incomes because workers are asking for more than they can produce.

But tariffs make this situation worse. They put an added burden on those industries where labor's productivity is still high relatively to the general level of wage rates. This burden consists of higher costs of materials and diminished markets at home and abroad.

Monopolies Reduce Gains from Trade

Whenever any producer starts getting by trade (i.e., buying) something which he formerly made for himself, he becomes more dependent on other people.

> He depends on them to keep on supplying the goods at less than it would cost him to make them for himself.
>
> He also depends on them to keep on buying his services so that he can get the money to buy theirs.

Economic progress is about proportional to the increase in this mutual dependency, or cooperation, between producers.

Again and again, however, producers and groups of producers have taken shameful advantage of this growing dependency of their fellowmen. They have organized monopolies to divert to themselves a larger and larger share of the gains from trade. Whether this leads to retaliation or not these monopolies reduce the total gains from trade and thereby discourage and restrict it.

> An outstanding example was the organization and policy of East Indies rubber producers. Their restrictionist policy, which continued even while the Japanese were sweeping towards their plantations, promises to be the chief obstacle to rebuilding their postwar markets. The American public no longer wants to be at the mercy of any such foreign power, private or public.*

Breakdown and prevention of such restrictionism must be, therefore, a prime requisite for increasing trade.

This includes a housecleaning for the United States as well as other nations.

> For example, our policy of crop restriction and government purchase of "surplus commodities" was precisely similar in aim and method to the restrictionist policy of the British and Dutch East Indies rubber producers.

*These monopolies, however, are usually temporary and incomplete. Despite increasing efforts to control the market, the British and Dutch rubber interests were unable to prevent a decline in the price of crude rubber from an average of 54.6 cents per pound in 1926 to 19.1 cents in 1929 and 3.5 cents in 1932.

By the Webb Act of 1919 we have permitted American export organizations to carry on in foreign trade monopolistic practices which are forbidden in domestic trade. Certain American producers took advantage of that act to gouge their foreign customers.

When will our housecleaning begin?

The first international agreement between the governments of England, United States, Canada, Australia and Argentine concerning postwar economic policy proposes a world-wide wheat cartel. This agreement of 1942 calls for allocation of world markets and price maintenance through trade restriction.

If postwar trade policies are to follow this line the Atlantic Charter becomes a mockery. Endorsement of such a proposal by the United States and the British Commonwealth is a betrayal of the liberal traditions which made these nations great.

It is black reaction towards medievalism.

Monopoly, to be effective for any length of time, usually requires the help of government. At least it must have the connivance of government. This is true of monopolies in both foreign and domestic trade.

Military victory will give the people of the United States and Great Britain power to destroy or emasculate the most important world monopolies. It will give them opportunity to break down the most restrictive trade barriers. Upon the way in which they use that opportunity will depend world peace and progress.

Does Foreign Trade Cause War?

The most important form of cooperation is economic cooperation. This means exchanging services for the purpose of making scarce and desirable things more abundant.

As nations grow in power to produce they can grow equally in power to cooperate—that is, in power to *trade.*

The most productive and industrialized nations are the world's best markets—the United States, Great Britain, Germany, France, Canada, Japan. In other words, *our chief competitors in foreign trade are also our chief foreign markets.*

The United States has had the world's second most valuable empire, but we have sold only 10 to 12 per cent of our exports to it.

Total trade of Germany with Great Britain before World War I was 20 times as great as her trade with her entire colonial empire.

> Holland customarily sold 8 times as much to Germany as to the Dutch East Indies—one of the world's most valuable colonies.
>
> Prior to 1914, France gained an African empire, rich in resources and about the size of the United States. By tariffs she sought to monopolize its trade. Yet her total trade with it was only about one per cent of her total foreign trade.
>
> "Pauper labor" makes a nation a poor market and a feeble competitor. Such laborers produce barely enough for their own needs. How can they produce large surpluses for export? What surpluses they can produce consist mainly of one or a few items for which their climate and natural resources are especially well suited.

The markets of backward nations are not worth fighting for.

> Great Britain lost in decreased trade with Germany after World War I seven times as much trade as Germany's entire prewar colonial trade. Yet, even when Britain acquired the German colonies she could not have monopolized their trade except by restricting and destroying much or most of it.

It is not possible to win the trade of advanced nations by war, even by victorious war.

In destroying trade competitors, war also destroys markets, for our chief competitors are our best customers.

FALSE IDEAS about possible gains from war and conquest may help cause war.

> Japanese and German militarists sold their people the notion that they could win markets by war. This belief is a fraud. It is such delusions which cause war.

Trade is a force for peace between nations as it is a force supporting law and order in domestic affairs.

> Informed traders want peace. The Japanese militarists had to assassinate and terrorize hundreds of leading Japanese businessmen and their political representatives in order to get their way.

Competition in trade means competition in service; war is competition in destruction.

In trade, all can gain. In war, all can lose.

By trade, backward nations advance along with the rest of mankind, not by dragging down or plundering their richer neighbors, but by learning from them and cooperating with them to increase prosperity for all.

IX. RECIPROCAL TRADE AGREEMENTS

The United States Reciprocal Trade Agreements program is one of the rare cases in which government is *removing* restrictions on private enterprise.

War Debts and Tariffs, 1914-1930

During World War I United States exports expanded rapidly with the aid of our loans to the Allies.

> The prosperity of our farmers in particular came to depend more and more on these foreign markets.

To repay these loans and to continue buying from us these European nations had to sell us goods in return.

In 1922, however, the United States raised its tariff rates to the highest level in our history, a level exceeded only by that of Spain.

European nations likewise erected new trade barriers during the next several years under several pretexts:

1. Nations who now owed us money were obliged to reduce their imports, while maintaining or increasing their exports, in order to pay their debts to us.
2. The fact that our tariffs restricted their sales to us made necessary an additional cut in their purchases from us.
3. England and France also said they must protect themselves against German goods made cheap by the depreciation of the German mark.
4. Newly formed nations, like Poland, said they wanted to build their own industries so as to be more independent of Germany, Austria and Russia from whom they had been separated.

To maintain our exports in the face of these new barriers our government encouraged private agencies in the United States to make new loans to foreigners, especially to Italy, Germany and various Latin American countries.

> These loans were justified on the ground that they helped the foreign nations build new industries or make old ones more efficient. It was argued that this would enable them to increase their exports, despite the trade barriers, and thus get the means to repay us their borrowings and to buy more of our goods.

These artificial credit props were withdrawn from our foreign trade when the stock market collapsed in 1929.

The Hawley-Smoot Tariff Act, 1930

As the years pass it becomes harder to excuse those responsible for increasing United States tariffs again in 1930.

Called together in special session to do something for the farmers, Congress in 1929 fell into a shameless orgy of logrolling for special privilege.

The following table of tariff increases on imported watches shows why this Tariff Act of 1930 had world-wide repercussions:

Class of Watch Movements	Cost Net U. S. A.	Duty Tariff 1922	Duty Tariff 1930
No. 731	$1.41	$0.75	$3.75
No. 751	2.24	2.00	4.35
No. 737	1.68	0.75	4.25
No. 757	2.41	2.00	5.85
No. 159	7.06	2.00	7.10
No. 258	5.20	2.00	7.10
No. 879	8.33	3.50	8.50

Rate classifications were made so detailed as to aim specifically at products of particular nations or of individual foreign concerns. This made our tariffs appear discriminatory.

Large rate increases were made on articles which were insignificant in relation to our total trade but which were vital to producers in other lands.

These increases in our tariffs came at a time when sound policy called for decreases.

1. We were insisting that foreign loans made by the United States must be repaid. Yet these repayments could be made only in goods. Even if the payments were made in gold most foreign countries, not producing gold at home, had to sell their goods abroad to get the gold.
2. Our most distressed domestic industry was agriculture which needed prosperous foreign markets.
3. Every nation was suffering more or less from falling prices and rising inventories. Increased freedom for traders to search out new markets was the best way to check this decline. (See above, pp. 68-69, 72-74.)
4. International goodwill had been increasing up to that point and political leadership throughout the world was more pacific and liberal than for many years. The political trend abroad was distinctly towards freer trade and closer international cooperation.

During the making of this tariff official representatives of 38 leading nations made formal protest. Popular indignation in these nations rose to fever heights when these protests were ignored.

News of our proposed rate increases were front page items in foreign newspapers.

Chambers of commerce and producer associations in foreign countries held protest meetings and demanded preparations for retaliation by their own governments.

Tariff Retaliation and Its Effects on Our Trade*

The Hawley-Smoot Tariff Act of 1930 started the worst tariff war of all time. In the following 12 months there were 60 major tariff revisions by the world's leading nations, most of them aimed particularly at excluding United States goods.

Four days after the Hawley-Smoot Act was signed, Mussolini announced that Italy in future would buy no more from the United States than we bought from Italy. (We had been selling twice as much to Italy as we bought from her.) Within two weeks greatly increased duties were levied on American products. For example, the duty on the cheapest Ford car was raised from $350 to $815 per car. As a result, the United States lost its position as leading exporter to Italy and Germany took our place. Agencies for American cars were closed out by November.

The day after President Hoover signed the Hawley-Smoot bill the Spanish government announced it planned a revision of its own tariff. Even Spanish *exporters* were calling for higher tariffs on American goods. Five weeks later the new Spanish tariff went into effect. Increases in duties on commodities which Spain had been buying from the United States ranged from 100 to 700 per cent, with special rates still higher on imports from "non-European" countries. Spain also repudiated the most-favored-nation policy towards the United States and immediately began negotiations with France and Italy to reduce rates to the old levels for goods from those nations.

The Swiss people organized effective boycotts of American goods and cancelled contracts for the showing of American automobiles in their Industrial Exhibition. As a result, while total Swiss imports in 1930 declined 5 per cent, imports from the United States fell 30 per cent, with almost all of this decrease coming in the second half of the year. In 1931 the Swiss government imposed numerous tariffs and quotas against the United States, often mentioning American products by name. At the same time she initiated a series of reciprocity agreements with other nations.

Similarly Canada and England, our chief foreign markets, retaliated with major tariff increases. Shortly afterwards, through the system of "imperial preferences" and through trade agreements with other nations, United States exporters were made to feel the chief burden of these tariff increases.

*Cf., J.M. Jones, *Tariff Retaliation*, University of Pennsylvania Press, 1934.

> France, long ultra-protectionist, in 1927 had begun to move towards a more liberal policy. She agreed to give the United States most-favored-nation treatment in return for our promise for a "most friendly" examination of her claims for reduced duties on French exports. Following our 1930 Act, however, France repudiated this most-favored-nation agreement with us and set quotas limiting imports of American goods. Meanwhile she negotiated trade agreements to reduce tariffs on goods from nations other than the United States.

All nations lost as a result of these new trade restrictions, but the United States lost most. Our exports fell as fast as imports and our share of world trade rapidly declined.

Imperialistic and militaristic parties were greatly strengthened and became dominant in Germany, Italy and Japan. Mass unemployment and depression destroyed representative government and economic liberty. Invasions of Ethiopia and Manchuria and the rise of Hitlerism are in large part attributable to the stupidity of the 1930-1932 tariff war which we began.

Sir Arthur Salter, English economist, proved a true prophet when he termed this act "a turning point in world history."

> It turned the world from increasing international cooperation to a new era of growing nationalism, trade wars, imperialism, armament races and war.

Reciprocal Trade Agreements

Under the 1930 Tariff Law the President was given power to raise or lower duties by 50 per cent, or less, on recommendation of the United States Tariff Commission.

This provision proved to be of little use in reducing even prohibitive tariffs as long as the aim of tariff policy was "to equalize costs of production."

1. Difficulties of determining differences in costs are usually, if not always, insurmountable.
2. The whole idea of basing tariffs on the principle of equalizing costs of production is nonsensical. Tariffs which "equalized costs of production" would stop all foreign trade. The only reason for buying a foreign-made article is that it is cheaper. Whenever foreign commodities come in it is because the tariff has failed to "equalize costs of production."

The flexible provision of the 1930 law was also of little value as a weapon to prevent discrimination against the United States. Our tariffs had risen so high that threat of further increases had little deterrent effect on other nations.

The Reciprocal Trade Agreement Act of 1934 permits the flexible provision to be used for obtaining concessions in rates from other nations. It adds nothing to the President's tariff-making powers. Instead, it limits this power in three ways:

1. Tariff reduction for any commodity must be made first in the agreement with the chief supplier of that article.
2. Compensating concessions in tariffs on American goods must be granted by the foreign nations with whom agreements are made.
3. Opportunities must be provided for public hearings for those likely to be affected by the agreements.

The Trade Agreements Committee in charge of the program is composed of representatives of the Departments of Agriculture, Commerce, Treasury and State, as well as the Tariff Commission. Each of these agencies has a voice in the making of these agreements.

> Indicating the difficulties involved in negotiating agreements and the care exercised, is the fact that the time taken for negotiating the first 18 agreements has ranged from 6 to 35 months, with 16 months as the average.

Agreements made under this Act may be terminated upon 6 months' notice.

In case of discrimination against the United States by a nation with which we have entered into an agreement, our Government may suspend the agreement immediately.

Trade agreements must also follow the "unconditional most-favored-nation" principle.

The "Most-Favored-Nation" Principle

This principle, which might better be termed "equality of treatment," was formally incorporated into United States commercial policy in 1923 by President Harding and Secretary of State Hughes in response to a demand by Congress expressed in the (Republican) Tariff Act of 1922. In this Act Congress directed that the United States Government demand unconditional equality of treatment from all other countries, and empowered the Executive to impose penalty duties, if necessary, on the goods of countries refusing to accord us equality.

Obviously to secure this equality treatment from other nations we were obliged to give it to them in return.

The need for this policy arose from the fact that foreign nations were making agreements with one another providing special concessions in tariff rates on one another's commodities. By means of such agreements they were gradually excluding American goods from their markets. All advantages from any agreements we might make with them or any concession we could obtain, could be offset by new agreements which they later made with other countries. This injured trade and was the source of much international illwill.

Among nations which have accepted this "equality of treatment" principle, the negotiation of a new trade agreement between any two of them becomes a matter for all-round cooperation, because each one benefits from every new agreement.

Benefits to the United States from acceptance of this principle are illustrated by the results of our reciprocal trade agreement with Canada, which ranks second only to the United Kingdom among our customers.

> Prior to our Trade Agreement with her, Canada had made numerous treaties giving special rates to various foreign nations other than the United States. When we made our new agreement with her under the Reciprocal Trade Agreements Act we secured the benefits of all of these treaties in addition to the other concessions which we secured. Altogether this one factor reduced Canadian duties on 700 different American products besides the reductions on various specific products mentioned in the agreement.

Should Congress Pass Upon Trade Agreements?

Agreements made under this Act do not require Senate ratification.

> During the past 150 years the United States Government has entered into over 1000 such executive agreements with foreign nations, covering matters such as commercial and consular relations, patents, trademark and copyright protection, postal conventions, navigation, radio and aviation agreements, and settlement of claims. The courts have upheld the constitutional validity of such agreements whenever the question has been raised.

Congress still retains its full right to make tariffs. Therefore, it may in effect veto or repeal any trade agreement. Moreover, Congress outlines the principles under which the reciprocal trade agreements program shall be administered.

It seems reasonable that an administrative body should set tariff duties for particular commodities for the same reasons that administrative bodies fix railroad rates or administer price controls—if we must have discriminatory tariffs.

> That representative bodies are not well fitted for such tasks is demonstrated by the unholy mess which our own Congress has made of tariffs from 1816 to 1930. Representative bodies in most

other nations, e.g., France, have done no better in this matter. Whenever a representative body begins handing out public favors to particular trades, classes or individuals, the public interest is endangered by logrolling for special privilege.

Results of the Program

The trade of the United States, from 1935 to 1939, expanded much more rapidly with the trade-agreement nations than with the others. Our exports to the trade-agreement nations have increased somewhat faster than imports from them. This probably does not indicate that we "out-traded" them by getting greater reductions in their tariffs than we made in our own. But at least it is an answer to the opposite charge—that the United States made the greater "concessions."

> The idea that a nation makes a "concession" to others when it reduces its tariffs arises from the fallacy that the gain from foreign trade comes from exports, rather than from imports.
>
> In fact, however, imports are the only sound economic reason for exports, for the same reason that what a producer gets in return for his labor is his economic reason for working.
>
> Furthermore, the only sound reason for exchanging our services is that we thereby get things *more cheaply* than if we produced them for ourselves.
>
> Therefore, the gain from reducing or removing a trade barrier, such as a tariff duty, goes primarily to the importing nation which is thereby enabled to get its goods more cheaply. The gain to the exporting nation comes indirectly through increased power to buy in return, but only when that purchasing power is exercised to increase imports is there any gain from increased exports.
>
> A reduction in United States tariffs benefits us as well as the rest of the world. The gain is still greater, however, when foreign nations also reduce their tariffs, as they do under the Reciprocal Trade Agreements program.

Frequent complaints are heard concerning threatened or actual loss to home producers from Reciprocal Trade Agreements. That was to be expected. What is surprising is the insignificant amount of damage that has been done to any group and the large gains accomplished in stimulating trade for many leading lines of American agriculture and industry.

Vested Interests Often Resist Progress

Any method for cheapening commodities requires changes on the part of competing producers. "Adapt or die" is a law of life no people can safely ignore.

Improvements by one producer or opening of cheaper sources of supply compel other producers to do one or more of the following:

a. suffer decreased incomes;

b. adopt the new methods;

c. change to other occupations.

These changes are more or less distasteful or costly. At best they make it necessary for producers to give up other things they would like to do with the time and energy necessary to avoid loss. At worst they cause serious loss of income, unemployment, or bankruptcy to the less inventive, enterprising and adaptable producers.

Producers threatened by cheapening of their commodities find it easy to believe that the change is injurious to the nation as well as to themselves. Therefore they often organize to prevent the change.

Successful opposition to cheapening of commodities is all the easier when the gains consist of small decreases in price for thousands or millions of consumers.

The cost of protecting United States sugar producers in 1938 was estimated by the Department of Agriculture at $350,000,000 a year. Total value of sugar cane and sugar beets produced in the United States was about $70,000,000 a year and customs receipts on imported sugar amounted to less than $45,000,000. Total net cost to the United States, therefore, was over $200,000,000 per annum without counting in what the sugar growers could have produced in other lines.

This cost, however, amounted only to about $1.50 per customer. As against this small per capita cost is the fact that average subsidy payments to sugar beet growers in 1937-1938 were $365 per annum, or $23 per acre of harvested beets in addition to gains from higher prices brought about by the quota system.

Few consumers would consider it worth while to contribute money for a campaign to save themselves $1.50 a year through repealing the uneconomic sugar tariffs and subsidies. Domestic sugar producers, on the other hand, can afford to make sizable contributions to fight for its continuance.

Under these circumstances the public interest is protected only by courageous and farsighted leadership, particularly leadership of business enterprisers.

What Hurts Consumers Hurts Business!

Businessmen must realize that as a class they have more interest in the consumer's prosperity than in maintaining the profits of businessmen in other lines.

Slogan of the American Knights of Labor was "the heart of labor beats with a common throb." The economics of this was no better than its physiology, but it had wide popular appeal. Many businessmen fall into a similar error in supposing that what helps *any* business helps *all.*

Business concerns compete for the consumer's dollars as wage-earners compete for jobs.

> When one business, through monopoly or tax subsidy, takes more money from consumers, other lines of business get that much less.

Business concerns in one line have a common interest with concerns in other lines in increased *production.* Each benefits from the success of his suppliers and his customers in reducing costs and expanding output. However, they have conflicting interests in *price policies.* Each loses as the other is successful in getting more dollars for a given output.

Subsidies and restriction of imports for the benefit of high-cost lines injure the more advantageous industries:

1. by depriving them of markets at home and abroad;
2. by raising their costs of living and costs of materials.

So widespread is the injury from our present tariff barriers that many American producers whose costs are now higher than those of foreign competitors are losing more than they gain from our protectionist system. They lose more from restriction of the domestic market and from increased costs of the goods they buy than they gain from higher prices on their own products.

The Gain from Foreign Trade

The gain from trade, foreign or domestic, lies in the saving of labor.

> Trade is a labor-saving device which promotes prosperity in the same way as labor-saving machinery. That is, both trade and labor-saving machinery make goods cheaper and more abundant. They free labor and purchasing power for increased production and purchase of other goods.

Increased freedom for foreign imports usually stimulates exports. By these exports we pay for the increased imports. But the gain in exports is not the real gain to the nation from increased foreign trade. The gain is in the *imports* and this gain would be still greater if we were given these imports free of charge.

Let us suppose that 1000 workers have been producing for home consumption 1000 tons of glass marbles per annum at a total cost of $1,000,000.

Now let us suppose that a foreign nation found a way of supplying these marbles to us at a cost of only $100,000. What is the gain from accepting the foreigner's offer?

The gain is not in the $100,000 of exports which would go to pay for the new import, or in the employment of 100 new workers in the exporting industries.

Instead the gain would consist in the $900,000 which consumers saved in purchase of marbles. That money is now available AT HOME for buying new, home-produced articles for which otherwise there would have been no market.

The gain in labor consists in 900 workers now freed to produce the new commodities.*

The gain from foreign trade is to be measured in terms of the cheapness of the imports as compared with the costs of home production. The cheaper they are, the greater the gain.

Sunlight is a very cheap service coming not only from a foreign country but from another sphere. Would we be more prosperous if we boarded up our windows and refused to profit from the cheapness of free sunlight? Industries supplying artificial lighting might gain new business, although even this is doubtful. But certainly the nation as a whole would lose.

Increased freedom for trade builds new industries for the very reason that it enables consumers to satisfy former wants with less money and less labor.

This explains why fears that trade may result in over-specialization of a nation's industries are groundless. Trade promotes prosperity and the more prosperous a nation becomes the greater is the diversification of its occupations.

Postwar Opportunities in Foreign Trade

Reciprocal trade agreements offer a most effective means for promoting freedom of enterprise, prosperity and international cooperation after the war.

1. The war and preparations for war have greatly multiplied re-

*However, importing foreign goods so that we may transfer our own workers to new industries is very different from importing foreign laborers who have to look for jobs in *existing* industries. Tariff duties *depress* wage levels by raising costs of living. Immigration restrictions *raise* wage levels by reducing competition for jobs.

On the other hand, immigration restrictions also differ from restrictions on employment, such as exorbitant trade union initiation fees. Restriction of immigration reduces the nation's total labor supply relatively to demand. Employment restrictions for one's fellow citizens merely shove workers out of one occupation into others less attractive, or else force them into the ranks of the unemployed.

strictions on private traders throughout the world. These can be most effectively attacked by the give-and-take methods of trade agreements.

2. Many industries in all countries have built capacities far beyond probable domestic requirements. Opening of foreign markets will help many of these to avoid drastic deflation.

3. European and Asiatic nations, devastated by war, will need food, machinery and raw materials for rehabilitation. Their only hope for buying these lies in foreign trade.

4. Hopes of United Nation workers for a better world after the war, including high wage levels, can be fulfilled only by utmost efficiency in use of labor. This means:

   a. mass production,

   b. specialization of labor and machinery in lines for which they are best fitted, and

   c. trade, including foreign trade.

5. United Nations leaders have maintained that all people should have equal access to the world's sources of raw materials. This can be accomplished only through creating corresponding equality of opportunity for all peoples to sell their goods to the owners of these raw materials. A large share of the sources of these materials are owned by United States citizens. That means we also must open our markets to foreign nations so that they can buy from us goods which they can hardly produce themselves.

Civilized peace means cooperation between free peoples. And the most important form of cooperation is economic cooperation. This means exchanging services for the purpose of making scarce and desirable things ("economic goods") more plentiful.

As nations grow in power to produce they also grow in power to cooperate, that is, in power to trade. Development of such powers of production and trade is the basis for economic prosperity and for all human progress.

The danger of war may never be removed. Insofar as it persists, certain restrictions on enterprise, both in foreign and domestic relations, may be necessary for national defense.

For example, the United States probably will deem it wise for some years to come to maintain a certain amount of synthetic rubber production at home, no matter how cheap natural rubber may become relatively to the synthetic product. We may also decide to conserve certain exhaustible resources through embargoes on exports.

Nevertheless, these restrictions should be recognized for what they are—part of the price of national defense—not as promoters of "employment" or "prosperity." They should, therefore, be kept down to the minimum necessary for national defense and constant attention should be given to reducing them where possible.

> In some cases private enterprise or government may maintain stockpiles of imported materials needed for war production. In addition, through subsidies or favorable government contracts, a nucleus of the domestic industry may be kept going in peacetime. In wartime the stockpiles may be used to tide the nation over the interval necessary to expand this industrial nucleus to wartime needs.
>
> Such a policy may promote national security better than a protective tariff which would raise costs for all domestic users of the critical materials and thus restrict peacetime progress. The first battles and campaigns of a war are won by the nation which is better prepared. But the final victory usually goes to the nation with the greater industrial capacity. This industrial superiority is not built by a policy of huge armaments and self-sufficiency, but by mass prosperity based on specialization and trade.

The future strength and security of the United States depend on:

1. great industries to produce high levels of welfare for all the nation in time of peace and superiority of armaments in time of war;
2. the friendship and cooperation of foreign nations.

Foreign trade must play an ever-expanding role in building these foundations of national greatness and world peace.

X. RESALE PRICE MAINTENANCE

The "fair trade" law permits a producer of branded or trademarked articles to require that the buyer of his products shall not resell them at prices below those fixed by the producer.

These laws also make such a price-maintenance agreement binding on all sellers of the goods in a given state if it has been accepted by any one seller.

The effect of this law is to enable one merchant or a group of merchants, through agreement with a manufacturer, to set the markup for all other merchants dealing in that manufacturer's products.

The markup is the price of the merchant's services. Therefore, the "fair trade" law permits one producer and any one of his distributors to fix the price which all other merchants must charge for their services.

This legalizes fixing of standard rates of pay for distributors of "fair trade" commodities.

> Similarly, fixing standard wage rates for all workers in a given trade, even those working on relief projects, is a chief aim of trade union policy. When a union wins an agreement with one employer calling for a higher rate of pay, it contends that all employers should come up to the same standard.
>
> It argues, of course, that this does not standardize wage rates, since any employer is free to pay *more* than the union standard. Advocates of resale price maintenance use the same sort of argument in reply to the standardization charge.

The first of the "fair trade" laws legalizing resale price maintenance contracts was passed in California in 1931. In 1933 this act was extended by the provision that a contract with one distributor becomes binding on all distributors of the particular article. This law set the pattern for the other 44 states which now have this type of legislation.

The Miller-Tydings bill, passed by Congress as a rider to an appropriation act in 1937, gave Federal sanction to resale price-maintenance agreements.

Theory of the "Fair Trade" Laws

The purpose of these laws is to restrict price competition.

> To a large extent they are a by-product of the 1930-1939 depression, which greatly intensified price competition. In 1931-1932

most of the nation's business was conducted at a loss. In other words, "selling below cost" was a general practice. The idea that this price cutting was the cause of the depression produced the N.R.A. and helped secure the enactment of the "fair trade" and "unfair practices" acts.

Arguments for these acts are:

1. Price cutting destroys the value of the trademark and the customer goodwill built by the producer.
   a. It makes consumers believe the article is inferior.
   b. Other merchants refuse to stock articles subject to price cutting.
2. Price cutting is fraudulent when a merchant sells a well-known brand below cost in order to attract trade.
3. A producer should have the right to set the price at which his own goods are to be sold.

Enforcement of "Fair Trade" Laws

Legal means for enforcement of these laws is the injunction process.

More effective, however, have been legal or illegal agreements and boycotts among distributors. Dr. Edwards, Economic Consultant for the Anti-trust Division of the United States Department of Justice, states:

> "The bill originated with retailers' pressure, and has been used by them to force the issuance of contracts whether the manufacturer wanted them or not . . . Repeatedly the officials of retail drug organizations have had to urge their members not to be too hasty in boycotting manufacturers who announce retail prices lower than the retailer thinks necessary."

> "In California, an aspirin manufacturer was forced by boycott to issue resale price contracts against his will . . . In the same state the manufacturer of Pepsodent toothpaste, who had experimented with resale price contracts under the California law, decided to withdraw these contracts . . . Thereupon the druggists organized a campaign to put Pepsodent under the counter and to switch to other brands. This campaign was so effective that the offending company made public apology at a subsequent convention of the National Association of Retail Druggists and, as a token of its contrition, subscribed $25,000 to a fund to lobby for resale price maintenance in other states."*

*"Memorandum for the Assistant Attorney General," February 10, 1941. Cf. Ralph Cassaday, "Maintenance of Resale Prices by Manufacturers," *Quarterly Journal of Economics,* May 1939, p. 459.
It has been my own experience that proposals for putting more "teeth" in the "fair trade" laws come mainly from secretaries and officers of certain retailers' associations. So do most letters of protest against criticisms of these acts.

Others testify to the same collusive influences:

> "Fair-trade committees, composed of independent retailers for the most part, have been organized and the manufacturer who wants to avoid trouble will work through these groups . . . Members of the retail associations which these committees represent may refuse to sign any contracts that do not carry the official approval of the committees. This usually means that manufacturers with nonconforming agreements may have difficulty in getting cooperation and their sales may start sliding down."*

> " . . . the manufacturer of consumer goods in his dealings with wholesale and retail distributors has faced the organized attempt to force on him a price policy distinctly determined by the interests of these groups . . . In some industries retail associations exercise almost dictatorial power over retail margins and have become the determining factors in the shaping of the entire merchandising policy of producers."**

Enforcement of this price control for retailers requires no such elaborate bureaucracy as the Agricultural Adjustment Administration. Because it has fewer members an organization of merchants can restrain competition with a much less complicated apparatus than is needed to reduce competition among farmers. However, the objectives and results upon community prosperity are much the same in the two cases.

"Fair Trade" Laws Restrict Competition

1. By a contract with one merchant, a manufacturer under this law can legally force all dealers in a "fair trade" article to act precisely like a combination in maintaining the stated price.
2. The law increases the incentive for illegal collusion among merchants to compel manufacturers to issue fair trade contracts. It does this by providing a legal means for enforcing such contracts once obtained.
3. Opportunity to control resale prices also encourages price "understandings" among manufacturers to maintain their own prices.
4. By restraining price competition price maintenance increases the tendency for competition to take less desirable forms, such as special advertising allowances and generous "free samples."
5. Under this law a chain store is still free to carry out a cut-price raid on an independent store through use of its private brands. However, the independent cannot retaliate and defend himself because he is handcuffed by fair trade contracts.

*_Printers' Ink_, August 19, 1937, p. 80.
**_Dun's Review_, July 1938, p. 15.

"Fair Trade" Laws Raise Living Costs

1. About 50 per cent of total retail trade is in identified (trade-marked or branded) items which may be made subject to the law. Surveys show that prices of items covered by "fair trade" contracts were raised on the average 30 per cent or more in the chain and cut-rate drug stores.
2. These laws eliminate or reduce seasonal price cutting.
3. Reduction of excess stocks is made more difficult. This increases need for costly hand-to-mouth buying by merchants.
4. Manufacturers bid for business by raising the retailers' margin instead of by offering consumers a better product at a lower price.
5. Competition among merchants takes the form of more aggressive advertising, uneconomic use of stamps and premiums, and price-cutting on a few items not covered by resale price contracts instead of competition in reducing over-all distribution costs.

The Manufacturer's Interest in the Loss Leader

Use of an article as a loss leader temporarily increases sales volume and builds consumer knowledge of the product.

Long-range effects on the manufacturer depend on:

a. his comparative efficiency in production;

b. the proportion of manufacturing cost represented by promotional work, advertising, or "puffing."

1. Merchants who refuse to stock an article which has been subjected to loss leader pricing help build the markets of other merchants in that commodity. Long-run demand for the commodity is stimulated because the price cutting introduces the article to new customers. If they like it they will come back for more. The price can then be restored to a level covering production and distribution costs for the nearest competitor in respect to productive efficiency.

2. In case of those commodities whose price covers disproportionately large expenditures for advertising, or high profits for successful promotion, loss-leader price cutting opens opportunities for substitute articles at lower prices. In this way "puffing" expenses are squeezed out of costs. Competition is diverted from promotion to production, a change common to all occupations as they "come of age."

In preventing this development resale price maintenance keeps business in the medicine-man stage.

It restricts opportunity for producers who aim at giving consumers maximum value for their money. This it does by encouraging merchants to patronize manufacturers who "fair trade" their products at high markups which can be maintained only by costly advertising.

Whose Product Is It?

But should not a manufacturer have the right to set the price for his own product?

1. Before the "fair trade" laws were enacted any producer distributing through bona fide agencies and retaining title to the goods until their final sale could fix retail prices as he pleased.

2. Any producer could announce the retail prices he desired and could refuse to sell to distributors who did not maintain these prices.

When a producer, however, sells an article at his own price to another person who then is the owner?

The distribution, or resale, of the article is the service of the merchant. It is the price of this *merchandising service* which is set by the "fair trade" contracts, not the price of the *manufacturer's* product.

Under competitive conditions the merchant's markup varies from one merchant to another, even for the same article. Types of merchandising service vary widely and they command a variety of prices.

> For example, the neighborhood independent may provide delivery service and credit, whereas the chain store operates on the cash and carry plan. The neighborhood store offers convenience, the downtown store may offer lower prices. One store maintains a wide selection of goods and the services of a prescription counter. Another specializes in popular packaged and trademarked articles.

Resale price-maintenance contracts standardize the price of the merchants' services and thus force merchants to charge and consumers to pay the same price for widely different types of service.

The "fair trade" laws, therefore, operate to restrict competition between merchants and they lead merchants to patronize manufacturers who cooperate in this restrictionism.

Do "Fair Trade" Laws Make Trade Fair?

1. Loss-leader price-cutting is a bargain offered to draw trade.
   a. It is an economical and efficient form of advertising—"money talks."
   b. It is honest to the extent that the buyer gets his money's worth in purchase of the loss-leader commodity.
2. Abuse of the loss-leader device is restricted in several ways:
   a. Prices cannot be placed below wholesale levels without attracting purchases by dealers.
   b. Consumers know from experience that cheapness in one line does not mean cheapness in all. Therefore, they tend to concentrate their purchases on the "loss-leader." This discourages the practice by most merchants.
   c. Altogether apart from the "fair trade" laws, manufacturers have the right to refuse to sell to merchants to whose price policies they object.
3. "Fair trade" laws divert competition from "more for less" to "less for more."

   Dealers push the high markup items for which costly advertising by manufacturers builds and maintains the market. "Puffing" the reputation of high-priced items replaces price competition.
4. Resale price maintenance restricts the opportunity for low-cost merchants to expand at the expense of high-cost merchants. Therefore, it retards progress in distribution methods.

*"For sporadic cases of under-pricing it proposes to substitute a universal policy of over-pricing."**

Price Maintenance Causes Unemployment

A rapid decline in general price levels, such as that of 1930-1932, which gave rise to a wave of "fair trade" legislation, is a *symptom* of depression, not the primary *cause.*

Causes of depression are as numerous as the types of catastrophe which may befall mankind from natural causes or from human errors.

They bring about reduced output of goods and services (as in the case of a drought or flood), or contraction of credit (as in the case of unwise investments or "over-speculation"), or both.

In any case the community's total rate of spending is reduced.

*Belmont Frank, *Four Free States*, p. 29.

This means that buyers must either

a. pay less for each commodity and service, or

b. buy fewer goods and services.

Price maintenance forces buyers to the second alternative—purchase of fewer commodities and services. This causes reduced output and unemployment. Thus it accelerates the downward spiral of declining production and falling incomes.

When all prices, profits, wages, salaries and interest charges decline together the losses are widely distributed. Unemployment and loss of real buying power are kept to a minimum.

Attempts at price maintenance aggravate the losses and tend to concentrate them on fewer persons (that is, on those who are less well organized or whose services are considered less essential by the buying public).

General price maintenance is impossible when the community's total spending is declining. Maintenance of commodity prices, rates of markup or hourly rates of pay merely intensifies unemployment and aggravates the decline of wage incomes, salaries and profits, which are the real prices of producers' services.

Why Resale Price Maintenance Restricts Enterprise

Resale price maintenance, therefore, restricts enterprise in two ways:

1. by retarding growth in efficiency necessary for expansion of real buying power in good times;
2. by increasing unemployment and thus aggravating the decline of real incomes in depression.

XI. POSTWAR BOOM OR DEPRESSION?

From January 1, 1942, to December 31, 1943, the total amount of money, bank deposits and government bonds in the hands of individuals and unincorporated business increased by $62 billion. This compares with "savings" of less than $10 billions for the best year prior to 1941.

In other words, these two years have been six boom years in two. And the end is not yet!

War Boom Psychology

This rising tide of money and the increased rate of spending again is making the business future seem bright and fair.

> A Fortune Management Poll, published in October 1943, showed 70 per cent of America's business executives expecting a "general boom" after the postwar reconversion period.
>
> Nearly 75 per cent believed that private business will then be able to provide "reasonably full employment," although a year earlier nearly 60 per cent were expecting fairly large unemployment.
>
> "Wartime shortages and wartime savings," it is argued, "will give us after the war the best business in our history. All we need do is plan for big markets and we shall have them."

Many people, in fact, say that our first postwar problem will be the prevention of a runaway inflation and boom.

> Hence they advocate retaining price controls and rationing until production has caught up with demand.

Some persons say that the war spending by government has shown us how to prevent depressions and unemployment.

> "In two brief years enlarged government spending *(spending had been very timid under the New Deal)* was able to translate a situation of unemployment into one of full employment . . . and [we] have doubled the national income. *It has been done entirely . . . because the government decided to buy some eighty billion dollars' worth of the goods . . . and to distribute them, free of charge . . . .*"*

Others only slightly less inflation-minded say, "If private enterprise does not provide full employment after the war, government must, can and will."

*J. Donald Kingsley, The University of Chicago Round Table discussion, August 22, 1943. Italics ours.

So have inflationary booms in other years and in other generations brought hope that the secret of perpetual prosperity had been discovered at last. Such waves of mass optimism are what make booms—and also depressions.

"If Wishes Were Horses . . . ."

But, if money, credit and reckless spending could perpetuate prosperity, depressions would have vanished from the scene long ago.

> One nation after another, throughout recorded history, has tried the inflation cure. As far as we know the attempt has always ended in disaster.

If the destruction and privations of war made for good business, we could create history's greatest boom by continuing the war until all wealth is destroyed and nothing is left but piles of paper money, government bonds, and bank books.

If shortages of goods create markets and jobs, China and India should have been the best places to do business and look for work over the past century.

If unsatisfied desires for goods make markets United States business should have been booming in 1932 after consumers had experienced two or three years of lean living.

Would the half-naked Bushmen of Australia make themselves more prosperous by exchanging I.O.U.s? Would they build markets by printing bales of money and bonds?

After the war our people will own two or three hundred billion dollars' worth of government bonds. But bonds mean debts and debts don't ordinarily create prosperity.

> At best, the payment of interest and repayment of principal will merely transfer money from one class (the taxpayers) to another (the bondholders).
>
> At worst, producers will be taxed for the benefit of many nonproducers. Taxes are burdensome to the individual even when he knows that the proceeds are going to a fellow citizen.

Or is there some magic in United States Government debts that other government debts do not possess?

Of course, those who regard government bonds as a future guarantee of good business expect that the bonds will be converted into money after the war, not through taxation, but through expansion of the currency, including deposit currency.

> In other words, the magic, if any, which some people see in our government debt really comes, not from the debt, but from the inconvertible paper money which they expect to be issued with the debt as backing. They are subject to the delusion that such backing somehow removes the curse usually attached to inconvertible paper money.

But does an abundance of money assure prosperity and jobs?

No Lack of Money in 1939

In 1939 the people of the United States had more money than ever before in our history. They had $625 of money and bank deposits per capita as compared with only $525 per capita in 1929.

Yet in 1939 the net income per capita was only $523 as contrasted with a per capita income of $654 in 1929.

In 1939 our total supply of money and deposit currency was about $81 billions as compared with about $46 billions in 1920. Yet the total net income of the nation was $68 billions in both years.

In 1939 average unemployment was 8,795,000 compared with average unemployment of 429,000 in 1929, 558,000 in 1920, and 4,754,000 in 1921, the highest figure prior to 1931. (National Industrial Conference Board figures.)

The money was there but something was keeping it from circulating as fast as in the boom years of the '20s.

Some people believed that government spending was making private investors hold back from fear of inflation.

For a few months in the fiscal year 1938, however, with the help of social security taxes and a reduction in rate of spending, the Federal Government more or less accidentally balanced its cash income and outgo. Instead of this bringing about further recovery, it was accompanied by a sharp business recession.

> This seemed to confirm the widely held theory that private enterprise could no longer get along without the aid of inflationary spending by government. Outcries arose for fresh doses of this artificial stimulus and the Federal Administration obliged by increasing the rate of spending for relief works.
>
> Not, however, until the war inflation of 1941-1942 was unemployment reduced to the level of the '20s. And even in these years of war and inflation the working force was still not as fully employed as in 1929 since average working hours per week were 10 to 20 per cent less than the average for the earlier decade.

Causes of Business Stagnation in 1939

What was keeping money from circulating to maintain full employment and production in 1939?

Have these causes of business stagnation been removed? If not, why should we expect private enterprise to thrive better after the war than before?

> The same 1943 poll which showed 70 to 75 per cent of American business executives expecting a postwar boom showed 63 per cent expecting less freedom for enterprise after the war than before. Is freedom no longer necessary for business prosperity as long as the people have plenty of money, fat bank accounts and fistfuls of government bonds?

The factors which brought on the depression, intensified it and prolonged it have been discussed. (See above, pp. 39-52.) These factors should be reviewed in relation to 1939 conditions.

1. Discriminatory taxes on job making

   Heaviest tax rates rested on job-makers and on the chief sources of funds for industrial expansion. In 1939 a corporation with headquarters in the Midwest, for example, was liable for the following taxes:*

Federal	*State*	*County and Municipal*
normal income	income	real property
capital stock	franchise	personal property
old age benefits	out-of-state corporation	privilege license
unemployment insurance	sales	railroad siding
manufacturer's excise	vehicle licenses	inspection fees
unjust enrichment	unemployment insurance	
federal gasoline	gross income	
	gross receipts	
	use	
	chain store	
	gasoline	

   In 1939 net earnings of all corporations before taxes were only 20 per cent less than in 1929. But total taxes on these corporations were 53 per cent greater. Consequently total net corporation earnings after taxes in 1939 were only 50 per cent of the 1929 total and were 30 per cent less than in 1927, a year of business recession.

   The nation's railroads paid $361 millions of taxes in 1939 and had left $141 millions of earnings. In 1938 their total deficits were $87 millions after paying taxes of $346 millions.

*Adapted from "The Problem of Business Incentives," E. P. Schmidt, United States Chamber of Commerce, p. 24.

The aim of tax policies and government benefit payments in many cases seemed to be to penalize job-makers (employers) in order to make job-seeking (unemployment) more attractive.

2. Uneconomic wage policies

The theory of trade union and government policy in 1939 was that higher prices for labor's services cause an increase in number of wage earners hired.

This theory has not worked in practice and it has not been supported by the weight of opinion among professional economists. Nevertheless, it has been treated as a sacred cow by most politicians and is still "the party line" for all good trade unionists.

Under the influence of this fallacious theory hourly wage rates in leading industries were forced upwards or maintained with little regard for demand and supply relations in the labor market.

> In 1938, for example, a year of sharp business recession, hourly wage rates in manufacturing remained almost entirely unaffected by the great increase in number of workers looking for jobs. At the same time, the Federal Wage and Hour Law was adopted to raise wage rates for low-wage groups.

An increase in wage rates and wage income resulting from an increase in demand for labor is all to the good. Such an increase raises scales of living without increasing unemployment.

But increases in rates which are brought about merely by fiat of government or by restrictive policies of labor organizations cause unemployment and reduce total wage income.

The second type of increase in wage rates, an increase effected by coercion and restrictionism, played a major role in putting an end to business recovery in the summer of 1933 and again in the spring of 1937.

3. Making work illegal

One of the most curious superstitions of modern times is expressed in the trade union slogan, "The shorter the hours, the higher the pay." The popularity of this superstition is shown by the way in which the restrictive provisions of the Federal Wage and Hour Law have come to be accepted as "social gains."*

*Proponents of the measure say, "The Federal Wage and Hour Law does not restrict working hours per week. It merely requires time-and-a-half pay for extra hours." But if the time-and-a-half provision does not reduce average working hours then neither do fines for speeding slow down traffic.

The over-time provisions of the law were intended to reduce working hours. That they had that effect is well demonstrated by the difficulty this nation has experienced in raising average hours during the war. Only by means of wasteful cost-plus-fixed-fee contracts, by reckless expenditure of government funds, and by radical extension of

Reduction in length of the working day or week may be a social gain when it results from increased productivity and increasing competition for labor among employers. In this way average daily and weekly hours were reduced at least one third during the century from 1830 to 1930. (See below, p. 149.)

Very different is the reduction of hours effected by coercion. At best this coercive restriction of hours is a job-sharing device.

Workers with jobs are forced to give up part of their employment to the unemployed.

But when weekly output per worker is reduced while government or a union insists that weekly wages remain the same, restriction of hours increases unemployment. This is because it raises labor costs per unit of output, puts more employers "in the red" and thus reduces the demand for labor.

Coercive restriction of hours also adds to unemployment by creating industrial bottlenecks. For example, when bricklayers lay fewer bricks the demand for brickmakers and hodcarriers declines.

4. Restriction of investment

In 1939 only about 12 per cent as much new capital was going into business through investment in stocks and bonds as in the years 1923-1926.

This decline in rate of investment was partly due to the increase in taxes and decline in net income experienced by the investor classes,—individuals with net incomes over $5,000. (See above, pp. 47-49.)

In part, however, it was also due to restrictions on investment arising out of the securities and exchange legislation of 1933-1934. Costs and difficulties of selling new securities have been enormously increased by new requirements set up by law and by the Securities and Exchange Commission.*

5. Restriction of output

Organized restriction of output through crop control and featherbedding in 1939 was restricting purchasing power for all classes. For example, tons per man-hour handled by San Francisco longshoremen declined 40 per cent from 1933 to 1938 because of organized labor slow-downs and make-work regulations. Over the same period the efficiency of Los An-

bureaucratic control over the labor market has the average working week been raised above 40 per week.

The Federal Wage and Hour Law held back war production 10 to 15 per cent in 1940 and 1941. That lost production cost many precious lives and did much to prolong the war.

And since then it has been a leading factor in promoting costly and dangerous inflation.

*Cf. Benjamin M. Anderson, "What Can the Government Do to Promote Postwar Reemployment?" *Commercial and Financial Chronicle,* October 21, 1943, p. 1600.

geles and Long Beach workers declined 31 per cent and that of longshoremen in Seattle and Portland 20 per cent. In the same class of restrictions on output should be placed our Federal Government's annual license fee of $600 per annum on each manufacturer of oleomargarine. To this Wisconsin adds another $1000 per annum.

6. Restriction of trade

Besides its prohibitive tax on the manufacturers of oleomargarine, Wisconsin has a tax of $500 per annum on wholesalers who handle it, $25 on retailers, and taxes of $5 to $25 on boarding houses and hotels which serve it, besides a special sales tax of 15 cents per pound. California forbids its public schools to use textbooks printed outside the state. Maine levies a license fee of $3,000 on distillers, brewers or wineries using out-of-state agricultural products as compared with a fee of $100 for users of Maine products.

The California Pro-rate Commission and Director of Agriculture, on vote of 65 per cent of the growers (representing 51 per cent of the production), may restrict the marketing of any farm crop (except figs and certain grapes) for the state as a whole or for local zones. These restrictions have been applied from year to year to a number of California products.

In 27 states there are laws and taxes discriminating against margarine; 32 states restrict sales of out-of-state eggs; 20 prohibit importation of filled milk (a low-cost pasteurized and vitamized food made by extracting animal fat from milk and substituting an equal amount of vegetable fat); 27 states discriminate against out-of-state wine or against wine made from out-of-state grapes; and 24 states have similar discriminatory measures relating to beer.

Restrictions on out-of-state trucks and political pressure to maintain or raise freight rates on purchases outside the local community are other common methods of restricting trade.

Almost every chamber of commerce in the United States has helped build or maintain such trade barriers.

Such discriminatory measures multiplied rapidly during the depressed '30's. In restricting trade, slowing down the circulation of money and reducing purchasing power, they were precisely similar to a partial destruction of our transportation systems. The scarcity theories used to support such restrictive policies, if carried to their logical conclusion, would have us tear up our railways and destroy our roads in order to protect local industries against outside competition.

Have 1939 Obstacles Been Removed?

Only the artificial stimulus of inflation enabled private enterprise to carry on under the anti-enterprise conditions of 1939.

Will the burdens and restrictions on enterprise be less numerous and repressive after the war? The way in which various vested interests continue their restrictionism in wartime bodes ill for the postwar period.*

Or can government's inflationary spending—buying goods to give them away, as Kingsley puts it—continue indefinitely to maintain employment and production? Why cannot government finance peacetime construction as it finances wartime destruction, that is, by creating new money and buying goods to give away?

To answer the inflationists we must show

a. why inflation must stop;

b. how purchasing power and employment may expand without inflation. (See below, pp. 112-129.)

Let us first consider why inflation eventually must end.

"Easy Come, Easy Go"

Money is useful only when it is scarce and hard to get.

> Then people will work to get it. If stealing and other predatory methods of getting it are blocked and if they cannot print it or find it easily, then they will produce goods to exchange for money. Thus we get the production and trade necessary for prosperity.
>
> But when large numbers of people can get money without earning it they stop working so hard in production for the market. They also tend to spend lavishly and consume extravagantly.
>
> Thus they waste their own time and that of others whose products they consume. This waste is more than failure to do better. It soon becomes actually injurious to the welfare of all concerned.

This is true for government as for individuals.

> When government can get money without earning it by services to its citizens the results are waste and tyranny. (See above, p. 58.)

*Cf. "Featherbedding Hampers the War Effort," by John Patric with Frank J. Taylor, *Barron's*, Feb. 8, 1943; "Remove Union Restrictions and Increase Shipyard Production by One Third," by John Patric, *Reader's Digest*, June, 1943; "Here's Why There's Nothing to Spread on Your Bread," by Harland Manchester, *Reader's Digest*, December, 1943.

Wartime inflation is somewhat less dangerous than peacetime inflation because:

1. War needs are simpler, fewer and more readily determined than peacetime needs.
2. Fear of the enemy and desire for victory restrain extravagance.
3. The end of the war leads to a reconsideration and revision of policies.

But even wartime inflation does not create prosperity. Aside from its use as an artificial stimulant to overcome the effects of anti-enterprise restrictions, the chief effect of inflation is (1) to conceal the impoverishing effects of war and (2) to shift the costs of war from certain classes to others.

> War guts the national economy. The new facilities built for war production are worth only a fraction of their cost when reconverted to peacetime uses. Furthermore, the facilities needed for peacetime production deteriorate because of increased rate of wear and decreased rate of repair and replacement.
>
> As war drags on producers, therefore, find themselves holding increasing quantities of paper (currency and bonds) while their productive facilities deteriorate.
>
> War inflation also weakens the economy by placing a disproportionate share of the war costs on the fixed-income groups.

As the national economy deteriorates efficiency declines and costs of production rise despite all price controls. Therefore, ever-increasing doses of inflation are necessary to maintain employment.

That is why inflation, once started, is hard to stop.

> Like a habit-forming drug, it sets up within the national economy destructive forces which increase the craving and apparent need for more and more liberal doses.
>
> A wealthy nation, like the United States, can endure more of the inflation poison than a poorer nation like Germany, just as a strong and healthy person can usually stand up longer under repeated doses of a harmful drug. This has made some people believe that this nation is immune from the evils of inflation.

But inflation never fails to exact its toll of waste and disorder. Numberless depressions, as well as demoralizing booms, are evidence of this fact. Like the marijuana habit, an inflationary policy must end sooner or later—and better soon than late—if the nation is to avoid a disastrous financial, economic, moral and political breakdown.

When Inflation Ends

The rate of inflationary spending by the United States Government may not decline until after the war.

> The inflation of World War I in the United States lasted for a year and a half after the war because government expenditures and deficits continued to increase. The "postwar boom" of 1919-1920 was, therefore, part of the war inflation. The slump occurred shortly after government spending and deficits began to decline.

The date at which United States Government spending and deficits will reach their peak in the present war depends on political decisions as well as on military events.

> For example, a decision to finance an increasing proportion of the war budget by taxes and by non-inflationary borrowings would hasten the time when the inflation would reach its peak.
>
> The extent to which the United States decides to police or aid other parts of the world would be another factor in determining the date at which government's inflationary spending might cease.

When that date arrives, however, a deflationary spiral and postwar depression will not be prevented merely by the huge existing volume of money and bank deposits.

Money must be spent if it is to stimulate business, and the rate at which individuals spend their money depends on the outlook for future income as well as on the volume of their savings. If they fear a decline in their incomes most people will reduce the rate of their spending even when they have considerable money in reserve. Therefore, a deflationary spiral may be expected to follow closely on the heels of any sizable reduction in government spending if total income of individuals declines.

Total individual income will decline unless spending by private enterprise expands as fast as spending by government declines.

Such expansion of private spending cannot be brought about by any program of heavy government spending because private enterprise cannot hire the workers supported by government spending. Somehow, sometime, 20 to 25 million workers and soldiers whose jobs now depend on government spending must transfer to jobs dependent on private spending. Any unnecessary spending by government slows down the transfer, retards the expansion of peacetime production, and makes more difficult the task of restoring private enterprise.

Holding a Bear by the Tail

When government embarks on an inflationary course it takes a bear by the tail. To hang on becomes more and more difficult. To let go becomes more and more dangerous.

To maintain the soundness of the currency, to protect its credit, and to permit conversion to peacetime employment under private enterprise, our Federal Government must reduce its rate of spending.

On the other hand, any reduction of government's deficits and spending threatens to set in motion a downward spiral of employment, individual incomes and spending.

The huge accumulation of money and bank deposits during the war will not in itself prevent this downward spiral after the war.

> Deflation and depression did not occur after other inflation periods because the total amount of money and deposit currency was suddenly reduced. They came about because the rate of inflation and the rate of spending declined.

These wartime "savings" do threaten to prolong the conversion period by making individuals more reluctant to accept new jobs.

They also add to the danger of runaway inflation in case government borrowing and spending after the war should destroy confidence in the currency or public credit.*

> In that event people would rush to buy commodities and real properties at any cost. This, together with government's spending, might cause a runaway inflation.

It is vitally important that government spending and the inflationary gap be greatly reduced after the war if we are to restore private enterprise in peacetime pursuits and prevent a runaway inflation.

But will private enterprise be able to take up the slack and maintain total purchasing power and employment?

How readily private enterprise can expand production, employment and purchasing power will depend on a host of factors, including:

freedom to produce,
freedom to bargain and trade,

*Those who expect price controls to hold down prices "until postwar production catches up with consumer demand" forget that this increased production will itself put enough new money into circulation to buy the increased output. The war-boom "savings" will remain intact, constantly adding to the inflationary pressure, as long as government pursues its inflationary course. This will provide a good excuse for continuing price controls and incidental bureaucratic regulation of business indefinitely.

tax burdens and their distribution,
adaptability, honesty and dependability of producers,
administration of justice,
class consciousness and class antipathies,
understanding leadership,
popular confidence in authority.

Are these conditions likely after the war to be more favorable to enterprise than in 1939?

Postwar Tax Burdens

Despite all foreseeable economies the present war, like other wars, is likely to keep the cost of our Federal Government far above prewar levels for many years.

Costs of the greatly increased war debt, a two-ocean or five-ocean navy, a far larger army, a vastly greater air force, aid to millions more war veterans, increased "social security" payments, and aid to foreign nations must all be added to the prewar budget.

These high costs of government seem to make necessary the maintenance of present tax revenues for several years after the war if the inflationary gap in the Federal budget is to be closed.

How will these revenues be raised?

Current tax rates and policies would effectively prevent expansion of private enterprise after the war. In fact, private enterprise could not hold its own under prevailing tax rates on profits and on high incomes, even if all other war restrictions were removed.

Only war inflation is maintaining a sufficient level of profits to offset the crushing effect of war taxes on business.

The destructive effect of current taxes is evident in the returns to stockholders after payment of Federal taxes. Consider, for example, a corporation earning 8 per cent on the stockholders' capital and paying out in dividends all profits left after paying the minimum 40 per cent corporation income tax. The following table shows the rate of return to stockholders in various income brackets after they pay their Federal income taxes.

Stockholders in	\$ 4,000-\$ 6,000	surtax	bracket	get	3.41%
"	10,000- 12,000	"	"	"	2.83%
"	18,000- 20,000	"	"	"	2.16%
"	50,000- 60,000	"	"	"	1.10%
"	100,000- 150,000	"	"	"	.48%

Such returns are not sufficient to attract or hold private capital in business. Yet these slight returns are subject to further depletion in states having personal income and property taxes. And nothing is said of excess profits taxes, or of the effects of the graduated features of the "normal" corporation tax, or of the multiplicity of other taxes to which business is subject.

Will the American people at the close of the war permit immediate repeal of the excess profits tax, rapid reduction in corporation income tax rates, and rapid reduction in surtaxes on incomes above $10,000? If not, equity capital will be in short supply and private enterprise will decline.

Tax increases are not, however, the only wartime addition to burdens and restrictions on enterprise.

New Restrictions on Enterprise

1. Since 1939 a host of new bureaucratic restrictions have been placed on business in the name of price control and production control. Many of these may continue after the war.

   For example, after the war continuation of price controls will be urged (1) to prevent postwar deflation or inflation, whichever seems imminent at the moment; (2) to equalize consumption; (3) to allocate scarce materials to those employers who will expand employment most quickly.*

   Price controls and other regulations seriously restrict enterprise in wartime. Not only must the enterpriser, as before, get agreement among wage earners, investors and customers as to what shall be produced, how it shall be produced and how the produce shall be distributed. Now he must also get agreement among various government officials, boards and bureaus on the same questions. This slows down business, raises costs, and diverts business energy and initiative from other tasks necessary for the expansion of private employment and prosperity. The restrictive effect of these controls, however, will be more apparent after the stimulus of war inflation ends.

2. Government ownership of industrial facilities and materials will add to the difficulties and risks of private business.

   By the end of the war, government will own 30 to 40 per cent of the nation's industrial facilities. For government to operate these facilities will prevent expansion of private enterprise.

   Yet if government disposes of them to private producers at low prices it will create problems for competitors operating facilities paid for at higher prices. On the other hand, if govern-

*This proposal for postwar allocation of materials has been advanced by business spokesmen as well as by government officials and has a well-established place in many postwar plans. Yet it calls for prolonging the war distortions in the labor market. Postwar readjustment should involve transferring millions of workers from manufacturing to trade and service lines. If government aids *any* industries according to the amount of peacetime employment which they provide, it should aid those industries which call for relatively few workers in manufacturing compared to the number needed to distribute and service the product.

ment holds them off the market or holds them at high prices it will deprive the nation of important opportunities for jobs and goods while creating a source of continual business uncertainty concerning what use is to be made of them.

Similar problems will arise in connection with some $20 billions of surplus products and materials which government will find on its hands.

At the end of the war industrial capital will be frozen in partly finished work for more than $75,000,000,000 worth of unfinished war contracts. Invested in these contracts will be the funds which industry must have to meet reconversion costs, pay rolls, and the bills for new materials and supplies. This contrasts with only $7,500,000,000 frozen in outstanding war contracts on November 11, 1918. The ability of private enterprise to get working capital for reconversion will depend on the promptness and generosity with which government pays on these uncompleted contracts. This problem is all the more serious because war taxes have prevented business from building reserves such as helped to speed the conversion after World War I. For example, United States Steel Corporation did twice as much total business in 1942 as in 1916. But the amount set aside for future needs was only $11,800,000 in 1942 in contrast with $201,800,000 in 1916.*

3. Postwar reconstruction will be made more difficult by many wartime changes in markets and production facilities.

   For example, the United States will have capacity to produce many materials and commodities far in excess of demand even at prices covering merely labor costs.

   East Indies producers may have to find new crops to replace rubber. Japan will be looking for new commodities to replace silk.

   Solution of these problems will not be made easier by the fact that the war is intensifying international hatreds, fears and suspicions.

   Disruption of private markets in foreign exchange, destruction of credit standing for whole nations, and widespread demoralization of peoples will add to the difficulties. In some nations by the end of the war the private enterpriser will have been almost entirely replaced by the totalitarian bureaucrat.

4. In the United States unbalance in wage rates as between occupations, together with increasing power of trade unions and their continued aggressiveness in maintaining and raising hourly rates, constitutes a serious obstacle to postwar reemployment of labor in peacetime pursuits.

*"Postwar Problems," reprinted from *Nation's Business*, August, 1943.

From August 1939 to August 1943, for example, average hourly wage rates in Los Angeles County rose 53 per cent for bakery workers, 48 per cent for aircraft workers, and 47 per cent in the canning and preserving industries. But they rose only 15 per cent for furniture workers; 12 per cent for workers in the laundry, dry cleaning and dyeing industries; and 3 per cent or less for workers in printing, newspapers and periodicals.*

Postwar labor markets are likely to be subject to changes in demand and supply as great and as rapid as those which have produced these wartime changes. Will labor organizations and government bureaus permit the corresponding changes in wage rates necessary to restore peacetime equilibrium? Or must there be long and costly strikes and lockouts before adjustments can be made?

Money Must Circulate

No matter how much money a nation has, business will stagnate unless the money circulates.

This circulation can be completed only if producers spend in maintaining production while consumers spend in maintaining consumption, and savers spend in building investments.

Most of the nation's spending is done by producers. Sales of goods to final consumers make up a relatively small fraction of the nation's gross volume of business transactions, possibly 5 to 10 per cent in the United States in a prosperous year.

Business often slows down and workers lose their jobs even while consumer spending is increasing. This happens when the ratio of costs to selling prices becomes unattractive to a sufficient number of enterprisers and investors. Business owners then liquidate their stocks of goods and allow funds to accumulate in idle bank balances.

Will postwar conditions encourage spending by producers as well as by consumers?

Let us suppose that any decrease in spending by discharged war workers and returned soldiers is offset by an increase in spending of war savings by those who still have jobs.

Will the profit margins (after taxes) be such as to induce producers to maintain the spending cycle?

*Freezing these wage discrepancies into place after they have performed their function of drawing workers into more essential industries has helped intensify wartime labor difficulties.

Some producers, of course, will make profits. Others will have losses. Those who make profits will keep going. If their profits are high enough they will expand.

But will the number of profitable and expanding enterprises be more than sufficient to offset the losing and contracting ventures?

The answer will not depend on the amount of money in consumers' hands to be spent at the end of the war, but on the abundance of opportunities for producing at a profit.

A Nation Can Readjust—If Free

History shows that a nation can readjust to peacetime conditions in a few months, or at most in two or three years, if producers are free to arrange the terms of trade and to reap the rewards of their own industry and skill.

It also shows that, regardless of monetary conditions and policies, unemployment and economic stagnation may persist for many years if freedom of enterprise is restricted by government or by private organizations of vested interests.

Which course will America choose?

Government deficit-financing and extravagant spending in the postwar period may postpone the necessity for making the choice. But it will increase the difficulties of readjustment when this policy stops as sometime it must. It will continue at an ever-increasing pace the economic degeneration of inflation, the moral degeneration of legalized racketeering, and the political degeneration of totalitarianism.

But if government should end its inflationary policy at the close of the war, could free private enterprise generate and circulate enough buying power to restore and maintain employment in peacetime production?

XII. GOOD MONEY IS ALWAYS SCARCE

Can free enterprise provide consumers with enough money to buy all the products of industry at profitable prices?

Some people say that wage earners, under private enterprise, are not paid enough to buy the products of their own labor.

This, they believe, leads to periods of overproduction, unemployment and depression.

This "under-consumption theory" of depressions is a basic idea in Marxian communism and in most socialist thinking.

Many of its adherents, however, sincerely believe themselves to be friends of enterprise and opponents of socialism.

The under-consumption theory of depressions is used to support various measures supposedly designed to put more money in circulation and increase consumer buying power:

a. increased public spending financed by inflationary methods;

b. discriminatory taxation of the investing classes;

c. monopolistic and restrictive policies by government, trade unions, farmer organizations, and business;

d. increasing "social security" payments to non-producers.

These policies are rapidly destroying private enterprise. Their results are socialistic whether those who advocate them consider themselves socialists or not.

The fallacy of the under-consumption theory, therefore, must be exposed if we are to restore and preserve private enterprise. Otherwise, unsound monetary and financial policies will destroy it even while everyone professes to favor it.*

Money Is Essential to Progress

The economic progress of every tribe or nation has kept close pace with improvements in its monetary and financial policies.

Economic progress depends on increasing production.

Increasing production depends on increasing specialization among workers, as well as on increased use of tools and machinery.

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*Stuart Chase is an outstanding exponent of the doctrine that we must accept socialist monetary and financial theories and adopt socialistic tax and spending programs in order to "save" private enterprise. See, for example, his *Where's the Money Coming From?* published by Twentieth Century Fund, N.Y., 1943.

Increasing specialization by workers depends on development of trade.

Development of trade depends on progress in use of money.

Monetary and financial progress has been closely related to the development of constitutional government.

The currency has had to be protected against counterfeiting by private citizens and against debasement by government.

A sound banking system can exist only where the citizens' savings are secure against arbitrary seizure by government, as well as against theft by bandits.

Moral progress, in the form of increased honesty and mutual confidence, also has been an essential factor in monetary and financial progress.

Both in private finance and public finance, improvements made during the 250 years before 1914 compare favorably with the progress in natural science and industrial techniques.

How Banking Began

In making these monetary and financial improvements, private enterprise in banking played a major role.

Modern banking in England began with the goldsmiths who accepted deposits of gold and other valuables for safekeeping.

As their deposit receipts began to change hands in place of the gold which those receipts represented, these goldsmith-bankers helped to reduce costs of handling money and to speed up the rate of circulation. They were also thereby providing a more convenient medium of exchange than gold.

At the same time their accounts were important in helping to preserve records of business transactions.

Gradually these goldsmiths took to lending part of the funds left with them, sharing profits with the depositors.

As time went on bankers found themselves dealing more and more in claims on wealth other than gold. These claims consisted of property deeds, mortgages, bonds, promissory notes and the like.

They accepted these property rights in repayment of loans.

They also made loans on the basis of such property instruments. That is, they "accepted," or honored bills drawn against them by borrowers who pledged with them their rights to real estate or other sources of income.

This last mentioned development of banking, in the view of some observers, gives banks power to manufacture credit and money (deposit currency).

Through centralized control of this power financial reformers seek to stabilize business.

By raising the price of bank credit or by restricting the supply of it in boom times they hope to prevent inflation. By reducing the price of bank credit and increasing its supply when business begins to decline they hope to restore prosperity.

Values Create Credit

Under private enterprise, however, the power of the banker to manufacture credit and currency is essentially the same as that of every producer—no greater and no less.

This is the power that arises out of owning valuable goods or being able to render valuable services.

A shoe manufacturer who owns a stock of shoes can sell these goods on credit to a merchant. The merchant may give the manufacturer his promissory note. This note is a new credit instrument which the manufacturer may use in trade.

The merchant, in return, gets this credit from, or "has credit" with, the manufacturer because he is able to perform valuable services in marketing the shoes.

If the merchant and manufacturer were sufficiently well known, their promissory notes could circulate like bank checks or paper currency.

They could use such "due bills" to pay their workers and meet other expenses of doing business.

Those who received these bills could use them to buy the finished goods.

Suppose, for example, that there were 1000 pairs of shoes which the manufacturer "sold" to the merchant on credit for $5000. Suppose, further, that the merchant gave the manufacturer 5000 promissory notes for $1.00 each, which the manufacturer could endorse and pass on to wage earners and suppliers of materials, so that he could meet his expenses in manufacturing new shoes to replace those he had just sold.

Then suppose that the merchant met all of his other expenses of doing business (rent, interest, wages and so on) with similar small-denomination promissory notes to a total of $4900, and that he then issued $100 worth of such notes to himself for his own salary and profit.

The merchant has then issued $10,000 worth of notes. He has put into circulation $10,000 worth of credit instruments which are essentially similar to bank checks.

If, meanwhile, he has priced and sold his stock of shoes for $10,000, he can meet and retire all of his promissory notes, including those which he issued to himself as profit and to his creditors as interest.

Thus producers could create the circulating medium necessary to take their goods off the market. There would never be too much or too little credit, or currency, outstanding as long as the total prices of goods offered for sale equalled the total value of currency issued and spent.

In fact, the coins and notes issued by well-known merchants have circulated like money at various times in history. During the depression of 1930-1939, for example, the due bills of businessmen had considerable local circulation in New York City.

Under private enterprise, therefore, credit may arise with the production of valuable commodities, properties and services, as producers learn to know and trust one another and as they develop knowledge of values and markets.

The volume of this credit depends on estimates of the value of goods and services offered for sale or as pledges for loans.

This is essentially the way in which private credit is created and circulated. The role of the banks is not to manufacture credit but to investigate it and endorse it.

Bankers Speed Circulation of Credit

Bankers specialize in circulating credit.

In the above example the banker may accept the shoe merchant's note as security for a "line of credit," or a checking account, to be used by the merchant in marketing the goods.

Or he may accept the shoe manufacturer's note, possibly with the merchant's note as additional security, for a line of credit to be used by the manufacturer in continuing production.

In either case the banker is not "manufacturing" credit any more than the merchant or manufacturer does when the merchant gets the credit directly from the manufacturer.

The banker is merely substituting, on the credit instrument used for general circulation, his own better known name for that of the manufacturer or merchant. He is permitting the merchant or manufacturer to use checks, or orders to pay, drawn on a bank instead of the promissory notes of some less well-known producer.

This makes credit instruments circulate more easily. In other words, it gives "currency" to credit.

Farmers, merchants and manufacturers help create credit by producing valuable goods and services.

The banker for the most part merely *endorses* the credit thus created by producers.

Under private enterprise, he adds to the total volume of credit only as he helps producers increase output of goods by specializing more effectively in their own lines.

When government enters the banking field, however, it may give bankers power to manufacture credit by enabling them to convert into legal tender credit instruments not backed by other values.

This has been a chief cause of inflation, deflation and economic instability in modern times.

"To Him that Hath Shall Be Given"

Credit is self-renewing when it is used to produce goods whose value in the market-place is equal to the costs of production.

Loans used in this way can always be repaid out of the proceeds of the enterprise.

They perpetuate the loan fund, or total volume of credit.

When credit is used unproductively one of two things may happen:

a. The loan may not be repaid. In that case the lender's future power to advance credit is reduced.

b. The loan may be repaid by the borrower's drawing funds from other uses, perhaps selling property which he had intended to keep. In that case the borrower's future credit will be reduced.

In either case unproductive use of credit eventually reduces the total amount of it available to the economy as a whole.

For a time any individual, group or nation can look prosperous on borrowed money. But if the funds are used wastefully, the final result is greater poverty than before.

Since the loss falls first on the borrowers and lenders most nearly responsible for unproductive investments, credit tends to gravitate to more efficient producers.

Those who use it more productively are better able to repay their borrowings and to accumulate property-rights. Thus credit grows with their productive ability and the value of their properties.

With this growth in credit goes increased opportunity to expand operations and to direct or control production.

Conversely, under free enterprise, inefficient producers sooner or later experience decreasing credit and lose power to direct or control production.

This does not mean that free enterprise increases the concentration of wealth and economic power.

On the contrary, free enterprise opens opportunities in proportion to each producer's ability to make use of them.

Every producer's abilities are limited. As he attempts to expand his control beyond his abilities he makes more mistakes and thus reaches the limit of his power to use credit effectively. This leaves open opportunities for competitors.

Furthermore, efficient use of credit by one producer expands opportunity for producers in non-competing lines by increasing their incomes. These increased incomes provide increased opportunity to save and invest.

The more complex the economy the greater is the amount of intelligence required to direct it and the greater is the number of individuals required to share financial responsibility. (See above, p. 10.)

In a free economy every producer shares the responsibility for planning. At least he is responsible for choosing his occupation, seeking a job, budgeting his income and spending for his own needs.

As he increases his earning power he correspondingly increases his opportunity to buy or to lend. Increased buying or lending means increased economic influence and responsibility, because through buying and lending we induce others to do our bidding.

Mob Psychology in Use of Credit

Wide diffusion of responsibility under free enterprise is necessary to get the advantages of mass enterprise and mass initiative.

But this wide diffusion of freedom and responsibility makes a free economy subject to the risks of mob psychology.

To some extent the errors of individuals may compensate for one another. The unforeseen losses from unsuccessful investments, for example, are offset by the unexpected gains from unusually successful ventures.

At times, however, large numbers of producers may make the same type of error. Then there is first a boom while they hope-fully make their investments, followed by a depression when the returns prove insufficient to pay the costs or to meet the obligations incurred.

Booms result when borrowers and lenders become overoptimistic concerning the amounts which can be produced and the prices at which goods can be sold.

The face value of the credit instruments in circulation then expands faster than production of goods. This causes rising prices and rising incomes in terms of money.

Some lines become over-expanded in the sense that consumers will buy the output only at prices which are too low to cover all the costs of production. Rising prices in domestic trade may also cause an adverse balance of payments in foreign trade. This adverse balance of payments causes loss of gold and securities and necessitates a contraction of credit.

These conditions cause losses to investors and creditors and necessitate deflation of prices and credit.

If these losses are quickly absorbed and widely shared, no serious decline in employment need occur.

Depressions result from widespread pessimism concerning prospects for production and prices.

Credit then contracts faster than production. This causes falling prices and declining money incomes.

If all prices and incomes fall together, no harm need result.

But some producers who are favored by long term contracts or who are better organized, for a time may be able to maintain their prices and incomes. This concentrates the losses on other producers, some of whom are forced to close down entirely because their prime costs (i.e., costs other than "overhead" costs) exceed selling prices. Thus the losses spread.

"Agree With Thine Adversary Quickly"

A nation may increase unemployment:

a. by restricting the freedom of producers to accept terms offered for their services;

b. by creating discontent among producers with the terms being offered for their services; or

c. by permitting or encouraging producers to insist on being paid more than their services are worth to others.

Money may be plentiful and prices high. Yet large-scale unemployment may persist because wage earners are asking for more

than the value of their services in production, or because government or trade unions forbid them to accept what employers can afford to pay.

When all members of an enterprise are on a percentage basis, no one need lose his job merely because the total income of the firm declines. Each member gets less but each still gets something as long as any business remains.

Whaling expeditions used to operate in this way.

However, when most of the workers and investors in an enterprise insist on rates of pay determined before the returns are in, the whole burden of declining business falls on a few.

These specialists in risk-taking make more in good times by this arrangement, but they often find themselves getting less than nothing when business falls off. Then they shut down operations and everybody loses.

Even in good times the average profit margin is comparatively narrow.

In 1928-1929 the average net income after taxes of all United States corporations was 5 per cent of gross receipts. In 1941-1943 it was 3.56 per cent. From 1919 to 1935 total corporation profits were 2.17 per cent of gross receipts.

Only a slight rise in costs, therefore, or a comparatively small decline in prices and sales volume suffices to turn profit margins intc losses for great numbers of business concerns.

To stabilize employment, production and real purchasing power, therefore, one of three things is necessary:

a. greater flexibility in wage rates, rents and interest charges; or

b. wider profit margins for risk takers; or

c. increased supplies of equity, or venture, capital.

The more easily the enterpriser can adjust wages, rents and interest charges in times of declining business, the narrower can be his margin of profits in good times as well as bad, and the more stable will be employment and production.

Flexibility of wage rates is especially important because wages make up roughly 70 per cent of the total cost of production.

In 1940 employee compensation amounted to 70.4 per cent of the total realized income of the United States. Interest, rents and royalties together made up about 10 per cent. Net profits of incorporated business were about 7 per cent of the total national income. Incomes of farmers and unincorporated enterprises accounted for the remaining 12 to 13 per cent.

In recent decades wage rates have become more and more inflexible in times of depression. This, not the supposed disappearance of our frontiers, is the reason for the growing problem of unemployment. Unless wage earners will readily agree to accept reductions of wage rates when business is declining, we must expect periods of mass unemployment, with consequent intensification of business depressions.

Why Depressions?

Some critics ask, however, "Why should business ever fall off? Why should it not continue to grow as long as people want goods? All that is needed is to put enough money into their hands and we shall create a perpetual boom for every business."

The answer lies in the limitations of human intelligence and the instability of life, especially progressive life.

> Man rules the animal kingdom because he preferred progress to stability. Creatures like snails and turtles, who put security before progress, were long ago left behind in the struggle for domination.
>
> But progress requires experimentation, trial and error. It means suffering losses from mistakes as well as enjoying the gains from successes. It requires elimination of the wrong as well as survival of the right.
>
> Probably most new ideas are wrong. At least many of them are. But men often must spend their own time and resources, as well as those of other people, in trying out a bad idea before they discover what is wrong with it. Such mistaken expenditures of time and resources are bad investments. Yet they are an unavoidable price of progress.

Governments often have tried to make business booms perpetual. These attempts always have failed because they meant perpetuating mistaken investments as well as wise investments.

Bad investments cannot be liquidated without losses to the investors and to others depending on them. And when these investments have been financed by borrowed funds, or loan capital, the results are especially disastrous.

> Some of these bad investments are on a small scale and are offset by effects of good investments by other people. Average wages, for example, advanced on the average about 3 per cent per annum in the United States from 1922 to 1929, not because the average wage earner was working harder, but because he was sharing in the gains from increasing use of machinery and labor-saving methods.

> Every now and then, however, great numbers of people are carried away together on a wave of enthusiasm for some form of investment. Then excesses result even though there was a sound basis for some expansion.

Booms and depressions, therefore, are inherent in all progressive societies, and attempts to prevent them have often made them worse.

This is not to imply that nothing can be done or has been done to guard against business depressions and reduce the wastes resulting from them.

> Those who say that our financial institutions have failed to keep pace with the progress of industrial methods forget that our industrial progress would have been impossible without the development of modern financial methods.
>
> Unwise interference with these financial techniques is now threatening to destroy or hamstring the industrial efficiency which some people mistakenly believe has "solved the problem of production."
>
> Especially dangerous is the interference which transfers banking functions from the hands of competing enterprisers to centralized, bureaucratic agencies.
>
> Such restriction of enterprise and centralization of control does not simplify the task of financial management. Neither does it increase the amount of intelligence brought to bear on it. Instead, it puts all of the community's financial eggs in one basket.
>
> *And this basket is too large for any small group of individuals to carry.*

In a press statement, March 13, 1939, the Board of Governors of the Federal Reserve System said:

> "Experience has shown, however, that (1) prices cannot be controlled by changes in the amount and cost of money; (2) the Board's control of the amount of money is not complete and cannot be made complete; (3) a steady average of prices does not necessarily result in lasting prosperity; and (4) a steady level of average prices is not nearly as important to the people as a fair relationship between the prices of the commodities which they produce and those which they must buy.
>
> "Steady prices and lasting prosperity cannot be brought about by action of the Federal Reserve System alone, because they are affected by many factors beyond the control of the Federal Reserve System."

Non-banking Sources of Credit

The truth is that even the banks, with the help of all the other specialized financial agencies—investment houses, insurance companies, security market operators and the like—cannot discharge all of the financial responsibilities of our economy without help.

These responsibilities are shared by all investors, lenders, merchants, and other producers who act as creditors and enterprisers.

Most of those who borrow for productive purposes also have some capital of their own invested.

This capital which producers own is their "equity." It is used as security for borrowings. It is also used to extend credit to others. *It is the seed-corn of credit.*

Non-banking credit is one of the most important sources of buying power.

Loans between individuals, charge accounts, open book accounts, and due bills are illustrations of this non-banking credit.

It helps determine the volume and direction of buying and production.

Since it can increase or decrease independently of bank credit it acts in some degree as a counterweight to bank credit.

It is used to finance numerous, small, individual enterprises which the professional financier will not, or cannot, handle.

Often these small beginnings become large undertakings. For example, non-banking sources supplied the capital for the beginnings of the Bell Telephone Company and the Ford Motor Company.

Purchasing Power Is Produced

The problem of maintaining purchasing power is essentially a problem of organizing and directing production in all of its aspects, including marketing.

Purchasers can buy only what has been produced.

Credit depends on possession of valuable goods or ability to produce them.

The role of government in maintaining the purchasing power ot its people should be considered in relation to its ability to encourage production.

The following principles, therefore, should determine monetary policy:

1. Money is useful only when it is scarce.

   Food and clothing would still be useful even if they were produced in such abundance that everyone could get all he wanted without paying for them.

   But money is useful only when people don't have enough of it.

   Then they will work to get it. In working for it they produce food, clothing, entertainment and other things needed for national prosperity and strength.

2. Money does its work by going from one person to another, that is, by *circulating.*

   In this also it differs from other useful things, like bread or shoes, which finally stay with someone who uses, or "consumes," them.

3. The amount of buying and spending depends on the velocity of circulation as well as on the total amount of outstanding money and credit.

   The amount of money and bank credit in the United States was about 30 per cent greater in 1939 than in 1929, but prices and the volume of business were considerably below 1929 levels because of a lower velocity of circulation.

4. Circulation of money creates purchasing power and prosperity only when it gets useful things produced and moving into the hands of consumers.

   Policies which restrict production and trade hold back buying power no matter how much money is put into circulation.

5. Most of the nation's spending is done by producers in the process of production, not by the final consumers.

   Farmers buy land, machinery, seed and labor to raise crops.

   Processors erect buildings, buy machinery and materials and hire labor to make the finished goods. Distributors spend money in transporting and marketing them.

   In this buying and selling for production and trade, credit is generated and money is circulated.

   Whatever slows down these processes slows down the creation of both credit and values. Whatever speeds it up increases the rate and amount of spending.

6. Producers will continue their spending and circulation of money only as long as profit margins promise to be sufficient to cover the risks and responsibilities involved.

7. **Unproductive use of credit ultimately reduces the community's purchasing power in two ways:**

a. Such use of credit wastes productive resources and reduces the supply of goods offered for sale. This reduces the purchasing power of money.

b. It ultimately leads to a contraction in the total volume of credit or in the velocity of its circulation, or both. Loans that are repaid out of the sale of goods remain available for further use. Such funds can be reloaned again and again. But loans used to finance waste or idleness must be repaid, if at all, out of money drawn from other uses. If not repaid, the lender's future power to lend and the borrower's future power to borrow are so much reduced.

8. Periods of deflation, following unproductive uses of credit, are often aggravated by disputes over how the losses should be distributed. Recovery is often delayed by excessive costs and red-tape involved in making necessary adjustments of capital structures, prices, wage rates and methods of production.

9. All classes should be encouraged to build reserves of credit to aid in reconstruction and recovery from periods of deflation.

   For business concerns this calls for creation of "equity capital."

   This equity capital, built in large part out of reinvested profits, provides the assets on which may be based needed credit expansion in times of emergency. The greater the volume of equity capital the greater is the power of business to obtain credit or to give credit.

10. Repeated experience has shown that free private enterprise can generate more than enough spending power to keep pace with the output of goods.

    In periods of deflation, such as that of 1930-1932, credit is contracting. The supply of it is insufficient to distribute (at the prices being asked for them) all of the goods and services offered for sale.

    But such shortages of credit result from previous misuse, or waste, of credit.

    Continuous expansion of credit along with production is possible only as long as the credit is wisely used. That is, it must be used to produce goods in such proportions that buyers will take the entire output at prices covering costs of production. If the quality of credit is good, quantity will be adequate.

11. Repeated experience has shown that government is less economical and efficient in use of credit than is private enterprise.

    The greatest inflations have been carried out by governments, e.g., those of the United States during wartime, those of Germany, Russia and other European nations during and after

World War I, and the inflation of the French Revolution. Government also played a leading role in the 1922-1929 inflation of private credit in the United States. (See above, pp. 39-40.)

Government agencies are operated by human beings capable of mistakes like other people. Methods of selecting government officials are on the whole inferior to methods of selecting leaders in private enterprise.

More important, however, is the fact that government officials are not risking their own funds. Therefore, they have less direct incentive for economy and efficiency in spending those funds, especially borrowed funds. To newcomers in Congress the political cynics say, "If you want to be reelected, vote *for* all appropriation bills and *against* all tax measures."

Because of government's coercive powers it can carry mistaken policies further than can private enterprise. By taxation or by repudiation of contracts (e.g., abandoning the gold standard) it can continue unsound policies by shifting losses to groups which are politically weak, although they may be economically important. Private enterprise, fortunately, does not have such privileges.

How Government May Help

However, government in several ways may aid private enterprise in generating purchasing power and in directing it to productive uses:

1. Government agencies can help collect and make available facts needed by private enterprise in planning for the future.

2. Government can help remove obstacles to production and free exchange, such as monopolies, trade barriers, and needless red-tape.

3. It can help break down rigidities during a period of readjustment and thus facilitate recovery.

   For example, bankruptcy proceedings, which are for the purpose of revising contracts with investors and creditors, should be made simple, economical and rapid. Trade unions should be prevented from maintaining barriers to free exchange of services. Business monopolies should be prosecuted.

4. Government can encourage the building of private equities, which are the chief sources of private credit.

   At the present time this requires a large reduction in tax rates on business profits. Profits provide an incentive to business spending. Reinvested profits furnish assets on which an expansion of bank credit may be based.

Profits also permit expansion of output by those producers who, because of their efficiency, can pay higher wages to labor, provide higher returns to investors, and give better bargains to consumers.

5. Government can to some extent postpone *needed* public works to be carried on in periods of abnormal unemployment.

   So far governments have not shown themselves to be more successful than the general run of private investors in business forecasting. They usually have done most of their borrowing and building in boom times along with private enterprise and so have been compelled to retrench in depressions.

   The chief obstacle, however, to use of government investment as a counter-weight to private investment is the tendency to use government credit as a means of maintaining prices and wage rates. This prevents necessary readjustments and prolongs the period of readjustment and depression.

   Government spending, even in depressions, should be governed by the same economic considerations as influence private enterprise. This means keeping costs low, using efficient methods, paying no more than necessary for labor and materials, and spending only for those things which will repay their costs through increasing the efficiency of the nation as a whole.

What Government Should Not Do

Several things government should not do because they discourage and prevent the development of private sources of purchasing power.

1. It should not undertake projects which can be carried on by private enterprise. The WPA, for example, drove private contractors out of the field of public building. This caused a contraction of private spending and private employment.

2. Public relief for the unemployed and the unemployables should be undertaken as a means of relieving suffering, not as a means of increasing purchasing power.

   Hand-outs to non-producers—for example, payments to farmers for plowing under their crops—reduce the nation's purchasing power in the same way that unproductive use of credit by private enterprise reduces purchasing power. It reduces quantities of goods to be purchased, deprives producers of credit, raises costs of production and reduces profit margins.

   Needlessly generous payments to the unemployed discourage their enterprise and prevent their re-employment.

3. **Above all, government should not attempt to make money abundant.**

To the individual an increase in his supply of money means an increase in his purchasing power. He sees in money the key to all the economic goods he wants.

To the community, however, money is useful only insofar as people don't have enough of it and will work to get it.

The real national income, or total national purchasing power, is increased by production of goods, not by manufacture of money.

Therefore, sound government policy should be directed to increasing the amount of useful work done for the money which the community has to spend.

This means removing obstacles to production, especially man-made obstacles, such as monopolistic agreements which prevent would-be producers from making the most efficient use of their abilities.

To the inflationist or "managed currency" advocate, however, insufficiency of money seems a chief obstacle to production and a chief cause of restrictionism by organized labor, farm and business groups:

"Wartime inflation abolished unemployment in the United States and elsewhere. It caused trade unions to give up many restrictive policies. Instead of farmers' asking for crop restrictions they now complain of shortages of labor and machinery needed to increase output."

The advocate of a "managed currency" grants that a runaway inflation would be costly. But he asks, "Why repeat the mistakes of other nations who carried a good thing (currency expansion) too far? Let us continue inflation only up to the point of full employment. Beyond that point we can prevent inflation by curtailing government spending, by raising rediscount rates and by increasing taxes so as to keep total demand for goods in step with total supply."

"If All the Land Were Apple Pie . . ."

What inflationists and managed currency advocates overlook is that the *quantity* of money, credit or wealth depends on its *quality.*

A carload of German paper reichsmarks in 1923 represented less real money than one American paper dollar.

A bushel of bonds may be worth no more than a bushel of newspapers.

One piece of metal is waste for the scrap pile while another is a valuable instrument, depending on differences too minute to be visible to the naked eye.

Differences in the way money and credit are used ultimately determine their quantity. Decreases in quantity arise from waste, or misuse, of money and credit. While such abuses continue, attempts to increase quantities in circulation are futile.

National prosperity does not depend on how much money people have or on how hard they work so much as on what they spend their money for and how *effectively* they use their time.

Economic progress is much more than a matter of multiplying the quantities of articles and services.

> The average American in 1929 was enjoying nearly 3 times as much real income per annum as his grandfather did in 1849. But the 1929 income did not consist in 3 times as much of the same kinds of things as people consumed 80 years ago. Doubling the quantities of every commodity and service now available to consumers would not double the national income. Most of the extra food, for example, would go into garbage cans to increase the difficulties and costs of garbage disposal.

The most difficult problems in expanding production are *not* maintaining full employment or multiplying quantities of commodities.

Instead, the really difficult problems are:

1. finding out the new proportions in which goods and services will be wanted by people whose incomes are rising;
2. devising the new types of commodities and services which prospering people will want;
3. inducing workers and investors to make the necessary changes in types of work and investment.

These problems are especially difficult for a nation like the United States, which is the economic proving-ground for all the world.

Even the consumers themselves have only vague notions of what forms they want new wealth to take, and they are constantly changing their opinions as they try out first one thing and then another.

Is it surprising that a nation must take time out every now and then to reconsider and revise its economic plans and methods?

Trying to avoid or shorten these "time-out" periods by injecting new currency into the economic system is like trying to avoid interruptions in a football game by doping the players.

A nation can minimize depressions by providing opportunity and encouragement to thrift, industry, inventiveness and enterprise on the part of all the people. This is the course followed by nations which set the pace for world progress.

XIII. WHO OWNS AMERICA?

Helping to promote destructive tax and spending policies of government has been the widespread notion that a few people are far too rich and that a few big corporations own and control far too large a portion of American business.

> Do 60 families own America?
>
> Do 200 corporations own or control its business?
>
> Do the millionaires get most of the national income or enjoy most of the goods and services annually produced?

If private enterprise benefits only a few very rich families and if its opportunities are monopolized by a small number of Wall Street magnates, then perhaps socialism is preferable even if it is less efficient in production.

We find, however, that economic inequality may be viewed in many ways. We get different results and find different problems as we consider:

> inequality of wealth,
> inequality of control,
> inequality of income,
> inequality of consumption,
> inequality of enjoyment, well-being, or opportunity.

Certain of these aspects, in turn, may be considered in several ways, including:

> proportion or amount of wealth (or income, or control) possessed by the *upper* x per cent of owners (or income recipients);
>
> proportion or amount of wealth (or income, or control) possessed by the *lower* x per cent of owners (or income recipients);
>
> proportion or amount of wealth (or income, or control) in the hands of those possessing more (or less) than a certain sum.

Millions Share Responsibilities of Ownership

According to estimates of Dr. Willford I. King, outstanding authority in this field, approximately 20,000,000 small-property families, with wealth ranging from $2,000 to $10,000 per family, in 1936 owned 40 per cent of all private wealth.

> Their wealth included nearly 60 per cent of all household and other consumer goods, nearly 50 per cent of the value of all automobiles, and 56 per cent of the life insurance.

Another 20 per cent of the wealth was owned by 300,000 upper middle class families having from $10,000 to $40,000 worth of property each.

About 5 per cent of the wealth was owned by 9,000,000 poorer families, those with less than $2,000 worth of property per family.

At the upper end of the scale, some 530,000 families who had $40,000 or more of wealth per family, owned approximately 35 per cent of the privately owned wealth.

These figures, however, are a poor measure of economic inequality.

> Much wealth yields little or no income to its owners. For example, even in prosperous years from 40 to 60 per cent of America's corporations pay no dividends to their stockholders.
>
> On the other hand, a large share of the benefits from wealth goes to consumers, tenants and employees who own comparatively little of it. One does not need to own a house in order to live in it. Most of the benefits of our factories, farms, railways and mines go to workers and their families, not to the owners.

Ownership of wealth, especially productive wealth, means work and worry. Like other kinds of work, therefore, ownership tends to fall into the hands of those who can better meet its responsibilities.

> For example, some farmers make excellent tenants but poor farm owners. Unless land is very cheap, most farmers do well to learn by working as hired hands or tenants under supervision instead of beginning as farm owners.

Consequently, we shall find that income is much more evenly distributed than ownership of wealth; and enjoyment, or well-being, is more evenly distributed than income.

The 200 Largest Corporations

It is often said that 200 largest corporations own or control half or more of all business in the United States. This is a misuse of certain figures given in *The Modern Corporation and Private Property,* by A. A. Berle and G. C. Means, published in 1932.

The original statement by Berle and Means was that the largest 200 non-banking corporations in 1929 *"controlled"* 49.2 per cent, or nearly half, of all *"non-banking corporate"* wealth.

> Assuming that 78 per cent of American business wealth is in the hands of corporations, these authors concluded that the 200 corporations *"controlled"* 38 per cent or more of all *business* wealth.

Taking the National Industrial Conference Board estimate of the national wealth at $367 billions in 1929, Berle and Means concluded that these 200 corporations *"controlled"* 22 per cent of the national wealth.

Following are a few of the criticisms directed by other statisticians at these conclusions:

1. Incorporated business is only 60 to 65 per cent of all private business, not 78 per cent.
2. Nearly half of the 200 companies listed by Berle and Means were railroads and other public utilities. These have been granted a quasi-monopoly position as a matter of public policy and they are subjected to detailed regulation and supervision by government.
3. The "wealth" of the 200 corporations included bank balances, receivables, intangibles (good-will, patents, leaseholds, treasury stock, organization expenses), prepaid expenses, claims for tax refunds, mortgages, bonds and foreign investments. These were not included in the Conference Board estimate of national wealth with which Berle and Means compared the assets of the 200 corporations.

Allowance for these qualifications would reduce greatly the Berle and Means figures concerning the relative importance of the largest corporations.

For example, the 106 industrial concerns in the list, other than utilities, controlled only 22 per cent of the non-financial, non-utility *corporate* assets, only about 15 per cent of all non-utility *business* assets, or about 7 per cent of the national wealth.

After deducting intangibles from the assets of the 200 corporations, we find that the proportion of national wealth controlled by these corporations, including the railroads and other utilities, is nearer 15 per cent than the 22 per cent given by Berle and Means.

These additional facts should be kept in mind:

1. Many lines, especially in the service trades, have relatively small amounts of invested capital compared to their volume of business. The Berle and Means statement, therefore, does not give a fair picture of the concentration of control of business *activity,* as distinguished from control of business *wealth.* Figures showing the proportion of gross business done or showing the proportion of the nation's working force in the employ of the largest firms may be better than comparisons of assets as measures of the degree of concentration of economic control.

   At any rate, these show less concentration of control than is indicated by comparisons on the basis of assets.

2. The 200 largest corporations are the very companies which have the largest number of security holders and the widest distribution of ownership.

3. Competition in the industries to which the largest concerns belong is often as active as in any other lines. Even the public utilities, e.g., the railroads, must compete with other producers for labor, capital and markets. Large size, therefore, does not mean economic dictatorship.

That these concerns are subject to the same democratic control which is exercised by customers, employees and investors over other private enterprises is indicated by the number of business failures among large concerns. Concerns with assets of $50,000,000 or more showed the following percentages of mortality in the 15 years from 1920 to 1934, inclusive:

for industrial corporations,	19.8 per cent
for public utilities,	17.4 per cent
for railroads,	29.2 per cent*

How Much Income Do the Rich Get?

The usual method for describing the extent of inequality in the distribution of income is to state the percentage of national income received by the top 1 per cent or 2 per cent of income recipients.

> According to one study covering the period 1918-1937,** the top 2 per cent of income recipients received at most about 20 per cent of total individual income. This was in 1928-1929, the two years of greatest inequality in that period of 20 years.
>
> In most other years covered by the study the highest 2 per cent received from 14 to 16 per cent of total income.
>
> Conversely, the lower 98 per cent of income recipients from 1918 to 1937 received at least 80 per cent of total individual income and usually 84 to 86 per cent. This way of presenting the figures seems less sensational and perhaps that is why it is seldom used.

The picture presented by these figures is less disturbing when we discover that the "highest 2 per cent" included all incomes down to $5,390 in 1928 and $5,380 in 1929. In other years it was necessary to go well below $5,000, even below $4,000, to take in 2 per cent of all income recipients.

> According to the National Industrial Conference Board, the share of individuals with net incomes over $5,000 in the national

*_Big Business: Its Growth and Place_, Twentieth Century Fund, Inc.

**_Concentration and Composition of Individual Incomes 1918-1937_, Monograph No. 4 of the Temporary National Economic Committee, Washington, D.C., 1941.

income fluctuated between 9.1 and 12.0 per cent in the years 1930 to 1941.

Most people, however, are not greatly concerned over incomes below $10,000 or even below $25,000. Instead, they want to know how much the really rich get—the "millionaires" and "plutocrats."

Dr. King's figures show that those with incomes over $25,000 in dollars of 1913 purchasing power or $41,000 in 1926 dollars received 4.6 per cent of the national income in the United States from 1914 to 1926, inclusive. Since 1930 this percentage is much less.

According to the temporary National Economic Committee study mentioned above, individuals getting more than $48,510 in 1928, or $44,750 in 1929, received 8 to 9 per cent of total individual income.* They made up 1/10 of 1 per cent of all income recipients .

In most years from 1918-1937 the highest 1/10 of 1 per cent of income recipients received from 4 to 6 per cent of total individual income. But, except for 1928-1929, this top 1/10 of 1 per cent included incomes far below $44,000. In most years it included incomes below $30,000.

In other words, at least 91 to 96 per cent of total individual income was received by the 99.9 per cent of individuals receiving less than $48,510 in 1928, less than $44,750 in 1929, and less than $40,000 or $30,000 in other years from 1918 to 1937.

To find the share of the national income going to the really rich it is necessary to see what the upper 1/100 of 1 per cent of income recipients get.

In 1928 the upper 1/100 of 1 per cent included incomes over $239,750 and accounted for 3.5 per cent of total income. For 1929 the corresponding figures were $231,000 and 3.55 per cent.

Income tax returns show that incomes over $100,000 in 1928-1929 amounted to about 5 or 5½ per cent of total income before taxes.

In most other years from 1918 to 1937 the top 1/100 of 1 per cent received considerably less than 2 per cent of total income.

This included incomes below $120,000 and in some years below $80,000.

If $100,000 be taken as the minimum level for the "plutocrat" class, we may say that the rich received at most from 1 to 5 per cent of the national income in the years 1918-1937.

*According to the figures of Dr. Rufus Tucker, however, it is necessary to take in all incomes down to $10,000 to include 10 per cent of the national income in 1928-1929. *Quarterly Journal of Economics*, August, 1938, p. 558.

Except at the peak of the stock market boom in 1928-1929, these plutocrats received from ½ of 1 per cent up to about 3 per cent of the national income.

In other words, 99.99 per cent of income recipients received at least 96.5 per cent of the national income. Usually they received 97 to 98 per cent of total income.

Persons getting less than $75,000, the salary fixed by law for the president of the United States, normally received about 98 per cent of the national income.

But this is not the whole story.

How Much Income Do the Rich Keep?

The above figures include capital gains which are not true income except for professional speculators.

> Great Britain, France and various other nations did not tax capital gains as income prior to World War II.
>
> Including capital gains causes the figures of income distribution to show greater inequality than otherwise in 1928-1929 and less in 1930-1934. In 1929 capital gains constituted from 36 to 59 per cent of total income going to those in the brackets above $100,000. In 1928 the percentages were larger.
>
> Most of these gains turned out to be merely paper profits which were wiped out in 1930-1932.

Allowance should also be made for higher taxes paid by the rich and well-to-do. In addition to taxes paid by other classes, the higher income groups pay higher rates of income taxes.

> Effective Federal income tax rates on upper bracket incomes in 1925-1931 ranged from 12 or 13 per cent on incomes of $100,000-$150,000 up to 15 or 16 per cent on incomes over $150,000.
>
> In 1932 the rates ranged from 20 per cent on incomes of $100,000 up to 46 per cent on incomes over $1,000,000.
>
> In 1934 the rates rose to slightly over 32 and 55 per cent and in 1936 to more than 37 and 71 per cent, respectively.

The percentages given above, therefore, for the share of national income going to the rich and well-to-do should be discounted by these tax rates in order to find out how much these classes were permitted to keep for themselves.

> For example, in 1940 those receiving $100,000 or more had about $375,000,000 after deduction of Federal income taxes.

This compares with $3,700,000,000 in 1929.

If, furthermore, the upper bracket income recipients were permitted to keep a minimum income, the remainder would have been much less than the 1½ to 5 per cent estimated to have been the total share of income going to the rich.

If all income above $100,000 in 1928-1929 had been taken by taxation, the total "take" above the taxes actually collected from these classes would have been about 2½ per cent of total individual incomes. In 1930 the total thus obtained would have been slightly less than 1 per cent of total individual incomes.

In 1937 it would have been about 1/50 of 1 per cent.

In 1937 it would have been necessary to level down all incomes to approximately $25,000 in order to get 1 per cent of total individual income over and above what actually was obtained by taxation from those in brackets above this level.

How Much Do the Rich Consume?

Savings and investments should also be considered in measuring what the rich and well-to-do take out of total consumer income.

These go to help increase the output of goods and services for other people. They are essential to progress in raising scales of living for lower income groups.

For incomes of $15,000 to $20,000, the rate of savings has been estimated at 40 per cent of total income, with higher rates for incomes above $20,000.*

Gifts and contributions are also a factor to be considered in estimating what the rich keep for themselves.

Average gifts and contributions of the rich amount to 5 to 10 per cent of total income going to upper income groups.

These percentages look small when viewed through the eyes of a college president or community chest worker.

An economist, however, may offer on behalf of the rich the defense that savings and investment, even though made for "selfish" reasons, should also be considered as contributions to the general good.

Private philanthropy has been immensely helpful in building our libraries, schools, colleges and hospitals.

**Consumer Expenditures in the United States*, National Resources Committee, Washington, D.C., 1939, pp. 21-22. These rates of saving are lower than estimates given in the Brookings Institution Study, *America's Capacity to Consume*. The Brookings figures, however, are vitiated by including capital gains which bulked so large in the 1929 incomes of the well-to-do.

> But private investment provides the jobs which make the majority of people able to support and care for themselves, and able to pay for the education and care of their children.
>
> The highest type of philanthropy is that which makes people able to support themselves.

After allowing for the transitory nature of capital gains, for taxes, for philanthropic contributions, and for savings contributed to providing jobs and goods for the public, what is left for the personal enjoyments of the rich has not been a startling proportion of total national income.

> For example, in the years of greatest inequality since World War I, those with incomes over $100,000 kept for their own enjoyment an amount equal to less than 3 per cent of the national income. In most other years the amount was usually less than 1 per cent. In fact, since 1930 this class has probably been living on its capital.

According to the National Resources Committee study of consumer expenditures for 1935-1936, individuals and families with incomes below $20,000 consumed 96.8 per cent of the goods and services.

> They consumed 98.5 per cent of the food and tobacco, enjoyed 96.5 per cent of the housing, bought 95.9 per cent of the clothing and 96.9 per cent of the house furnishings, and made 94.8 per cent of the expenditures for automobiles and automobile services.

Those with incomes below $5,000 consumed approximately 90 per cent of total goods and services.

> Income recipients below $5,000 ate 93.1 per cent of the food and smoked 92.8 per cent of the tobacco. They enjoyed 88.4 per cent of the housing, bought 85.4 per cent of the clothing and made 82.5 per cent of the expenditures on automobiles.

The Rich Are Not Getting Richer

In 1927 P. Sorokin, after examining many sources of information, concluded that the nations of Western Europe have shown "no perpetual trend" towards greater economic equality or inequality.

> "During the past few centuries their stratification has been fluctuating up and down; that is all."*

A. P. Usher stated that we must go back to the Middle Ages to find greater equality than has existed in England following the Industrial Revolution of the 18th Century. He believed that the English artisans and middle classes gained ground relatively to the

*_Social Mobility_, p. 62.

rich during the 19th Century. Furthermore, he found no evidence that the share of the national income going to the propertied classes had been increasing during the preceding century.*

> Considerable evidence is given by Sorokin, Paul Douglas, Simon Kuznets and W. I. King that the share of labor in the national income has been increasing over the past 60 years, and especially since World War I.

Dr. Rufus Tucker, after a study of income distribution in the United States since 1860,** concludes that income was more concentrated during and just after the Civil War than since 1916. He says,

> World War I "did not increase the concentration of income, but greatly diminished it."
>
> "There can be no doubt that the millionaires of 1916 suffered severely from the War, although the War did create a few new millionaires."***
>
> Persons with incomes equivalent in purchasing power to between $4,000 and $10,000 in 1929, he finds, have become a larger proportion of the population since 1916. Those with incomes of $50,000 or more have become a smaller proportion.
>
> "Even in 1916 the middle class was more important than in 1870, but since 1916 its growth has been more rapid than that of the very wealthy class, whether one measures to 1929 or to 1935."

Studies of Tucker and J. C. Stamp for England from 1860 to 1914 likewise show growth in relative and absolute importance of the middle classes, great improvements for wage earners and improved distribution of income.

In all studies of income distribution it should also be remembered that the rate of turnover among the rich is high.

> As Dr. Tucker says, "It is plain that the large incomes in this country since 1914 have been received by a heterogeneous and shifting group of persons. Millionaires carried up to the heights by the wind of a boom have sunk back, sometimes into bankruptcy, during ensuing depressions."

Since 1929 the decline in fortunes of the rich and well-to-do has been spectacular. The depression, together with increases in surtaxes levied on upper bracket incomes during the 1930's, went far

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Industrial History of England, p. 511.

**"The Distribution of Income, 1863-1935," *Quarterly Journal of Economics*, August, 1938.

***Dr. King's work confirms this statement. See *The National Income and Its Purchasing Power*, p. 172.

toward flattening down the economic pyramid. Taxes now in effect establish a virtual ceiling of $25,000 on all incomes. Is this radical redistribution of income a "social gain"?

The Luxury of Risk-Taking

Certainly, levelling down does not bring about a corresponding levelling up.

> The reduction in income of the wealthy during the 1930's was accompanied both by a reduction in the national income and by a reduction in the share of the income going to the poorest 10 to 20 per cent of income receivers.*

In the building of prosperity the savings of the well-to-do play a vital role as a chief source of the capital necessary to create new jobs and increase production. This capital is of two kinds, *venture capital* and *loan capital. Venture capital* is invested on a profit-and-loss basis. *Loan capital* is invested on a fixed-return basis.

The owner of venture capital is the last to be paid. He takes what is left after paying to wage earners, suppliers of materials, bond holders and management the amounts for which they bargained in advance.

> Oftentimes nothing is left over and the owner of venture capital gets no reward for his investment, or a loss results, so that he gets back less than he put in.

Without venture capital business stagnates because there is no one to guarantee a return to wage earners and to investors of loan capital.

Only the rich, the well-to-do and the successful business concerns can afford to supply this venture capital. They can afford, with at least part of their savings, to take chances which small savers cannot.

> The rich, those with incomes of $50,000-$100,000 and over, formerly supplied about one-third of such capital. Another one-third seems to have come from those getting from $3,000 or $5,000 up to $50,000 or $100,000. The other third came from reinvested profits of successful business companies.

This venture capital acts as a business energizer.

1. It finances production of new and untried products.
2. It finances introduction of new machinery and new methods.
3. It finances hiring of new and untried workers.

**Enterprise and Social Progress*, National Industrial Conference Board, p. 125.

4. It supplies the equity capital necessary to encourage the expansion and circulation of credit along with expanding production and trade.

Savings Are Essential to Progress

Loan capital also has come largely from the well-to-do and has helped finance the nation's economic progress.

Is there any way to improve ways of living without capital?

> Whether it be through education or coercion, through business or philanthropy, through introduction of new commodities and services or through increased abundance of existing ones—in every case someone's savings are necessary to make the improvement.

More than half of the nation's annual savings, however, normally goes into consumption goods, such as homes, automobiles, refrigerators, radios, house furnishings, and so on.

> On the whole these increase welfare and in the long run help to raise the efficiency of producers.

But increased output of goods and increased wage levels result chiefly from producers' savings. These supply industrial equipment and finance trade. As Dr. Carl Snyder says,

> "For every dollar of additional value added per annum in manufacturing, as far back at least as 1850, something more than an additional dollar of new capital has apparently been required. This ratio of capital to annual value of product has been rising slowly in the eighty years from 1850 to 1930, so that it now requires nearly twice as much capital to produce a given value of product. . . .
>
> "The entire increase in average wage per wage earner, or in real wages, has been due directly to one factor and to one alone: the growth in capital investment. This must be so, because wages are paid out of product, and the larger product per worker has been wholly due to the increased application of machinery.
>
> "The increase in mechanical equipment was possible, only because of the increase in the supply of capital. Therefore, the well-being of the great body of workers has been improved solely through the provision of an adequate supply of capital for investment."*

The amount of savings going into production, therefore, largely determines the rate of a nation's progress.

Capitalism the Creator, pp. 126-127. By permission of The Macmillan Company, publishers.

> Snyder estimates the amount of such new investment in 1929 at slightly more than four billion dollars and for the decade of the 1920's at three billion dollars to four billion dollars annually.

The private savings of the American people, however, are supplied by approximately 10 per cent of the income recipients.*

> The excuse is often made that most people are too poor to save anything. But these low-income non-savers in the United States spend billions of dollars annually on luxury goods which only the well-to-do can afford in other countries.
>
> Thrifty persons are far-sighted and self-controlled. They work harder and more efficiently for the same reasons that they save more. Consequently they earn more and are able to save more.
>
> Their savings, in turn, increase their incomes and their margin for savings. True, their wealth increases their power to save.
>
> But their willingness and ability to save is a primary factor in the growth of their wealth.

The Menace of Equalitarianism

The levelling-down of personal incomes over $50,000 prior to 1940 had destroyed the source of fully one-third of America's business savings and about one-half of the venture capital.

The attack on profits, through taxation and "collective bargaining," had gone far to wipe out the source of another one-third of business savings, most of which was invested as venture capital.

War taxation is now attacking the middle class and well-to-do—those with incomes between $5,000 and $40,000. It probably has wiped out most of their margin for savings.

Inflation for the moment seems to have increased profits and partly restored this source of new capital.

This, however, is temporary at best. In part, it is also illusory, because current methods of measuring profits make insufficient allowance for postponed repairs. In any case, current business savings will be needed to meet post-war conversion costs.

In the absence of the abnormal conditions created by inflation, equalitarian policies already in operation will destroy the power of private enterprise to create new jobs or raise the general level of wage incomes in the United States. These policies, therefore, promise to bring to a close the era of rapid progress which made America the hope and envy of all the world.

**Consumer Expenditures in the United States,* National Resources Planning Board, p. 54.

The Myth of Social Equality

Levelling up by levelling down has always looked like an easy shortcut to Utopia.

Yet inequality exists in every thriving organization.

No group of people can cooperate efficiently unless organized into a pyramid of authority and influence.

Leaderless orchestras, armies without officers, schools without teachers and work crews without foremen have been tried. They don't operate efficiently enough to stay in operation.

Religious organizations, schools, trade unions, business concerns, armies and governments show wide ranges of inequality from

> layman to bishop, or pope,
> beginning student to graduates,
> union member to union president,
> office boy to manager or president,
> buck private to commander-in-chief,
> private citizen to president, premier, or king.

Even communist and socialist societies, while advocating equality in society at large, are unable to achieve it within their own ranks.

> As Sorokin says, these "levellers" tend to develop within their own organizations a higher degree of inequality and oligarchy than most other social groups. And when they become victorious, they often "exhibit greater cruelty and contempt toward the masses than former kings and rulers."
>
> *"Unstratified society, with a real equality of its members, is a myth which has never been realized in the history of mankind."**
>
> As the Russian Bolshevist experiment showed, a share-the-wealth program may increase rather than diminish social inequality. It may create a new set of masters more tyrannical than those they dispossess. In addition, general impoverishment for the masses is likely to ensue while the new masters learn their trade.

Most people, even among the poorest, recognize these facts. They know that leaders are necessary and they believe in rewarding these leaders generously.

Many, however, have been given an exaggerated notion of the extent of economic inequality. This has led them to believe that the "rich" can pay most of the nation's taxes and still have plenty left over in salaries, dividends and interest to provide adequate incentives for business management and investment. They fail to

*P. Sorokin, *Social Mobility*, pp. 12-13.

realize that this false idea is causing them to destroy leadership by taking away the opportunity for the more efficient producers and savers to enlarge their field of service to the nation.

"Whosoever Will Be Chief Among You . . ."

The progress of a people requires improving methods for selecting, training and inspiring its leaders.

On the whole, America may well be proud of her economic leaders.

> Foreign visitors remark on the long hours, high-speed pace, short holidays and frugal diet of our businessmen. They call us money-mad dollar chasers.
>
> But this hard work and dollar chasing made American business a model for the rest of the world in efficiency, honesty and generosity of service.

American businessmen have been proud of their calling and proud of their success in creating jobs and giving service. It is to the interest of all of us to maintain that pride and self-respect and to rebuild it where indiscriminate criticism has torn it down.

> This is necessary to get the most out of our present leaders.
>
> It is also necessary to persuade able young men to choose business careers.

The progress of America will be limited by the progress of its leadership in understanding and ability.

". . . Let Him Be Your Servant"

Wealth often is gained and used in anti-social ways. So is political power.

Progress, therefore, requires improvements in suppressing fraud by means of which individuals may win wealth.

> This fraud may consist in false promises to customers or investors.
>
> On the whole, however, we seem to have made much more progress in reducing fraud in business than in government. Promises of politicians at election time and financial policies of governmental agencies make current business misdeeds look comparatively innocent and harmless.

Progress also calls for improvements in ways of using wealth, both in private spending and in business investment.

> Ostentatious waste is a vice of the rich which tends to arouse the covetousness of the poor.

Everyone has the same responsibility for learning to spend his money as he has in learning to make it. "The world belongs, by a law of nature, to the disciplined and productive races and not to those who devote themselves to graceful idleness and self-indulgence."*

Trusted leadership is necessary for human progress.

Suspicion that others are doing too little and getting too much turns our energies from useful work to quarreling and thus makes us poor.

We must learn not to suspect or attack others merely because they have wealth and power.

Such envy is a vice of selfish, small-minded people who cannot amount to much.

We must honor, trust and reward efficient leaders as thoroughly as we punish those who betray our trust.

Penalties for wrong doing mean little except as they are contrasted with rewards for right conduct.

One good way to keep leaders from abusing their power is to have a large supply of candidates, or competitors, for positions of leadership.

These competitors are eager to discover better ways of doing things. Thus they keep the leaders always on their toes.

A large supply of substitutes also helps keep down the salaries and profits of those at the top. It makes for a more equal distribution of wealth and power while improving the quality of leadership.

The best leaders, being only human, will make mistakes.

If we regulate business so carefully that no one can go wrong, we shall also thereby take away all chance to do better. The only one who never does wrong is he who never does anything.

We, the people, therefore, must practice some of the restraint, patience and good will which we expect of our leadership.

True it is that a few wealthy persons do some foolish things with their incomes. No economist worthy of the name defends the vulgar display, gambling and extravagant self-indulgence of certain wealthy play-boys and glamour girls.

But the rank and file of the American people have much more to gain than to lose by restoring the high prizes which provided incentive to effort and opportunity for service.

*T. N. Carver, *The Religion Worth Having* (1940 ed.), p. 20.

XIV. A PROGRAM FOR FREE ENTERPRISE

A good society—prosperous, strong and free—is achieved only by hard work intelligently directed.

The conditions necessary for its development are numberless.

Its workings are too complicated to be described or even understood.

A man who had never lived in a modern, industrialized nation would scarcely believe such a complex society could function. Its existence depends on synchronizing the efforts of millions of individuals, each of whom is also a complicated and delicate mechanism. Yet somehow these individuals do what is needed at the right time and place, so that their efforts fit in with the efforts of millions of others of whose existence each is barely conscious.

Is it surprising that we do not fully understand how and why it works, or that the most intelligent and best informed students disagree on what is needed to improve it?

Yet a few basic facts and principles most of us can agree upon. One of these is that a good society can be built and preserved only by a people zealous in performing the duties necessary for vitalizing their rights.

Rights Flow From Duties

We often boast of our Bill of Rights, a list of liberties embodied in the Constitution of the United States.

Do we at the same time list the duties which go with these rights? And do we as fervently pledge ourselves to discharge these duties as we proclaim our determination to protect our rights?

Every right implies a corresponding duty and full enjoyment of the right depends on full discharge of the duty.

The right of free speech involves the duty not to abuse that right, as, for example, by calling a false alarm of "fire!" in a crowded theater.

It rests on the duty of other people not to infringe on that right, as for example, by mobbing an unpopular speaker.

It also rests on the duty of the police and courts to help restrain those who abuse the right or infringe on the rights of others.

Rights are the fruits of justice; and justice springs from the character of the people. But good character is far more than good intentions and pious words. It is doing things which help make a good nation, one in which a Bill of Rights is a living reality.

> In some nations a Bill of Rights remains a scrap of paper no matter how often it is enacted or how loudly it is acclaimed.
>
> In our own nation it is too often flouted by legal forms or unlawful violence.

Free institutions do not spring full-fledged from written documents, but evolve slowly along with the people's progress in understanding and good conduct.

Prosperity Expands Opportunity

We can also agree that prosperity provides tools and opportunity for enjoyment of rights.

> Freedom of speech and press means far more as a people can afford books and newspapers, churches and schools, telephones and telegraph, radios and loudspeakers.

Property laws and property rights are rules for using these tools.

> Anyone who buys a theater ticket or rents a house or a room is acquiring a property right. A theater ticket gives its owner a right to a certain entertainment at a definite time and place. A lease gives the tenant a right to use a farm, a house or a shop for a stipulated time and under certain definite conditions. The acquisition and use of such rights are governed by property laws.

As wealth of many sorts is necessary for civilized living, so are the complicated rules we call property laws and the rights we call property rights.

> If everyone grabbed what he wanted, paying no attention to property laws or the rights of others, the result would be anarchy, rioting and civil war. Soon everyone would be reduced to the level of the lowest savage.
>
> On the other hand, property arises as soon as people are protected against violence and fraud. Then they make things and exchange them as the only way to make a living. So production and trade arise.

In nations where producers and traders are protected against fraud and violence, the individual's success depends on his ability to make things or perform services which other people want.

> For example, the success of a Henry Ford, an Edison or a George Eastman depends on his ability to devise things which millions of other people want and on his ability to organize the production of these things in large quantities.

The more successful a producer is the more he adds to (a) the purchasing power of other people's money, (b) the value of their services, and (c) their opportunities for enjoyment and well-being.

> The more millionaires which a country develops in this way the greater is the prosperity of all the people.

Progress Depends on Production

A third fact upon which we should be able to agree, therefore, is that our individual and group progress depends on increasing production of commodities and services which promote human welfare.

> It follows that every policy is reactionary which reduces the incentive or opportunity of any person to produce to the maximum. Progressive policy seeks to enlarge opportunity for production.

> As between the inflationist who wants to print currency to enlarge markets and the restrictionist who wants to restrict production or trade to maintain prices, the inflationist seems less obviously reactionary. Both the inflationist and the restrictionist lack faith in free enterprise. They doubt that free enterprise can supply enough purchasing power to distribute all that can be produced. But at least the inflationist votes for full production as well as high prices, whereas the restrictionist asks only for high prices.

Production, however, is far more than processing of materials. It is a far more complicated matter than multiplying goods of a particular kind.

> Economic progress means expanding output of goods faster than population increases. It means improvements in the kinds of goods produced, changes in the proportions in which they are supplied, and advances in the methods of producing them.

> The rate of economic progress, therefore, depends on the amount of thrift, industry and enterprise devoted to improvements in the tools and methods of living and working.

Primarily, production is service. And the possibilities for service in a great and good nation are limited only by the vision, intelligence, ability and industry of its people.

Man's Work Is Never Done

Some there may be who hope that someday—after the war, perhaps —we in America may relax, sit back and take it easy.

> They believe we should adopt a 30-hour week. They believe that incentives and tools for increasing output are no longer needed. They say that, with modern equipment, we can guarantee a rich living for all with little work and no sacrifice.

This hope, or belief, is false and vicious. This, not "free trade," threatens to "give our country away."

> The present war, no matter what its military outcome, will not end the struggle between nations and between ways of living. That struggle will last as long as life itself because its roots lie deep in the will to live.

Nations, families and individuals who measure progress in terms of shorter hours and increasing opportunities for self-indulgence lose out in life's battles to those who measure success in terms of expanding opportunities for work and achievement.

The future lies not with those who ask for security, but with those who demand increasing opportunity to grow in efficiency and power.

How Much Is a Man Worth?

By the same token, the value of a man to his nation does not consist in the amount of money he spends on himself or on the goods he consumes. This spending and consumption constitute the cost of keeping him.

Instead, the value of a man lies in the surplus of his production over his consumption.

> This surplus adds to the strength and welfare of his own and later generations.
>
> It adds to the owner's credit and to the nation's wealth.

This surplus of production over consumption may be increased (a) by raising productivity, (b) by reducing consumption, or (c) by raising productivity faster than consumption.

> Probably progress comes mainly through raising productivity faster than consumption. The more productive person is likely to consume more—as, for example, in equipping himself with a better education and in experimenting with new ways of living.

What will be our attitude, then, to questions of shorter hours, distribution of tax burdens, and "social security" when considered from this point of view?

1. Shorter working hours will represent a social gain when they result in an increase in the workers' net contribution to production. This means that increases in leisure time must be so used that the workers produce more in their remaining working hours.

   This additional output, however, must exceed any increased consumption in the leisure hours. The contrary result—decreased output, or increased consumption as compared to production—represents reaction and degeneration.

2. Taxes should be levied only to support functions of government which directly or indirectly increase the national strength, efficiency and productivity.

   These taxes should be levied so as to reduce as little as possible the power and incentive of the people to produce.

   By all means let us tax in proportion to "ability to pay." But let us measure ability to pay, not in terms of ability to *produce,* but in terms of ability to *consume.*

   Taxation on this principle would bring about an equality in individual well-being greater than any proposed by the average socialist or communist. But it would stimulate production to levels which would make possible the abolition of poverty as we now conceive it.*

3. The term "social security" now covers all forms of government relief, or aid. The fact that those who receive it at one time help pay for similar aid to other people at another time does not change the fact that it is government charity on a mass basis.

   Some charity, or relief, of this sort there must be. As a producer protects his machinery against rust when it is not in use, so the nation will try to prevent deterioration of its working force when idle.

   But scientific philanthropy is that which helps people help themselves. It converts non-producers into useful workers. Both the extent of the aid and the way it is given under this principle will be vastly different from the extent and method of relief under inflationist or restrictionist theories.

"And the Greatest of These Is Charity"

Sentimentalists object that such emphasis on production, efficiency, competition and success is "materialistic" and "hard-hearted."

The charge of materialism comes from failure to appreciate the broad scope of economics.

*Poverty in the sense of "less successful" we shall always have, because opportunity for quality creates inequality. But poverty in the sense of hunger and physical suffering can be made as rare as typhoid or smallpox.

> Economics deals with the production and distribution of economic goods. Economic goods are those which are undersupplied compared to people's desires for them. They include the services of religionists, philosophers, doctors, scientists, musicians, baseball players, and economists. The budgetary problems of the churches ought to bring home the fact that even religious progress is an economic as well as a religious problem.

The charge of hard-heartedness springs from failure to see that nature, not the economist, created the facts of scarcity, desire, struggle and competition.

> Competition can be humanized, but it cannot be abolished.
>
> To humanize competition means to organize it so that the winners are those who contribute most to the production of goods which other people want and need. The more productive farmers win control of the farms, the more capable employers hire the workers, the more efficient merchants get the trade, and so on. Even the less competent and the helpless benefit from such competition.

Someone may ask, "But isn't it more blessed to *give* than to *receive?*"

1. In reply one may point out that a gift of money is worthless unless goods are being produced and offered for sale. It is the fact that someone has produced more than he consumed which makes real giving possible.

2. A business investment is the best way to help most people.

   Suppose, for example, that a philanthropist owns a stock of goods sufficient to support 1,000 persons for a year. If he gives them away, at the end of a year his charitable work is finished.

   But suppose he gives these goods on condition that the recipients in return will produce for him goods like those he is giving away, or other goods which he may sell or trade for the necessaries of life. At the end of the year he then has a supply of goods with which he can continue his giving. If he has been an efficient manager he may have at the end of each year as much as he gave away. In that case his good work may continue indefinitely. If more is produced than is consumed during the process of production he can expand the scale of his good deeds accordingly.

   Which is the better way to "bestow one's goods upon the poor"?

Some charity there must be for those who can never make any return. The virtues and values of such charity are not easy for an economist to describe, but they are none the less real. At the very least it is a "comfort," or "luxury," which a civilized community can well afford.

The total amount of such charity, however, is insignificant compared to that which can be justified on strictly economic grounds when it is scientifically administered.

"By Their Fruits Ye Shall Know Them"

The highest type of giving, however, is the giving of service in producing goods which other people need.

That such service is usually paid for in money or goods does not necessarily detract from the moral merit of the giver.

> When used to maintain and increase the producers' usefulness the payment for service is like a loan or a trust to be returned later to the community in the form of new production. This is true whether it is used to buy food and other necessaries of life, to buy equipment to aid in production, or to pay for education which will increase efficiency and capacity for further service.
>
> Only when rewards for service are used in wasteful self-indulgence do they subtract from the social value of the individual giving the service.

The ideal society would be made up of individuals who would produce and serve to their maximum capacities and consume only according to their needs.

> This ideal is expressed, *"from each according to his abilities, to each according to his needs."*

This is the moral ideal of all great religions and ethical systems, including Christianity. Communists claim it as their own, as do single-taxers, socialists and others.

Opinions differ widely, however, on how to promote this ideal.

> On the one hand, Christianity, as usually interpreted, holds it as a moral goal for the individual. It seeks to show him by precept and example that his own welfare is ultimately best promoted by a life of maximum service to his fellows. This provides freedom for the individual to work out with his fellows the specific ways in which each can serve best.
>
> At the other extreme, the Communist Party and most socialists set up the principle as a legislative policy. They seek, through the power of the State, to coerce the individual into service. They hope that eventually the mass of mankind will serve without coercion. They believe, however, that a large amount of coercion is necessary to teach the masses the advantages of such service. Therefore, during a transition period, at least, they would reduce or abolish the individual's freedom to decide whether he would serve or how. They would give the power to make and enforce these decisions to bureaucratic officials and agencies.

Freedom of Choice Is Necessary for Progress

An advocate of free enterprise holds that people will progress more rapidly towards the ideal society under conditions of freedom.

1. The ideal society is one in which there is a minimum of conflict between the individual's view of his self-interest and his actual duties. In such a society each person will give maximum service at minimum cost because he prefers that course to any other. Such a society will have a minimum of coercion and a minimum of conflict. It will be a free society. And how can people prepare for freedom except in freedom?

2. Within a large field of human behavior, no person or group of persons can decide for an individual as well as he can decide for himself what he can do best to serve the community. Within that field, a constantly shifting one, the individual must be left free to follow his own inclinations, subject only to such *non-coercive* pressure and persuasion as his fellows may find it in their interest to use.

3. The proper scope for individual liberty is greater in a nation, like the United States, which is in the van of progress than in less advanced societies. The less advanced nations can learn from the experience of the others. The people of the more advanced nation must learn by trial and error under conditions of individual liberty. This liberty is dangerous, but it is an unavoidable risk of leadership and a necessary condition for progress.

Freedom of choice, however, means absence of coercion, not absence of control.

> In a free society the individual will remain subject to pressures from other individuals and groups of individuals—parents, relatives, playmates, school teachers, fellow students, churches, business associates and so on.
>
> This pressure is exercised mainly by persuasion and by offers of reward for good conduct or by withholding reward in case of bad conduct.
>
> These pressures build preferences, loyalties and habits which control the individual's conduct. Thus they build self-discipline which makes a free society work, in contrast to the coercion of a slave state.

"Make Sure You Are Underpaid!"

A free enterprise motto to express the ideal of maximum service and efficiency in consumption might be,

> *"Make sure you are underpaid!"*

Of course, the only way for anyone to make sure he is underpaid is to produce to the limit of his ability. And the only way to make sure that he contributes to the community more than he takes out and that he will never become a community charge is to consume only according to his needs.

> The communist will say that this motto is intended only to enslave and exploit the workers.
>
> That might be true if it were accepted only by wage earners and if employers were permitted to organize capitalistic monopolies to take advantage of workers and consumers.
>
> Under competition, however, the results are different. In fact, some of the most underpaid people in America have been certain high-income business executives and owners who have contributed to production and to the national income many times what they have been paid and many times what they have consumed.

But how could such a motto be sold to the individual?

1. Under competitive conditions the wage earner who makes sure he is producing more than he is paid will not have to worry so much about the security of his employment.

2. If all the workers in an organization, including the managers, have the same attitude, the company is more likely to grow than to fail. Therefore, it pays each individual to sell to his fellow workers the idea of trying to keep ahead of every pay raise. And, of course, one good way to sell the idea is by setting a good example.

And if this motto were accepted generally throughout the nation a number of desirable results would follow:

1. The supply of capital, especially of venture capital, would increase.

2. Output of all goods and services would expand.

3. The demand for labor would rise, unemployment would decline and wages would increase.

4. Strikes for shorter hours and higher wages would be replaced by worker agitation for more efficient methods of production.

5. Conspiracies to form monopolies and restrict output or trade would be replaced by keener rivalry in reducing prices and improving service.

What difference would such an attitude make in politics?

Demagogy vs. Statesmanship

Politicians and government officials, if they tried to make sure they were underpaid, would become statesmen.

> They are paid by all the people. They would try, therefore, to serve all the people, not a particular class or group.
>
> They would regard public funds as a public trust. They would spend only for those things which would yield the community more than they cost.

Citizens would promote statesmanship by working for the election and appointment of public officials possessing courage, ability, experience and knowledge.

> They would not seek rubber stamps for their special interest groups or patronage hounds for party hacks.
>
> They would see to it that government officers had the necessary facts on which to decide and administer policies in the community interest. But they would not try to high-pressure, threaten or bribe their servants into policies promoting the interests of the few at the expense of the many.

But let us be more specific and list in detail some of the steps which might be taken by citizens and government to expand opportunity and increase incentive for maximizing production and service.

It should be clearly understood that the following proposals represent only my own opinions.

And at this point I wish to express my sincere appreciation for the freedom of expression which the Los Angeles Chamber of Commerce has permitted me, a freedom as great as that which I found in the academic institutions with which I have been connected in the past. In the presentation of my views within or outside the Chamber no restriction has been placed upon me other than those which were dictated by my own sense of propriety and good taste. The tolerance of criticism and open-minded search for truth which I have met in this and other business organizations in recent years has made me proud to be known as a "chamber of commerce economist."

—V. ORVAL WATTS.

First Steps Towards Freedom and Prosperity

A. *Taxation*

1. Abolish or greatly reduce all taxes on business profits, which are capital until paid out as dividends to the owners.
2. Reduce greatly the surtaxes on personal incomes, especially in the upper income brackets.
3. If tax increases should be necessary to meet costs of government, increase taxes on income receivers below $10,000 and tax less essential items of consumption, e.g., tea and coffee.
4. Abolish discriminatory taxes on chain stores.
5. Simplify the tax structure as it affects business by abolishing certain low-yield taxes, e.g., the capital stock tax and the declared-value excess profits tax.

B. *Price Policies*

1. Repeal the "fair trade" laws and other forms of price maintenance legislation.
2. Abolish crop loans and other devices designed to maintain prices for commodities.
3. Abolish the Office of Price Administration and abandon price ceilings, rationing and allocations. (For wartime price-control policy see above, pp. 65-66.)
4. Abolish state and local government devices for maintaining prices of commodities and services, e.g., prices of milk and prices for services of barbers, beauty shops and dry cleaners.
5. Gradually reduce and abolish all "protective" tariffs in foreign trade.
6. When maintenance of an industry appears justified on grounds of national defense, use subsidies or government contracts, instead of tariffs, to maintain the nucleus considered necessary.
7. Abolish all interstate and intercity trade barriers except those for control of certain pests and diseases which could do more damage than the costs of control.
8. Reduce business license fees to the point that they no longer act as restraints on competition.
9. Enforce anti-trust laws and make this legislation applicable to organizations of farmers (including farm cooperatives), as well as to organizations of business owners, wage earners and professional workers.

C. *Banking and Finance*

1. Restore the gold standard.

2. Liquidate and abolish the Reconstruction Finance Corporation and other governmental lending agencies.
3. Restrict governmental control of private banking by eliminating the special privileges of governmental securities as a basis for monetary expansion.
4. Amend the Securities Act and the Securities Exchange Act and modify the administration of these laws:
   a. to reduce costs, delays and risks for dealings in corporation securities;
   b. to remove the power of government officers to influence security prices through changes in margin requirements or through other means.
5. Repeal usury laws.

D. *Labor Policy*

1. Amend the National Labor Act to increase protection for wage earners against intimidation and high-pressure methods by union organizers and union members.
2. Amend anti-racketeering laws to make them apply to members and officers of trade unions.
3. Amend anti-trust laws so as to outlaw organized labor boycotts and organized labor restrictions of output.
4. Repeal the Federal Fair Labor Standards Act and all state minimum wage laws.

E. *Public Works*

1. Abolish all work relief projects except for prison labor.
2. Place public works expenditures on a business basis.
   a. Undertake only such public works as may be expected to repay their costs, including interest and upkeep, through increased community efficiency. Returns from expenditures on schools, parks and playgrounds can only be roughly measured. But certainly these returns should be considered and expenditures for such purposes should be limited accordingly.
   b. Place all public works on a contract basis.
   c. Reduce costs of public works by encouraging contractors to hire labor and buy materials in competitive markets.
   d. Plan to postpone public works when costs are high, so that they may be undertaken in periods of low prices and low wages at a saving to taxpayers.
3. Avoid public enterprises, such as electric power projects, which private enterprise will undertake.

* * *

A utopian program? Revolutionary? Reactionary? Politically impossible?

Perhaps. But perhaps free enterprise is impossible after all.

Certainly many of these proposals must be adopted if our progress in freedom and prosperity is to continue and if we are to save our representative institutions.

How can such changes be brought about?

By talk, mainly.

This Simian World

As Clarence Day, in *This Simian World,* points out, human beings, more than any other animals, love to chatter. In this they resemble monkeys and other ape-like creatures.

But this talkativeness has been one of man's most useful traits.

> His ability to talk has made cooperation possible, and this cooperation has been the basis for all human progress, including progress in "individualism."

In general the talkers have ruled even the bullies and the strong men.

> Hitler and Mussolini rose to power, not because of their physical strength, or intellectual genius, but because of their ability to talk fast, loud and long. Hitler's "Propaganda Ministry" was a leading agency for Nazi conquest, first in Germany and later outside of Germany.
>
> The Japanese militarists had to have the help of talkers, such as priests and politicians, to help them enslave their people.
>
> Business is organized and run largely by talkers—promoters, salesmen, and managers.
>
> Politicians usually rise to power in large part through their talking ability.

Freedom of speech and press is our greatest hope for reversing recent trends towards monopoly and bureaucracy in the United States and the British Empire.

Talking Points

Following are lines along which those who believe in economic liberty may direct their talking.

1. **Explain that increasing production is necessary for increasing national strength, prosperity and purchasing power.**

2. Show how payment for effort, thrift, inventiveness and enterprise according to market estimates of worth stimulates output of goods desired by productive and thrifty people and by their dependents.
3. Show how freedom of exchange, with prices and rates of pay determined by supply and demand in competitive markets, is necessary to (a) freedom of choice as to occupation and ways of living and (b) full production and employment.
4. Expose such fallacies as the underconsumption (oversaving) theory of depressions, the technological theory of unemployment, the Marxian myth of the Industrial Revolution, Midas theories and Robin Hood economics.
5. Explain the difference between scientific and unscientific philanthropy.
6. Point out the elements of compulsion in governmental activity and show the limitations, as well as the usefulness, of compulsion as a method of promoting human progress.
7. Inform the public concerning the share of owners and managers in the national income and show the uses made of their income.
8. Impress upon the well-to-do the responsibilities that go with wealth and large incomes.
9. Show that enjoyment of rights depends on performance of duties.
10. Show that the individual finds greater self-satisfaction in work and achievement than in idleness and dissipation.
11. Explain the nature of self-interest and the importance of harnessing it to community ends.

Do We Care?

As Eleanor Roosevelt recently said: "The war for freedom will never really be won because the price of freedom is constant vigilance over ourselves and over our Governments."

One of the chief dangers to our liberty comes from the very prosperity that it has given us.

> A successful nation, built by long practice of the economic virtues, may be demoralized by its success. "Imagining itself unassailable it may then begin to waste its energies, to devote itself to self-expression, graceful consumption, eminent leisure, or motionless contemplation of its own perfections. Under such conditions the carnal mind is peculiarly open to the arguments of the 'pig-trough' philosophy of life, which conceives that the purpose of life, of labor and of wealth is enjoyment. But this

> process also will come to an end because the society in which such a degenerating process gains headway will eventually give way before a society with sounder ideals—ideals of self-discipline, efficient production, and growth.
>
> "The world belongs, by a law of nature, to the disciplined and productive races and not to those who devote themselves to graceful idleness and self-indulgence."*

Well-to-do and prosperous individuals, those who have greatest opportunities and responsibilities for leadership, often become more interested in their hobbies than in public service. Or they become more concerned about protecting their present positions than in seizing new opportunities.

America's greatness was not built by the stay-at-homes interested only in security. Nor will it be carried forward by those whose sole ambition is to cling fast to what they have.

If every farmer and every worker, every businessman and every professional man is determined only to go on doing the same old things, in the same old way, in the same old place, at the same old prices and incomes, American progress must stop. This cowardly conservatism finds expression in price-rigging, restrictions on output, and the clamor for government handouts. All these have been holding us back, keeping us poor, and threatening our political liberties.

The nation that tries to stand still, in fact, will not hold even what it has. The march of science and the world-wide surge of human desire will carry other nations forward and leave the craven, vested-interest nations impoverished and defeated.

"The Monopolist is a Sissy"

—ERIC JOHNSTON

America can continue to lead the march of human progress. But she cannot do it merely on the strength of her resources or her past record. If we are to lead, we must preserve competition and freedom for enterprise in order to incite and enable men to do their best. We must be willing to make the changes necessary to keep step with new methods. As our efficiency in production increases, labor and capital must be shifted to new industries. That means some workers must learn new jobs and owners of wealth must write off the value of old investments and make new ones.

We must stop trying to hold onto our places as long as possible.

*T. N. Carver, *The Religion Worth Having*, (1940 ed.), p. 64.

We must stop asking governments to give us special privileges and to support us so that we may continue producing goods under uneconomic conditions. We must stop trying to get what we have not earned.

And we must drop the silly excuse for anti-social grabbing that taking things from others benefits them as well as the grabbers.

Security—in the sense of abundant opportunity to work, achieve, and prosper—depends on high standards of work and production. These high standards of work and production depend on political and economic freedom, on abundance of capital seeking investment, and upon voluntary enterprise. Except as business keeps on giving jobs and turning out goods, no social insurance scheme and no scheme for "planned" production is worth anything. For without business prosperity there can be no taxes, no unemployment insurance or relief, no old age pensions, no incomes, and no worth-while security for anybody.

Prosperity is a fragile thing, a rare achievement, like life itself. It can be built only by hard work and sacrifice. It can be maintained only by ceaseless struggle. It depends on high qualities of mind and character: faith, mutual trust and respect, tolerance, good sportsmanship, and willingness to cooperate. All of these are easily destroyed and hard to rebuild. They are the price of prosperity and progress. Are Americans willing to pay it?

OLYMPIA IMPRESSIONS

THE ECONOMIST OBSERVES*

"Business people in Olympia, no less than elsewhere, are thirsty for a philosophy of business, a justification to themselves and others of the value of the thing they are trying to do and an ability to distinguish right from wrong in business and economics. Most of them don't want to argue or defend themselves very much. They want religion! That means a moral fervor on behalf of the best in business and inspiration to defend it against enemies and traducers.

"Although the lectures belabored certain business practices and policies, they also showed how essential were the businessman's functions. The businessman is today the 'forgotten man', and he is beginning to hunger for a little social recognition. He is willing to do a good deal in the way of reforming business policy and accepting responsibility for the mess we are in, if he can see a way to win back public esteem which he lost in 1929-39.

"This experience ought to quiet any fears that businessmen can't 'take it' or that they would be antagonized by straight talk. A new generation is in the saddle, and they want the best of the old, plus something new. These businessmen have the attitude of a good golfer who finds himself taking a beating by a dub from whom he used to win easily. Such a fellow is ready to run to the 'pro', asking, 'What's wrong with my game?' Ever since 1929 the businessmen have been losing out in prestige, political influence, and, most of the time, in wealth. Now they are asking, 'What did we do wrong?'

"Labor representatives came to the meetings reluctantly, somewhat suspicious and antagonistic. Before the sessions were concluded, however, some of their suspicions and antagonisms were gone. If more meetings were held, the labor representatives would feel much more hurt and suspicious at being left out than they could possibly be by anything the speaker might say."

LABOR REPRESENTATIVE (A. F. of L.):

"I think that the course on economics and free enterprise has been very educational. A program of this type conducted by different economists throughout the nation would be beneficial to the public. It would be particularly helpful to capital and labor, giving them a better understanding of each other's problems. In my opinion, free enterprise is the assurance of our future.

*Excerpts of letter from Dr. Watts written on conclusion of his lectures in Olympia.

"I would suggest that the Chamber of Commerce make every effort to continue its economic courses."

UTILITY EXECUTIVE:

"The economic study classes have been based on common sense. We must carry on these important discussions if we expect to halt the trend toward socialistic government."

LUMBER COMPANY PRESIDENT:

"These classes have clearly demonstrated an important need: that groups of people should understand, and carefully consider, fundamental economic laws when making decisions affecting their relationship with other groups or with the general public.

"We should see that our Chamber of Commerce has a permanent Committee on Economics. This committee should do everything possible to inform and instruct the citizens of Olympia and Thurston County in the fundamentals of economics. The committee should make it a further duty to help all groups in the practical application of economic knowledge to their affairs."

PUBLIC SCHOOL SUPERINTENDENT:

"This has been one of the most interesting and valuable examples of 'democracy in action' that I have ever seen. I believe we still have to do some of our own thinking about economic problems, and these discussions have stimulated mightily that thinking.

"We should have more groups of business, professional and labor leaders getting together to exchange ideas on the preservation of free enterprise."

LABOR REPRESENTATIVE (C. I. O.):

"As a representative of the C. I. O. in Thurston County I have attended the course in economic studies conducted under sponsorship of the Olympia Chamber of Commerce. While I do not agree with all of the theories presented, I did find the meetings very constructive and I feel that a lot can be accomplished through this type of meeting where a cross-section of the population of any community is represented.

"I trust that at any future meetings of this kind I or some other representative of the C. I. O. will have the opportunity to attend."

RETAIL STORE PROPRIETOR:

"The classes have been excellent. They brought us the first facing of FACTS rather than attempts to gain personal or business class advantage—a willingness to look issues in the face and decide them with an eye to the welfare of the people as a whole. The classes attempted to jolt every type of businessman, professional worker and labor representative out of selfish positions and get them back on the road of real Americanism—'one for all and all for one', with the good old competitive spirit, honest rules and fair play.

"We must continue this program and get our fellow businessmen interested. We must do what every Chamber of Commerce and service club—both somewhat outmoded—fail to do. We must face facts, study controversial issues, both political and economic, and get information from really broad-viewed economists and social scientists."

OIL COMPANY EXECUTIVE:

"The manner in which these problems have been presented to us shows the way to settle misunderstandings among the various classes of Americans. Frankly, it was the first time I ever listened to this kind of a discussion and carried away from it well-formed thoughts."

JUSTICE OF THE PEACE:

"I believe the series of lectures has met a great need. Many, possibly, a majority of, businessmen today do not have a broad, organized and intelligent understanding of the essentials of free enterprise.

"It should be emphasized that a serious study of business theories and practices of the past, as they are affected by present trends, and future consequences upon free enterprise, is a definite and wholesome contribution to the war effort. It is a patriotic thing to give time and study in determining just where our nation is headed and to chart that course intelligently and honestly.

"We know that it is the highest sort of moral order that leads to the spontaneous action of individuals in producing goods wanted by others, and in exchanging those goods for goods which the others have produced. Society thus acts together in supplying its wants. There is nothing anti-social, anti-moral or anti-Christian in such free enterprise.

"Keep up the good work. Definitely you are on the right track!"

STATE PROGRESS COMMISSION OFFICIAL:

"These classes have offered an opportunity to crystallize opinion as to action needed on the part of business, the public and government, if we are to have an intelligent policy toward free enterprise after the war.

"A permanent Committee for Free Enterprise should be created. Let this committee adopt a policy of action to include:

1. Continuing study of economic developments to keep all of us up-to-date on conditions.
2. Machinery for expression of opinions and conclusions through media of public information, such as the press, radio and speakers, and for transmission of this information to members of Congress.
3. Cooperation with other groups of similar nature in the Pacific Northwest and on the Pacific Coast, and ultimately over the nation."

DEPARTMENT OF UNEMPLOYMENT COMPENSATION OFFICIAL:

"These classes have been very much worth while, primarily as an initial step in a constructive attempt to preserve the things that are best in our economic system. Factors which have made this country great are being rapidly undermined. Unless an organized defense of them is established, it is entirely possible that we are headed for a long period of decline. It is certainly patriotic and worth while to attempt to preserve the best economic structure the world has yet found.

"The program (1) should be carried to all important communities in the country; (2) should be expanded after basic principles have been agreed upon; and (3) should then be translated into action on a nationwide basis. Local organizations should be maintained for continued study."

HIGH SCHOOL PRINCIPAL:

"This has been a very constructive program. I believe conferences of this type can be continued. I am sure the group should be made up of a cross-section of farmers, workers, and business and professional men. The more people brought in contact with such studies, the better."

BANKING EXECUTIVE:

"The classes have been both interesting and instructive. With the ground work so well laid, every effort should be made to continue the studies, and with very much the same pattern followed.

"An economist should be selected to guide the studies, with a supporting group of committeemen working in close cooperation. Classes should not be restricted to members of the Chamber of Commerce.

"The work is far too important to drop after such an excellent start."

SOCIAL SCIENCE INSTRUCTOR:

"This is a very fine course. It brings out prominently many of the most important problems of today. It lays down certain fundamental economic principles which are invaluable in understanding the present American scene."

BANKING EXECUTIVE:

"The course of lectures has been a source of inspiration to the group of Olympia businessmen attending. Thoughts developed in the discussions will, to my mind, cause many to take a new inventory of their plans and practices to see if they have been operating on a basis that would perpetuate their usefulness to society."

Y. M. C. A. OFFICIAL:

"A widespread exposure to these economic principles so popularly presented should result in much greater unity of ownership, management and labor interests. It is clear gain just to get these representatives together under Chamber of Commerce auspices."

INSURANCE BROKER:

"The course gives heartening hope that the Chamber of Commerce can provide a new kind of leadership, not only for business but for general society. What is needed is enlightenment and understanding of a few fundamentals. That businessmen want to know more about them has been proved by the increasing numbers who have attended this course.

"The Chamber of Commerce can save free enterprise by a vigorous program of education along this line—motivated by unselfish service and constructive civic interest."

MAYOR OF OLYMPIA:

"I cannot commend these studies too highly. I recommend the work to all chambers of commerce with the hope that the discussions be opened to as many business and professional men as possible. I believe a thorough understanding of the doctrine of free enterprise is necessary to the postwar future of this country and the world.

"The Chamber of Commerce should continue these economic studies through the medium of a permanent committee, with attendant radio and newspaper publicity."

INSURANCE COMPANY OFFICIAL:

"The classes have been practical and have not dealt in schoolroom abstractions. The studies did not show any class, industry or 'special interest' bias.

"If private enterprise on a basis of free competition is the best safeguard for our prosperity, people must be given a chance to have a knowledge of the facts in support of such a conclusion."

DEPARTMENT OF SOCIAL SECURITY OFFICIAL:

"If we were to do it again I would favor discussion periods—discussion of the application of the fundamentals—specifically, what should be done about tariffs, the state's Fair Trade Practices Act, which monopolies should we try to break up and how, what is the best way to deal with unemployed persons when they exist in large numbers, etc.

"Economic laws can be ruthless, and the question of letting ourselves be dominated by such laws at all times, or using them only so long as they help us, merits further discussion.

"We should continue to hold forums, listen to competent speakers on different sides of a question, and have discussion periods following their talks."

CEMENT COMPANY EXECUTIVE:

"This series of lectures has presented a complete picture of fundamental economic problems confronting us. Keen analysis and common sense have pointed the way toward mutual understanding and a free competitive enterprise that can maintain and improve the American standards of living.

"For their own salvation, it is time that businessmen got down to a study of these problems with representatives of labor and agriculture. We must learn to understand the various factors influencing our economic conditions, and then through mutual effort we must strive to eliminate the evils and restrictions that obstruct our system of free competitive enterprise."