FIRST PRINCIPLES

In Morality and Economics

Volume V*

1959

MORAL ASPECTS OF MONEY, BANKING AND THE BUSINESS CYCLE

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126	21	*yould* should be *would.*
211	23	*brought* should be *bought.*
280	15-16	transpose lines 15 and 16 between lines 11 and 12.
347	18	*hown* should be *own.*
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FIRST PRINCIPLES
IN MORALITY AND ECONOMICS

on which depend personal well-being and social health and harmony

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The "Field" Of Morality And Economics

The title of this publication describes its field, namely, the restatement for modern society of basic principles of morality and economics. The *morality* to which reference is made is the *ancient* morality of the Hebrew-Christian religions; the *economics* to which reference is made is in the "great tradition" of freedom, of equality before the law, and of the validity of private ownership of property.

Our term *economics* should not be interpreted to mean that the subject matter is to be limited to the production and distribution of *material* goods only. People seek nonmaterial values as well, and often place a higher estimate on the nonmaterial. Everything that has *value,* whether material or nonmaterial, is in the field of economics.

There is, it is obvious, a *welfareshortage* in the world. The welfareshortage pertains to both material and nonmaterial "things." The means fully to satisfy the welfareshortage are not adequate. The needs, values and objectives of men require all kinds of *human action* to obtain all kinds of goods — spiritual, cultural, aesthetic and utilitarian. In this publication, everything pertaining

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to any human action is its field, including, for example, such varied human action as the collection of interest, the earning of profits, foreign missions, domestic race segregation, or raising the standard of living.

There are other magazines concerning themselves with the relation between morality and economics, which in their respective fields present material admirably, such as *Christian Economics, Faith and Freedom, Freedom First, The Freeman,* and others.

The effects in this life of personally adhering to first principles of morality and economics are, in general, that there is greater *personal* well-being than if these principles are not followed. The health and harmony of society in general are also dependent upon adherence to these first principles. Nevertheless, individuals who adhere to moral and economic first principles are not systematically favored by natural events, which usually depend on natural laws, which are no respecters of persons. An individual who obeys principles of morality and economics is not justified in reaching a conclusion that the weather will therefore be favorably affected for his needs *only*. Further, if one man adheres to first principles but his fellows do not, he may be unfavorably affected by the evil which his neighbors do, despite his own good conduct. Although recognizing these two important qualifications, it is still true that, in the large, holding to first principles in morality and economics should, *other things being equal,* result in improved personal well-being and in better general social health and harmony.

To have been born, to have grown up, and to have lived in the United States in the first 58 years of the present century may result in the conclusions that the world is a wonderful place in which to live, that the kingdom of heaven on earth has now arrived, and that dangers seemingly threatening the present state of affairs will fade away. But it is not realistic to look upon "the good life" in the United States as being secure. Greeks and Romans in their great days probably did not anticipate the devastation of their societies, nor contemplate any return to semi-barbarism. Nevertheless that is what happened.

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Prosperity paradoxically brings with itself internal and external dangers. There is, for one, a softening internal effect from luxury. And then, too, external envy stirs up those who do not have it so good, and they watch for a favorable time to attack the prosperous. Nothing is really secure in the United States or anywhere in this world. It has always been necessary and will always be necessary to protect prosperity by a willingness to fight for first principles.

To protect ourselves, to do well to others by good example, and to be able to induce others to accept what is really good for them requires knowledge of and confidence in first principles of morality and economics.

Accumulative Versus Multiplicative Cooperation

In the July, 1958 issue, page 222, we declared that the very existence of society depended on the existence of natural and acquired *inequalities among men.* We wrote:

> God made everything and everybody different from all others. It is this infinite variety which is a presupposition to Ricardo's Law of Association. If everybody was equal to everybody else in every activity, then no cooperation between men would be profitable. Then Strongman and Feebler would have no purpose of working together because they would be equal in everything in an *equal* degree. The important item is not that people are equal or unequal, but that they are *unequally unequal.* Strongman was unequal to Feebler, in regard to the fact that Strongman excelled above Feebler in every activity; in a sense that was a divisive factor. But they were not equally unequal; and that unequal inequality is not divisive but is the reverse; it is a bonding factor; it cements men together because it is beneficial. Feebler was *one-fourth* as good as Strongman in sawing logs, but he was *two-thirds* as good in pounding nails. It is the *unequal* inequality which not only permits Ricardo's Law of Association to operate, but which is an *essential* feature of it. This feature is indubitably in accordance with reality; we are all very definitely unequally unequal. If it were not for that unequal inequality, society could not hang together.

In a brief (interrupted) conversation with an economist friend (Mr. Percy Greaves; until recently, well-known columnist for *Chrisian Economics*) it was brought to our attention that a specific task may be too great for one man to perform, for example, removing a large stone. Two men equally equal, and who would therefore not cooperate according to Ricardo's Law, which is what we were explaining, would nevertheless find it profitable to use their *combined* strength to remove the stone. This obviously correct critique persuades us to analyze the situation with greater caution at this time.

The problem can be discussed by considering various meanings of the word *cooperation.* Three types of cooperation, by which men better themselves, readily come to mind: (1) cooperative labor of men *with nature;* (2) cooperative labor of men with men to increase *cumulative strength* (the kind of case of moving a stone just cited); and (3) cooperative labor of men with men according to Ricardo's Law of Association which involves non-cumulative effort, specialization of labor, and exchange of the products of specialization, and which we shall call *multiplicative cooperation.* Although the parallel is not perfect, the case for *cumulative cooperation* yields a result, for example, of 3 plus 4 or 7; but the case for *multiplicative cooperation* is the same 3 and 4, but multiplied this time to yield 12. Ricardo's Law of Association in essence involves this multiplicative or proliferating aspect, something not demonstrated in mere cumulative cooperation.

Cooperation With Nature

A large fraction of the efforts of men to "cooperate" consists of cooperating not with each other but with *nature,* that is, the so-called "natural laws" of the world.

Now it happens that advancement of well-being beyond a primitive stage depends upon the existence of *capital.* Capital consists in men having produced an *intermediate something* which gives them greater control over nature; that is the very essence of capital. A gasoline engine is capital. It can do an enormous amount of work. What does this gasoline engine do? It is an intermediate instrument to "harness" certain forces of nature: (1) gasoline which has explosive potentiality; (2) electricity which when timed right and made available in the right place explodes the gasoline; (3) a mechanical design which results in transmitting that power to move a vehicle, or pump water, or do some kind of work. It is not we that work harder to get more product. We have merely combined raw forces of nature — gasoline, electricity, a metal design — in order to utilize more effectively the powers of nature. *Altered* nature does the extra work.

Or we "harness" cotton fibres to obtain cloth: we plant cotton seeds, we cultivate the plant, we pick the cotton, we design machines to process the cotton, to spin and weave it; then we dye it and fashion the cloth into a garment. The garment protects our bodies from becoming cold and wet. We "converted" raw nature into certain intermediate products so that nature would work better for our specific needs and would have a greater utility for us. By such, and many other and various indirect means or intermediate products we make the forces of nature, in regard to a certain thing for a specific purpose, cooperate with us.

Cumulative Cooperation

In the second place there is that form of cooperation among men which merely *adds* their strengths, but does not *increase* their performance beyond mere aggregation or accumulation. This was the case of the stone already cited. Something weighing 300 pounds needs to be removed. One man tugs and strains but to no avail. He calls his neighbor. Let us assume each can lift 160 pounds. The two lift together and then the obstacle is successfully removed. Here were men with equal lifting strength *cooperating* to advantage. We should have called attention to this type of case resulting in cooperation even among equally equal men. (Those who remember the days of threshing machines will think of the *cooperation* involved between neighboring farmers to get their grain threshed. The *size* of the job in the time to get it done and to match the output of a steam engine and a thresher required massing labor not so much for division of labor as aggregating it. Obviously this cooperation *was* important.)

Our first thought was that this type of case is rather unimportant, and relatively this type of cooperation among men is not of great importance compared with cooperation of men with nature, previously mentioned; the *cases* are fewer; and the *effects* are less. Whereas harnessing nature yields tremendous *multipliers* of power, this method yields a simple *addition* of power. But this cooperation should not be ignored or despised, and a primitive society would exist on this ground alone, if for no other reason than to get the benefit from *aggregate* self-defense against enemies. Ten men fighting together against a common enemy have a great advantage compared with each man protecting himself in isolation. Our friend's critique is, therefore, significant and corrective in an important way.

Multiplicative Cooperation

Next, there is a third type of cooperation, namely, the type which we have called *multiplicative* cooperation rather than cumulative cooperation. This is the kind of cooperation which is involved under what is known as Ricardo's Law of Association. Such cooperation, we believe, is more important than cumulative cooperation; the most effective binding force in society resides in this type. However, the peculiarity of this type of cooperation is that it is practically universally not understood nor even known to exist. It requires an analytical approach and the use of mathematics to *understand* how Ricardo's Law works. Although the Christian religion has long incorporated the *consequences* of Ricardo's Law into its moral teaching, it has not, however, presented the analytical, mathematical evidence. The *effect* is accepted, but the *cause* is not understood.

Ricardo's Law of Association in its broadest formulation is simply this: *voluntary* cooperation by people results in benefits far beyond mere addition or cumulation; everybody participating benefits more than cumulatively; the strongest, wisest and most talented person gains from humble cooperation with the weakest, most foolish and least-talented person; but vice versa, the feeblest, least-wise and most-ungifted person gains inescapably from the cooperation of the strongest, wisest and most gifted persons. As long as the participations are voluntary, there are inevitable *mutual* gains, except that there be an error of judgment on somebody's part, which of course will be discovered promptly by experience and will therefore be eliminated.

In this formulation of Ricardo's Law the inclusion of the word *voluntary* is essential. The law is impaired if the word *voluntary* is left out. This calls attention to the fact that Ricardo's

Law will not function well if the strong coerce the weak, (or for that matter if the dishonest cheat the innocents; but this latter will be corrected by "experience"; coercion, contrarily, is not necessarily corrected by experience). Underlying Ricardo's Law, then, is an assumption, namely, that coercion and violence are not present in the *attitude* of the participants; or, if present, that it is *controlled* and *restrained* by the group as a whole against individual members, or by some agency such as the state.

This points to the basic importance of the ancient command in the Mosaic decalogue, the Sixth, *Thou shalt not kill.* In this statement *all* coercion is obviously condemned (except restraint of evil, of course). When coercion is absent, action becomes voluntary. In the New Testament of the Christian religion the condemnation of coercion gets a positive formulation, to wit, meekness is strongly praised. "Blessed are the meek, for they shall inherit the earth" (Matthew 5:5). If "inheriting the earth" means getting along well and being prosperous, then no text in Scripture more strongly confirms Ricardo's Law than this beatitude. *Meekness* means to leave matters *voluntary;* to leave matters voluntary means to increase greatly the *mutual production* for society, which must necessarily be for mutual *advantage* or else the participation was not (as it was by definition) voluntary.

In the July issue we gave an example of Ricardo's Law. We assumed that two men, named Strongman and Feebler, would experiment to find out which was more profitable — working together or working separately at building houses for themselves. But to make the case "hard," we assumed Strongman was *more capable in everything* than Feebler. The conclusion that nearly everyone, at first, reaches is that Strongman would be better off building his own house, and that his selfish interests are served by letting the incompetent Feebler struggle along by himself. But that is a gross error. We quote from the earlier issue, page 208:

> Both men need a shelter. Both men have the same size families and need the same space. They are both going to build simple shelters of the same size. All the material that they need is 2,000 logs (or boards) apiece and 9,000 nails. We shall assume that both men have a hammer and the nails, but that the logs or boards must be cut and the nails pounded.

According to an assumption we have already made Strongman will exceed Feebler both in sawing logs (or boards) and in pounding nails. Strongman can saw 100 boards an hour and pound 300 nails an hour. Feebler can saw only 25 boards an hour and can pound only 200 nails an hour.

What will it require of Strongman to build his shelter? This is easily computed. If he must saw 2,000 logs or boards at the rate of 100 an hour, it will take 20 hours of sawing. Similarly, if he must pound 9,000 nails at the rate of 300 an hour, that will require 30 hours. The 20 hours of sawing and the 30 hours of pounding make a total of 50 hours.

Feebler's position is different. He can saw 2,000 logs at the rate of only 25 an hour, and so sawing will require 80 hours for him. He can pound his 9,000 nails at the rate of only 200 an hour, and so pounding nails will require 45 hours. It will require 125 hours of work for him to build a shelter compared with only 50 for Strongman.

The 125 hours of work for Feebler plus the 50 hours of work for Strongman total 175 hours as is shown in Table 1.

Table 1

Two Unequally Unequal Men Working Separately

STRONGMAN		FEEBLER	
2,000 logs at 100 an hour =	20 hours	2,000 logs at 25 an hour =	80 hours
9,000 nails at 300 an hour =	30 hours	9,000 nails at 200 an hour =	45 hours
Total	50 hours	Total	125 hours
The two together (50 + 125) = 175 hours			

On the surface there appears to be only one thing for Strongman to do, namely, to do all his own work, and let Feebler struggle alone by himself. Is that, for him, the smartest way to be "selfish"?

He goes over to the Feebler plot of land and discovers Feebler is at a very serious disadvantage at sawing logs, but that he is not at so serious a disadvantage at pounding nails. And so he suggests to Feebler that they work together building their two shelters.

There are two things which might be advanced against this. It might seem to be against Strongman's interest to share his strength with Feebler, and Feebler in his weakness may be inclined to say to himself that there can be nothing in it for him. Nevertheless, Strongman comes up with this proposition which is very simple. He says, "I will saw all the logs and you will pound all the nails."

But Feebler shakes his head and says that it is impossible to make a deal because he (Feebler) admits that he cannot even pound nails so fast as Strongman can. He says, "It is not possible for me to pound nails for you because you can pound nails 50% faster than I can; I can pound only 200 an hour and you 300 an hour."

To that Strongman answers: "Let us figure this out. If I saw all the logs for both of us, I will have to saw 4,000. If you pound all the nails for both of us, you will have to pound 18,000. Let us see how many hours that will take. First I saw the 4,000 logs at 100 an hour, that is, I work for 40 hours. Then you pound the 18,000 nails at the rate of 200 an hour, that is, in 90 hours." It works out like this:

Table 2

Two Unequally Unequal Men Working Together

4,000 logs at 100 logs an hour = 40 hours labor for Strongman
18,000 nails at 200 nails an hour = 90 hours labor for Feebler
The two together = 130 hours

The result is astonishing. The time required to build the two shelters is now only 130 hours compared with the 175 hours shown in Table 1! The saving is 45 hours. In the way we have set up the example, the savings are distributed to both Strongman and Feebler. Previously Strongman spent 50 hours to build his own shelter. Now he has to work 40 hours for exactly the same shelter. He saves 10 hours.

Similarly Feebler makes a saving. Building his own shelter required 125 hours but now by working with Strongman he will have to work only 90 hours. He has a saving from 125 hours down to 90 hours, or 35 hours.

For several variations in the calculations, see as well the August and September 1958 issues.

When we use the term, *multiplicative cooperation,* we refer to the operation of Ricardo's Law of Association, which demonstrates the spectacular benefits which accrue from that type of cooperation. The benefits are not merely cumulative; they are multiplicative.

Ricardo's Law of Association is, unfortunately, not recognized to be one of the very greatest laws governing human relationships. Ricardo (1772-1823) himself was an operator on the London stock market, who retired young after making a fortune. He interested himself in financial and trade problems, including foreign trade and tariffs on such trade. To answer the question whether foreign trade was profitable to all concerned Ricardo worked out the law known by his name. It shows that two nations, one rich and powerful and the other poor and weak, would *both* profit from trade with each other. It sounds unbelievable that two men (or two nations) one of whom is stronger and more productive *in every regard* than the other man (or nation), can *mutually* profitably cooperate (trade with each other). But that is what Ricardo's law indubitably shows. Free cooperation *always* pays well for anyone and everyone. *Both* gain. Those gains result from the character of creation (inequality of men) and from division of labor; or in more fundamental language, the profit from cooperation derives from the *unequal inequality* of men (see July, August, September 1958 issues) caused by creation and by human effort.

Ricardo worked this out for foreign trade, but what is true of foreigners living long distances apart and under different governments is equally true of next door neighbors. Ricardo's Law is of *universal* application. However, it is a strange phenomena that, although Ricardo's Law is absolutely fundamental and universal, one never hears of it in moral and religious circles. It is the most unknown great law that exists. The consequences of this are serious. Not knowing Ricardo's Law of profitable cooperation, men turn to the two alternatives, namely, (1) to coercion, and (2) to charity. To hold society together men think they must have recourse only to these two. Because charity is not forthcoming (so it is believed) in sufficient quantity for the welfare of society, there is further recourse to coercion. What was charity is thereby converted into a governmental type of

Robin Hoodism — the government by means of compulsion takes from some in order to give to others.

In proportion as society finds it necessary to revert to compulsion or coerced "charity," — and in proportion as it is ignorant of and neglectful of relying on Ricardo's Law of Association — its character deteriorates. To the extent society can rely on Ricardo's Law (and its premises) that society is a good society.

In this connection a remark of Adam Smith, the greatest of the early economists, and the general teaching of Scripture are both worth noting.

Adam Smith, analyzing economic freedom, and *free markets*, referred to the wonderful benefits that accrued from them. Although not a religious man in the Christian sense of the term, Smith referred to the blessings that seem to come bountifully and mysteriously from freedom and free markets as "by an invisible hand." He wrote as follows (*The Wealth of Nations*, p. 423) Modern Library edition (our italics):

> But the annual revenue of every society is always precisely equal to the exchangeable value of the whole annual produce of its industry, or rather is precisely the same thing with that exchangeable value. As every individual, therefore, endeavors as much as he can both to employ his capital in the support of domestic industry, and so to direct that industry that its produce may be of the greatest value, every individual necessarily labours to render the annual revenue of the society as great as he can. He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it. By preferring the support of domestic to that of foreign industry, he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led *by an invisible hand* to promote an end which was no part of his intention. Nor is it always the worse for the society that it was no part of it. By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it. I have never known much good done by those who

> affected to trade for the public good. It is an affectation, indeed, not very common among merchants, and very few words need be employed in dissuading them from it.

What Adam Smith is saying is that the blessings of noncoercion (from obeying the Sixth Commandment, Thou shalt not coerce (kill),) are beyond addition and beyond expectation. They appear mysteriously good and almost illogical. But the "invisible hand" was essentially Ricardo's Law. What was happening was neither illogical nor unaccounted for by mathematics.

Similarly, the Christian religion, especially in the Wisdom Books in the Old Testament, declares that the blessing of God rests on obedience to his commandments. The constant refrain is *obey;* obey and it will go well with you. Obey what? The Ten Commandments of Moses; then God will reward you. How? By a miraculous act of some kind? Would you wake up some morning with extra grain in your granary, extra cows in your pasture, extra jewelry on your wife's fingers? No such mysterious events have ever occurred. But the prosperity which is repeatedly mentioned and which is held out as a bait to good conduct — and which is considered something extra for you, something more than cumulative, something really *multiplicative* — is an obvious manifestation of Ricardo's Law. But to understand this it is necessary to remember that Ricardo's Law has premises underlying it, on which it depends, namely, obedience to the Decalogue, especially obedience to the Sixth Commandment.

The mysterious part of "blessings from God" are always (1) from the operations of Ricardo's Law (which is not known and understood and consequently appears to be *special* although it is not), or (2) from direct theistic acts of God. When the ancient lawgivers and prophets of the Hebrews forecast blessings on obedience and punishment on disobedience of the commandments of God, it is not known to what extent the eventual result was based on the operation of Ricardo's Law and to what extent on miraculous theistic intervention. But whichever the means relied on, the prophecies were correct.

Some Christians have a melancholy and defeatist attitude. To be a Christian, and to obey the Commandments of God, (according to their view) involves a penalty, a handicap, and requires facing the prospect of nonsuccess. If they are correct about that, what Scripture teaches is in error, and Ricardo's Law is not mathematics after all. The trouble comes not from obeying the Mosaic commandments nor from Ricardo's Law — the trouble comes from exactly the opposite side — from *disobedience* somewhere, somehow, by somebody, of the Mosaic Law of Morality. The foundation of society, and of Ricardo's Law, is the Decalogue of the Hebrews. Ricardo's Law will always operate unless a man himself violates the Ten Commandments, or unless one or more of his fellows violates those commandments.

Charity Has Never Yet Sustained Society

The natural tendency for religious people is to promote *charity,* and to put forth the idea that *that* is the real bond of society and of brotherly love.

That charity has a function as a bond for society is not to be disputed, but its position is strongly subordinate. Charity is only a supplemental, fractional agency for making a good society; a customary figure might be selected, say 10 percent. When much beyond that, charity, except in emergencies, is a divisive, and certainly a psychologically destructive factor in society.

Marxian socialism-communism pretends it relies *solely* on charity as its principle for a bond for society. Religious people, when they engage in practical affairs, often turn hopefully to the same principle, because it is the *only* principle that they know, except coercion. They are reluctant openly to be in favor of coercion. They wish to do something. They appear to be uninformed on "cooperation" as a principle. Their only recourse therefore is to charity. Brotherly love becomes synonymous with charity. The simplest descriptive term for the social gospel is charity. The same can be said for socialism-communism. The "Kingdom of Righteousness" or the "Kingdom of Heaven" on earth, in this type of thinking, are imaginary constructions of society. They never come into real existence. They are fantasies of wishful thinking.

This was registered on our mind anew when we read an editorial in *Christian Economics* (January 6, 1959) with the title "Charity vs Welfare State." We quote it:

Charity Versus Welfare State

A correspondent vigorously defending the welfare-state quotes the scripture as follows:

> "If any man has this world's goods and sees his brother in need, yet closes his heart against him, how does God's love abide in him?"
>
> (I John 3:17 R.S.V.).

We are in perfect accord with this statement of St. John. When A sees B in need, if he is a Christian, he will help him. That is Christian charity, a very important part of the message of Jesus.

But when A sees B in need and robs C and D, either in person or by means of the power of government, in order to help B, that is welfare-statism. The two are as far apart as the poles.

Christian charity builds good will between giver and receiver and stimulates both to increase efforts. Welfare-statism causes ill-will among the parties concerned. Those on the receiving end never get as much as they think they should have and those forced to pay feel that they are the victims of injustice.

Welfare-statism or socialism is not Christian, was not taught by Jesus, destroys good will, decreases production, puts an end to freedom, and in the end brings hard times and slavery upon us all.

This matter is so plain and so clear that we see no reason why intelligent Christians should confuse Christian charity, the responsibility of the individual to aid suffering, with welfare-statism which is the use of coercive power to rob some and, after taking care of the bureaucrats, to give what is left to those whom the bureaucrats think are most deserving, or have the most votes.

The only kind of *charity* is voluntary charity. The moment that the *voluntary* aspect is removed, the gift is no longer charity, but coercion. Now *voluntary* charity is exactly what the advocates of an earthly "Kingdom of God" are not satisfied with; they consider it inadequate; people do not *give* enough. Therefore, they favor requiring *compulsory* giving, through the medium of taxes and expropriation.

Of the three principles for "organizing" society — coercion, charity and cooperation — the principle of "charity" is the first to drop out. It will not "work." Even those who appeal to "brotherly love" and "righteousness" as principles for organizing society are never satisfied with *voluntary* charity. In other words, if "brotherly love" and "righteousness" are indeed real principles then the words must mean something else than charity. And they do. Essentially, they refer to *cooperation* among men and not *charity* among men. At least the ancient Hebrew ethics referred to *cooperation* as the basis of society, and not charity. And the ethics of New Testament times did not deviate from the Old Testament principle.

But if *cooperation* and not charity is the basic *ethical* principle binding society together, then what does *cooperation* mean? Should not religious leaders define *cooperation* so that it means something more and better than charity. Or have they no such definition? Is there in fact any other definition possible than Ricardo's Law of Association?

Of the three principles potentially able to bind society — coercion, charity and cooperation — the following is one way to look at them:

1. Charity is a fractional bond. On the average maybe good for 10%. To expect more than that will probably result in disappointment, and probable psychological damage to receiver and giver. To *insist* on more than that — or more than is voluntary, whatever that may be — is to resort to coercion; *charity,* as a principle, has been abandoned by the very act of compulsion.

2. Coercion plays a necessary and vital role in society for resistance to domestic and foreign evil. For those purposes coercion is meritorious, but for no other. The most fundamental ethical commandment in the Mosaic Decalogue completely forbids coercion (Thou shalt not kill) except to resist evil.

3. That leaves only one *general* principle for bonding society together, namely, *cooperation,* to wit, voluntary exchange between men. If Ricardo's Law is understood, men selfishly seeking their own gain in a *voluntary* framework never can do good to *themselves only.* In *that framework,* they can *never* help themselves without helping their neighbors simultaneously.

Who hurts his neighbors by being selfish in a bad sense? He who goes off by himself; he who will not develop his own skills and specialize in his own work; he who wants a primitive society rather than a complex, mutually dependent society; he who, like Gandhi, wishes society to return to individual self-sufficiency.

And who really abides by the principle of cooperation? He who specializes and develops great special skills; who, therefore, must *exchange* his surplus for the surplus of other specialists; he who makes these exchanges without coercion or threats of coercion; he who rejoices in the *more complex* society becomes, because the more complex it becomes the more "cooperative" it must be, and *consequently the more prosperous it must be for everybody.*

It is *Ricardo's Law plus the premises that underlie it,* namely, the ethical commandments in the Mosaic Decalogue, which constitute the basic principle of a "just society" or "social righteousness" or the "Kingdom of Heaven" on earth.

James Madison Versus Karl Marx On The Origin Of Property

Karl Marx (1818-1883) opposed private ownership of property because (he said) it made men unequal. *Private* property was cause; resulting inequality was effect.

James Madison (1751-1836), fourth president of the United States, took an exactly contrary position. He declared that men were born unequal in abilities: *that* (his exact expression, probably selected to de-emphasize inequality, was "diversity of faculties") was cause. He declared that the effect of that cause was that some men had property and others did not.

Is inequality of men an effect of private property as Marx alleged; or is inequality of men the cause of private property as Madison alleged?

The answer to these questions has an interesting bearing if one believes in a God who created the human race. If God created men unequal (a condition Madison declared men were in) then God is the ultimate cause of private property, and it was valid for Him to legislate against theft. If on the other hand, God made men equal, and if He wants them kept equal (so that equality presumably manifests brotherly love!), then private property is an evil because it is one form of inequality. There is also the question that, if God did not make men equal, should He have done so, and whether His failure to have done so is a blemish upon His act of creation. Finally, if He failed to be a good Creator (alleged on the ground that He did not make men equal), then there is the question whether men should undertake to work towards equality in order to correct a basic deficiency of the act of creation by God.

As a question of individual and social objectives, the problem can be phrased this way: should men strive to be equal or to be unequal? Or as a question of morality: is gross inequality (or any inequality for that matter) evidence of injustice or lack of brotherly love? Or as a question of church doctrine: is private property ultimately the result of a *good creation by God,* or is private property ultimately the result of the *sins of men?* Madison ascribes the existence of private property to an act of God (or at least to a physiological fact), to creation or evolution whichever he may have believed. Marx, contrarily, ascribes the existence of private property to "sin," — the exploitation of the weak by the strong.

Whether or not Madison explicitly step by step developed his doctrine that private property depends on the inequality of men is not known to the writer. But Madison reveals enough of his thinking in the Tenth of *The Federalist Papers* so that his reasoning can be adequately traced. This Tenth of *The Federalist Papers* is one of the best. In it Madison effectively develops the idea that a *republic* is a better type of government than a *democracy.* In the course of his argument he frankly meets up with the question of *faction* in a *popular* society (as distinguished from a monarchic or an aristocratic society). He declares that there will always be special interests or *factions.* The most conspicuous case is the one between property owners and the propertyless. It is at that point that he makes statements as follows (our italics):

> The second expedient [for removing the *causes* of faction] is as impracticable as the first would be unwise. As long as the reason of man continues fallible, and he is at liberty to exercise it, different opinions will be formed. As long as the connection subsists between his reason and his self-love, his opinions and his passions

will have a reciprocal influence on each other; and the former will be objects to which the latter will attach themselves. *The diversity in the faculties of men, from which the rights of property originate, is not less an insuperable obstacle to a uniformity of interests. The protection of these faculties is the first object of government. From the protection of different and unequal faculties of acquiring property, the possession of different degrees and kinds of property immediately results;* and from the influence of these on the sentiments and views of the respective proprietors, ensues a division of the society into different interests and parties.

The latent causes of faction are thus sown in the nature of man; and we see them everywhere brought into different degrees of activity, according to the different circumstances of civil society. A zeal for different opinions concerning religion, concerning government, and many other points, as well of speculation as of practice; an attachment to different leaders ambitiously contending for pre-eminence and power; or to persons of other descriptions whose fortunes have been interesting to the human passions, have, in turn, divided mankind into parties, inflamed them with mutual animosity, and rendered them *much more disposed to vex and oppress each other than to cooperate* for their common good. So strong is this propensity of mankind to fall into mutual animosities, that where no substantial occasion presents itself, the most frivolous and fanciful distinctions have been sufficient to kindle their unfriendly passions and excite their most violent conflicts. *But the most common and durable source of factions has been the various and unequal distribution of property. Those who hold and those who are without property have ever formed distinct interests in society.* Those who are creditors, and those who are debtors, fall under a like discrimination. A landed interest, a manufacturing interest, a mercantile interest, a moneyed interest, with many lesser interests, grow up of necessity in civilized nations, and divide them into different classes, actuated by different sentiments and views. *The regulation of these various and interfering interests forms the principal task of modern legislation, and involves the spirit of party and faction in the necessary and ordinary operations of the government.* [*The Federalist Papers* (Selections), Henry Regnery Company, Chicago, 1948.]

Madison makes an affirmation about the natural conflicts between men; the statement reads: "The diversity of the faculties of men, . . . is . . . an insuperable obstacle to a uniformity of interests." Madison here begins with a creational, or at least a biological fact, namely, "the diversity of the faculties of men." This is the basic premise from which he reasons. He does not endeavor to substantiate the proposition. He apparently takes it as an axiom, beyond proof or so obvious that it does not need proof. But then he slips in a subordinate idea so that the complete sentence reads: "The diversity in the faculties of men, *from which the rights of property originate,* is not less an unsuperable obstacle to a uniformity of interests." In short: men are unequal in abilities; therefore (1) they cannot have the same interests; and (2) they acquire *rights* to property.

Then Madison goes on to make additional statements, equally impressive whether they are right or wrong. He declares that "The protection of these faculties is the *first* object of government." One might ask how a government can "protect" created or acquired faculties; they are in existence despite government and independent of government by virtue of creation. But what he obviously means is that it is the function of government to prevent anyone from frustrating *the exercise* by another of his special faculties. The sentence reads clearer and less-objectionable if three words are inserted: "The protection of [*the free exercise*] of these faculties is the first object of government." This is simply the proposition that the purpose of government is to protect each man's freedom. How could freedom be more significant than in the untrammeled exercise of abilities? Then Madison states his conclusion: "From the protection of different and unequal faculties of acquiring property, the possession of different degrees and kinds of property immediately results; . . ."

In the second paragraph quoted Madison shows the ultimate cause of the existence of private property; he writes: "The latent* [ultimate] causes of faction are thus *sown in the nature of man.* Marx declared just the opposite, namely, that property existed solely because of *man-made laws.*

Madison later makes the statements: "But the most common and durable source of factions has been the various and unequal distribution of property. Those who hold and those who are without property have ever formed distinct interests in society." If that means that the two interests (the property holders and the propertyless) *think* that their interests are contrary, the statement is above reproach. But if it means that there is a *genuine* conflict of interest between the property holders and the propertyless, then the statement is a profound error. Undoubtedly, Madison meant that the two classes, especially the propertyless, *think* that their interests are opposed. In fact, they are not; the great mistake lies in *thinking* it. The detailed proof must await another time. But one point will immediately be obvious to everyone: if *A* may not keep *his* property, then no one else should expect his own to be safe. If a man does not have property and if acquiring ownership is not made safe, he will not work hard or be thrifty to obtain it, because having done so, it will be taken from him, as he himself previously approved taking *A*'s property from him. Then, generally, people will voluntarily *neither work hard nor save any more.* Then *capital per capita* will decrease. As sure as the sun rises and sets, and that all men are mortal, prosperity *for men collectively* — property holders and propertyless — will then decline. Eventually, there will be severe poverty, because prosperity depends on the amount of *capital per capita.* Other explanations of the immediate cause of prosperity are erroneous.

However, if individual men do not save, and if desperate poverty will then result for everybody, there is still the possibility of *collective saving,* via the government. These are known as Five-Year Plans, or the like, of tyrannical and despotic governments. Obviously, prosperity and liberty alike depend on *private* ownership of property, regarding the protection of which Madison, at the end of the quotation says: "The regulation of these various and interfering interests [largely relating to property] forms the principal task of modern legislation..."

*The dictionary gives as the first meaning of *latent:* "not visible or apparent; hidden . . ."

Madison's reasoning appears to be sound. His conclusion follows from his premises. But the *ultimate* question remains: Did God make a mistake when He made men unequal in faculties? This is indeed fundamental. Fortunately, David Ricardo showed mathematically that *inequality* is a great blessing. From Ricardo's* mathematical demonstration of the Law of Association only one inference is possible: God was infinitely wise when He made men unequal in the fullest sense of the term. If inequality were not a fundamental ingredient in creation, human society, in any significant sense of the term, would not exist.

Government Versus Constitution

In the November and December 1958 issues, we quoted from the early section of John C. Calhoun's *A Disquisition on Government,* and we indicated our estimate of Calhoun as a political thinker. We concur with the prevailing estimate that John Calhoun is the foremost political philosopher that the United States has produced.

In the sections previously quoted, (in November 1958) Calhoun outlined his views that man never lives in isolation but that he is essentially social in character. He neglects mention of the theories of Rousseau about man being good in nature and spoiled by association with fellow men. Calhoun states only his own affirmative opinions. It is, of course, necessary for him to explain why everything is not "sweetness and light" in society. He does this by a simple and fundamental proposition, namely:

> "...while man is created for the social state and is accordingly so formed as to feel what affects others as well as what affects himself, he is, at the same time, so constituted as to feel more intensely what affects him directly than what affects him indirectly through others, or, to express it differently, he is so constituted that his direct or individual affections are stronger than his sympathetic or social feelings."

Calhoun says man was created that way, and implies therefore that it is not sin in itself to have "individual affections... stronger than... sympathetic and social feelings."

Calhoun's profound and simple way of showing how man was created keeps him from an erroneous conception of sin;

*See July through September 1958 issues of PROGRESSIVE CALVINISM.

(obviously, it is not sin that we were *created* as we were). An understanding such as Calhoun's of the nature of man and of the nature of sin has the consequence that his subsequent thinking is on a sound foundation rather than an unrealistic one.

With simplicity and force, Calhoun, in four and one-half pages explains the nature of man and the necessity of government. Without making his presentation parochial, by using Biblical terms or categories of thought in regard to creation, society and sin, he nevertheless in effect begins with completely Biblical premises; (but contrary, however, to premises which are popular but erroneous *interpretations* of Scripture). In those four and one-half pages Calhoun also calls attention to the moral validity of pursuing self-regarding interests, although he specifically avoids the use of the word "selfish." With cogency he shows that a society based upon anything else than self-regarding interests would become chaotic. (See also May 1958 issue, pages 156ff., and elsewhere in this publication for arguments on the same subject and to the same effect as Calhoun's.)

Calhoun makes clear that society cannot exist without government. But he immediately meets up with a problem of what the character of government is, and whether there are dangers in connection with the existence of government. Calhoun looks at government from two viewpoints: (1) that it is an absolute necessity and a great good; but (2) that it is potentially dangerous and evil because government may oppress rather than protect its citizens. We quote from pages 7-10 of The American Heritage Series issue of Calhoun's *A Disquisition on Government.*

> But government, although intended to protect and preserve society, has itself a strong tendency to disorder and abuse of its powers, as all experience and almost every page of history testify. The cause is to be found in the same constitution of our nature which makes government indispensable. The powers which it is necessary for government to possess in order to repress violence and preserve order cannot execute themselves. They must be administered by men in whom, like others, the individual are stronger than the social feelings. And hence the powers vested in them to prevent injustice and oppres-

sion on the part of others will, if left unguarded, be by them converted into instruments to oppress the rest of the community. That by which this is prevented, by whatever name called, is what is meant by *constitution,* in its most comprehensive sense, when applied to *government.*

Having its origin in the same principle of our nature, *constitution* stands to *government* as *government* stands to *society;* and as the end for which society is ordained would be defeated without government, so that for which government is ordained would, in a great measure, be defeated without constitution. But they differ in this striking particular. There is no difficulty in forming government. It is not even a matter of choice whether there shall be one or not. Like breathing, it is not permitted to depend on our volition. Necessity will force it on all communities in some one form or another. Very different is the case as to constitution. Instead of a matter of necessity, it is one of the most difficult tasks imposed on man to form a constitution worthy of the name, while to form a perfect one — one that would completely counteract the tendency of government to oppression and abuse and hold it strictly to the great ends for which it is ordained — has thus far exceeded human wisdom, and possibly ever will. From this another striking difference results. Constitution is the contrivance of man, while government is of divine ordination. Man is left to perfect what the wisdom of the Infinite ordained as necessary to preserve the race.

With these remarks I proceed to the consideration of the important and difficult question, How is this tendency of government to be counteracted? Or, to express it more fully, How can those who are invested with the powers of government be prevented from employing them as the means of aggrandizing themselves instead of using them to protect and preserve society? It cannot be done by instituting a higher power to control the government and those who administer it. This would be but to change the seat of authority and to make this higher power, in reality, the government, with the same tendency on the part of those who might control its powers to pervert them into instruments of aggrandizement. Nor can it be done by limiting the powers of government so as to make it too feeble to be made an instrument of abuse, for, passing by the difficulty of so limiting its powers without creating a power higher than the government itself to enforce the observance of the limitations, it is a sufficient objection that it would, if practicable, defeat the end for which government is ordained, by making it too feeble to protect and preserve society. The powers necessary for this purpose will ever prove sufficient to aggrandize those who control it at the expense of the rest of the community.

In estimating what amount of power would be requisite to secure the objects of government, we must take into the reckoning what would be necessary to defend the community against external as well as internal dangers. Government must be able to repel assaults from abroad, as well as to repress violence and disorders within. It must not be overlooked that the human race is not comprehended in a single society or community. The limited reason and faculties of man, the great diversity of language, customs, pursuits, situation, and complexion, and the difficulty of intercourse, with various other causes, have, by their operation, formed a great many separate communities acting independently of each other. Between these there is the same tendency to conflict — and from the same constitution of our nature — as between men individually; and even stronger, because the sympathetic or social feelings are not so strong between different communities as between individuals of the same community. So powerful, indeed, is this tendency that it has led to almost incessant wars between contiguous communities for plunder and conquest or to avenge injuries, real or supposed.

So long as this state of things continues, exigencies will occur in which the entire powers and resources of the community will be needed to defend its existence.

When this is at stake, every other consideration must yield to it. Self-preservation is the supreme law as well with communities as with individuals. And hence the danger of withholding from government the full command of the power and resources of the state and the great difficulty of limiting its powers consistently with the protection and preservation of the community. And hence the question recurs, By what means can government, without being divested of the full command of the resources of the community, be prevented from abusing its powers?

The question involves difficulties which, from the earliest ages, wise and good men have attempted to overcome — but hitherto with but partial success. For this purpose many devices have been resorted to, suited to the various stages of intelligence and civilization through which our race has passed, and to the different forms of government to which they have been applied. The aid of superstition, ceremonies, education, religion, organic arrangements, both of the government and the community, has been, from time to time, appealed to. Some of the most remarkable of these devices, whether regarded in reference to their wisdom and the skill displayed in their application or to the permanency of their effects, are to be found in the early dawn of civilization — in the institutions of the Egyptians, the Hindus, the Chinese, and the Jews. The only materials which that early age afforded for the construction of constitutions, when intelligence was so partially diffused, were applied with consummate wisdom and skill. To their successful application may be fairly traced the subsequent advance of our race in civilization and intelligence, of which we now enjoy the benefits. For without a constitution — something to counteract the strong tendency of government to disorder and abuse and to give stability to political institutions — there can be little progress or permanent improvement.

In answering the important question under consideration it is not necessary to enter into an examination of

> the various contrivances adopted by these celebrated governments to counteract this tendency to disorder and abuse, nor to undertake to treat of constitution in its most comprehensive sense. What I propose is far more limited: to explain on what principles government must be formed in order to resist by its own interior structure — or to use a single term, *organism* — the tendency to abuse of power. This structure, or organism, is what is meant by constitution, in its strict and more usual sense; and it is this which distinguishes what are called "constitutional" governments from "absolute." It is in this strict and more usual sense that I propose to use the term hereafter.

There is a statement in Scripture about government, by the Apostle Paul, which can almost be said to be unfortunate; the statement reads: *The powers that be are ordained of God* (Romans 13:1b). This text has resulted in much idolatry, patterned after the idolatry of Ferdinand Lassalle, the German socialist agitator and cordially hated "competitor" of Karl Marx, who said: *The state is God.* Unless Paul's text, "The powers that be are of God," is interpreted differently from Lassalle's remark, "the state is God," the Christian religion is perverted into gross idolatry. That is the way, however, that Paul's text is frequently interpreted! But the text, interpreted *in its context,* makes clear that there is a qualification to the statement, namely, that that state (which is said to be "of God") rewards the good and punishes the evil (see verses 3-6). In other words, the state is "of God" when and only when it rewards the good and punishes the evil. If, contrarily, the state must always be obeyed, then there can be no question about it, the state *is* God.

Calhoun was not so naive as to accept the idea that *all* governments are of God, although he has in the preceding long quotation the dubious statement: "Constitution is a contrivance of man, while government is of divine ordination." Why the distinction?

Calhoun is writing an essay on government and he finally ends up with the idea that a government cannot be good unless it is restricted to its proper functions by something that frustrates it from doing evil, namely, a *constitution.*

People are proud that they live under a constitutional government. They are, in other words, proud that they have means of frustrating that institution (the government) of "divine ordination." If the instrument to accomplish that is a constitution, then it is a wonderful thing to keep a government from doing evil. But what if a constitution does not exist, or what if it is flouted, or what if it is perverted (as the constitution of the United States is perverted at the present time), is there no other legitimate tool than a "constitution" to resist evil perpetrated by a government? What about open rebellion — as the American colonies against Great Britain, or the Provinces of the Low Countries against Spain? If a constitution may properly restrain a government, so may other tools or agencies do so.

Calhoun fails to assign a good reason why government is "of God," and constitution (which is presumably above government) is only of men. The preferable view, it seems to us, is that governments and constitutions are equally of men.

God does not enter into the picture (if we may use that figure of speech) except as a declarer of *principles* of government. A government following moral principles can for all practical purposes be considered to be "of God." Rebellion against such a government would be unwise and pointless. But even a "good" man might rebel, become king in place of the man he ousted, and then continue the government according to the same moral principles as the predecessor. An identification of a specific govenment with the government of God is, it seems to us, open to critique. But what is not open to critique is that a government, operating according to the *principles* of the moral law declared by that God, can genuinely be said to be "of God."

What has always appeared so illogical and impractical to us is the proposition by Christian political thinkers that a government is "of God" but that they also believe in constitutions. If a government is "of God," then there need be no constitution to protect people from that agency of God. The idea of a "constitution" essentially negates the idea that a government (that is, a *specific* government) is "of God." In our thinking both governments *and* constitutions are "of the people"; neither is "of God" in the naive sense.

We would have preferred it if Calhoun had reversed the statement so that it would read: "Government is a contrivance of man, while constitution is of divine ordination." But that is not satisfactory either, because a constitution, as well as a government, can be contrary to the principles of the moral law of God.

But the main thrust of the foregoing quotation from Calhoun is, we believe, indisputably right, to wit, (1) governments need constitutions to restrain them; (2) the constitution must not weaken a government, because a government must provide against external danger and internal disorder, and (3) the great difficulty is properly to restrain a government from evil without making it too weak to be effective. The problem is just that — the balance between power and responsibility.

The American "Tax-Consuming Interest"

The Democratic Party had its representative in the presidency of the United States from 1932 through 1952. Then the Republicans elected their candidate and he has occupied the position of Chief Executive of the United States since then.

In the Democratic administrations, from 1932 to 1952, a huge bureaucracy was built up. That bureaucracy continued *practically unchanged* into the new Republican administration. It appears now that any president will be almost the puppet of this bureaucracy rather than its head.

Calhoun had a prophetic insight into the nature of the executive department of a government, which he outlined in the section of his *A Disquisition on Government* which describes the British Constitution. This section, which reads as follows, is singularly applicable to the United States at the present time (pages 75-78):

> The origin and character of the British government are so well known that a very brief sketch, with the object in view, will suffice.
>
> The causes which ultimately molded it into its present form commenced with the Norman Conquest. This introduced the feudal system and with its necessary appendages — a hereditary monarchy and nobility; the former in the line of the chief who led the invading army,

and the latter that of his distinguished followers. They became his feudatories. The country—both land and people (the latter as serfs)—was divided between them. Conflicts soon followed between the monarch and the nobles—as must ever be the case under such systems. They were followed, in the progress of events, by efforts on the part both of monarchs and nobles to conciliate the favor of the people. They, in consequence, gradually rose to power. At every step of their ascent they became more important — and were more and more courted — until at length their influence was so sensibly felt that they were summoned to attend the meeting of the parliament by delegates, not, however, as an estate of the realm or constituent member of the body politic.

* * *

As it now stands, the realm consists of three estates: the king, the lords temporal and spiritual, and the commons. The parliament is the grand council. It possesses the supreme power. It enacts laws by the concurring assent of the lords and commons — subject to the approval of the king. The executive power is vested in the monarch, who is regarded as constituting the first estate. Although irresponsible himself, he can only act through responsible ministers and agents. They are responsible to the other estates — to the lords as constituting the high court before whom all the servants of the crown may be tried for malpractices and crimes against the realm or official delinquencies and to the commons as possessing the impeaching power and constituting the grand inquest of the kingdom. These provisions, with their legislative powers — especially that of withholding supplies — give them a controlling influence on the executive department and virtually a participation in its power — so that the acts of the government, throughout its entire range, may be fairly considered as the result of the concurrent and joint action of the three estates — and, as these embrace all the orders, of concurrent and joint action of the estates of the realm.

He would take an imperfect and false view of the subject who should consider the king in his mere individual character, or even as the head of the royal family—as constituting an estate. Regarded in either light, so far from deserving to be considered as the First Estate and the head of the realm, as he is, he would represent an interest too inconsiderable to be an object of special protection. Instead of this, he represents what in reality is habitually and naturally the most powerful interest, all things considered, under every form of government in all civilized communities — *the tax-consuming interest or,* more broadly, the great interest which necessarily grows out of the action of the government, be its form what it may — the interest that *lives by the government.* It is composed of the recipients of its honors and emoluments and may be properly called the government interest or party — in contradistinction to the rest of the community, or (as they may be properly called) the people or commons. The one comprehends all who are supported by the government, and the other all who support the government; and it is only because the former are strongest, all things being considered, that they are enabled to retain for any considerable time advantages so great and commanding.

This great and predominant interest is naturally represented by a single head. For it is impossible, without being so represented, to distribute the honors and emoluments of the government among those who compose it without producing discord and conflict; and it is only by preventing these that advantages so tempting can be long retained. And hence the strong tendency of this great interest to the monarchical form — that is, to be represented by a single individual. On the contrary, the antagonistic interest, that which supports the government, has the opposite tendency — a tendency to be represented by many, because a large assembly can better judge than one individual or a few what burdens the community can bear and how it can be most equally distributed and easily collected.

In the British government, the king constitutes an Estate, because he is the head and representative of this great interest. He is the conduit through which all the honors and emoluments of the government flow, while the House of Commons, according to the theory of government, is the head and representative of the opposite — the great taxpaying interest by which the government is supported.

> Between these great interests there is necessarily a constant and strong tendency to conflict, which, if not counteracted, must end in violence and an appeal to force, to be followed by revolution, as has been explained. To prevent this the House of Lords, as one of the Estates of the realm, is interposed and constitutes the conservative power of the government. It consists, in fact, of that portion of the community who are the principal recipients of the honors, emoluments, and other advantages derived from the government, and whose condition cannot be improved, but must be made worse by the triumph of either of the conflicting Estates over the other; and hence it is opposed to the ascendency of either and in favor of preserving the equilibrium between them.

In the United States the bureaucracy in Washington has become in a special sense *the tax-consuming interest,* or the interest that *lives by the government.* Having come to be significant and powerful, it will not be easily restricted. This *tax-consuming interest* is sure to continue to exist whether the government be Democratic or Republican. It continued to exist beyond the administrations of Franklin Roosevelt and Harry Truman. It will probably continue to exist beyond the administration of Dwight Eisenhower. As Calhoun says: it "represents what in reality is habitually and naturally the most powerful interest . . . under every form of government."

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FIRST PRINCIPLES
IN MORALITY AND ECONOMICS
on which depend personal well-being and social health and harmony

VOLUME V FEBRUARY, 1959 NUMBER 2

Contents

Ricardo's Law Of Association Operates Simply

There are several reasons for emphasis on Ricardo's Law of Association: (1) although it is one of the greatest discoveries in the social sciences, the law is practically unknown to business men, to moralists, and to nearly everybody; (2) although it is a fundamental law in the field of ethics, it is not taught in theological seminaries; and (3) although the Scriptures of the Christian religion declare repeatedly that God rewards the good and punishes the evil, nevertheless that idea is often repudiated with ridicule and rage by professing Christians, because (apparently) they lack knowledge and understanding how Ricardo's Law demonstrates that what Scripture teaches must be true.

Scripture unequivocally teaches that God rewards the good and punishes the evil; consider what appears in Joshua 1:6-8:

Be strong and of good courage; for thou shalt cause this people to inherit the land which I sware unto their fathers to give them. *Only be strong and very courageous, to observe to do according to all the law, which Moses my servant commanded thee: turn not from it to the right hand or to the left, that thou mayest have good success whithersoever thou goest. This book of the law shall not depart out of thy mouth, but thou shalt meditate thereon day and night, that thou mayest observe to do according to all that is written therein: for then thou shalt make thy way prosperous, and then thou shalt have good success.*

Is this statement to be interpreted as meaning that God personally, by *special* action, will reward whoever obeys the Mosaic Decalogue? Is what is commanded merely what ought to be done, plus a *special* reward; or is it *universal law* the existence of which is obscured only if an extraneous factor intervenes? Is the Decalogue limited to a moral imperative, or is it "scientific" law?

Our answer is that the Mosaic Law is more than a moral imperative; it is a *law* rooted in the nature of things as created. This *law* cannot be violated with impunity. The alternative view is that punishment does not reliably follow upon evil, nor reward upon good: there is no real *causal* relation.

Maybe it will be well to let the two views survive side by side with gentle tolerance on the part of the individuals who hold the two opposing views. But if an attempt is to be made to diminish the extent of the difference, Ricardo's Law will probably be the most helpful that can be found. Ricardo discovered the Law, which has his name attached to it, by making calculations on whether *free trade* between nations was a good thing *in total* and for *each party*. It is well known that most people are against free trade. They believe it hurts them, but that it helps the foreigner. Abandoning the precepts of their religion rather easily, they then decide they are justified in preventing the foreigner from prospering — and so they favor a "protective" (?) tariff (1) to "protect" themselves from a harm they fear (imagine); and (2) to hurt the foreigner by frustrating him. Ricardo demonstrated — the proof is incontrovertible — that the idea is unsound; he demonstrated instead that voluntary trade between nations helps *both* nations.

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(The situations justifying exceptions to free trade do not touch the basic principle involved, and cannot be discussed here.)

Ricardo's achievement was one of the foremost in the history of social thought. But it put him in conflict with most of the great thinkers of the ages — Plato, Aristotle, Montaigne — and many, many others.

Ricardo, to make his argument drum tight, made assumptions that most people would consider destructive for his case. He assumed one country richer, stronger, wiser, better *in every respect* than another which was unbelievably poor. The rich country, which by careless reasoning we all would say could not benefit by dealings with a wretchedly poor one, is *enriched* by the latter; and vice versa. They do *each other* good.

Once that has been worked out conclusively for foreign and domestic trade, it takes no great ability at generalization to conclude that Ricardo's Law underlies *all* human relations. It is a pity therefore that the Law is not taught in seminaries.

(For an explanation of Ricardo's Law see our Volume IV, Numbers 7, 8 and 9. See also last month's issue (Volume V, Number 1) for an abbreviated presentation. To avoid repetition we are not requoting the figures.)

Call the results of Ricardo's Law mysterious or the rewards of religion — call the results what you will — a reader's surprise is unabated unless he analyzes *why* the results are what they are.

Why, in the material referred to above, when Strongman and Feebler "cooperated" in building their houses, were both better off, the competent Strongman as well as the untalented Feebler?

The answer is: Feebler, the much less competent, let Strongman do what he could do *four times* better than Feebler. Feebler, on his part, took over work that Strongman could do only one-half better. *Full use was thus made of Strongman's best talents;* he could not have used his *extraordinary* talent to the full, *if poor Feebler had not taken over work at which Strongman was not so spectacular,* although still better than Feebler. Feebler was the genuine *benefactor* of Strongman; the weakling, Feebler made a debtor out of the superman!

Further, the counter side is equally comforting to Strongman. Strongman let Feebler do what he was *least incompetent* to do, namely, pound nails. Strongman freed Feebler from doing what he was *very* inefficient in doing (sawing), so that he could concentrate on the activity at which he was *relatively* the least ineffective.

That is the *logic* of the seemingly mysteriously good results of the operation of Ricardo's Law. No *mystical* explanation is necessary.

But what does Ricardo's Law have to do with religion, or morality, or the revealed will of God? Are these not irrelevant?

To this question the answer is *no*. Ricardo's Law cannot operate — is null and void — when unhinged from the Law of God, and it cannot have reality or meaning unless it is undergirded by the Sixth Commandment, *Thou shalt not kill*. The relationship may appear obscure, but not if the full meaning of the commandment is indicated by a variant in the phraseology, *Thou shalt not coerce*. If either Strongman or Feebler coerces the other — so that the "trade" is not voluntary — then the benefits are jeopardized. Why? Because if either of the men is coerced, he is obviously being compelled to do what is against his own interests. Then Strongman is no longer working at what he does four times better than Feebler; nor is Feebler working on what is his least inefficiency. Coercion is not necessary to persuade men to do what is good for themselves; it is only justified to frustrate them from doing what is bad for others.

Although Ricardo's Law is not the fundamental law and although the Sixth Commandment is, nevertheless Ricardo's Law explains *how* things happen when the Sixth Commandment is obeyed. The most important meaning of the Sixth Commandment is not discovered, unless Ricardo's Law is thoroughly understood.

Free enterprise is based, not on brigandage, or exploitation, or unmitigated selfishness. *Enterprise* itself (removing the word, *free*) might be based on such, but *free* enterprise must be understood to mean that neither party to a transaction is coerced by the other. The apologists for Capitalism always appeal to free enterprise *in that sense,* and with that definition. It is misrepresentation of Capitalism to imply that it does not favor *freedom* for all, but only for the Strongmans, not the Feeblers. The Strongmans do not really need to have recourse to coercion in order to be benefited by the cooperation of the Feeblers; nor vice versa. The system of *free* enterprise has its own motor mechanism. As to the brakes that the system needs — avoidance of coercion — the necessity of those brakes has never seriously been denied. Nobody, to our knowledge, has ever had the boldness to equate capitalism with anarchism.

Utilization of Ricardo's Law in the teaching of Christian ethics will eventually revolutionize those ethics. Presently the only manifestation of brotherly love that many people know and recommend is *charity,* even coerced charity (a contradiction in terms). Charity alleviates distress. But it does not create prosperity. Charity is, from the viewpoint of social welfare, a negative device. Ricardo's Law — elucidating how cooperation (in contradistinction of charity) works — describes a positive device; it explains how prosperity *is* created.

Mission propaganda abroad, if it formulates the law of brotherly love as charity (alms) or redistribution, is destructive of the growth of a primitive society. Brotherly love *based on cooperation,* that is, working according to Ricardo's Law, will genuinely result in increased welfare in those societies.

The prospects that Ricardo's Law will be properly incorporated into Christian ethics is not bright. The reason is that then it will be necessary to go back to the Law of God and obey it. Individual and group coercions will have to be condemned. It is not obvious that moralists are prepared to do that. More is the pity! — because *cooperation* à la Ricardo's Law will do many times more for mankind than charity (alms) or compulsory redistribution of capital ever will. That is why some moralists do not accept what was quoted from Joshua. They wish to follow the charity, or really the redistribution, route. They do not wish the benefits of obeying Scripture via Ricardo's Law to prove right, as was promised in Joshua; that outcome would discredit their own solution — voluntary alms and coerced alms (redistribution). But most explanatory of all is the probable fact that they do not *understand* Ricardo's Law; maybe even that assumes too much; they may never have actually *heard* of Ricardo's Law.

For the time being, this ends our comments on Ricardo's Law. We drop the subject reluctantly, because of its overwhelming importance.

Charity, As Psychological And Social Poison

Charity has two aspects, one attractive and the other unattractive.

The attractive aspect consists in relief of distress, helping the fallen, creating good will, and showing appreciation for help. *Charity* in that sense is wonderful.

The unattractive aspect of charity is hinted at in the statement by Christ: "It is more blessed to give than to receive." There must be something about being the recipient of charity which is not attractive.

In the first place, the *unworthy* recipient of charity has a guilt or unworthiness complex, if he receives charity *through some fault of his own* — such as irresponsibility, wastefulness, debauchery, or what have you. To be in need of charity has an obvious stigma attached to it, *if* folly or sin is the cause of the distress which needs to be relieved. It was ever thus, and always will be.

The case of the *worthy* recipient is much better — the case of the sick, the handicapped, the genuinely unfortunate, the incompetent who can do no better. But even in these cases the feelings of the recipient are likely to be embittered by the thought that he is not self-supporting, but dependent on the kindness of others. *Psychologically* to be the recipient of charity is almost always bad.

Two men may sit side by side in church. One may be a recipient of charity, the other may be a giver of funds to charity. Except in ideal cases, the recipient will feel inferior and bitter toward his fellow-occupant of the pew; and vice versa, the giver will have an unadmirable feeling of superiority. This psychology is deplorable, but is in the nature of things.

But if *cooperation* is substituted for *charity,* then the psychological and social relationship can become wholesome. We refer to cooperation in the Ricardian sense.

What is the psychology of two men also sitting next to each other in a pew on a Sunday morning, who have interpreted *brotherly love* to be essentially *cooperation* in the Ricardian sense? Let us assume one of the two is talented; and the other inferior. But they *cooperate* together in the Ricardian sense of noncoercive exchange of services. What can *both* of these men think, assuming they hear a sound teaching of the Law of God in that church that Sunday morning? They will hear this:

1. That the talented man was benefited, *enriched,* by his cooperation in Ricardian exchange with the inferior man sitting beside him. The strong man is "under obligation" to the weak man for increasing his (the strong man's) well-being! Remember the case last month of Strongman and Feebler. In that case Feebler (the wholly inferior man) reduced the working hours of Strongman (the superior man) by 10 hours, from 50 to 40 hours, or *twenty* percent. Strongman should not look down on Feebler but up to him, because Feebler is Strongman's benefactor.

2. That the inferior man also was enriched by his cooperation with the talented man. He cannot properly look at his better-endowed neighbor with hatred, because he (the inferior man) has benefited from the cooperation of his talented neighbor.

Say what you will about the sin of pride, each of these men can have a genuine sense of pride in what he "contributed" to the increased result, what he contributed to the other, and further he should also have a genuine sense of appreciation of what the other contributed to himself. Understanding of Ricardo's Law is the basis of a healthy psychology for each individual, and a sound basis for social good will. Why should not this indisputable benefit from cooperation be vigorously taught in pulpits?

In all Scripture, there is no explanation of Ricardo's Law of (brotherly) cooperation, but only an acceptance of its consequences. That acceptance shows up in the form of a promise of prosperity as a result of living according to the premises underlying Ricardo's Law. The modern church should decide to teach explicitly and emphatically the *logical* explanation for promises in Scripture (for this life), or whether it will leave the explanation in the limbo of the unknown. Further, it should decide whether it will teach that *charity* is the essence of brotherly love, as has often been erroneously taught; or whether it will teach that *cooperation* is the real essence of brotherly love. If it teaches the latter, there will be less poison in men's minds and in social relations.

Skepticism Of Security In Old Age

A man may deceive himself, it is alleged, about the future security of his soul. That subject has been argued with sincerity and vehemence and skepticism. It is worth considering whether he is also living in a dream world of unreality about his *security* provisions for his old age, in this life, in the United States of America, in the decade 1950.

There are, we submit, four possible bases for security in old age, namely, (1) savings in kind; (2) charity of relatives or friends; (3) a contract between men involving eventual performance easily and without coercion; and (4) a contract involving coercion.

Is Social Security Not Funded But Founded On Pure Coercion?

Twenty-two years ago in my youth we were sitting around an evening dinner table in the Blackstone Hotel in Chicago. The meeting was for business, but had drifted to a discussion of social security. The dinner party consisted of local professional men, and the partners of a New York investment banking firm. The senior partner, under whose name the firm operated, and who was to become nationally known in the councils of the government of the United States, finally made this remark: *"There is nothing behind social security than the future taxing power of the United States."*

Now that was a startling statement. Nothing behind social security than the *future taxing power* of the United States? Is the social security fund not funded? (*Funded* means that a fund of assets exists or is being accumulated to assure ability to make disbursements in the future; a non-funded plan means that such assets do not exist.) Has the obligation not been actuarily computed and payment rates set accordingly?

"Taxing power" in the future is not a savings fund. If the money had been saved, then all that needed to be done was to draw on the fund; no taxing *power* would be required. On the basis of this famous man's statement, what is being paid into the social security fund now is not what is going to be drawn out in the future. He did not explain what was happening to what was being paid in now. His statement was really a strong one, that there is *nothing* behind social security than the *future* taxing *power* — that is, the future coercion — of the government of the United States.

The foregoing makes clear that one man with a lucid mind did not consider social security to be funded in a real sense, and he indicated that all the belief that we are "saving" to supply funds for us to draw out in the future is self-deception. If an informed man makes a statement as we have quoted, then it should be worth the trouble to analyze thoroughly how social security in the United States really operates.

Types Of Old Age Security

In *Alice In Wonderland* the expression is used, *Things are not what they seem.* In economics, and in life generally, the same is true, things often are indeed not what they seem, because although *first* consequences of an action are easily observed, that is not true of the *ultimate* consequences. Economics can be described as the sciences of *final* (or even more accurately, *total*) consequences of an action of some sort. Economics laboriously traces the *chain* of consequences, and does not stop with the first link. Looking at the first link only often results in self-deception.

Social security is looked upon by many people as a system by which their employer and they set money aside up to the time they become 65 years of age, and then the money is paid back to the employees, and they have "security" in their old age. They presumably deny themselves something now (or the law requires it), and later they enjoy the fruits of their self-denial. It seems as simple as that. Nevertheless there is much more to the operation than appears on the surface, and it is these nonobvious phases of social security which we shall be exploring.

First, the question should be asked, who pays for social security? The *obvious* answer is — the employee one-half and the employer one-half. This impression is created by the fact that the employee suffers a deduction from his pay for one-half the monthly payment. The law reads that the other one-half is paid by the employer. As far as *accounting* is concerned that is true, but as far as *reality* is concerned, it is a fiction.

The employer pays nothing of social security, after the system has become regularly established. That a relatively few employers in a country would be paying one-half of the support in old age provided for the millions under social security is fantastic merely as an idea. What happens then? The employers — *of necessity* — pass the cost of their one-half of social security back (1) either to the employee, so that he really pays all; or (2) to the consumer, in the form of higher prices, which means that John Public is paying for that part of social security.

There is ever a great game of self-deception being played throughout the world — the game of trying to get something for nothing — something for yourself at the expense of the other fellow. And the game is at times partially successful, especially when the scheme devised is new and sudden in its application. But eventually experience (if not intelligence) results in people "adjusting" effectively so that they are not being victimized by others.

In regard to the real payment for social security, the employer is only an agent. He is like the paymaster of a corporation: he pays out a great amount of money, but it is not the paymaster's own money. The same is true of the social security reputedly paid by the employer; actually he is an agent either for the employee or the consumer. If for the employee, then it means that the employee would otherwise have received in the form of cash pay what the employer deducts to help pay for social security. If for the customer, then the employer is merely passing on to the social security fund an increase in the price of products equivalent to the amount that he is putting into the so-called old age fund.

I. Old Age Security by Saving in Kind

In order to explain an important phase of old age security we shall begin with the oldest and most fundamental kind of security attempted by men, namely, *savings in kind.*

In his old age, when he cannot work any more, a man will need food, clothing, shelter, etc. The first thing he can consider doing is to "save" in the form of nonperishable food, clothing, and shelter. That is the most primitive way of "saving in kind", or having what is now called "old age security." It may sound strange to pose the problem in that way, because few think in those terms. Nevertheless, this is one inescapable aspect of the reality of what takes place in a system of taking care of a man and his wife in their old age when they can no longer work for food, clothing and shelter.

This type of saving, or this way of obtaining *security,* is obviously the *only* way in an isolated situation. If there are no others than one man and his wife, they will surely die of hunger when they can no longer produce food because of feebleness in old age, unless they have saved for that situation a store of nonperishable supplies. It is either saving in kind, or else starvation or death from exposure.

Saving in kind must be performed by either a man himself, or by society in some manner for him. No clever device can save men from the problem of saving in kind. Unless this problem of "saving in kind" is candidly faced — in one way or another — no subsequent thinking on social security, whether simple or complex, will be realistic.

Savings in kind constitutes a *funded* plan.

II. Old Age Security Via Charity

But a man and his wife, both approaching feeble old age, may obtain security via *charity* — in the broad sense that their children or friends or society generally will support them. This means that the old people will be living off the easy surplus of the younger people or, if there is no easy surplus, they will be living off the hardship of the younger people. But in either event, the problem has been solved by *charity*. Only in very well ordered societies, where children *willingly* assist aged parents when they need it, is charity an acceptable solution. Charity may be a communist and also a religious ideal, but it is indicated in Scripture that *charity* is often a bitter solution *for the recipient*. When was residence in a poor house or on a county farm a dignified honor? When kept within family ties, charity as solution of old age security problems is tolerable; but no more. Outside of family ties, charity involves loss of position for the recipient, and dishonor — except (as said before) when the person is a victim because of a providential event beyond his foresight or control.

Charity is an *unfunded* plan.

III. Old Age Security By Contract

Neither saving in kind (*by a man himself*) nor charity having been found a satisfactory solution to the old age security problem, we come to a third type of solution, namely, by contract.

In this situation we shall consider three men: (1) Mortal, who wishes to provide for his own and his wife's old age; (2) Vestor, a young man, who is one of the two men to whom Mortal looks as being a potential source of food, clothing and shelter in his old age; and (3) Promise, the other young man, whom Mortal is also considering as a potential source of supplies in his old age. The problem for which a solution is being sought is: how does Mortal *insure his own security* in old age, when he in actual practice is unable to make adequate savings in kind.

It is at this point that Vestor and Promise come in for consideration. Mortal has a plan which he proposes to them. He wishes to discuss the problem with them to discover who will offer him the more favorable proposition.

Let us assume Mortal is now forty years old and Vestor and Promise both twenty years old. Mortal proposes to them that he will help them either to get more schooling, or will loan them money to build houses, or will finance their buying of equipment, and many other things — provided they will, after 25 years, when Mortal will be 65, thereafter supply him with a certain quantity of food, clothing and shelter. To simplify this, he puts his proposition in terms of money. He will pay them so much a month for the next 25 years. They will use the money temporarily, but they will eventually reimburse Mortal in the form of a monthly pension, which is calculated on the basis of paying back to Mortal all that he paid in, plus compound interest on the payments. (This interest factor is a complication which is not vital to our illustration and will hereafter be ignored.)

What Mortal is here doing is suggesting a contract consisting of turning over either to Vestor or Promise what might be called *present goods* (that is, for the next 25 years) in the expectation of getting back *future goods* (beginning only after 25 years). The contract involves an act of trust, namely, that Vestor (or Promise, whoever is selected) will honor the contract, namely, pay back what was paid him. In this *contract*, the risk is with Mortal. He pays money to the other man for 25 long years; in all that time he will get nothing back. Only in the 26th year and thereafter will Vestor or Promise have to perform their part of the bargain.

Getting back to *goods* rather than money, for the moment, this is what really must happen: Mortal helps support Vestor or Promise with goods (while he, Mortal, is in his high productive years and Vestor and Promise are struggling along), on condition that later when they are in their prime and have a good start they will then support him.

The proposed transaction, although a risky one for Mortal, has what is known in business as *mutuality;* it is good for both parties if the contract is honorably kept, and therefore it should be worth considering.

The probabilities are that Vestor and Promise will both be favorably disposed. They think of their present urgent need for help to get started on their careers. The amount which they must begin to pay after 25 years looks rather small to them because of the distance in time. Men are naturally optimistic. They may sensitively recoil from a commitment which must be paid next month, but they do not recoil fearfully from making a commitment to make payments far in the future. The present good means more to them than the future liability. Mortal, therefore, is in a position to choose with whom he wishes to make the contract, either with Vestor or Promise.

Now it happens that Vestor and Promise are men of different types. Promise is a man who enjoys living well. On investigation Mortal finds that Promise proposes to "save" nothing of what he (Mortal) will pay to Promise for 25 years. If he makes a contract with Promise, then all he will finally have as surety for payment is Promise's promise. Promise will not have any assets which he can sell when Mortal's pension is due, nor will Promise have any equipment in which he has invested, in order to increase his productivity so that it will be easy for him to pay Mortal his pension. In banking terms, Promise will have no *collateral* behind his commitment or note; his promise to pay is what bankers call *unsecured.* It is only as good as Promise's honor and future ability. That means that Promise, who will have been living well for 25 years partly on what Mortal paid him, will then have to live less well because instead of his income being his own earnings *plus* what Mortal paid him, his income then will be his own earnings, *minus* what he must pay Mortal as his pension. Two things disturb Mortal; he knows, if he deals with Promise that he (Mortal) will have no security behind his pension, and he knows Promise will be worse off when he must pay Mortal than he (Promise) has been for many years. Surely, dealing with Promise cannot appear to Mortal to be a good contract for him. A contract with Promise is, in pension terms, an unfunded plan.

Mortal turns to Vestor and considers him. Vestor is a different type; he is living below his income. He is saving money. He is buying property. He is acquiring machinery. He is expanding. But he is short of money, and is anxious to make a deal with Mortal. If Mortal pays him (Vestor) money now, Vestor is prepared to pay back later because he will have more machinery (and other property) working for him 25 years hence, and paying Mortal his pension then will be easy. In this instance, Mortal will be obtaining from Vestor two things; Vestor's promise *plus* the security of Vestor's assets and higher earnings because of his assets. Vestor's promise will be "secured" by his collateral, that is, assets which he possesses. A contract with Vestor is, in pension terms, a funded plan.

A man of good judgment, under the circumstances assumed, would not make a pension deal with Promise. Mortal will, therefore, probably turn to Vestor and make a deal with him. It gets down to this: Mortal helps Vestor by making payments to him. Vestor wisely *invests* those funds; he does not *spend* them for perishables. The investments he makes have a long life, and produce earnings for Vestor for many years, including those years when Mortal must be repaid.

Before the days of social security in the United States most "pension funds" were of the kind described in the deal of Mortal with Vestor — a secured, collateralized deal.

The program of Vestor cannot exactly be called "savings in kind." But in principle it is. He *invested* the money in *real* capital, factories, equipment, tools, etc. Such capital will gradually wear out, but while in the process of doing so, will "throw off" a larger quantity of products than would otherwise be available of consumers goods — food, clothing and shelter. What Vestor did was put Mortal's payments into what might be called *intermediate goods* — capital — which were, in a sense, not yet fully "savings in kind," that is, "savings in kind" which were in the process of "maturing" into consumers' goods which Mortal could genuinely consume, progressively as the years rolled along after he reached the age of 65.

IV. Old Age Security Via Compulsion

Let us introduce a few more people into our illustration, named Weeks, Sapp and Chain. They are not one generation behind Mortal but two generations. These three men are twenty years old when Mortal is 65, and Vestor and Promise are 45.

Let us assume that Mortal unwisely made an unfunded deal with Promise and not with Vestor. Further let us assume that although Promise has *invested* none of the money paid to him by Mortal, but has spent it in his daily living, nevertheless he (Promise) is a forceful person — he can bully the three young men, Weeks, Sapp and Chain effectively so that he can extract from them enough to pay Mortal his pension. Suppose, to make the point comparable to reality, that it happens that Promise is the mayor of the community in which the men live, and he taxes or assesses them enough so that he can pay Mortal the pension due him. This is, obviously, a case of "robbing Peter to pay Paul," but Weeks, Sapp and Chain may be comforted by the thought that a generation later they will be 45 years old and will be in a position of power, and then they will do the same thing to the next batch of 20-year-olds. This scheme, although one of compulsion and extortion, can be made to work, if Weeks, Sapp and Chain are stupid or weak.

Mortal, from his viewpoint, *appears* to have done as well by his "foolish" deal with Promise, as he might have done by his wise deal with Vestor. He received his pension money, did he not? What more does he want or care? In fact, why should not each series of pensioners as they come up to their pension age say to themselves: "We were subjected to extortion to pay the pension of the previous oldsters, but now it is our turn to take advantage of the generation coming up behind us, as the previous generation took advantage of us."

The transaction described can still be viewed as a contract. Instead of savings in kind by Mortal himself, a contract was made by him with a spendthrift who made no savings in kind in the form of investments or any form, but who had extortion power, when the time of payment had arrived, and who extracted from the weak or the deceived enough to pay Mortal's pension.

Such are the four ways in which old age security can be obtained: (1) simple savings in kind; (2) charity; (3) a funded contract involving an indirect savings in kind (the contract with Vestor, who accumulated *capital* by wise use of the prepayments by Mortal); and (4) an unfunded contract involving no savings in kind but supplementing the lack thereof by eventual extortion from third parties; or if not extortion, then by fraud; and if not by fraud, at least by taking advantage of the weakness or stupidity of third parties (usually younger people).

Of the four types two involve genuine *saving* or *investment* (funding), cases (1) and (3). And two involve no genuine saving nor investment (funding), cases (2) and (4). The latter two have one thing in common — the younger generation supports the older generation, but with this difference, it is charity in the first case, and compulsion in the second.

But if either method (1) or (3) is used then the older generation is not a burden on the younger, because the plan has been *genuinely* funded, the savings in kind do exist, or because something equivalent to savings in kind and better in fact than savings in kind, namely, real capital genuinely exists.

One important question is: what is the nature of the *capital* which Vestor accumulated?

Further, what happens under social security in the United States? Is the money paid into Social Security *spent* or *invested?* Is our social security *really secured by real savings in kind or its equivalent in the form of capital,* or is there nothing behind our social security except a promise, enforceable only by extortion? Is the agency to whom we paid social security taxes squandering the money as Promise did in our illustration? Is there in fact "Nothing behind Social Security in the United States except the future taxing power of the government"? Has Social Security in the United States followed the Vestor or the Promise pattern?

First, let us consider what the nature of *capital* is.

Bohm-Bawerk On Certain Aspects Of Capital

In an earlier issue (Volume III, pages 275-285) we quoted from Eugen von Böhm-Bawerk's *Capital and Interest* under our title of "What is the Character of Capital, Something Which God Did Not Create."

The purpose of that quotation was to show that *capital* is something which the first man did not have, but which he direly needed. The consequences inescapably were that the first man was *very* poor, and lived on the perilous edge of survival. Adam, *as Moses plainly indicates*, was destitute in the semi-swamp lands of the delta of the Euphrates — without clothes, without a sure food supply, without any shelter — surviving not by husbandry which was at the time probably above him but as a wandering berrypicker; without soap, sanitary facilities, scissors or a comb. (The contrary representations in children's Bible books are misleading.)

The reason why Adam was destitute was because he did not have any *capital.* In his case and in the case of all his descendants, the standard of living does not depend on natural resources, (which are not capital, in the correct sense), but on the development of capital by men. Where the amount of *capital per capita* is high — as in the United States — the standard of living is high; and vice versa, where the amount of *capital per capita* is low — as in Africa — the standard of living is low. This fundamental idea should not be ignored because, if it is, subsequent economic thinking will be erroneous.

Our interest in capital at this time is for a special reason, to wit, how can *capital* function as *saving in kind,* or as a substitute therefore, so that a man *can* have *security* — has a real fund to draw on in the old age. If comprehensive *saving in kind* is not feasible in the form of the twenty-year supply of nonperishable foodstuffs, and an equivalent amount of underwear, suits and dresses — and it is certainly *not* feasible — then is there no equivalent of real *savings in kind* possible — and consequently is there nothing *real* behind any old age security except either charity or coercion?

We here quote from Böhm-Bawerk's *Capital and Interest,* Volume II, with the sub-title, *The Positive Theory of Capital.*

When in what follows we quote extracts from this book, such extracts cannot be more than fragmentary. (The word *capital* has been defined in many ways by many people so that it is impossible to cover the subject adequately by short quotations. Because of the brevity of such quotations there is also danger of considerable loss of clarity.)

First we quote what Böhm-Bawerk in turn quoted from Turgot, the French economist (page 19):

> "Whoever acquires each year more goods than he finds it necessary to consume, can lay aside the excess and accumulate it. *It is these accumulated goods that are called capital . . .*"

Turgot's definition points to finished consumers' goods — genuine *savings in kind.* This simple definition is not adequate.

Böhm-Bawerk himself, for reasons which were decisive, defines capital *in general,* and then in two subdivisions, *social capital,* and *private or acquisitive capital.* He wrote (page 32):

> Let us call capital, in general, an aggregate of *products which serve as a means of acquiring goods.*

That is his *general* definition; it excludes surplus finished goods *in the consumers' hands,* like the goods Mortal (theoretically) might have stored up in his warehouse for twenty-five years from his 40th to his 65th birthday, and then consumed between his 65th and 85th birthday. Such a "hoard" of finished goods in Mortal's possession was not "products which serve as a *means of acquiring goods.*" Mortal's stock will be only a static hoard.

The fact is that there will *never* be a high standard of living if savings consist *only* in hoarding whatever surplus there is in the form of finished goods in consumers' hands. The storage and "keeping" problem is too great. Further, the hoard is only a *surplus;* it is not *an aid to increased production* which is what capital should ideally be.

Next, Böhm-Bawerk defines the subdivision of capital which he calls *social capital* as follows (page 32):

> Within this general concept [just quoted] let us set apart a narrower concept of *social capital.* We may define social capital as an aggregate of products which serve as a means of the acquisition of economic goods by society. Or, since such social acquisition of goods is possible only through production, we may call it an aggregate of products intended to be used for further production. . . . Let us cut it short and say an *aggregate of intermediate products.*

If Mortal is to have "*physical* security" in his old age in the form of real goods, then he needs for that a supply of what Böhm-Bawerk calls "intermediate products." These are products in the process of "maturing" into finished goods; every day, month and year, some will be coming to "maturity." In the meanwhile they are "intermediate products." It is also important that they do not all "mature" at the same time, but in steady sequence.

Later, on page 70, Böhm-Bawerk lists the items in *social capital* as follows:

> Social capital, as an aggregate of products intended to serve for further production, comprises the following.
>
> Productive improvements, adaptations and installations affecting real property insofar as they preserve independent character. This means such things as dams, pipe lines, fences, and the like. On the other hand productive installations that become completely identified

with land are to be excluded from capital for the same reasons that impelled us to eliminate land itself from capital.

Productive buildings of every kind — workshops, factories, barns, stables, shops, streets, railroads, etc. But social capital does not include dwellings or any other buildings which serve directly any cultural or consumption purpose, such as schools, churches, and courthouses.

Tools, machines and other productive implements.

Work animals and beasts of burden used in production.

Raw materials and auxiliary supplies used in production.

Consumption goods that are stored or kept "in stock" by producers and merchants.

Money.

We shall dispense with his elaboration and explanation of this.

Böhm-Bawerk excludes from capital the two *primary* sources of production — *nature* and *labor* of man. They are *not* social capital in any sound sense. Unimproved land is to be excluded for obvious reasons; it is always *there*. It is not saved; nor increased in quantity. Bare land means little unless cultivated. And so the bare land is not something being added, and therefore is "security" for Mortal in his old age. If bare land constitutes old age security, then Adam had the greatest security of any man who has ever lived — the whole world practically. Mere natural resources do not establish or constitute a genuinely *funded* plan.

The emphasis of Böhm-Bawerk is on "intermediate goods," which are in all stages of approaching a finished state and moving steadily in that direction. These "intermediate goods" were not created by God, nor are they pure labor; they are a combination of nature and labor, or better said, of nature "altered" by labor, so that "nature" is more useful when in the form of capital.

Now, what can happen? Mortal can reduce his consumption and save between his 40th and 65th year, and use what is saved to "support" either Vestor or Promise, whomever he selects, and that will permit these younger men, by being relieved of producing all the *consumers goods* they then need, to work at producing *capital*, for example, an engine that will save a lot of labor and last maybe for 25 years. That engine will permit greatly increased production; one engine may do the work of a hundred men.

But gradually the engine will wear out, while it works. In a figurative sense, daily fractions of the engine are transformed into the product it produces, ounce by ounce, and piece by piece, as fast as the engine depreciates. Clearly, in this kind of a situation Mortal's *saving* (what he sets aside to pay Vestor or Promise) is something that is better than very perishable food, clothing or shelter, although this capital is also perishable (maturing); but it is perishing rather *slowly*. Further, when Vestor or Promise pay back to Mortal what he put in earlier, then they are paying back, out of the proceeds of a piece of capital, which would not be in existence if (1) Mortal had not *saved* and (2) helped support them while they were building the engine (investing).

Or more accurately, in our assumptions, Vestor only would have used the support he received from Mortal to invest in *capital,* of longish life and productive. Promise, according to our assumptions, would merely have lived as much better, as Mortal was living less well. Between Mortal and Promise that would be merely a transfer of consumption; Mortal consumed less so that Promise could consume more, in the expectation that the roles would later be reversed and that then Mortal would consume more and Promise less. Contrarily, in the transaction between Mortal and Vestor, Vestor did not consume more, but *invested in capital.* That capital was in a sense a *savings in kind,* but savings in the early stages, and savings which would gradually mature, at a rate depending on the length of life of the kind of capital in which it was invested.

How shall we visualize this maturing as taking place? We quote Böhm-Bawerk, page 105ff:

> Let us imagine a community of 10 million able-bodied workers. Its annual allotment of productive forces therefore amounts to 10 million labor-years. In order to present the problem without presenting unnecessarily complicated figures, I shall ignore the currently available uses of land. Its hitherto accumulated stock of capital we shall assume to represent the fruits of 30 million labor-years (plus, of course, the corresponding quantity of uses of land), which during prior economic years have been invested in intermediate products. Let us examine the structure of this stock of capital more closely.
>
> Every capital is by nature composed of a mass of intermediate products, all of which have as their common goal, to mature into means of enjoyment, that is to say, into consumption goods. They reach that goal through a continuation of the production process in the course of which they themselves come into existence. They are all, as it were en route to the destination of maturity for consumption. But the roads that lead them there will vary. That is in part due to the circumstance that different areas of production have circuitous paths of production which vary in length. Mining or railroad building goes a far more circuitous road than wood carving. But it is also due in part to the fact that the goods which comprise at a given moment the total amount of the community's capital are located at very different points along the respective production roads. Some intermediate products have just set out upon a very long roundabout path such as, for instance, a boring machine that is destined

to dig a mine shaft. Others are midway to the goal and still others are close to the terminus of the "long trail" of producton they must cover, such as bolts of cloth which are about to be made up into suits and overcoats. The inventory of capital constitutes, so to speak, a cross section of the many processes of production which are of varying length and which began at different times. It therefore cuts across them at very widely differing stages of development. We might compare it to the census which is a cross section through the paths of human life and which encounters and which arrests the individual members of society at widely varying ages and stages.

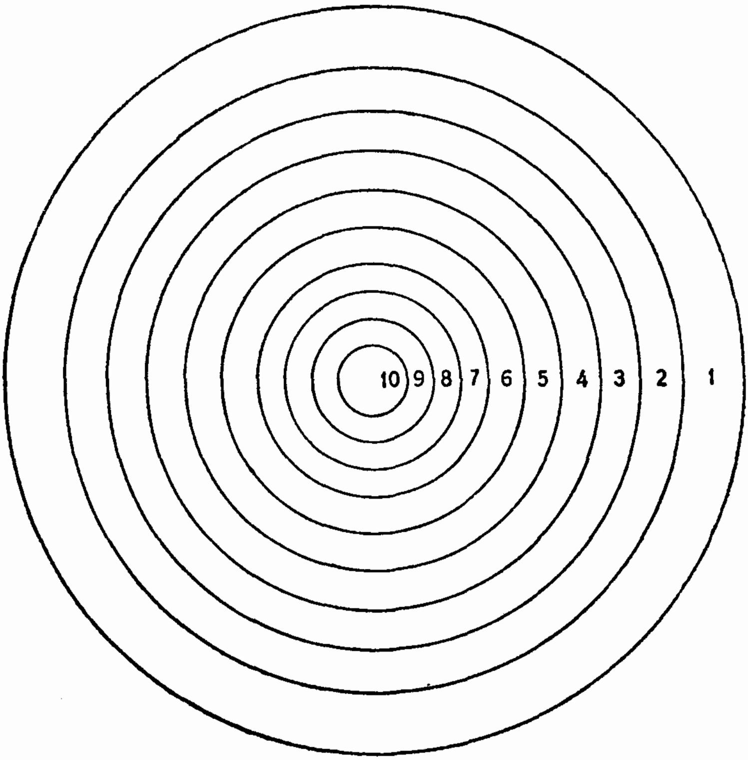

FIGURE 1.

With respect to the varying remoteness from readiness for consumption, the composite mass of capital adapts itself to a highly appropriate scheme of presentation as a number of concentric annual rings each representing a yearly class, or what might be termed a "maturity class." The outermost annual ring *(see Fig. 1)* embraces those parts of the capital which will become finished consumption goods within the following year, the second outermost ring represents the capitals which will mature into consumption goods in the second year and so on. In a community where capitalist production is not yet strongly developed, the inner rings will shrink in rapidly progressive proportion *(see Fig. 2)*. This is because in such a community lengthly circuitous processes of production, which come to fruition only after a period of many years, are rarely and sparingly adopted. In rich and well-developed economies, on the other hand, a considerable number of well-developed circles can be distinguished, and of these the inner rings will have an area or content that is relatively smaller, to be sure, but by no means inconsiderable.

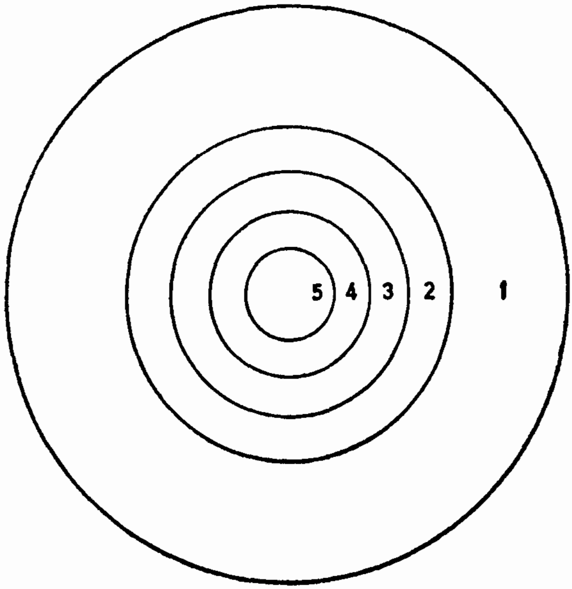

FIGURE 2.

Representation of the maturity classes by concentric circles is particularly appropriate because that picture provides a felicitous method of helping us to visualize the relative magnitudes of those classes. The outermost of the concentric rings has the greatest area, and the areas of the succeeding rings diminish gradually. In exactly the same way the greatest proportion of the total capital of a community will at all times consist of the first maturity class, the goods that are at a point in the production process closest to completion. Similarly, the increasingly remote maturity classes will represent a progressively diminishing proportion of the community's capital. There are two reasons for this. The first is that in the various areas of production roundabout methods of production are adopted which vary in length by reason of their varying technical nature. In some, the entire production process from the initial preparatory operations to the production of the final product ready for consumption, is completed within the course of a single year. In others, two, three or five years are required; in only a few do production periods measure 10, 20, and 30 years. As a result, the highest maturity classes (those most remote from maturity) draw their membership from only a few areas of production. Intermediate products in a stage, let us say, that assigns them to the tenth maturity class can come only from areas of production where the production period lasts at least 10 years. The lower maturity classes *do* draw their membership from these last-mentioned areas of production (since the intermediate products must pass successively through the classes closer to maturation); but they also draw from the areas of production where the duration of the production period is shorter. Thus the quantity of intermediate products becomes greater as progress is made toward the first maturity class. In that class every area of production, without exception, is represented. But a second circumstance works in the same direction. The maturation of intermediate products into consumption goods necessitates a constant addition of current productive forces. At each stage of the production process new labor is added to the intermediate products handed on from the preceding stage and they are then in turn delivered over to the succeeding stage. At one stage, the intermediate product wool is transformed by the addition of labor into yarn; in a later stage labor is again added to transform it into the intermediate product cloth, and so on. The natural consequence is that within each production area the amount of capital invested increases with every forward step to a succeeding stage of production, that is to say, with every forward step to a lower maturity class. For that reason the lower maturity classes do not only comprise representatives from more numerous areas of production, as set forth in the preceding paragraph, but the membership has fattened on relatively larger amounts of capital. That makes the lower classes exceed the upper classes in two respects — their membership is more numerous and also more weighty, with the first class taking complete precedence.

Let us now set down in figures these relations which are present in our example. In order to make the situation easier to grasp at a glance I shall assume that the total amount of capital in our community is composed of only 10 annual rings. If that total capital embodies labor-years in the amount of 30 millions (again ignoring the invested uses of land, for the sake of simplicity) then we can assume some such distribution of the maturity classes as follows:

Maturity Class No.	Contains intermediate products embodying labor years to the number of
1	6 million
2	5 "
3	4 "
4	3.5 "
5	3 "
6	2.5 "
7	2 "
8	1.7 "
9	1.3 "
10	1 "

Each year, in the normal course of events, the outermost annual ring is completely severed from the total amount of capital, and is converted into consumption goods which serve to satisfy the wants of the community. Each of the inner rings receives the addition of new labor, and this both advances it one stage in the production process, and also increases its mass; as a result each ring advances to the next succeeding maturity class. Thus the first class becomes consumption goods, the second becomes the first class, the third becomes the second, and so on.

Mises On The Significance Of Capital

In October 1952, Professor Ludwig von Mises gave an address at the University Club of Milwaukee which he entitled *Capital Supply and American Prosperity.* His theme is fundamental: *Prosperity is dependent on the supply of real capital.* Governments do not create prosperity; unions do not create prosperity; social security does not create prosperity. Adam, the first man, was not poor because a government did not help him, nor because he was not a member of a union, nor because he had no social security; *he was poor because he had no real capital.*

Mises began his speech as follows:

> One of the amazing phenomena of the present election campaign is the way in which speakers and writers refer to the state of business and to the economic condition of the nation. They praise the Administration for the prosperity and for the high standard of living of the average citizen. "You never had it so good" they say, and "Don't let them take it away." It is implied that the increase in the quantity and the improvement in the quality of products available for consumption are achievements of a paternal government. The incomes of the individual citizens are viewed as handouts graciously bestowed upon them by a benevolent bureaucracy. The American Government is considered as better than that of Italy or of India because it passes into the hands of the citizens more and better products than they do.
>
> It is hardly possible to misrepresent in a more thorough way the fundamental facts of economics. The average standard of living is in this country higher than in any other country of the world not because the American statesmen and politicians are superior to the foreign statesmen and politicians, but because the per-head quota of capital invested is in America higher than in other

countries. Average output per man-hour is in this country higher than in other countries, whether England or India, because the American plants are equipped with more efficient tools and machines. Capital is more plentiful in America than it is in other countries because up to now the institutions and laws of the United States put fewer obstacles in the way of big-scale capital accumulation than those foreign countries did.

It is not true that the economic backwardness of foreign countries is to be imputed to technological ignorance on the part of their peoples. Modern technology is by and large no esoteric doctrine. It is taught at many technological universities in this country as well as abroad. It is described in many excellent textbooks and articles of scientific magazines. Hundreds of aliens are every year graduated from American technological institutes. There are in every part of the earth many experts perfectly conversant with the most recent developments of industrial technique. It is not a lack of the "know how" that prevents foreign countries from fully adopting American methods of manufacturing, but the insufficiency of capital available.

* * *

As it was forty years ago, the world is divided into two camps. There is, on the one hand, the capitalist orbit, considerably shrunk when compared with its size in 1914. It includes today the United States and Canada and some of the small nations of Western Europe. The much greater part of the earth's population lives in countries strictly rejecting the methods of private property, initiative and enterprise. These countries are either stagnating or faced with a progressive deterioration of their economic conditions.

Let us illustrate this difference by contrasting as typical of each of the two groups conditions in this country and those in India.

In the United States capitalist big business almost every year supplies the masses with some novelties; either improved articles to replace similar articles used long since or things which had been altogether unknown before. The latter — as for instance, television sets or nylon hosiery — are commonly called luxuries as people previously lived rather contented and happy without them. The average common man enjoys a standard of living which, only fifty years ago, his parents or grandparents would have considered as fabulous. His home is equipped with gadgets and facilities which the well-to-do of earlier ages would have envied. His wife and his daughters dress elegantly and apply cosmetics. His children, well fed and cared for, have the benefit of a high school education, many also of a college education. If one observes him and his family on their week-end outings, one must admit that he looks prosperous.

* * *

Now let us look at India. Nature has endowed its territory with valuable resources, perhaps more richly than the soil of the United States. On the other hand climatic conditions make it possible for man to subsist on a lighter diet and to do without many things which in the rough winter of the greater part of the United States are indispensable. Nonetheless the masses of India are on the verge of starvation, shabbily dressed, crammed into primitive huts, dirty, illiterate. From year to year things are getting worse. For population figures are increasing while the total amount of capital invested does not increase or, even more likely, decreases. At any rate, there is a progressive drop in the per-head quota of capital invested.

In the middle of the eighteenth century conditions in England were hardly more propitious than they are today in India. The traditional system of production was not fit to provide for the needs of an increasing population. The number of people for whom there was no room left in the rigid system of paternalism and government tutelage of business grew rapidly. Although at that time England's population was not much more than 15 per cent of what it is today, there were several millions of destitute poor. Neither the ruling aristocracy nor these paupers themselves had any idea about what could be done to improve the material conditions of the masses.

The great change that within a few decades made England the world's wealthiest and most powerful nation was prepared for by a small group of philosophers and economists. They demolished entirely the pseudo-philosophy that hitherto had been instrumental in shaping the economic policies of the nations. They exploded the old fables: that it is unfair and unjust to outdo a competitor by producing better and cheaper goods; that it is iniquitous to deviate from traditional methods of production; that labor-saving machines bring about unemployment and are therefore an evil; that it is one of the tasks of civil government to prevent efficient businessmen from getting rich and to protect the less efficient against the competition of the more efficient; that to restrict the freedom and the initiative of entrepreneurs by government compulsion or by coercion on the part of other powers is an appropriate means to promote a nation's well-being. In short: these authors expounded the doctrine of free trade and laissez faire. They paved the way for a policy that no longer obstructed the businessmen's effort to improve and to expand his operations.

* * *

Let us look again at India. India lacks capital because it never adopted the pro-capitalist philosophy of the West and therefore did not remove the traditional institutional obstacles to free enterprise and big-scale capital accumulation. Capitalism came to India as an alien imported ideology that never took root in the minds of the people. Foreign, mostly British, capital built railroads and factories. The natives looked askance not only upon the activities of the alien capitalists but no less upon those of their countrymen who cooperated in the capitalist ventures. Today the situation is this: Thanks to new methods of therapeutics, developed by the capitalist nations and imported to India by the British, the average length of life has been prolonged and the population is rapidly increasing. As the foreign capitalists have either already been virtually expropriated or have to face expropriation in the near future, there can no longer be any question of new investment of foreign capital. On the other hand the accumulation of domestic capital is prevented by the manifest hostility of the government apparatus and the ruling party.

The Indian Government talks a lot about industrialization. But what it really has in mind is nationalization of already existing privately owned industries. For the sake of argument we may neglect referring to the fact that this will probably result in a progressive decumulation of the capital invested in these industries as was the case in most of the countries that have experimented with nationalization. At any rate nationalization as such does not add anything to the already prevailing extent of investment. Mr. Nehru admits that his Government does not have the capital required for the establishment of new state-owned industries or for the expansion of such industries already existing. Thus, he solemnly declares, that his Government will give to private industries "encouragement in every way." And he explains in what this encouragement will consist: we will promise them, he says, "that we would not touch them for at least ten years, maybe more." He adds: "We do not know when we shall nationalize them." But the businessmen know very well that new investments will be nationalized as soon as they begin to yield returns.

We shall next consider the profound significance of this for social security.

How Evaluate Social Security In The United States?

Having simplified the explanation of what "goes on" in a scheme called old age security, it is now possible to describe what occurs under Social Security in the United States and how to evaluate it. The four possibilities are:

1. That the present system arranges for savings in kind.
2. That it is a charity scheme, with a new name.

3. That it is a contract with a thrifty man, an accumulator of capital, a "funder," who by his accumulation of capital protects the sums paid in, and also increases production; or

4. That it is a contract with a spendthrift, who is not an accumulator of capital and who by not accumulating capital is not "securing" his promises by real collateral. Under this fourth category there are two sub-possibilities:

(a) The debtor will be unable to pay social security, and will default simply because he has no assets; or,
(b) The debtor may meet his obligations by extorting payments from new arrivals on the scene (young people). These may be lulled into confidence that all is well, by the promise that 45 years hence they will then be the fortunate recipients.

The unfeasibility of *savings in kind* for the benefit of future pensioners has already been made apparent, although by its farm program the United States is accumulating surpluses of foodstuffs (a "savings in kind"). However, the accumulation is unrelated to social security as such. *Savings in kind* can be removed from serious consideration.

Secondly, social security in the United States has some charity aspects, which we shall present at some other time. But United States social security is not intended to be a charity scheme. The beneficiaries are supposed (in the aggregate) to take out no more (in the aggregate) than they put in. Actuaries have made computations to show how input and output balance, or can be made to balance.

The system therefore must be a contract, and the contract is either with a thrifty trustee or with a spendthrift. The trustee in this case is the Government of the United States. Is it, as trustee, thrifty or spendthrifty? Is the government of the United States a Mr. Vestor? or is it a Mr. Promise?

Everybody knows the answer: the United States is a Mr. Promise, spending not only its whole income, but, in the post war years, on the average, spending more than its intake. Some of the expenditures of the United States eventually go into capital assets of a sort, such as housing projects or a Tennessee Valley Authority. But that is only a part of the total. It is not feasible to consider here how much or how little of government funds go into *real* assets, and how much of this is *capital* and how much is not. But the percentage that is not capital, and most of it is not, indicates that to that extent social security is not *really* funded.

What is the United States putting into the vaults to protect its Old Age pension hopefuls? Pieces of paper. These sound important because they are called *bonds*. But that name does not make them more than pieces of paper. *Real* prosperity will *never* be based on such pieces of paper.

Promise, when collecting money from Mortal, could do the same thing, and in order to keep the bookkeeping straight would surely do so. Upon receipt of every payment made by Mortal, Promise would do two things: (1) spend the money; and (2) slip into the vault in its stead his promissory note: "Forty years from now I promise to pay to Mortal a sum of .... dollars with interest at .... percent, for value received." But Mortal, if alert, would realize that that promissory note is probably worthless. What is the promissory note of any spendthrift worth? When private persons are involved in a situation of this kind, the solution is bankruptcy of the debtor, and a default in payment.

But that is not what will happen in this case. There need be no fear that the United States government will default. It will certainly pay in one of two ways: (1) it will slip in more and more new bonds by running the printing presses; (a private individual may not do that); or (2) it will increase taxes on the workers (the younger people). The oldsters will undoubtedly get their pension money. Peter will be robbed to pay Paul.

And so it is approximately correct what the international banker said, whom we have quoted earlier in this issue, to wit: *There is nothing behind social security in the United States than the future taxing power of the government.*

It seems that *power* — the power of the government to tax — can make a bad contract a good one; that is, admitting that it would be bad for an individual (as Promise) to act as the United States government is acting, those bad consequences can be and are annulled when the United States government can exercise its *power*. But this is a hallucination.

100 Percent Social Security (A Spurious Seventh Heaven)

If social security, as operating in the United States is an admirable scheme, why not extend it? No, not extend it by 10% or 50% or 100% above what it is now — but extend it so that *it constitutes the whole savings scheme of the American people for their old age.*

Further, let us assume the government will continue to spend what it takes in, probably for all kinds of enlarged welfare schemes *involving current consumption.*

Would such a system not be a seventh heaven of old age happiness — protected as it would be by billions on billions of government bonds — pieces of paper? No, because, unfortunately, *no real capital* would then be provided for any more.

Where would the United States be, after say 50 years of such complete and perfect social security? It would approximate the conditions today in India. Consider again what we quoted from the Mises speech.

Pieces of paper in the form of bonds may assist in *redistributing* income but it does not help in *producing* income. Under 100% social security the redistribution would be perfect and might endlessly increase in dollars, but *real income* would go down and down until people had reached bare existence levels when the death rate would go up.

In other words, *the more social security of the present kind* that we have in the United States, the lower the real income of *the people of the United States will be.* Further, the less social security we have in the United States under the present plan, the higher the real income of the people of the United States will be. Basically, our so-called social security is a hoax, and will be from a *social viewpoint* until the United States government, as trustee, invests the social security payments in *real* capital.

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FIRST PRINCIPLES
IN MORALITY AND ECONOMICS

on which depend personal well-being and social health and harmony

VOLUME V MARCH, 1959 NUMBER 3

Contents

Which Of These Two Principles Is Christian?

"Everyone is really responsible to all men for all men and for everything."
— Dostoevski

"The primary and sole foundation of virtue, or of the proper conduct of life, is to seek our own profit."
— Spinoza

Dostoevski and Spinoza disagree irreconcilably. One must be right and the other wrong.

Fëdor M. Dostoevski (1821-1881) was a Russian novelist, author of *Crime and Punishment* and *The Brothers Karamazov.* At the age of 28 he became involved in the communist plots of Petrocheffsky, and spent seven years in the salt mines in Siberia.

Baruch Spinoza (1632-1677) was a Jewish philosopher who lived in the Netherlands, grinding lenses and developing his own pantheistic thought.

Dostoevski's statement sounds noble and fraternal — a perfect definition of what is known to some Christians as *brotherly love.*

Spinoza's statement sounds selfish, unbrotherly and destructive. The number of moralists professing Christianity who will accept Dostoevski's propositions probably outnumber those who will accept Spinoza's propositions.

Whether a man accepts Christianity or not, if he is to have a social philosophy, he must accept either Dostoevski's principles or Spinoza's. A compromise between them may be attempted, but the issue is not really subject to compromise. We are our brothers' keepers, or we are not.

The idea of our being our brother's keeper comes from Cain, the first murderer — of his brother, Abel. When called to account, he brushed off the inquiry with the question, "Am I my brother's keeper?" If this source, circumstance and question constitute valid legislation on the basic relation between men — that they are indeed their brothers' keepers — then there is at least one dubious extension beyond Cain's own question which should be recognized. Cain asked, "Am I my brother's keeper?" He did not ask, "Am I my brothers' keeper?" He referred to only *one* other, his natural brother Abel. He spoke of a singular, not a plural, obligation. He questioned whether he was responsible for *one* other man, not *all* other men. The responsibility becomes more than human if each man is responsible for *all* other men.

An idea about brotherly love similar to Dostoevski's has been developed in recent times by Bishop Anders Nygren of Lund, Sweden. Nygren has defined brotherly love in Dostoevski's vein, and has used one of the Greek words for love, *agape,* which is alleged by Nygren to indicate, in Scripture, how unqualifiedly we should give our fellow men precedence over ourselves. Nygren's idea of love, *agape*, is probably the prevailing one in Christendom today; not in practice, of course, but in doctrine. Because the practice of the doctrine is an impossibility, even though there were no sin in the world, the doctrine is pure sanctimony.

But whether the reader be a Christian or an infidel, which principle does he himself prefer — that of Dostoevski or Spinoza? Let him face the issue squarely, without attempting to evade it.

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It cannot, in fact, be evaded. The kind of social structure men set up is determined by whether they accept the principles of Dostoevski or Spinoza. Before reading further, choose your own principle; act as Shakespeare has one of the suitor's for the hand of Portia (in the play, *The Merchant of Venice*), say: "Here choose I, *joy be the consequence.*"

* * *

Ultimately and primarily, the selection of either the idea of Dostoevski or Spinoza is an *intellectual* rather than a *moral* question.

CAN a man be responsible for *everything, for all men,* and *to all men?* Is that within a finite man's capability? If it is, each man can be held accountable. But if it is not, then it is ridiculous, as well as unjust, to hold each man accountable for everything, to all men, for all men.

To ask the question is to have the answer. Everybody knows that Dostoevski's propositions are *intellectually impossible* to any man. Dostoevski's propositions might apply to an omniscient God, but certainly not to the finite and feeble being known as man. What Dostoevski has formulated cannot be accepted as having any foundation whatever in Christianity, because Christianity teaches that man is not God, but a pitiable creature in many respects.

Spinoza's formulation of the basic law of ethics is closer to the truth than that of Dostoevski. The *basic* part, but not the whole of Christian ethics, is expressed in what Spinoza formulated: "The prime . . . foundation of virtue, or the proper conduct of life, is to seek our own profit." The hiatus marks indicate that we have left out the words "and sole"; that proposition is erroneous. But we have left Spinoza's main proposition stand, because it is the only realistic one. More comprehensively and accurately formulated it might read: "The prime and dominating (but not the whole) foundation of virtue, or the proper conduct of life, is to seek our own profit." Whereas Dostoevski is wholly wrong, Spinoza is mostly right.

For each man to "seek his own profit" is, more or less, within his intellectual capabilities, and consequently is a reasonable proposition.

A man's responsibilities for his fellows decline at least in proportion as his intellectual capabilities to understand the needs of his fellows decline. That decline is precipitous. What fraction one man knows about all the needs of all the men is so small that for practical purposes it is nil. In everyday life men assume the responsibility only for one wife and for their minor children, especially the latter and then only in their minority.

In a *broad* sense, a man is not even "responsible" for his wife. No man is entitled to make *all* decisions for his wife. That is Dostoevski's proposition because, in the last analysis, making all the decisions for another, is what "responsible to all men for all men and for everything" means. What woman would be happy if her husband made *all* the decisions? In the closest bond existing in life Dostoevski's proposition will not work or will create acute unhappiness and discord.

Dostoevski's proposition is "immoral," and Spinoza's proposition is "moral." Dostoevski's proposition inescapably involves coercion of the choices of one man over another, or over those of his wife. Otherwise, his proposition is meaningless or at least hopelessly qualified.

In the Hebrew-Christian Scriptures, any compulsion of the choices of one man over another (except to restrain him from specified evils) is considered to be *coercion*. The Sixth Commandment reads, Thou shalt not kill, which obviously means, Thou shalt not coerce. *Therefore, any imposition of the choices of one man upon another man, and making the first man's choices overpower the latter's, is a violation of the Sixth Commandment.* The reformulation of the statement in the Sixth Commandment in positive form reads as follows, "Blessed are the meek, for they shall inherit the earth" (Matthew 5:5). Meekness (avoidance of coercion) in all matters, *except resistance to evil,* is the quintessence of Christian ethics.

Therefore, on the basis of the Hebrew-Christian Scriptures, *if a man is to avoid coercion,* he must limit himself as Spinoza declared, to the welfare of himself, or "to seek [his] own profit." Only then does he meet two requirements: (1) know what he is doing; and (2) avoid imposing his choices on his neighbor.

The foregoing, consisting in a man minding his own business rather than acting as a busybody interfering into the affairs of others, is the first principle of virtue, because what else is there for a man to do, if he desists from trying to impose his choices on all his neighbors.

By his formulation Spinoza indeed covered two basic ideas: (1) by a man minding his own business he would *leave to his neighbor his own priceless freedom,* and (2) by "seeking his own profit" he would, as one phase of that, defend himself against evils his fellows might endeavor to inflict on him (as coercion, fraud and theft); but these ideas need supplementation. Spinoza over-reached himself when he declared that by minding his own business a man had fulfilled the whole requirement of virtue.

Hebrew-Christian ethics have supplied the necessary supplements. Those important supplements are:

1. The need for a man to show *forbearance,* if a neighbor violates the ethical law against him;

2. The necessity of *charity;* a distinctly *limited* responsibility, and obviously distinguished from being "responsible to all men for all men for everything." There is a deep abyss between Hebrew-Christian charity and Dostoevski's totalitarianism.

3. The requirement to *teach the gospel* — the whole counsel of God — so that a neighbor's thinking and conduct is helped to be as right as possible for life and death, and for this life and a life to come.

These ideas do not qualify, but supplement, what Spinoza wrote. Neither forbearance, nor charity, nor teaching the gospel is *coercion* over another; certainly they are not when conducted according to Biblical requirements of being meek and gentle. And, in a broad sense, these three supplements are conducive to the "profit" of any man that practices them. They may not be *immediately* profitable, but they are "as bread cast upon the waters which will return after many days."

That Spinoza's rule is the main aspect of the scriptural one is also evident from the "summary" of the ethical part of the Law of Moses which had taken on a positive form by New Testament times, and which reads, Thou shalt love thy neighbor *as thyself.* Self-love is clearly the scriptural standard. Self-love cannot be exercised except a man possess his own freedom; in parallel manner, a neighbor cannot manifest his self-love unless he has his own freedom; consequently, all substitution of the choices of one man over another without the latter's genuine concurrence is coercion, and violates the great Law of Moses.

That we agree substantially with Spinoza in this matter does not imply that we agree with Spinoza on any other part of his thought; assuredly, not in regard to his pantheism.

Dostoevski has completely bastardized the requirements of morality between man and man. Spinoza has impaired the full requirements of morality between man and man. The ethics of neither compares favorably with the incomparable ethics of the Hebrew-Christian religion.

Do We "Need A Vast Expansion Of Social Security"?

Leon Keyserling some years ago was chairman of the President's Council of Economic Advisors. He has been an influential person and continues to be. He is now president of the Conference on Economic Progress.

Keyserling in a recent issue of *Business Progress,* published by the Americans for Democratic Action, writes as follows:

"We need a vast expansion of social security . . ."

Contrarily, in this publication the view is taken (1) that existing social security is an unfortunate institution, (2) that it should not be increased but decreased, (3) that a "vast expansion of social security" will be injurious to everybody, and (4) that 100% social security would be eventually synonymous with a return to primeval poverty. See the preceding issue, and the following information in this one.

Men Want Security And Prosperity; What Is The Real Origin Of Security And Prosperity?

Last month we showed that Old Age Social Security is not really *security,* when the funds currently being collected from employees and employers are invested in government bonds.

That idea will be surprising to people who consider government bonds to be the finest and safest investment in the world. The United States government systematically urges upon its citizens the purchase of government bonds. Banks are glad to sell them. Many companies promote or at least cooperate in pay-deduction plans, by which employees regularly make payments on the purchase of government bonds. On all sides the purchase of government bonds is recommended.

Nevertheless, as was analyzed last month, it would be calamitous, if *all* the "savings" of citizens were "invested" in government bonds. If that were done for 50 or 100 years, the economy of the United States would become like the economic condition today of China, India and Africa. We would become primitively poor, in the *real* sense of the term.

But that idea needs considerably more explanation in order to be understood and accepted. It will be helpful to that end to define further two critical terms, (1) *capital* and (2) *funded* security. We have already mentioned briefly what *funded* means; and we have also already defined *capital* in a *general* sense, and capital in a *social* sense, but not in a *private* sense.

We also printed the simple but profound and basic idea, quoted from a speech of Ludwig von Mises, that prosperity depends (not on governments, etc., but) on the amount of *capital per capita.* Mises's thesis, which he is right in emphasizing at all times, is that real prosperity depends on how much *capital* there exists to assist the production of each person in a country. He alleges, undoubtedly correctly, that the prosperity of the people of the United States is founded on the fact that there is an enormous amount of productive equipment behind each worker; that that is why we are prosperous as a nation; and that, conversely, because the people of no other nation have so much capital behind each worker, *therefore*, their prosperity is proportionately lower. Failure to recognize this fundamental truth (emphasized by Mises more than by any other economist) is the reason why damaging fallacies are widely held. Indeed, the basic fallacy to which we refer, it should be admitted, is held by any reader of the foregoing who believes the statement made earlier to be absurd, to wit, that United States Old Age Pensions are not really *social security.* Who smiles and rejects that statement is, unfortunately, not sufficiently sceptical and is deceived, because "Things are not what they seem." United States Old Age Pensions are *private* security but not *social* security.

The problem is worthy of further analysis. Mises's statement is that the prosperity of a people depends on the amount of *capital per capita.* Of this ratio, the number of people is not ambiguous, but can for all practical purposes be determined accurately enough. But the situation is different with the concept *capital*. *That* term is ambiguous and its proper meaning is sharply disputed. Mises' formula takes on full meaning only when *capital* is understood as it should be.

We ourselves, in the previous issue, may have contributed to confusion by quoting from Böhm-Bawerk. In the February issue, pages 50-51, we quoted his definition of *social capital*. Readers may remember that the last item in Böhm-Bawerk's list of what constitutes social capital is *money*.

Now *money* is, in this country at the present time, pieces of paper, as much as bonds are pieces of paper. Shall we then add money (pieces of paper) into the definition of *capital* before we divide by the number of people to get the *capital per capita?* If so, will the capital be twice as high if, say, the money supply is enormously increased, but nothing else is increased, that is, if *real* capital is not increased?

All who use the words of the formula, *capital per capita,* find themselves faced with the need for a definition of *capital*. Some of them may think that the *capital per capita* is not increasing in the United States. Nevertheless, prosperity *seems* to be becoming more and more prevalent. Here is a serious apparent contradiction.

In fact, all *conservatives* are faced with a profound problem. They are under present circumstances prophets of future disaster. But few people listen to them. Men generally believe the lamentations of conservatives to be spurious and even ridiculous. How, they say to themselves, can these prophets of future trouble be right, when on all sides prosperity is increasing; *"we never had it so good"!* The issue obviously depends on whether capital per capita *is increasing or is decreasing,* and on whether it will or will not continue to do so.

The subject being discussed is, therefore, an elusive and confusing one. At least two requirements are necessary if the analysis is not to end in confusion and lack of cogency: (1) *capital* must be defined correctly for the purpose of the reasoning; and (2) it must be determinable whether *capital,* as purposely defined, is in fact increasing or decreasing per capita. Neither of these tasks is an easy one.

But of one thing, some may say, there need be no doubt whatever: if *capital per capita* is increasing, the feelings of the public about their prosperity are an accurate reflection of the facts.

A critic may dispute even that; he may say *capital per capita* may be increasing and the people may still feel less prosperous because they are accumulating capital faster than it throws off production of *consumption* goods. Or, vice versa, he may say, *capital per capita* may be decreasing now, but prosperity may appear to be currently but temporarily higher because people are *consuming* past accumulations of capital; we are, he may say, *living well,* like a squandering son coming into his inheritance, but we shall suddenly wake up and discover we are genuinely poor. In other words, the question arises: is the *current rate of consumption of consumption goods* a good measure of real *and permanent* prosperity, and does it evidence capital accumulation or decumulation? Obviously, we are beset on all sides with genuine difficulties when we try to state categorically that capital per capita is increasing or decreasing.

Finally, the illusion may be created that the abstract idea of capital per capita is the *ultimate* determinant of prosperity. If so, is the moral teaching of Scripture irrelevant? Nowhere does Scripture teach lucidly that prosperity depends on *capital per capita;* instead, it teaches that prosperity is determined by obeying the Law of God. Is there then a conflict, and irrelevancy, between morality and economics? We believe not. The reason is that the accumulation of *capital per capita* depends on certain *moral* conditions. And so morality is more fundamental than economics — unless the two are ultimately largely identifiable, which happens to be the case.

Maybe the number is relatively few who accept *capital per capita* as the key to prosperity. Maybe still fewer have a clear concept of what is meant by *capital* in the formula, *capital per capita;* and, finally, maybe still fewer know not only the foregoing two, but also that ultimately prosperity and security depend on what is known as morality, as formulated in a specific case as follows: "This book of the law shall not depart out of thy mouth, but thou shalt meditate thereon day and night, that thou mayest observe to do according to all that is written therein: for *then* thou shalt make thy way *prosperous,* and then thou shalt have *good success*" (Joshua 1:8).

The Only Sense In Which Paper Money Is Social Capital

The question, Is paper money capital, sounds academic and everybody will be disposed to answer, *yes*. We do, too.

Readers of the February issue will remember that we quoted Böhm-Bawerk's definition of *social capital,* and that Böhm-Bawerk includes money as an item in social capital (see page 51).

On the other hand, *money* in the United States is presently in the form of mere pieces of paper. We disparaged the idea that more *pieces of paper* would make a people more prosperous or give security. If the quantity of money was greatly increased by running the printing presses faster, and by increasing the denominations of the bills (printing ten-dollar bills rather than one-dollar bills), we as a people and as individuals would not be more prosperous or more secure. In fact, we would be just the contrary. *Money,* as capital, is therefore worthy of some special attention.

Böhm-Bawerk included in his social capital not only factories and warehouses, but also the facilities to transfer goods from factories to warehouses, and all other means which *facilitated exchange,* and by facilitating exchange also increased production and well-being. The argument is unobjectionable. Then Böhm-Bawerk extended the argument to include money. Money, he said (and he was undoubtedly correct), greatly facilitates exchange and by so doing increases production and well-being. Therefore, he concluded, money must be included in capital. Money, correctly understood in this connection, is valuable to society and promotes its productivity.

To include the existing stock of money in the concept of capital, because that stock of money greatly facilitates exchange, is unobjectionable; but to conclude further that the greater the quantity of money, the greater would be the prosperity, is a fallacy. If money is legitimately part of social capital — and it is — it does *not follow,* in the case of money, that social capital is increased by the addition of even one paper dollar to the money supply. When the quantity of real goods is increased — factories, tools, warehouses, etc. — then the well-being of the community *is* being promoted; but if the quantity of money is increased, the well-being of the community is not being promoted.

That idea may not be readily accepted. The present financial structure of the United States is based on the mistaken and injurious idea that the quantity of the currency, for (1) seasonal, (2) cyclical, and (3) long-term growth purposes, should be varied up and down by the deliberate judgment of certain fallible and ordinary mortals, although able enough as men go, namely, the members of the Federal Reserve Board. This is part of the quicksand under the American (and, for that matter, the world's) economic structure, constantly disturbing prosperity, confusing the calculations of citizens, and constituting the sure basis for eventual uncontrollable, devastating inflationism, probably involving political as well as economic upheaval, and maybe delivering the world to communism — a jump which, if made, will be from the frying pan into the fire.

The beguiling and insidious form in which this principle is presented is that it be (1) only in *modest quantities* and (2) for price-stabilizing purposes. In terms of morality this idea would be re-formulated as follows: (1) sin only a little and retreat before there are consequences, and (2) sin for a good purpose. But it is ancient moral doctrine that every sin, no matter how small, carries a proportionate penalty. It is self-deception in finance as in other matters to believe that you can without consequences sin only a little, and can retreat early enough and successfully to avoid consequences.

When it is admitted that money is capital, it should not be concluded that more money means that there is more capital. This second idea (maybe it sounds paradoxical) does *not* follow from the first. It is outside the scope of this analysis to digress into the intricacies of money, an admittedly difficult subject. This discussion had the limited purpose of calling attention to the "special case" of paper money as a category of capital in Böhm-Bawerk's definition of social capital.

The case of a metallic currency (gold or silver) is not different in principle, as far as such metals function as currency. They do have, however, a contributing independent value, namely, uses for ornament or for fabrication. In *that* sense, increasing the quantity of gold increases prosperity. But contrarily *increasing* the quantity of gold for *monetary* purposes does not contribute to prosperity. The old quantity would have served as well (assuming flexible prices for commodities).

If, then, it is desired to measure the *capital per capita* in order to conclude whether prosperity and security are being promoted by an increase in *capital per capita,* it is necessary, in order to avoid self-deception, to note carefully whether the amount of *paper* money — which is part of social capital — has been increased or decreased and how much.

The foregoing must suffice for the present; the subject is a complex one, and it does not fit our presentation to go into details here.

Bohm-Bawerk's Definition Of Private Or Acquisitive Capital

Whereas economists frequently think, for their special purposes, in terms of *social* capital, the average man almost always thinks in terms of *private* or *acquisitive* capital only. In popular thought, if a man "has capital" the idea is that he has wealth, and that it is *his,* and in that sense that it is *private.* Further, he can use his capital to acquire what he wants and so it enables him to be acquisitive. Such is the derivation of the words, private or acquisitive capital.

To distinguish most easily between social and private capital, we shall begin once again with social capital and then go on to private capital.

Böhm-Bawerk's definition of social capital, which we quoted last month (February issue, p. 50f.), did not include:

1. The raw forces of nature, including land, minerals, oil, timber, etc.; nor
2. Labor, or men themselves; nor
3. Consumers' goods — as food, clothing, houses — which are *already in the possession of consumers.*

What does that leave in Böhm-Bawerk's definition of social capital:

1. Firstly, *things produced by man,* as contrasted to things created by God.
2. Secondly, such things *only when used for further production.*

Böhm-Bawerk somewhere condenses his definition of social capital into the compact phrase: "*the produced means of production.*"

That exactly is what points (1) and (2) cover.

Here is Böhm-Bawerk's definition of *private* capital or *acquisitive* capital; he uses the two terms interchangeably:

> We can conclude by setting down that *private* capital comprises the following:
>
> 1. All goods that constitute social capital; and
> 2. Those *consumption goods* which are not being used by their owner, but are employed by him for the acquisition of other goods through some form of exchange (sale, renting out, loan). Examples are such goods as apartment houses, lending libraries, means of subsistence advanced to their workers by entrepreneurs, and more of the sort. Many economists include here certain rights and relations such as patents, customer relationships, legal claims. Naturally, I reject them at this point on principle, and for the same reasons as apply to my refusal to create for them an independent category of capital.

The first idea that is obvious is that private capital, as defined by Böhm-Bawerk, is broader than social capital, simply because it includes social capital *plus* "consumption goods . . . used . . . for the acquisition of other goods through some form of exchange."

Böhm-Bawerk devotes many pages to determining what is to be included in capital and what is to be excluded. The subject is a much disputed one in economics by economists. We cannot here go into detail, because the question is beyond our scope.

But in any event it is desirable to ask a question: When Mises refers to *capital per capita* as determining prosperity, what should capital be taken to mean in this connection, *social capital* or *private capital?* Is the ratio for determining *capital per capita,* and thereby measuring prosperity, $\frac{\text{social capital}}{\text{number of people}}$, or $\frac{\text{private capital}}{\text{number of people}}$?

The problem, in fact, becomes more complex the more one thinks about it. Land and natural resources, for example, were excluded from the definition of social and acquisitive capital. The characteristics of land differ so much from the "produced means of production" that it is not valid in most chains of reasoning to lump them together. But in this case we are endeavoring (1) to measure production per capita, as a measure of *prosperity;* and (2) the amount of intermediate goods as a measure of the real *security* behind the present expectations of pensioners in the future. Maybe the idea, *capital per capita* requires its own special definition of *capital.*

Mises's Definition Of Capital

Mises himself resolutely rejects the distinctions made by other economists between social capital and private capital. He writes that the basic concepts pertain to what is *capital* and what is *income* (*Human Action,* Yale University Press, 1949):

> [For Mises the] whole complex of goods destined for [use in] acquisition . . . evaluated in money terms is capital . . . [and] is the starting point of economic calculation. The immediate end . . . is to increase or . . . preserve the capital. That amount which can be consumed within a definite period without lowering the capital is called income. If consumption exceeds the income available, the difference is called capital consumption. If the income available is greater than the amount consumed, the difference is called saving. (P. 261f.)
>
> . . . Capital is the sum of the money equivalent of all assets minus the sum of the money equivalent of all liabilities as dedicated at a definite date to the conduct of the operations of a definite business unit. It does not matter in what these assets may consist, whether they are pieces of land, buildings, equipment, tools, goods of any kind and order, claims, receivables, cash, or whatever. (P. 262.)

Mises is an exponent of the famous Austrian school of economics. That school was in a sense theoretical, but a major part of its achievement was Occamish in character, accomplishing a thorough discrediting of vague and incorrectly defined ideas. Mises out-does all his predecessors and contemporaries in simplifying the old ideas and giving them a radically different setting. He has done that also in the foregoing quotations. He breaks, for his purposes, with his predecessor, Böhm-Bawerk, and much more so with others, and shifts to the customary accounting approach. The effect of this is that his definition is closer to that of what the average man would consider capital, than is otherwise the case. For example, departing completely from his predecessor Böhm-Bawerk, Mises includes land in his definition of capital.

But serious difficulties remain, of which Mises is obviously fully aware. On page 261 he wrote: "Among the main tasks of economic calculation are those of establishing the magnitudes of income, saving, and capital consumption." These are formidable tasks.

It will have been noted that Mises began his definition of capital as "a sum of money equivalent . . ." But, as he comments elsewhere, the unit of measurement, *money,* is subject to changes, especially during inflationism, which makes measurement of "the magnitudes of income, saving and capital consumption" most difficult.

Who *knows,* then, whether *capital per capita* is increasing or decreasing — whether there is *saving* or *capital consumption* going on at the present time, in the United States, and in other geographical areas in the world? Apparently nobody does; everybody appears to be guessing. Many conservatives say capital is being consumed here and throughout the world; other conservatives disagree. Mr. John Public, in the United States, also apparently disagrees; men make the statement to each other in the vein: "We never had it so good."

Maybe in regard to what changes are taking place in *capital per capita* we should be cautious and grope for our conclusion like a blind man exploring with his white cane.

But if it is not possible to say positively what the net trend is in regard to *capital per capita,* it can be affirmed with complete assurance that, if all money savings were siphoned off into government bonds in a social security system, then *capital per capita* would decrease. Indefinitely increasing our present so-called social security will be catastrophic in its ultimate consequences.

There Are More "Unfunded" Private Pension Plans Than Many Are Aware

Whatever may be the method for simplifying thinking on capital accumulation (saving) or capital decumulation (consumption), it will be dangerous to assume that acquiring private capital is identical with real *funding* of pensions.

There are three types of pension plans worth considering:

(1) the obviously unfunded plans; (2) the apparently funded but the not really funded plans; and (3) the really funded plans.

(1) The first consists in a plan where there is nothing behind the promise to pay the future pensions than the continued financial strength and existence of the company. No *fund* of assets is being set aside, independent of the company's life and prosperity.

(2) The second, the "apparently funded but not really funded" private pension plan consists in there being funds set aside to pay future pensions, but those funds are invested in bonds issued by a spendthrift who is not accumulating *capital* with the funds turned over to him. Really, from a *social* viewpoint, a private pension plan, invested in U.S. government bonds, is not funded in *real* assets. From a narrow *private* viewpoint, the plan is funded; from a broad *social* viewpoint, it is not funded.

(3) Finally, there is the genuinely funded private pension plan. The managers of such a pension fund have seen to it that the funds have gone into the construction of *real* capital in Böhm-Bawerk's sense.

Curiously, the labor unions have in some cases insisted that private pension plans, which they can influence, operate according to the second pattern, namely, own government bonds, thereby favoring a pension scheme which is only "apparently funded but not really funded."

The High Evaluation Placed On Social Capital By Communism

It is a mistake to think that the concept of private capital is important, but that the concept of social capital is not important. Communist and socialist theorists know full well the importance of social capital for the prosperity of a socialist or a communist state. It is interesting to observe how they think.

They begin with the idea that for their society (1) social capital comes first, and (2) that the comfort and well-being of the citizens comes last.

If there is no significant private ownership permitted, as hardly exists in a communist state, then the workers themselves will be not be disposed to accumulate capital. Therefore, a communist state has a perfectly natural tendency toward poverty; men will either not work hard because it is not for themselves or their immediate family; or, if they work hard, they will wish to consume their whole produce before the state takes away from them what they have produced by their *extra* effort.

To insure the production of social capital (and so avoid complete destitution) the communists develop what are called Five-Year Plans. These plans have one purpose: the development of *social* capital, especially in the so-called heavy industries, which will produce heavy machinery and/or permit military production. The Five-Year Plans determine what is to get priority of production. A certain amount of materials and supplies and a certain number of people — adequate for the Five-Year Plan, that is, for the production of *social* capital — are set aside ahead of all else. If that means hardship, because so little is left over for comfortable living, no great weight is given to that.

The expression by the National Socialist government of Hitler was "guns, not butter." A more comprehensive way to express the same idea is to say: "*production of social capital, not consumer's goods.*"

Socialist-communist countries are indeed concerned about *capital.* A major purpose in their accumulation of social capital is to have a large war potential — to attack others or defend themselves.

In advanced socialist-communist societies, as distinguished from primitive societies, there is a strong tendency for the formation of capital to be the quintessence of their state program, and it has an ominous aspect. Not for nothing is most of the world afraid presently of Russian "might." Russian might consists not only in men but also in *social* capital; it is that which makes Russia formidable.

Is Social Security "Just" Or "Social"?

On January 1, 1959 the tax called social security, which previously had been at the rate of 2¼% of the employee's pay (for the employee and for the employer each) on the first $4,200 of annual wages, was increased to 2½% on the first $4,800. The social security per person increased, on the above-mentioned dollar amounts, from $189 to $240 per year, or 26%.

The Man Who Gets Too Little

If a person begins work at twenty years of age, and works until he is 65, that is, if he works for 45 years under the new rates, he will have put into the fund $10,800. At compound interest rates at 4%, the $10,800 will have increased to approximately $30,000. He can begin to collect for himself and his wife at age 65 at $174 a month or $2,088 a year. For him to recover his $30,000, allowing for interest of 4% on the unpaid balance, will require that both he and his wife live more than 21 years after retirement. Obviously he is likely to have paid in more than he will take out. The "inequity" comes from the fact that the contributions have been over a long period of 45 years.

But it is also possible to collect social security after having paid in for as little as four years. In fact, sound policy on the part of everybody should consist in putting in the least and taking out the most. Anyone who does not do that is naive.

The Man Who Gets Too Much

A few years ago the farmers were put under social security. The law required that a farmer had to make contributions for at least four years before he could get social security. In the case of a farmer 61 years old he would put in a maximum of $807. In the first year after qualifying he would receive for himself and his wife, $142 a month, or $1,704 a year, more than twice what he put in altogether. Farmers close to 65 years of age, being astute people, decided that the thing to do was to stay on the farm for another four years, pay the social security and then collect during the rest of the years of their lives. It is the best "investment" they ever made!

An acquaintance of the writer two years ago moved from one country town to another, and consequently had a house for sale. But the bottom had dropped out of the market for houses. Upon inquiry the reason given was that farmers were not retiring to live in town as they ordinarily would, because they were staying on their farms and farming in a nominal way for four years in order to qualify for social security. The people of this country wished the farmers to have social security. The farmers, that is, the *old* farmers were undoubtedly glad to have it, because they were required to put in very little and they could take out much. It may be different in the case of young farmers. They can, over a period of time, put in the $30,000 previously quoted (after accumulation at compound interest). They, in contrast to the old, will find social security unprofitable.

We know of the case of a man who is self-employed and he has paid social security in one year only. He is now 61 years old. Although he has been losing money in his business, it is possible that he could have a net earned income at least in three of the remaining four years before he is 65 years of age. He will then have to pay social security for those three years. But having done that, he can collect social security for as long as he and his wife live after 65 years of age. The people of the United States wish this self-employed person to receive social security. Why should he not endeavor to qualify? It will be highly profitable for him to do so. He may put in a total of about $909 and he might easily collect thirty times as much.

We know of another case of a widow in her sixties with only a limited income, hardly earning enough to qualify for social security deductions. She was a part-time employee. Her employer, realizing what social security would mean to her, induced her to increase her hours of work, collected the social security from her and paid it to the social security administration, and just before she was 65 she qualified to collect social security. She had put in less than $600, and has already collected many times that amount.

The word *social* in social security is clearly a misnomer *if* by the word is meant that the system is sensible and fair *between contributors and participants.* If the system is clearly understood, it is obvious that it is one of the smoothest ways for the old to rob the young that has yet been devised, unintentionally, of course; or more accurately said, it is one of the smoothest ways of favoring the short-time contributors at the expense of the long-time contributors.

Edmund Burke, On A Certain Type Of Mind

It is undoubtedly true, though it may seem paradoxical; but in general, those who are habitually employed in finding and displaying faults, are unqualified for the work of reformation: because their minds are not only unfurnished with patterns of the fair and good, but by habit they come to take no delight in the contemplation of those things. By hating vices too much, they come to love men too little. (Page 241.) —Edmund Burke, *Reflections on the Revolution in France* (Gateway Edition, dist. by Henry Regnery Company, Chicago, 1955)

The Fallacy In The Attack Of The World Council Of Churches On "Laissez-Faire" Capitalism

(*An example of the logical error of* Ignoratio Elenchi)

The Resolution In Favor Of Socialism

In August 1948 leaders of the Federal Council of Churches met in Amsterdam, The Netherlands, to organize the World Council of Churches. At that meeting, communism and *laissez-faire* capitalism were condemned *equally.* The decision reads as follows:

> ". . . *the Christian churches should reject the ideologies of both communism and* laissez-faire *capitalism.*"

In the excellent book, *The Powers That Be* by Edmund A. Opitz (Foundation for Social Research, Los Angeles, California, 1956), the further comment is made: "At a press conference, John C. Bennett, who chaired the commission which produced this statement, said that the middle way between capitalism and communism which the report had in mind was something like the regime being worked out at the time by the Labor Party in Great Britain" (page 47). That government was socialist in character.

The *final* resolution has been quoted in the foregoing; a different resolution had been proposed earlier. The original resolution read so that communism and capitalism generally (without restricting capitalism by the word, laissez-faire) were condemned equally. An American business man, influential in the Federal Council, flew to Amsterdam and persuaded those who were maneuvering the resolution through the meeting to change the wording so that the condemnation fell only on *laissez-faire* capitalism, not on *capitalism* generally. That a business man should make such a dubious "distinction" — between capitalism and laissez-faire capitalism — is evidence of confusion and/or concession.

What Does Laissez-faire Mean?

In simplest English, the meaning for the French expression, *laissez faire,* is *free.* What the World Council condemned then was *free* capitalism. By changing from condemning capitalism generally to condemning free capitalism only, the Council exonerated unfree capitalism from its critique. What might this *unfree* *capitalism* be which the World Council was persuaded not to condemn; and what might this free capitalism, or *laissez-faire* capitalism be that it did condemn?

The *unfree capitalism* which was favored (or at least not condemned) was a "capitalism" thoroughly regulated by government under some alleged but vague principles of *righteousness* or *public welfare*. (See our Volume III, pp. 302ff.) Consumers generally and buyers, under this unfree "capitalism," are not free to buy and consume as their own interests direct them. Producers and sellers are not free to produce and sell as their own interests prompt them. But it is a misnomer to call this capitalism. It is instead a system of control known as interventionism; the government *intervenes* in economic matters and regulates by legislation, boards, commissions, decrees. The nominal title to capital remains private, but the *real* control lies with the state. The World Council, then, assumed that there are two kinds of capitalism, namely, *free capitalism* and *interventionist capitalism*. Free capitalism was condemned, but interventionist capitalism was, if not approved, at least not condemned.

Types Of Economic Systems

There is, however, really only one type of true capitalism. The essential characteristic of that capitalism is freedom (although that certainly does not mean *unlimited* freedom). Interventionist capitalism is of a different *genre* than capitalism proper, and so interventionist capitalism is not properly a subdivision of capitalism. The categories of economic systems should not be, for example,

1. Communism
2. Socialism
3. Capitalism
    (a) regulated capitalism
    (b) laissez-faire capitalism

but should be:

1. Communism
2. Socialism
3. Interventionism (allegedly regulated capitalism)
4. Capitalism (laissez-faire only)

There are, of course, other categories of economic systems, as syndicalism, anarchism, etc. The foregoing classification is designed to distinguish between interventionism and capitalism, with the intent of showing both terms in the right perspective.

Returning now to the original quotation from the World Council of Churches in Amsterdam, it is obvious that the World Council condemned communism and capitalism, leaving uncondemned either socialism or interventionism. It will be well to indicate the major differences between communism and socialism. Under both communism and socialism the ownership of capital is to be by the state; but under communism the means to accomplish and retain public ownership is considered to be properly attained even though the means be violent; but in socialism the means to accomplish and retain public ownership are to be by legislation and without brutal violence. The four classifications in our list have the following meanings:

1. Communism (ownership of capital by state, by violence if necessary)
2. Socialism (ownership of capital by state, without violence)
3. Interventionism (nominally private "ownership" (title) of capital, but the use by owners is to be regulated)
4. Capitalism (private ownership of capital, but the use to be free in certain respects; this is laissez-faire capitalism)

The Council condemned the two implied *extremes* — communism on one side, and laissez-faire capitalism on the other. The two in-between categories, socialism and interventionism, were not condemned. In other words "public ownership without violence" and "private ownership under regulation" were not explicitly censured. But as the supplementary remarks of Dr. Bennett (quoted earlier) indicated, what those who put the resolution through had in mind was "something like the regime being worked out at the time by the Labor Party in Great Britain," that is, they really had in mind as their ideal, socialism. In short, the formulators of the resolution were, indirectly, getting the delegates to express approval of socialism.

Ultimately, in the abstract, there are only two systems of government, the coercive and the noncoercive. The coercive are the communist, socialist and interventionist types. They *coerce* beyond the prevention of evil. They make it compulsory to do what they esteem to be good (and curiously, in the process, violate the principles they profess). The noncoercive are the *laissez-faire* capitalist types, who *limit their coercion* to the resistance of specified evils. But, in practice, the systems tend to merge into each other. There is no pure capitalism anywhere nor will there be pure communism anywhere either. There are varying "degrees" of communism, socialism, interventionism, capitalism, and other systems.

It appears justifiable to infer that communism and laissez-faire capitalism were *equally* condemned by the World Council. At least it gave no indication which it regarded as being worse. The owner of an American clothing store, operating as a practicing capitalist, was condemned as much as Stalin was condemned as a practicing communist. Stalin will probably go down in history as as monstrous a butcher and tyrant as has ever lived. An equal condemnation appears to have been passed upon a typical American business man, in the daily conduct of his business. The communists throughout the world undoubtedly were encouraged by being placed on a par with capitalists by the World Council. They can tell restive satellite people that if they wish to return to capitalism they will then have nothing better than they have now, because the World Council of Churches has condemned capitalism as much as communism.

What follows is a defense of laissez-faire capitalism (not so-called interventionist capitalism, or more correctly interventionism). In this defense we propose to take the following steps: (1) quote from Arthur Schopenhauer about attacking something which is not being defended; this is the case of setting up a "straw man" and then knocking him down; (2) show how that fallacy is generally applied by the critics of laissez-faire capitalism; and (3) finally, quote as good a summary as is known to us, regarding what the origin of *laissez-faire* is and what it really means.

Schopenhauer On Attacking A Fictitious Issue

Schopenhauer in an essay entitled, *The Art of Controversy*, begins his analysis of various kinds of fallacies by citing three examples of what are known as *ignoratio elenchi*, which refers to an "argument that appears to refute an opponent while actually disproving something not advanced by him" (Oxford Concise Dictionary); in other words, an *ignoratio elenchi* is to allow oneself to lose an argument because your opponent sets up a "straw man" — a proposition different from what you yourself are advancing — and then knocking down his "straw man", in order to create the impression that he has knocked down your real proposition. As a case in point, an almost universally used argument against laissez-faire capitalism is that it is amoral — without morality; ruthless; rugged individualism; hard-hearted selfishness; in short, not a capitalism free in any *restricted* sense at all, but a capitalism unlimitedly free and practically anarchic, a capitalism living by tooth and claw like a beast in a jungle.

If *capitalism* is such a system, then it is condemned just by definition alone. Who would wish to defend it? But the idea is a caricature.

Schopenhauer *begins* his sardonic thesis on how to win arguments, by fair means or foul, by warning to be wary of three types of *ignoratio elenchi,* to wit: (1) extension; (2) homonymy; and (3) confusing general and specific proposition. Schopenhauer, by giving this attention *first of all* to fallacies of *ignoratio elenchi,* indicates that the fallacy involved is a common and dangerous one.

In the case of the attack on laissez-faire capitalism, there is a fallacy of *extension.* This is what Schopenhauer has to say about this strategem in dishonest argumentation:

> The *Extension.* This consists in carrying your opponent's proposition beyond its natural limits; in giving it as general a signification and as wide a sense as possible, so as to exaggerate it; and, on the other hand, in giving your own proposition as restricted a sense and as narrow limits as you can, because the more general a statement becomes, the more numerous are the objections to which it is open. [Your own] defense [should] consist in an accurate statement of the point or essential question at issue.
>
> Example 1. I asserted that the English were supreme in drama. My opponent attempted to give an instance to the contrary, and replied that it was a well-known fact that in music, and consequently in opera, [the English had done] nothing at all. I repelled the attack by reminding him that music was not included in dramatic art, which covered tragedy and comedy alone. This he knew

very well. What he had done was to try to generalise my proposition, so that it would apply to all theatrical representations, and, consequently, to opera and then to music, in order to make certain of defeating me.

The "Extension" In The Charges Against Laissez-Faire Capitalism

Laissez-faire capitalism, that is, *free* capitalism, is defamed by extending the word *free* to mean *outlaw*, in the sense of one who habitually defies and breaks a supposed moral law; or as an institution which claims a freedom to which it is not properly entitled and which, if it has that freedom, will surely abuse it.

Now capitalism cannot properly be accused of systematically breaking the statutory law of the land. If so, why is it not regularly prosecuted in the Courts? The fact that relatively few cases are begun against business by the government is good proof that capitalism is not conducting itself as an outlaw. Capitalism, to the writer's knowledge, has never claimed for itself being above the law or outside the law, or independent of the law.

Whoever then wishes to initiate an attack on laissez-faire capitalism should visit the Prosecuting Attorneys in the United States and should show them that individual businesses are violaing the laws and are *claiming a freedom that the law does not presently allow*, and that court action should be begun against them. We do not know of a single delegate among the American clergymen at the meeting in Amsterdam who has ever brought a specific, actionable charge against a specific capitalist enterprise in the United States. But they condemn *laissez-faire* in the same breath that they condemn bloody communism.

Wherein does laissez-faire admit that it should not be free?

It seeks and asks no freedom to commit violence, coercion, theft or fraud. It admits it should be subject to the Sixth, Eighth and Ninth Commandments in the Mosaic Decalogue: (6) Thou shalt not coerce (or more narrowly, *kill*); (8) Thou shalt not steal; and (9) Thou shalt not lie. And further, it admits that it should be subject to specific legislation which defines and implements these basic laws against coercion, theft and fraud.

But in what does laissez-faire capitalism plead for freedom? Laissez-faire capitalism is founded historically on the principle that, beyond coercion, theft and fraud, it should be genuinely free.

It, therefore, says this: if *laissez faire* is to be *righteous*, then righteousness should not be defined more exactingly than Moses defined righteousness, namely, more exactingly than the three rules for action just quoted.

But if *righteousness* means something more holy than the laws of Moses, then two questions arise: (1) *specifically* what more is required; (2) and how enforce it in a practical sense.

Careful reflection will reveal that the additional claims against laissez-faire capitalism primarily consist in implying that *prices arrived at by the interplay of the interests of free buyers and free sellers are not "just" or "righteous."* For example there may be a big wheat crop. Supply presses onto the market. Prices decline. The price after the decline may be considered to be "not just" or "unrighteous"; by the seller of course, not the buyer. Or the case may be of another kind. There may be a great demand for a new product, of which the supply is limited for the time being. Prices rise. Then that high price is considered to be "not just" and to be "unrighteous"; by the buyer, of course, not the seller.

The widely accepted phrase to explain price changes is *supply and demand.* The idea under laissez-faire capitalism is to let those two influences or forces determine prices. The objection to laissez faire in this respect is formulated in this manner: somebody is to be authorized to interfere with the determination of prices ordinarily effected by means of supply and demand. Those somebodies are individuals designated by the state. A bureaucrat, therefore, is to determine prices (1) on the basis of his subjective judgment of what righteousness is (a righteousness, of course, beyond non-coercion, fraud and theft), or (2) on the basis of popular pressures.

In regard to such bureaucratic "righteousness" it may be affirmed that nobody has ever been given special insight, not even by the Holy Spirit of God, regarding what a *righteous* price is, beyond its basic, historical Biblical definition, (noncoercion, safety of property, truthfulness). Beyond that, *righteousness,* as an alleged standard, is pure subjectivity without merit. If in doubt, let any man define this higher righteousness in a manner that can be applied practically! It has never yet been done.

What is a righteous price in a besieged city? As the siege progresses, supplies become scant. Prices skyrocket. What is the purpose, or the logic of the famine prices? Food must be conserved; and the way to conserve it is to make it costly. By making food costly, waste is reduced and consumption restricted. Thereby the availability of supply is lengthened. The price will go no higher than the evaluation by the citizens of how great the need is to conserve foodstuffs.

Suppose a "righteous" (?) man is appointed to determine the price, and that he has a warm heart for the people in the city. He decides, in order to make it easy for them, to keep the price of foodstuffs low. Then waste continues and consumption is not restricted — stretched out. But suddenly the supply is completely gone, and the city must be surrendered. What is proof of *righteousness* in this case? There is no such proof. All that was done was that the judgment of one bureaucrat was substituted for the collective judgment of all the citizen-consumers in the beleaguered city. That is all that "price-control" beyond the control of "supply and demand" can mean. A question of *righteousness?* No, a question whether *one* man has special guidance, a vision or charisma from the Holy Spirt of God!, or whether the aggregative judgment of all men is better. *Laissez faire* says: the aggregative judgment of all is better than the pretended god-like judgment of one man.

Righteousness is not the word to describe the judgment of the bureaucrat; the correct words for the situation are *arrogance* and *impudence;* no man has such god-like judgment as to know what righteousness is beyond the Law of Moses.

Certainly, there is some *coercion* involved. But the word, coercion, must be defined in this case. There are two kinds of coercion: coercion *by men,* and coercion by *circumstances.* The Law of Moses legislates only against coercion by men. It does not legislate against coercion by circumstances. Moses, acknowledging the coercion by circumstances, declared explicitly "in toil thou shalt eat of [the fruit of the earth] all the days of thy life" (Genesis 5:17b). Economic circumstances coerce everybody; and always will. For a moralist to set out to accomplish a program to free men from the coercion of economic circumstances is for him to arrogate to himself to be a better and successor god to the Creator of the heavens and the earth, Who did not liberate finite men from the conditions of a finite world.

The only righteousness that the Hebrew-Christian literature has taught systematically is that coercion by men is evil, but that coercion by circumstances is inevitable.

The determination of prices by a bureaucrat is in essence a rebellion against the character of creation and the Creator who made it. Submission to the laws of *supply and demand,* which means humble admission that we are not gods, is the principle accepted by *laissez faire.*

Having defined what the freedom is that *laissez faire* seeks, and what the freedom is that it does not seek, we can now see clearly how the opponents of *laissez faire* have blackened the name of *laissez-faire* by an *ignoratio elenchi,* an *extension* of the meaning of the word, *free.* Instead of describing *laissez faire* as only legitimate and wise freedom in economic matters, it has implied that a *laissez faire* type of freedom is a claim for unlimited freedom, an outlawish freedom, an exploitive freedom, whereas as a matter of fact the theory of *laissez faire* submits to the restraint of avoiding coercion, fraud and theft.

That has been the *theory or principle.* Of course, there have been many violations of the rule against coercion, fraud and theft by capitalists. But those are processable under criminal law, and the sins against the Decalogue do not require, for their restraint, that there be abrogation of liberty, and the substitution of the judgment of one man for that of everybody aggregatively.

We ask: What is wrong with *laissez faire* when it holds to the principle of (1) obeying the Law of Moses, and (2) accepting the fact that there is economic pressure in this finite world, because there always has been, is now, and always will be a *welfareshortage* in the world, as already quoted from Genesis 5:17b? We can see nothing wrong. But when someone sets up a vague allegedly higher principle of morality his position is sanctimonious.

When men under a capitalist system, in which there is freedom, use that freedom to coerce, steal and lie, should those violations not be vigorously punished in the courts of law, and should not the matter rest there? Or should freedom generally be annulled not in the interest of applying the Law of Moses against evil men, but in the interest of trying to frustrate economic realities and eliminating a *welfareshortage,* which will actually *be aggravated by any measure interfering with free prices?*

The "straw man" set up by opponents of *laissez faire* is that *laissez faire* means lawless and unrighteous capitalism. On that *assumption* they condemn *laissez faire.* But that is not what laissez-faire capitalism is.

Edwin Cannan's Quotation On Laissez-Faire

Edwin Cannan, the late distinguished economist of Great Britain, in his book, *A Review of Economic Theory* (P. S. King and Son, Limited, London, Westminster, 1929, p. 25ff.) has this to say about *laissez-faire,* together with a quotation by him from de Gournay's "*Éloge de Gournay*" in *Oeuvres de Turgot,* ed. Daire, Vol. 1, p. 288:

> Restrictions and regulations had hampered internal commerce in France much more than in England, and protests had long been made. Turgot says, "In all ages the desire of commerce in all nations has been embodied in these two words: liberty and security (*protection*), but especially liberty. We know the saying of M. Le Gendre to M. Colbert: *laissez-nous faire.*" The phrase, shortened to *laissez-faire,* has been incorporated into the English language because even the full form of it is incapable of terse translation: the literalist's suggestion, "Let us do," is quite unacceptable: "let us be" or "let us alone" suggests inactivity; and "let us get on with our business in our own way," which gives the sense very well, is too long and flat.
>
> Men and women and children have always protested against interference with their activities, and we can well imagine that some equivalent of "*laissez-nous faire*" was frequently heard in the family circle of Adam. The specialisation and popularisation of the maxim [*laissez-faire*] is attributed to Vincent de Gournay, a merchant who lived from 1712 to 1759. He was not an author of any importance, but he exercised considerable influence over subsequent thought by conversations with the economic writers of his time, especially Turgot, who, perhaps idealising him a little, says in a passage which gives a good idea of the state of things prevailing when de Gournay was made an intendant [provincial administrator] of commerce in 1751:

"He [de Gournay] was astonished to find that a citizen could neither make nor sell anything without having bought the right to do so by getting at great expense his admission into a corporation . . . He thought that a worker who had made a piece of cloth had added something real to the aggregate riches of the State, and that if this cloth was inferior to some other cloth, there would be found among the multitude of consumers someone whom this very inferiority would suit better than a more costly perfection. He was very far from believing that this piece of cloth in default of complying with certain regulations should be cut every four yards and the unfortunate man who made it condemned to pay a fine sufficient to reduce a whole family to beggary. . . . . He did not think it desirable that manufacture of a piece of cloth should involve a plea and a tiresome discussion to ascertain whether it conformed to a long and often obscure regulation, nor that this discussion should take place between a manufacturer who could not read and an inspector who could not manufacture. . . .

"Nor had he imagined that in a kingdom where the order of succession was only established by custom, and where the application of the death penalty for several crimes is still left to the discretion of the courts, the Government would have condescended to regulate by express laws the length and breadth of each piece of cloth, and the number of threads of which it must be composed, and to consecrate with the seal of the legislature four quarto volumes full of these important details; and also to pass innumerable statutes dictated by the spirit of monopoly, of which the whole object is to discourage industry, to concentrate commerce in a small number of hands by the multiplication of formalities and expenses, by the requirement of apprenticeships and journeymanships of ten years for trades which can be learnt in ten days, by the exclusion of those who are not sons of masters, of those who are born outside certain limits, by the prohibition of the employment of women in textile manufactures, etc., etc.

"He had not imagined that in a kingdom subject to one and the same prince, all the towns would regard each other as enemies, would arrogate to themselves the right of preventing Frenchmen called foreigners from working inside their boundary, of opposing the sale and free passage of the commodities of a neighbouring province, and of thus fighting, for the sake of a trifling interest, the general interest of the State, etc., etc.

"He was no less astonished to see the Government occupy itself with regulating the price of each commodity, proscribing one kind of industry in order by that to make another flourish; putting particular hindrances in the way of the sale of the provisions which are most necessary for life; prohibiting the accumulation of stores of a thing of which the harvest varies every year while its consumption is always much the same; prohibiting the export of a thing subject to extreme depressions of price, and fancying that it ensured abundance of corn by making the condition of the cultivator more uncertain and unhappy than that of all other citizens, etc."

He knew, Turgot adds, that some of these abuses had once prevailed over a great part of Europe, and that "vestiges of them still remained in England," but he knew also that for the last hundred years "all enlightened persons, whether in Holland or in England, regarded them as the remains of Gothic barbarism and of the feebleness of all governments, which had neither known the importance of public liberty nor how to protect that liberty from the attacks made by the spirit of monopoly and personal interest."

So, as another of de Gournay's admirers, Du Pont de Nemours, tells us, he decided that commerce should "never be ransomed or regimented": he adopted "this maxim, *Laissez faire et laissez passer*," "Let people do what they want, and let them and their goods go where they please."

Of course, this "let people do what they want" refers to economic decisions *within the laws of morality* (no coercion, fraud or falsehood), but unhindered by bureaucratic interference.

In Turgot's time damaging intervention in business by the government was known as *mercantilism*. Today it is known as *interventionism*, as defined earlier in this article.

What the World Council of Churches decided in 1948 is that, if there is to be capitalism, then it should be of a type known as *mercantilism*, that is, detailed government regulation. The Industrial Revolution, based on *laissez faire,* burst loose from the restrictionism of mercantilism, which had involved such a high death rate of children that the population was practically stationary. Under the new laissez-faire system conditions immediately improved so drastically that the death rate of children decreased greatly. The *first* consequence of their survival was that they had to go to work early, under adverse conditions; the price of their surviving was that they had to go to work very young; that was *inevitable;* only an outright miracle of God could have prevented that *in the transition period,* and such a miracle would have been contrary-to-purpose. But the *eventual* consequence of *laissez faire* was a steadily rising standard of living.

The World Council of Churches wishes to return to the old mercantilist system, or according to Dr. Bennett, to something even worse, namely, socialism.

Can that hurt the wealthy nations? Of course it will, but the transition down hill will be as slow maybe as the transition was up hill from mercantilism to present-day Western world prosperity.

But there are people today who will be conspicuously damaged — literally cursed — by antagonism to *laissez faire* and preference for interventionism or socialism. Those people are the teaming millions of the backward nations — backward because they have never really accepted *laissez faire,* but instead have accepted unwisely interventionism or socialism, destructive programs uncondemned by the World Council of Churches.

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Proposal On How To "Experiment" With Socialism In The United States

The purpose of this article is to recommend that in the United States a special kind of thorough experimentation with socialism be adopted. The proposed program could be a blessing to the country as a whole.

* * *

When a business grows to be large, decisions on policy become momentous. The mere size of the operation makes bad decisions costly, and sound decisions profitable.

Imagine an automobile manufacturer who is considering the use of a new air-cooled engine. The engineers of the company declare that their air-cooled engine has advantages over a water-cooled engine, being both better and cheaper. Management is faced with the decision whether or not to switch over to air-cooled engines.

That is a major decision. Manufacturing methods will have to be changed; a large investment will be needed in new tools; the public will have to be educated to the idea of a radiator-less engine; servicemen must be trained to service the radically different car. Finally, will the public buy an automobile with an air-cooled engine? Indeed, what kind of a catastrophy will the company suffer if the design change is too radical — if the proposed new model fails to perform as well as the old, or if the public will not like it?

Imagine the policy makers of the company sitting around a conference table to decide, yes or no. In a sense, the future of the company depends on the decision. If it proves to be an error, the loss in prestige, position, and profit may be fatal. On the other hand, if this new model is a big advance over present models, then what an opportunity!

Big business men, whatever their strengths and weaknesses may be, usually have courage. Except in rare cases, men who rise to the top are not weaklings. But the boldest hold back when the success of their business is to be hazarded by *one* decision — by one roll of the dice, figuratively speaking.

Various decisions can be made in the situation we have imagined: (1) rashly take the chance; (2) back away from the risk; or (3) test the idea in a limited area, carefully selected, and with the experiment closely controlled. If the experiment does not work out well, discontinue it; if it is successful as promised, then (with the test having given the needed assurance) extend it to the whole United States. Probably policy number (3) will be followed. The other alternatives are too hazardous.

* * *

In regard to socialism for the United States it is, as in our radiator-less car illustration, a momentous challenge — shall we here in the United States adopt it or not? If we do, and if it fails, the cost will be terrific. If it succeeds, that will be wonderful.

There are obviously two views in the United States about socialism — one pro and one con — just as there were advocates

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in the motor car company of (1) a radiator-less engine and (2) an unchanged, conventional water-cooled engine.

How decide: (1) do nothing, and be tormented about the idea of an opportunity lost? or (2) try out socialism on a national scale and suffer a catastrophy, as some people predict? or (3) gradually mix the two systems on a country-wide basis, that is, impose partial socialistic measures while retaining partial capitalism? This last method of experimentation does not give a clear answer; there will be continued argument whether benefits or penalties are caused by the capitalistic phase or the socialistic phase of the system.

Number (3) is the system presently being followed in the United States, unfortunately. But there is a better system for *testing* socialism and communism in the United States. The purpose of this article is to recommend that method.

* * *

This union known as the United States has 50 states. Each of these is sovereign in matters other than war, foreign affairs, issuance of money, etc. What we need are two states who will be volunteer guinea pigs — one to try out socialism thoroughly, and the other to try out laissez-faire (free) capitalism thoroughly, for a period of maybe ten years. Let us, by that approach, settle definitively which is better for the United States — socialism or capitalism. In the United States we have a favorable opportunity to experiment, because we have (or have had in theory) a truly Federal system, and each state is genuinely *sovereign.*

We should not, however, be happy about nontypical states coming forward as the experimenters. Rhode Island is too small; Maine is not typical; nor Florida, nor North Dakota. We need "mixed" states, those with some balance between agriculture and manufacture. Michigan, for example, might be a good state to experiment with thoroughgoing socialism. Ohio might be a good state to experiment with a genuine return to laissez-faire capitalism. Other states might wish the "honor," or have the required conviction, to be the experimenters. Candidates are needed.

In any event, in the momentous decision of socialism versus capitalism, we are against desperately "rolling the dice" and staking all on theoretical judgment, even our own. We happen to believe, *theoretically,* that socialism is worse than cancer, but others say that we are wrong. Those who think that should welcome the thorough testing of their own new socialistic proposal. If they admit that socialism has not worked well abroad, but declare it will work better here, let us not risk this whole, great and grand nation. Let those pro-socialist theoretists concentrate in some state, and put their ideas wholly into effect. Let us laissez-faire theorists concentrate in another state. Let us try the two systems for a reasonable number of years.

At the end of ten years the Federal aid program for distressed areas will take care of the victim or victims.

In the end, we would have a more convincing answer than can presently be obtained from nationwide experimentation with a *mixed* economy. The quicker some U. S. state experiments 100% with socialism, the better for all the rest of the states.

Every Man In Economics Is A Dr. Jekyll And A Mr. Hyde Within Himself

Dr. Jekyll And Mr. Hyde

Robert Louis Stevenson wrote an interesting story called *Dr. Jekyll and Mr. Hyde.* These names did not designate two men, but one. In the daytime this man was an honorable physician, Dr. Jekyll, but at night a marauder and thief, Mr. Hyde; a dual personality.

In economics, every man is in a sense a Dr. Jekyll and a Mr. Hyde. He is Dr. Jekyll as a consumer; and he is Mr. Hyde as producer; a dual personality. Only when a man lives in complete isolation, by himself alone, and produces only for his own consumption, is there an identity within him as producer and as consumer. But at once, when there is more than one person involved and when there is division of labor and exchange of surplus products between them, a man's interests as a consumer begin to conflict — or *appear* to begin to conflict — with his interests as a producer. In any kind of *organized* society a man is in many respects separately and distinctly a consumer *and* a producer.

Now if such a man makes his basic decisions on how to "organize" society from the viewpoint of himself *as consumer* he is, in economics, as sound as Stevenson's respectable physician in daytime, as Dr. Jekyll. But if such a man makes his basic decisions on how to "organize" society from the viewpoint of himself *as producer* he is, in economics, as destructive as Stevenson's Mr. Hyde, a prowler and robber in the dark.

The idea can be illustrated in several ways.

A man as member of a labor union is a producer. This same man as head of a family is a consumer. As a producer and labor-union member he decides he wants more money; eventually he strikes to get it, and let us assume that he does. He has "helped" himself as a producer. But he has also hurt himself. The prices of what he produces go up; his cost of living rises. Labor rates are "costs" and must eventually be reflected in prices. (As an aside, it may be mentioned that the idea that labor rates can be increased *at the expense of capital ownership* — and consequently that one can benefit himself as producer without hurting himself as a consumer — is a pleasant idea to coddle in one's mind, but careful reasoning will completely dispel that hallucination. See Böhm-Bawerk's *Control or Economic Law* for the complete argument.)

Experience is proving daily that advancing labor rates can mean increased cost of living. The labor unions are operating as a cat chasing his tail; first, labor rates are forced up, by strikes if necessary to that end; then cost of living rises; then increase in cost of living becomes ground for another increase in labor rates. In this situation, a man's economic policy is controlled by his *viewpoint as a producer*. He is operating like a man who demands — give me what you have and what I want.

It may be thought that the consequences mentioned can be escaped. A man may say: "I will force my wages up *more* than others; then, *I* shall gain." True; what he produces goes up more in price for all consumers than their prices go up for him. But two — in fact all — can play at that game, and they surely will. Men discover that you are endeavoring to "rob" them. They retaliate by attempting to "rob" you. What labor leader has a chance of surviving who does not get wage increases comparable to what other labor leaders get (unless there are insuperable economic obstacles such as competition from substitutable products, or overproduction in an industry)? Under *present* rules, the competitive policy of labor leaders is fully justified. The rules are wrong.

(2) A retailer may think similarly; he may decide that he will arbitrarily raise his prices 5%; he is looking at himself as producer (distributor), not as consumer. But his customers leave him, unless he has a monopolistic and coercive organization too, which sees to it that other retailers raise their prices equally. Of course, if such a coercive organization does not exist, and if it is not protected by special laws in its special privilege of exploitation, the program of the individual retailer will fail. Others will not raise their prices; they will sell to his customers; he will go bankrupt. The reason is that it was against the self-interest of his customers to buy from him at a noncompetitive price.

(3) A manufacturer is in a similar case. He manages his business to serve his consumers, or he manages it to serve himself. The assumption often is that the most successful manufacturer is the one who gives the least product for the most money. In fact, it is the reverse: the most successful manufacturer is he who improves his methods of manufacture and distribution, thereby reducing his cost, so that he is able to offer the most product for the least money.

It *appears* that a business man offering lower prices and better merchandise does not seem to be motivated by great love for his customers nor by an urge to help them; it appears — and correctly so — that he is endeavoring to help himself. That is true, but in a more important sense it is false. There are *presuppositions* in the mind of this capitalist, profit-seeking business man. First, he avoids coercion of his customers; because, and just because, he leaves them free, he must exert himself to offer them more if possible than anybody else does — more product for less money. Otherwise they will not prefer to buy from him. In that sense, his decisions are fundamentally motivated by his customers' welfare rather than his own. Secondly, he assumes these potential customers will not be motivated significantly by anything else than their self-interest. If he assumed that they did not know what their self-interest is (to get the most for the least), or that they would be negligent about buying something costing more but worth less from some other manufacturer, then what would be the use of offering the most for the least. Obviously, when you leave your potential customer *free,* you in effect put it in his power to make you exert yourself always to offer the most for the least. Your neighbor is sovereign, not yourself. In this case, you operate as a Dr. Jekyll. If contrarily, you operate as a monopolist, in *restraint* of trade, that is, when you fall back on *coercion,* then you have changed character and are a Mr. Hyde. (Monopoly and restraint of trade are properly prohibited and enforced against business men, but improperly are not enforced against labor unions.)

What Religious Ethics Has To Say About Self-Orientation In Society As Producer Or Consumer

The decalogue of Moses — the well-known Ten Commandments — cannot be abbreviated without irreparable loss, but it is difficult to demonstrate that all of the ten are of equal rank. If the two most important are chosen, one out of the First Table and one out of the Second, then the First and Sixth Commandments probably outrank the others in each group The first is, Thou shalt have no other gods before Me; and the sixth is, Thou shalt not kill (coerce). This latter commandment is pertinent here.

The *ultimate* recourse of anyone who wishes to exploit his neighbor is the exercise of power, that is coercion. When seduction, theft, fraud and coveting fail to accomplish the purposes of an evil man, his final recourse is to coercion. If prospective victims know that a would-be aggressor can never have recourse to coercion, their will to resist seduction, theft, fraud and coveting is strengthened. They will say to themselves, "If we resist those methods successfully, then we have nothing more to fear." But if they must think differently, namely, that although they resist seduction, theft, fraud and coveting successfully, they must still face a worse and maybe overwhelming coercion, then much of their will to resist may be expected to be lost. *Thou shalt not coerce* is then probably the most important of the *ethical* commandments. The general case of Hebrew-Christian ethics pretty much stands or falls with this ultimate ethical demand — *no coercion* (except to resist evil).

This Sixth Commandment, Thou shalt not coerce, should be controlling in economic matters as in all others. The questions then are: (1) does a man avoid coercion if his ethics are oriented according to his activities as a *producer?;* and (2) does a man avoid coercion if his ethics are oriented according to his activities as a *consumer?* The answer to the first question is, *No;* when a man makes claims for himself *as producer* he becomes a coercer.

The answer to the second question is, *Yes;* when a man limits his making of claims for himself to his activity *as a consumer,* then he avoids becoming a coercer.

These systems are either/or; a man has no escape from making a choice; he is both a producer and a consumer in his own single person, but his *public* policy must be based on his orientation of himself in society in one category *or* the other.

Attempted solutions of this problem are subject to "confusilation" if the person looks at producers and consumers as two entirely different classes, unrelated to each other. *The fact is that everybody is within himself both producer and consumer. As one person he can have his ultimate liberty as consumer or as producer, but he cannot have both liberties. They are inconsistent with each other.*

Now, a man can be inconsistent. He can say something like this: "(1) I want my own way in regard to my production; people *must* accept what I produce at my price; but (2) when I change roles and become a consumer, then I want the rule to be reversed; they must not have the right to coerce me to take what they produce at their price; I demand having my way as consumer when I consume and as producer when I produce." Such rules of action would not be *general* rules. If the rule prevails for one, it should in justice prevail for all, and that in this case involves an impossibility. Only *general* rules are suitable for sound public policies.

If a man insists on having his own way as a producer and is prepared to grant that same privilege to everybody else, then consumers must be *compelled* to accept what is produced. This is violation of the Commandment, Thou shalt not coerce.

If a man insists on having his own way as consumer and is prepared to grant that same privilege to everybody else, then he and they as producers must be prepared to produce what is wanted, or else find no market.

Production is not for production's but consumption's sake. There is no merit in work in the abstract. Work is not good because Scripture alleges God has said that work is a good thing. Scripture presents what it alleges God says about work because work yields products valuable to consumers. If work yielded products valueless to consumers, work would not be praised in Scripture, nor anywhere else.

The Contrasting Answers Of Socialism And Capitalism

The differences between capitalism and socialism can be viewed from many viewpoints. But if we view them from the viewpoint of the subject under discussion — in what should a man's freedom be dominant, as a producer or as a consumer — then capitalism's answer is that a man should "have his way" as a consumer; and socialism's answer is that a man should "have his way" as a producer. The former promotes a free, rich and peaceful society. The latter promotes an unfree, poor and bellicose society (see Walter Lippmann's *The Good Society*).

In economics, the question whether a man within himself should be sovereign as consumer or producer takes the form of: what should determine price, (1) the *cost* to the producer in production (cost-plus), or (2) the *value* to the consumer in consumption (the market)? The socialist answer is that an ethical price must be based on the cost of production. The capitalist answer is that an ethical price must be based on the value to the consumer in his own estimation. These are two irreconcilable ideas. Either capitalism is right and should prevail, or vice versa, socialism.

What Term Stands Opposite To Coercion

The churches appear to be struggling with the term — and the idea — which should be used as the opposite of *coercion*. The churches cannot accept, if they heed the Hebrew-Christian Scriptures, coercion as a principle for the ordering of society, except to restrain recognized internal and external evils. How should the rest of social life be ordered?

The prevailing answer is that the opposite of coercion is *charity*. Many carry the *charity* principle to such an extreme that they declare that if charity (which is really voluntary in nature) does not operate fully, then coercion must be employed to enforce charity and becomes part of it; Peter is to be robbed to pay Paul, in the name of "justice" of some vague kind; and the slogan becomes, From each according to his abilities to each according to his need, which is perfect, coerced charity. *Charity* is the wrong antonym for *coercion*.

Many, too, look upon *competition* as an alternative system, but one that is to be rejected, in part or in whole, because it is a "warfare," a "cut-throat" system, a "competitive struggle," a "price *war*." But these are metaphors — mere figures of speech — not happily chosen, because competition is not war to destroy, nor struggle to injure, but rivalry to serve consumers who are free — in order to receive their patronage. In a free society he who serves best gets the business, the consumer being sovereign. *Competition* is not the word that describes the system itself, but only the method of that system which stands over against coercion.

Opposite to the evil known as coercion, as a system for organizing society, there must be some "good" which must have its proper name. That opposite — that alternative — cannot be charity, because charity as the principle for organizing society is as great a curse as is coercion. The "good" which is the real antonym to coercion, as the *organizing principle* of society is *cooperation* in the Ricardian sense (see Volume IV, No. 7, pp. 207-224). Of course, the principle of cooperation is not understood unless Ricardo's Law of Association is understood.

Proposal To Outbid Other Politicians

Edmund Burke has called attention to a problem for political leaders in a popular type government, namely, that they would be under inescapable inducements to outbid each other in promises of what they would, if elected to office, be doing for the voters. He described the situation in these words in his *Reflections on the Revolution in France* (Regnery Press, Chicago, Gateway edition; page 346):

> . . . To make a government requires no great prudence. Settle the seat of power; teach obedience; and the work is done. To give freedom is still more easy. It is not necessary to guide; it only requires to let go the rein. But to form a *free government;* that is, to temper together these opposite elements of liberty and restraint in one consistent work, requires much thought, deep reflection, a sagacious, powerful, and combining mind . . . But when the leaders choose to make themselves bidders at an auction of popularity, their talents in the construction of the state, will be of no service. They will become flatterers instead of legislators; the instruments, not the guides, of the people. If any of them should happen to propose a scheme of liberty, soberly limited, and defined with proper qualifications, he will be immediately outbid by his competitors, who will produce something more splendidly popular. Suspicions will be raised of his fidelity to his cause. Moderation will be stigmatized as the virtue of cowards; and compromise as the prudence of traitors: until . . . the popular leader is obliged to become active in propagating doctrines, and establishing powers, that will

> afterwards defeat any sober purpose at which he ultimately might have aimed.

Under that inducement ourselves — to obtain the goodwill of others — we shall outline what we believe will be good for the citizens of the United States. We shall outline a program to establish what Burke designates as a *free government,* in contradistinction from what he decries as mere *government* (tyranny), and what he disparages as mere *liberty* (which here means anarchy).

This program — to obtain popular approval — we propose to call a *Constitutional Welfare Platform.* We have given consideration to the term, *Constitutional Liberty Platform,* but have decided that presently voters are more interested in welfare than in liberty, and so the title we are selecting is: constitutional *welfare* platform.

In this unashamed appeal to the welfare or self-interest of the people we again quote Burke, this time in defense of efforts to please voters; he wrote (page 346):

> Neither do I wholly condemn the little arts and devices of popularity. They facilitate the carrying of many points of moment; they keep the people together; they refresh the mind in its exertions: and they diffuse occasional gaiety over the severe brow of moral freedom. Every politician ought to sacrifice to the graces; and to join compliance with reason [i. e., bend some with the wind as well as be rigorously logical].

We are out to please voters as much as we can. We shall "join compliance with reason."

Nor do we believe that any voter needs to be ashamed to use his own *self interest* as his guide. We approve his self-interest, and we advise him to be guided by it. *Self interest* is the most fundamental principle of society, as the Hebrew-Christian religion, source of the accepted system of ethics in Western society, has taught for 3300 years; (see preceding issues).

The moment that that *assumption,* that people will do what is in their own genuine self-interest, must be abandoned, then all "calculation" collapses, and foresight fails. On what basis, other than that men will be motivated primarily by their self-interests, can people be expected to act in a manner which is *predictable.* If they acted universally on some vague idea of *righteousness* unrelated to self, they would not be knowing what they were doing, and if they themselves were not well-informed on what thy were doing, how could another person predict what they would do. In matters of human action, the pursuit of self-regarding interests is the "rationalizing" factor. It is, therefore, a form of intellectual innocence to pretend that self-motivation is immoral. It is also a manifestation of intellectual innocence to consider that the pursuit of self-motivated interests *in politics* is immoral.

Self-regarding interests to which reference is made are assumed to be *enlightened* self-regarding interests. A bank robber pursues his self-regarding interests, but by a method which is short-sighted. A swindler pursues his self-regarding interests with zeal, but his means to attain his ends are not *eventually* suitable; he will come to be known as a man who swindles, and people will not deal with him any more.

And so we shall endeavor to cater to the people's self-interest, with that self-interest pursued in a *far-sighted,* moral manner; or in even more universal terms, with that self-interest pursued in an *effective* manner, that is, by *means truly suited to the end.*

When something is declared to be immoral, nothing more can be meant than that the principle involved cannot be made to function *universally* — is not good for everybody to employ. For something to be *moral,* it must be applicable universally in time, place and circumstance, and be for all people.

The self-regarding interests of a man are, of course, not strictly personal, but extend beyond himself to include wife and children; parents, brothers and sisters; friends and neighbors; country; church; fellow members in private associations of all kinds. His values and motivations are *his own* choices but the benefits are not for *himself alone.*

In outlining a Constitutional Welfare Platform, we shall discuss four subjects: (1) *Economic Security;* (2) *Justice;* (3) *Political safety;* and (4) *Prosperity,* for all men without immoral discrimination. Under Economic Security we shall begin by discussing booms and depressions; see later articles in this issue.

An Alternative To Denying People The Right To Vote

People who themselves think correctly on political questions are alarmed when they see unsound and disastrous policies being pursued throughout the world. They sometimes conclude that there will be no future stability except by restricting the franchise — the right to vote. They retreat to the idea that only *wise* people should vote. We have toyed with that idea ourselves, and although it has merit, it is, basically, a dubious idea; we shall briefly explore it, in order to indicate its dangerous character.

The idea of restricting the right to vote has a distinguished pedigree. Aristotle indicated that government should rest in the "superior parts" of society. Democracies of old did not provide widespread privileges of citizenship. In the oldest democracy whose history is well-known — that of Athens — there were relatively few citizens and a substantial number of slaves. Plato in his *Republic* (whose cardinal points, as everybody should know, included communism, free-love and infanticide) provided for a limited group of rulers at the top who were to be "philosopher-kings." Lord Macaulay, English historian, unsympathetic to participation in the franchise by those who did not give evidence of solidity by owning property, indicated he expected dire consequences from manhood suffrage in the United States, but he did not go into details but rested his case by saying, just wait and see what the Twentieth Century will do to the United States! (See his essay, *Mill on Government.*)

On the other hand, a completely unrestricted franchise has few advocates. Minors and felons are prohibited from voting in the United States. The right to vote is therefore not an indefeasible right.

It is worth while to consider why facile recourse to restricting the right to vote is dangerous. It is easy to say: Smith is not to be permitted to vote, because he is not qualified. That may be a fact, but the excuse for prohibiting him from voting should not be readily accepted.

In this publication there has frequently been critical comment about the idea that each man is his "brother's keeper" in the socialist sense of the term, or in the sentimental sense of the term as used by moralists. That proposition is believed to have no merit and to be more destructive to the recipient of the "loving-kindness" than to the giver.

The law of Moses legislates against injuring the neighbor, in the commandments forbidding violence, adultery, theft, fraud, coveting. All else is *free;* do what you please. Basically the *law* legislates freedom, not altruism (see previous issues).

But (it must be admitted that) the law of Moses legislated more than freedom. It also legislated *charity* — in a limited amount. Unlimited charity would make a man his "brother's keeper." But nowhere in the Old Testament is unlimited charity required. *Charity,* properly understood, is not a disguised substitute of slavery, that is, for making a man a slave under the guise of being obligated to exercise unlimited charity.

Moses also legislated a "gospel." The Mosaic Law was required to be taught. It is true, the Law was not required to be taught to foreigners in a foreign-mission enterprise. The *restriction* of the teaching of the Law to ancient Israel is a questionable phase of Israelitish legislation. But *within* Israel, each Israelite was obligated to help members of his family and other Israelites keep their thinking straight, by teaching the Law to them. In *that* sense, each Israelite was his "brother's keeper," and what he taught was a vital part of the "gospel" in that dispensation.

In the New Testament two features were added to what Moses taught; or more correctly, one thing was *added* to the substance of the Law; the other was a revolutionary clarification of the *extent of the application* of the Law.

What was added to the *substance* of the Law in the form of required teaching was a broader gospel: (1) it included even more clearly than before, salvation by the *mercy of God,* resurrection and immortality. This was a net addition to the content of the "gospel," because the Old Testament is not very vocal about resurrection and immortality, and had only a symbolic ritual to foreshadow the mercy of God. As the Old Testament required each Jew to proclaim the Law, so the New Testament requires the proclamation of the reality, salvation by grace. But the New Testament also was a broader gospel; its gospel was for *all* men and was required to be proclaimed to others than Jews. The substance of the gospel was enriched and its proclamation broadened.

But the really great improvement in the ethical content of the New Testament was the extension of the *application of the Law* in a unique sense. It is *this extension of the application* of the Law which constitutes the revolutionary ethical idea in the Sermon on the Mount and elsewhere in the Gospels. This *extension of the application* of the Law consists herein that a violator of the Law is declared never to forfeit and to lose the protection of the

Law himself. Jewish interpreters of the Law had taught that if *A* violated the Law against *B*, then *B* could retaliate against *A*. In effect, every failure to obey the law became a ground for a new violation of the law by the victim against the first culprit; an "eye for an eye, and a tooth for a tooth", etc. The Law, by such interpretation, eventually did not even control nonsinners; for once there was a wrong perpetrated, then the whole system was in effect annulled by permitting retaliation and vengeance. Christ's teaching, *in a revolutionary sense,* rejected that misinterpretation of the Law. He legislated forbearance, forgiveness, long-suffering, and gave a perfect example of it in His life. He sealed the paramount importance He ascribed to forbearance by His own death. This is the great *extension* in the ethical teaching of Christ. It was not an addition to the substance of the Law, but a declaration of the *universality* of the Law, the Law was not to be abrogated by *B* on the excuse of a prior violation by *A*.

What then is the gospel? Telling people what is necessary to get *all* of their thinking straight. Getting their thinking straight pertains to getting along better in this life, and preparing for the life to come. In ethics (and this is a publication in ethics) men are, by this approach, their neighbor's keeper in a *special* sense; they are required to exert themselves in-season and out-of-season to help get the neighbor's thinking straight. Beyond that point (except for true, that is, *limited* charity) no one is his neighbor's keeper in any sense.

We come finally to the relation between the right to vote and the law of brotherly love. Why are men inclined to wish to limit the franchise only to the wise and the good? Why do they say to other men: we do not want *you* to have the right to vote?

Men approach the right to vote in that manner, maybe because of a prior deficiency in their own conduct: maybe they *have not put forth enough effort earlier to get their neighbor's thinking straight so that they will be happy about his having the right to vote.* Because men have been deficient in preaching the ethical part of the "gospel", they desire to resort to reducing another's influence in politics and society in proportion to his estimated disqualification.

The people of this country vote for legislators. The legislators in turn vote for the kind of laws people want. The people, through their legislators, demand, in regard to money and credit, legislation of a certain kind. Now, if one thinks, as we do, that what people in the United States think today on money and credit is erroneous and eventually catastrophic, two approaches can be made: we can say: (1) deny those people the franchise and the right to vote; let only those people vote who think straight on matters of money and credit, or (2) try to get people's thinking straight on money and credit.

We are making the second approach. We shall begin, in what follows, to explain what might be called the "gospel" (what we think is sound logic and good news) in regard to important questions about money and credit. Instead of saying that people in this country, who are destroying it by unsound money and credit policies, should be prohibited from voting, we submit instead for consideration analyses of money and credit problems, in order to influence their thinking.

Marx's Legitimate Critique Of Booms And Depressions

The yearning for "security", prompted by self-interest, is a wise and worthy motivation. Prudent men are cautious because they have a strong motivation based on fear. Thrifty people are thrifty, because they have a strong sense of insecurity, and by their thrift seek to protect themselves against insecurity. The more calculating a person is, the more obviously he is motivated by a fear-inspired striving for security.

In a society which has an elaborate *division of labor*, jobs are insecure for such reasons as changes in demand, obsolescence of products, exhaustion of natural resources, calamities (so-called acts of God), miscalculations, etc. — and finally because of the *business cycle* — those alternating booms and depressions that everybody knows about and fears with terror. It is this last-mentioned cause of insecurity, general booms and depressions, to which attention is here being given.

Those booms and depressions (also called business crises) are considered to be inherent in the capitalist system. At any rate that was Karl Marx's conclusion. Marx and Friedrich Engels in 1848 wrote *The Communist Manifesto*: we shall quote first what they wrote therein about the rise of the *bourgeoisie* (pages 11-16), that is, the property-owning classes, or in other words, what they wrote about *Capitalism.* Note the mixture of criticism and praise, and the emotional, anti-intellectual approach. The reader should be wary of accepting this version of reality. Some things written are true, but some are in error. (When reading the quotation, the word *capitalism* can everywhere helpfully be substituted for *bourgeoisie;* for example, in the first line: [Capitalism], historically, has played a most revolutionary part." (Our italics.)

> The bourgeoisie, historically, has played a most revolutionary part.
>
> The bourgeoisie, wherever it has got the upper hand, has put an end to all feudal, patriarchal, idyllic relations. It has pitilessly torn asunder the motley feudal ties that bound man to his "natural superiors," and has left remaining no other nexus between man and man than naked self-interest, than callous "cash payment." It has drowned the most heavenly ecstasies of religious fervor, of chivalrous enthusiasm, of philistine sentimentalism, in the icy water of egotistical calculation. It has resolved personal worth into exchange value, and in place of the numberless indefeasible chartered freedoms, has set up that single, unconscionable freedom — Free Trade. In one word, for exploitation, veiled by religious and political illusions, it has substituted naked, shameless, direct, brutal exploitation.
>
> The bourgeoisie has stripped of its halo every occupation hitherto honored and looked up to with reverent awe. It has converted the physician, the lawyer, the priest, the poet, the man of science, into its paid wage-laborers.
>
> The bourgeoisie has torn away from the family its sentimental veil, and has reduced the family relation to a mere money relation.
>
> The bourgeoisie has disclosed how it came to pass that the brutal display of vigor in the Middle Ages, which Reactionists so much admire, found its fitting complement in the most slothful indolence. It has been the first to show what man's activity can bring about. It has accomplished wonders far surpassing Egyptian pyramids, Roman aqueducts, and Gothic cathedrals; it has conducted expeditions that put in the shade all former Exoduses of nations and crusades.
>
> The bourgeoisie cannot exist without constantly revolutionizing the instruments of production, and thereby the relations of production, and with them the whole relations of society. Conservation of the old modes of production in unaltered form, was, on the contrary, the first condition of existence for all earlier industrial classes. Constant revolutionizing of production, uninterrupted disturbance of all social conditions, everlasting uncertainty and agitation distinguish the bourgeois epoch from all earlier ones. All fixed, fast-frozen relations, with their train of ancient and venerable prejudices and opinions, are swept away, all newly-formed ones become antiquated before they can ossify. All that is solid melts into air, all that is holy is profaned, and man is

at last compelled to face with sober senses, his real conditions of life, and his relations with his kind.

The need of a constantly expanding market for its products chases the bourgeoisie over the whole surface of the globe. It must nestle everywhere, settle everywhere, establish connections everywhere.

The bourgeoisie has through its exploitation of the world-market given a cosmopolitan character to production and consumption in every country. To the great chagrin of Reactionists, it has drawn from under the feet of industry the national ground on which it stood. All old-established national industries have been destroyed or are daily being destroyed. They are dislodged by new industries, whose introduction becomes a life and death question for all civilized nations, by industries that no longer work up indigenous raw material, but raw material drawn from the remotest zones; industries whose products are consumed, not only at home, but in every quarter of the globe. In place of the old wants, satisfied by the productions of the country, we find new wants, requiring for their satisfaction the products of distant lands and climes. In place of the old local and national seclusion and self-sufficiency, we have intercourse in every direction, universal interdependence of nations. And as in material, so also in intellectual production. The intellectual creations of individual nations become common property. National one-sidedness and narrow-mindedness become more and more impossible, and from the numerous national and local literatures there arises a world-literature.

The bourgeoisie, by the rapid improvement of all instruments of production, by the immensely facilitated means of communication, draws all, even the most barbarian, nations into civilization. The cheap prices of its commodities are the heavy artillery with which it batters down all Chinese walls, with which it forces the barbarians' intensely obstinate hatred of foreigners to capitulate. It compels all nations, on pain of extinction, to adopt the bourgeois mode of productions; it compels them to introduce what it calls civilization into their midst, i.e., to become bourgeois themselves. In a word, it creates a world after its own image.

The bourgeoisie has subjected the country to the rule of the towns. It has created enormous cities, has greatly increased the urban population as compared with the rural, and has thus rescued a considerable part of the population from the idiocy of rural life. Just as it has made the country dependent on the towns, so it has made barbarian and semi-barbarian countries dependent on the civilized ones, nations of peasants on nations of bourgeois, the East on the West.

The bourgeoisie keeps more and more doing away with the scattered state of the population, of the means of production, and of property. It has agglomerated population, centralized means of production, and has concentrated property in a few hands. The necessary consequence of this was political centralization. Independent, or but loosely connected provinces, with separate interests, laws, governments and systems of taxation, became lumped together in one nation, with one government, one code of laws, one national class-interest, one frontier and one customs-tariff.

The bourgeoisie, during its rule of scarce one hundred years, has created more massive and more colossal productive forces than have all preceding generations. Subjection of Nature's forces to man, machinery, application of chemistry to industry and agriculture, steam-navigation, railways, electric telegraphs, clearing of whole continents for cultivation, canalization of rivers, whole populations conjured out of the ground — what earlier century had even a presentiment that such productive forces slumbered in the lap of social labor?

We see then: the means of production and of exchange on whose foundations the bourgeoisie built itself up, were generated in feudal society. At a certain stage in the development of these means of production and of exchange, the conditions under which feudal society produced and exchanged, the feudal organization of agriculture and manufacturing industry, in one word, the feudal relations of property became no longer compatible with the already developed productive forces; they became so many fetters. They had to be burst asunder; they were burst asunder.

Into their places stepped free competition, accompanied by a social and political constitution adapted to it, and by the economical and political sway of the bourgeois class.

A similar movement is going on before our own eyes. Modern bourgeois society with its relations of production, of exchange and of property, a society that has conjured up such gigantic means of production and of exchange, is like the sorcerer, who is no longer able to control the powers of the nether world whom he has called up by his spells. For many a decade past the history of industry and commerce is but the history of the revolt of modern productive forces against modern conditions of production, against the property relations that are the condition for the existence of the bourgeoisie and of its rule. *It is enough to mention the commercial crises that by their periodical return put on trial, each time more threateningly, the existence of the entire bourgeois society. In these crises a great part not only of the existing products, but also of the previously created productive forces, are periodically destroyed. In these crises there breaks out an epidemic that, in all earlier epochs, would have seemed an absurdity — the epidemic of overproduction. Society suddenly finds itself put back into a state of momentary barbarism; it appears as if a famine, a universal war of devastation had cut off the supply of every means of subsistence; industry and commerce seem to be destroyed; and why? Because there is too much civilization, too much means of subsistence, too much industry, too much commerce. The productive forces at the disposal of society no longer tend to further the development of the conditions of bourgeois property; on the contrary, they have become too powerful for these conditions, by which they are fettered, and so soon as they overcome these fetters, they bring disorder into the whole of bourgeois society, endangering the existence of bourgeois property. The conditions of bourgeois society are too narrow to comprise the wealth created by them. And how does the bourgeoisie get over these crises? On the one hand by enforced destruction of a mass of productive forces; on the other, by the conquest of*

> *new markets, and by the more thorough exploitation of the old ones. That is to say, by paving the way for more extensive and more destructive crises, and by diminishing the means whereby crises are prevented.*
>
> The weapons with which the bourgeoisie felled feudalism to the ground are now turned against the bourgeoisie itself.

The propositions of Marx and Engels in the foregoing are (1) that capitalism has a wonderful record behind it, (2) that capitalism, however, has an inherent defect, namely, alternating booms and depressions, with the depressions called *crises*, (3) the crises will get worse and worse; and (4) that these booms and depressions are really uncontrollable by capitalism; "modern [capitalism] has conjured up such gigantic means of production and of exchange, [that it] is like a sorcerer, who is no longer able to control the powers of the nether world whom he has called up by his spells." Obviously, if that is true, the situation is bad.

What are the facts?

1. Business crises are indeed a characteristic feature of modern capitalism. This is an indefensible defect. A business crisis terrifies people, because they do not really understand how it works or why. But crises are not an *inherent* characteristic, but a voluntary and correctible characteristic of capitalism.

2. Capitalism is charged with being the *cause* of business crises, but that cause is nowhere demonstrated by Marx or Engels. It is certain that they did not have the slightest understanding how the real causal mechanism producing business crises worked. They were able to see the *effect,* deplore it, rail against it, and then they ascribed it to capitalism which they hated.

3. The cure which they suggest for the situation is to liquidate capitalism entirely. For that purpose they outlined ten steps; as follows (pages 32-33); again the italics are ours:

> The Communist revolution is the most radical rupture with traditional property-relations; no wonder that its development involves the most radical rupture with traditional ideas.
>
> We have seen above, that the first step in the revolution by the working class, is to raise the proletariat to the position of ruling class, to win the battle of democracy.
>
> The proletariat will use its political supremacy, **to wrest,** by degrees, all capital from the bourgeoisie, to centralize all instruments of production in the hands of the State, i.e., of the proletariat organized as the ruling class, and to increase the total of productive forces as rapidly as possible.

Of course, in the beginning, this cannot be effected except by means of despotic inroads on the rights of property, and on the conditions of bourgeois production, by means of measures, therefore, which appear economically insufficient and untenable, but which, in the course of the movement, outstrip themselves, necessitate further inroads upon the old social order, and are unavoidable as a means of entirely revolutionizing the mode of production.

These measures will of course be different in different countries.

Nevertheless in the most advanced countries the following will be pretty generally applicable:

1. Abolition of property in land and application of all rents of land to public purposes.
2. A heavy progressive or graduated income tax.
3. Abolition of all right of inheritance.
4. Confiscation of the property of all emigrants and rebels.
5. *Centralization of credit in the hands of the State, by means of a national bank with State capital and an exclusive monopoly.*
6. Centralization of the means of communication and transport in the hands of the State.
7. Extension of factories and instruments of production owned by the State, the bringing into cultivation of waste lands, and the improvement of the soil generally in accordance with a common plan.
8. Equal liability of all to labor. Establishment of industrial armies, especially for agriculture.
9. Combination of agriculture with manufacturing industries; gradual abolition of the distinction between town and country, by a more equable distribution of population over the country.
10. Free education for all children in public schools. Abolition of children's factory labor in its present form. Combination of education with industrial production, etc., etc.

The italics call attention to a *credit* program of Marx and Engels. The state will directly control *all* credit.

Who controls *credit* now? In the final analysis the state does, but it has some middlemen, the men we know as bankers.

What, in fact, causes booms and depressions, that is, *business crises?* To this the answer is: *VARIATIONS in credit.* All other reasons advanced — overproduction, underconsumption, or what have you — are spurious reasons.

Who controls the *variations* in credit? The bankers. Who gives them the authority to vary credit? The United States government. Through whom? Through the Federal Reserve Board, a government agency.

Now what did Marx and Engels propose? To "centralize . . .

credit in the hands of the State by means of a national bank with State capital *and an exclusive monopoly*" (our italics).

Presently, the privately owned banks in the United States are the most-regulated institutions in the country. People look upon the railroads as being in the process of being ruined by government regulations; it can correctly be affirmed that they are being regulated to a slow death by economic strangulation; (the eventual outcome will be government ownership, as in Europe). But the regulation of the banking business out-does that of the railroads. Banking is the *most-regulated* industry in the United States and really is in a worse position than the railroads. Government regulation, although steadily ruining the railroads is ruining the railroads only; but government regulation of banks (credit) is slowly ruining *the whole economy,* by causing booms and depressions, and thereby terrifying people enough so that they seek to escape to even more government control — more interventionism or socialism. Of all regulation by government, the regulation of banking has the most vicious consequences.

Some people are allergic to penicillin; the more you give them, the sicker they become; give them more and more and they will die. The action of the United States government in regulating money and credit is a penicillin to which capitalism is basically and inescapably allergic. The more that the government regulates credit according to its present pattern, the surer the whole capitalist system will die of a fatal allergy.

What did Marx and Engels propose? More penicillin for the patient who is fatally allergic; indeed, they demanded complete monopoly of credit by the state.

The origin of the business cycle lies in credit; credit (as will be explained) finds its origin in state action; and so it is the state which causes business cycles. Marx's and Engels's program consisted in giving even more power to the present source of all the trouble.

Two Kinds Of Credit — Credit Available By Brokerage And Credit Available By Right To Create Fiat Credit

The term *credit* needs definition. It has, at least, two meanings. Unless a distinction is made between these two meanings there will be confusion in all thought on money and credit.

Arbitrarily, we shall describe one kind of credit as *brokeraged credit.* Assume a man goes to a bank to borrow $1,000, and that the bank loans him the money. From where does the money come? Suppose another man has just saved $1,000 and has deposited it in the bank in a savings account. The banker will be paying the saver interest, and will of course wish to put the money to work as soon as he can. The banker is a broker between saver and borrower. He must be paid for those services. He pays himself by charging the borrower 6% interest, and paying the saver 3%. So much for the *financial* transaction.

What happens behind the scenes in the world of goods rather than in the world of money or credit? The saver curtailed his expenditures by $1,000. He reduced demand for labor and material by not buying temporarily.

But the saver's reduction in demand is balanced by the increased demand of the borrower. The latter wishes to spend $1,000 more than his income. By borrowing the $1,000 he is enabled to do so.

Everything is in balance. This brokeraged credit is a wonderful thing. It helps the saver, the borrower, the banker; it neither increases nor decreases demand for labor or goods but only transfers it. And so it just *cannot* contribute to booms and depressions.

It might be argued that the activities of savers and borrowers do not always balance each other off perfectly; but there is a quick correction of that *in a free market.* Suppose people are saving too much; the banker as broker cannot find borrowers to use the money. A banker cannot be in business for love (which is something to be profoundly thankful for), and he will refuse to pay 3% interest to savers for money he cannot lend. He will reduce the rate to 2%. Then savers will save less. Next, the banker will charge maybe only 4% interest to borrowers. There will be more borrowers, then. Soon saving and borrowing will again be in balance. The purpose of variations in the interest rates is to strike a balance between saving and borrowing.

So much for brokeraged credit, an admirable economic institution.

The second kind of credit we shall call *fiat credit,* or created credit. In this case there is no saver in the picture at all. Then, from where can the credit money come? In this case, from the banker. He is authorized by law to *create* money. He is equivalent to an authorized counterfeiter. He is authorized *by law.* He is in fact compelled, if he is to stay in business and be competitive to other banks, to issue fiat credit. There is a profit to be made from fiat credit, and the banks all use the privilege, and the privilege has been utilized up to the point that no bank can survive unless it also puts out fiat credit. The banks are not to be blamed, but the people who vote for legislators, who in turn pass credit laws as the people want. It is the *voters* who are responsible for fiat credit.

Fiat credit is based on gold reserves. Gold is considered to be the best *money* that exists. If a bank has $1,000 in gold, it is authorized by law to put out more than $5,000 of fiat credit. The important thing then for a would-be banker is to acquire gold, and to get a bank charter to issue fiat credit. Let us go back to our original interest rate computations. On $1,000 at 6% the bank collected $60 interest in a year. It paid the savings depositor 3%, or $30 a year. The gross margin for the bank was $30, which it could use to pay its operating expenses and presumably retain some as profit.

But in the case of fiat credit the operation is far more profitable. First, the $1,000 of gold belongs to the bank, and in a sense is idle. On the $5,000 of fiat credit 6% interest can be charged. That amounts to $300 a year. Without going into all the intricacies involved, this fiat credit privilege of banks is obviously a big source of income to them.

This system is known as a *fractional reserve banking system.* Behind the fiat credit granted there is a reserve which is only a fraction of the credit granted; hence the term, fractional reserve system.

The question inevitably arises: how did this system come into existence? It grew up by custom, but a fatal one. When banking as we understand it today first developed in England, the basic money metal was silver, the pound sterling. Silversmiths did the smelting of silver and were the natural custodians of silver stock. They became the first "bankers." Merchants left silver on deposit in the vaults of silversmiths. When a merchant had to pay for something, he gave his creditor an order on his silversmith to pay out silver. When a merchant received silver he sent it to his silversmith for safekeeping and refining. Eventually, merchants shortcut as much as possible the physical transfer of silver metal by passing out or accepting receipts of the silversmith. If the silversmith gave *A* a receipt acknowledging that *A* had made a deposit of 10 oz. of silver, and if later *A* was required to pay *B* for something worth 10 oz., then *A* simply gave *B* the receipt of the silversmith by which *B* could collect from the silversmith. *The receipts became money.* Mere paper became money, *as long as it was trusted.*

The silversmiths eventually discovered — and this was catastrophic — that they always had silver on hand. The *float* of receipts was such that silversmiths never had to cash all their receipts at once. And so the *dishonest* practice arose of silversmiths putting out more receipts than they had silver! They "counterfeited" silver receipts. That fatal practice has become incorporated into the banking systems of the world. As the silversmiths, originally by subterfuge, had only a fractional reserve of silver against outstanding receipts, the banks of the United States are authorized by law to carry only a small fractional reserve of gold against outstanding fiat credit. The banks in the United States are authorized to have more than five times as much "receipts" outstanding as they have gold!

What happens behind the scenes under this system, in the world of goods and labor?

First, there was $1,000 of gold mined, let us say, by a gold prospector. He could buy $1,000 worth of goods or labor for it. But he "saves" it and sells the gold to a bank. They give him money of some kind for it, no matter here what kind. The bank now owns $1,000 in gold.

The miner probably goes out and spends his $1,000 on new equipment for an expedition into the mountains for more gold. He buys goods and labor. His purchases of labor and materials "balance" the gold buried in the bank.

But the banker can loan $5,000 of fiat credit money on the basis of the $1,000 worth of gold. Here is $5,000 of *new* purchasing power. Borrowers come in. They finally are loaned all the $5,000, and they go out into markets to buy $5,000 worth of goods and labor.

What now happens is that there is a boom. All these borrowers are *new* buyers. They do not offer goods in exchange for goods they buy. They offer instead this easily acquired fiat money. The supply of goods remains the same, but the supply of money has been increased. The *new* buyers jostle out the old buyers to some extent. Previously demand and supply of goods versus money were in balance. Now the balance is disturbed by there being more money because of this fiat credit. Buyers get nervous and start bidding up prices on goods. Sellers begin to make more profits. They, fallaciously, look on the phenomenon of more money as being a case of more goods, and consequently greater prosperity. And so they expand plants, buy excessively, and say to themselves, we never had it so good.

But this boom originating in fiat credit money is an ambush. Clearly there was a surge in demand when the fiat money was created. In regard to this there are only two prospects; the surge will be either temporary or permanent. If temporary, then the "expansion" will collapse and there will be a genuine depression. Even if the boom lasts long enough to appear to be permanent, those who expand will discover that the apparent prosperity is not real, but that nothing happens except that prices continue to go up. You will not have prosperity, but pseudo-prosperity, namely, inflation.

There is a limit, set by law, to the expansion permitted by fractional reserve banking. Presently, banks must hold gold in the amount of one-fifth or one-sixth of their fiat credit outstanding. These are their gold reserves. Once the reserve limit has been reached, the banks cannot issue more fiat credit by *creation* of fiat credit, but can only *substitute* a new credit for an old. If there is a boom up to the time the reserve limit is reached (or until the banking authorities become alarmed *before* that point is reached), then, when the fiat expansion slows, ends, or reverses itself, there is inescapably a depression.

A simple illustration should suffice. Assume ten people in a society. They buy $100,000 a year on a non-inflationary (that is, non-fiat credit) basis. Everything is in balance. Each consumes on the basis of what he produces himself, or exchanges freely for what others produce. Nobody is robbing anybody else of goods. In this stable economy, without booms or depressions the law (let us assume) is changed to permit the injection of $20,000 of new fiat credit. Not one bushel more of wheat, nor one yard more of fabric, nor one pound more of steel has been produced ; but two men (of the ten) each have double the old amount to spend; instead of $10,000 they have $20,000. What will they do? They will quietly buy up with their extra $10,000, $20,000 worth of goods that the others otherwise would have bought. They "rob" the other eight. In the process, the others will discover that two of their number, not having produced a whit more, are literally robbing them (because the two are buying with their extra $10,000 each). In order not to "get left out" the others begin bidding up prices. In fact they all begin to bid higher. But in the end, the two have robbed the other eight significantly.

But these two must pay back the fiat credit, say in the second and third years thereafter, at $5,000 a year each. Then the fiat credit, we assume, is cancelled by not being renewed. Now what happens? Buying power declines *below normal* by $10,000 each year. What is produced in goods will not be saleable any more at the current prices. Either merchandise will be unsold, or prices will have to drop. Here are the purchasing power figures by years:

Normal year (without fiat credit)	$100,000	— normal
Fiat credit-extension year	$120,000	— boom
First Fiat credit pay-off year	$ 90,000	— depression
Second Fiat credit pay-off year	$ 90,000	— depression

The $120,000 year is what people call a boom year; the $90,000 years are what people call depression years. This society of ten men would have been better off if they had never had the $20,000 fiat credit. The fiat credit did not enlarge their market; it only made it unstable.

The explanation of booms and depressions is as simple as that, but all kinds of incidental features obscure this fundamental fact. It should be emphasized that increases in fiat credit *always* create *booms;* decreases in fiat credit *always* create depressions.

But the people of the United States love fiat credit. We shall later give some examples.

Bankers and business men have never been able to keep *fiat credit* on an even keel. At one time they are cautious and reduce fiat credit. At another time they are optimistic and increase fiat credit. This instability is innate in the character of fractional reserves, as we may show sometime.

The banks can easily get themselves into a position where they have no freedom of action any more in regard to fiat credit. The closer they get to those basic reserve points, the closer they are to being obligated to stop the expansion of fiat credit, and thereby ending the boom, regardless of their inclinations. They are at the end of the fiat credit rope.

It is not true that booms are good and depressions are bad. Both booms and depressions are bad. The causes of the boom underlie the causes of depression. The people of the United States will never get rid of depressions until they first discipline themselves so that they do not yearn for and obtain booms for themselves.

The theory underlying fractional reserve banking is based on the premise that theft is not an unsound policy. Morality teaches the contrary. And so does good economics. The acceptance of the principle of fractional reserve banking is not something that the present-day bankers wickedly invented. They inherited it. They do not appear to be aware that it is morally wrong. We can give examples of devoutly religious men who accepted the fractional reserve banking system, naively, although they were famous bankers as well as Christians. They never challenged the presuppositions underlying what was commonplace in banking for them.

But the socialists have challenged business crises. They are right in doing so. However, their cure is worse than the present evil which is admittedly very bad.

Examples Of Arguments For Fiat Credit

To prove mathematically as was done in the foregoing, beyond logical doubt, that variations in fiat credit are the cause of business booms and depressions nevertheless fails to convince people. They have a firm opinion that fiat credit is a blessing. We shall cite examples, one of which occurred in January of this year, and the other this month.

1. In January we were assigned seats in the dining room of a Bahamian hotel where a big convention was being held. Four shy young people came over and sat at the same table. We introduced

ourselves as Chicagoans. They introduced themselves as Canadians, from a village in French-speaking Canada. The men, who were brothers, were retail dealers in heavy equipment; the women were their wives. The maximum age maybe of any of the four was 35. The youngest woman was maybe 25. One of the men did not speak English; the older brother and the two women did.

People in French-speaking Canada are in politics generally members of the Liberal Party of which Mr. St. Laurent, a distinguished French Canadian, has until recently been head. To make conversation, we asked them about their political affiliations. They declared themselves to be Liberals. But when we asked how they had voted in the latest election (which went against the Liberals), they said they had voted Conservative, for Diefenbacher's party. We expressed astonishment.

Why had these four people, traditionally Liberals, voted Conservative? When we asked, we were given the answer by the younger woman. She said: "We voted for the conservative candidates because they are good for business." We asked why. She answered, "Under Diefenbacher it is easier to finance the sale of industrial equipment; and so we can do more business; we are making more money."

This sharp-witted young French-Canadian woman was of course referring to fiat credit. According to her, the more a government promoted fiat credit, the better that government was.

This gave me an opportunity to present the argument against fiat credit, as outlined in the previous article. The logic of that is unassailable and the reasoning is drum-tight. But the young woman was wholly unconvinced.

This was her rebuttal: "We are now able to sell the equipment only because we can get the credit, which we could not get previously. The buyer of the equipment puts it to work, *and the equipment earns enough money to pay off the loan.* The equipment pays for itself; how can credit for that purpose be bad?"

2. Last week I was riding a commuters' train home. At an inbetween station a man maybe 40-45 years old came in and sat next to me. Seeing that I was reading a book, he said with a grin, "That looks like a substantial book that you are reading." (Mises's

Theory of Money and Credit, which name he could read in the running heads of the open pages.)

Not being disposed to be responsive to conversation from strange fellow travellers, I made some noncommital remark in order to shake him off, but it did not work. Obviously, he wished to talk. My next defense was to question him: who was he, where did he live, etc. He was a chemist, living in a fashionable suburb up the line.

He volunteered that *credit* was a wonderful agency for good for society. I concurred with him, if he meant brokeraged credit (as explained in the preceding article), but dissented if he meant fiat credit, which I also defined. But he disagreed. Strangely enough, he argued exactly as the French-Canadian girl had argued at the convention in the Bahamas. He said: "You can build a chemical plant with credit, *which will pay for itself.*"

I decided to chip around the edges first, and asked him about fiat credit for purposes of consumption rather than production. "If a man," so I argued, "has the money to buy a Chevrolet, but wants a Cadillac, and borrows fiat credit to buy the expensive car, which produces no wealth and does thereby not pay for itself, then what yould you say about such fiat credit? Then, would not the creation of the fiat credit produce a temporary surge in purchasing, which had to be compensated by a corresponding reduction to below normal purchasing when the fiat credit was being paid off? There are, you must admit, no earnings from fiat credit for consumption goods as distinguished from production goods."

But he was unconvinced; he said: "Fiat credit to buy consumption goods, such as an expensive automobile, would stimulate employment, which would be a good thing."

That ended the conversation because the train had come to the station where I had to get off.

Here are two cases illustrating the remarkable confidence people have in fiat credit as a boon to society. When these people vote on credit problems, they undoubtedly vote for the wrong policy. What is the solution to the problem: (1) deny them the right to vote? or (2) try to educate them on what really happens in the case of fiat credit, so that they will abandon their plausible fallacies?

Probably, most of the intelligent citizens of the United States consider fiat credit to be as necessary a saviour for present-day economic society, as devout Christians look to a Saviour for the life to come. But fiat credit is a false saviour.

* * *

It should be clearly recognized that not only rabble-rousers and anti-property agitators demand fiat credit, but also shrewd and respected business people. They all demand fiat credit, that is, *the right to engage in fraud.*

* * *

The foregoing articles are preliminary to recommendations to be made on how to remove the cause of booms and depressions. Such recommendations will be part of the *Constitutional Welfare Platform.* Readers will sense that under *welfare* it is proposed to present economic planks in the platform; and under *constitutional,* political planks. In economics, recommendations will be based on the ideas of Ludwig von Mises; in political matters, on the ideas of John C. Calhoun.

Knight's Critique Of The Prevailing Protestant Idea About Love

Exaggeration of the meaning and requirement of *love* is characteristic of present-day Protestantism. The classic expression of this exaggeration is in Bishop Anders Nygren's book, *Agape and Eros,* where *agape* (one of the Greek words for love) is defined as being necessarily nondiscriminating in the selection of objects; and as being independent of the merit of the object; the the expression is: *agape* must be *"unmotivated."*

Nygren has had so much influence on fanaticism about love, or has so sensitively reflected the climate of current Protestant thought, that his concept of *agape* permeates nearly all protestant theory concerning private and public ethics. Nevertheless, the doctrine is (unintentionally of course) sanctimonious and ridiculous, as has been indicated in earlier issues.

Professor Frank H. Knight, internationally-known economist at the University of Chicago, is joint author with Thornton W. Merriam of a book entitled *The Economic Order And Religion* (Harper & Brothers, New York, 1945). The book presents a debate; Merriam is a religious liberal and represents the viewpoint of the social gospel. Knight approaches ethical problems from the viewpoint of economic liberalism. We are unable to agree with the theology of Merriam, or the general scepticism of Knight, but in the field of ethics our views agree with Knight's. He writes (pages 34-5):

> The Christian view holds that universal love is the will of God for man and hence the duty of man. This logically excludes intolerance, but in so doing it raises equally serious difficulties for theistic ethics. Completely undiscriminating love is clearly without significance for action, and it is doubtful whether it is defensible as right, or is possible, or even intellectually conceivable. Human love is certainly discriminating and selective. For man, or God, to love equally and in the same way everything which exists or will exist seems to be practically identical with loving nothing. Thus the religious attitude in the moral life runs into a dilemma. When men take religion seriously, they incline either toward intolerance and fanaticism or toward a purely mystical, contemplative love of God. In this attitude, one may either love in a similar mystical fashion the whole world of nature and man, as the works of the loving God, or he may hate or despise the actual world, presumably as expressing an evil or negative principle, refuse responsibility and withdraw into the life of the spirit. The loving attitude is doubtless abstractly preferable to that of hating, but there is no visible difference for conduct; both eliminate selective choice and responsible action and destroy the moral life.

Knight's critique, that "completely undiscriminating love is without significance for action, and it is doubtful whether it is defensible as right, or is possible, or even intellectually conceivable," is (as we see it) a correct conclusion, couched in mild and polite language. Protestantism needs nothing so much as a purging of its sanctimony about *agape*.

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Contents

One Cause Of A Shortage Of Money

A "shortage" of money may be caused by the quantity being increased rapidly. If the question is asked how that can be, the answer is: when the quantity of money is being increased rapidly (as in rampant inflationism), sellers know that, and realize that they must charge prices high enough now so that when they will be buying later with the money they get from the current sale, they will have enough to buy at the higher prices prevailing at that future date, even though it is not distant. In other words, *price increases will have a tendency to move up faster than the printing presses can print money.* Such price increases are a type of defensive action by sellers to avoid suffering a shrinkage in their capital in the interval before they buy again.

The imagination of men can easily outrun the printing presses in the world. The pace at which prices are increased has a tendency to become furious because it is fired by fear of inflationism.

An *apparent* shortage of money, therefore, will be caused by an increase in money, if the current and prospective increase is known to sellers or is feared by them.

Hume: More Money Merely Raises Prices

An increase in the quantity of money does not increase the quantity of products. It only increases prices, not prosperity. Hume stated that clearly when he wrote in his essay "Of Interest" in his *Essays Moral, Political and Literary* (Grant Richards, London, 1903):

> "All augmentation [of money] has no other effect than to heighten the price of labour and commodities; and even this variation is little more than of a name. In the progress towards these changes, the augmentation may have some influence, by exciting industry; but after the prices are settled, suitable to the new abundance of gold and silver, it has no manner of influence."

The "issue" between the Canadian lady (to whom we referred in the preceding issue) who believes that increasing the quantity of money increases prosperity, and Hume, who held that increasing the quantity of money merely increases prices, is obvious.

(Note: The Canadian lady's argument involves what is known in technical economics as "forced savings," which some people may favor because they believe it affects aggregate production.)

Laughlin And Mises On An Important Phase Of An Alleged Money Shortage

J. Laurence Laughlin in *The Principles of Money* (Charles Scribner's Sons, New York, 1921) on page 413 wrote (our italics):

> . . . A man who needs means of payment is too apt to think "money" is scarce, or hard to get, when *in reality he is suffering from a scarcity of salable goods or securities.* In a time of stringency each man is thinking of how he can get the means to meet his obligations when due . . .

Why cannot a man meet his financial obligations when they

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are due? Usually, because (1) he has not produced at all, or successfully enough, to have merchandise for sale which will yield him the money he needs, or (2) he has at least miscalculated the time when he would have produced enough to obtain by sale the money he needs.

If people, in *ordinary* times, have not enough money to buy what they think they need, it is because they themselves have not first produced enough of what others want, and which could be sold to them. (In an acute crisis, that is, in *extraordinary* times, there will be another cause operating to create a money shortage. This will be discussed in a later issue.)

Mises has summarized the situation in his *The Theory of Money and Credit* (Yale University Press, New Haven, Connecticut, 1953), page 441:

> Inflation and credit expansion are the means [which are advocated or employed] to [obscure] the fact that there prevails a nature-given scarcity of the material things on which the satisfaction of human wants depends.

The trouble is a scarcity of real things. The solution which will solve the problem is *more production.* But instead many people turn to a wholly different solution, *more money* — more pieces of paper, more fiat credit.

According to the ancient Hebrew Scriptures, even the first man was told that there would be material shortages — and that prosperity would be attained only by work, by *more production* (Genesis 3:17c). If Moses had been as unrealistic in his thinking as some modern people are, he would not have written: "in *toil* thou shalt eat [from the fruits of the earth] all the days of thy life"; but instead: "by creating fiat credit (printing paper money or its equivalent) thou shalt eat [from the fruits of the earth] all the days of thy life."

Simply to contrast the two ideas is to make it obvious that Moses was not deceived about what was needed for people to be better off; what was needed was *work, not money in the form of fiat credit.*

The Counterfeiter's Sin

If a government may manufacture money, why may not an individual do the same thing? If it is morally right for a government to manufacture money, or to authorize certain people to manufacture money (let us say, bankers), then it should be morally right for any individual to manufacture money. It is a poor rule which does not apply equally to everybody.

Wherein does the *sin* of manufacturing money (fiat credit) exist?

Money problems are intricate and confusing unless a man has a knowledge of certain basic ideas regarding money. For our purposes here we shall accept the idea of money as a *medium of exchange*. Money exchanges for goods. A man acquires money by producing goods or services. He does something *first* — he *produces* or *performs a service*. Then with the money which he receives he conveniently buys what he wishes, namely, goods and services which others have produced. Such a man is never a buyer except when he has been an antecedent producer. And so the *real* transactions in life consist in the exchange of goods and services — the exchange of genuine objects of benefit between fellow men.

The issuer of fiat credit or the counterfeiter becomes a buyer on a different basis. He prints some paper but performs no service; he becomes a buyer *without having been an antecedent producer*. He withdraws goods from the reach of buyers who have genuinely been antecedent producers; he is therefore a cheat and a thief. He has violated the Eighth Commandment (Thou shalt not steal), and the Ninth Commandment (Thou shalt not bear false witness — deceive and defraud).

A banker operating under the Federal Reserve Banking Act who puts out fiat credit does not act significantly differently from a counterfeiter. A banker issuing fiat credit injects "counterfeit" purchasing power into the business situation just as a counterfeiter does. But his position is in part different. The actual buyer, using the bank-created fiat credit (one type of counterfeit purchasing power), is the customer of the bank rather than the banker himself.

The bankers, therefore, are *not* the real "beneficiaries" of the issuance of fiat credit. The "beneficiaries" are the borrowers of fiat credit — certain people in the United States. The bankers have utilized the lush income from fiat credit to perform all kinds of banking services *without charging adequately for them,* so that the privilege of issuing fiat credit, which would be enormously profitable to bankers if there were no competition among them, has been passed on or "distributed" to their customers in the form of not charging fully for banking services of one kind or another.

Although fiat credit receivers are *morally* in the same position as counterfeiters, *legally* they are in a different position — respected citizens rather than criminals. The root cause underlying this amazing inconsistency is a failure to distinguish between credit which has been brokeraged and credit which is created by fiat (without antecedent saving). *Everything* depends — if thinking on money, credit, the business cycle, employment and prosperity is to be sound — on *distinguishing always* between brokeraged credit and fiat credit.

An Unconscious Unfairness Of People Who Demand More Fiat Credit

There are two popular explanations of a depression. They are:

1. A shortage of money;
2. Overproduction.

These are old fallacies.

Adam Smith demolished the theory that the cause of bad business is "a shortage of money." (The basic cause of "bad business" or a low standard of living is low production.)

Jean Baptiste Say demolished the theory that the cause of bad business is "overproduction."

No one has ever successfully refuted either Smith or Say.

The Canadian lady referred to in the preceding issue was, obviously, of a school of thought that held that any deficiency in business, either a depression or business not booming enough, was essentially a problem of "a shortage of money," or at least a need for more money. She probably had never heard of Adam Smith, or his argument against the theory that a "shortage of money" was the explanation for bad business.

There is a subtle unfairness almost always present in the demand for more money (in the form of fiat credit or otherwise). Mises has outlined that in his *The Theory of Money and Credit* (Yale University Press, New Haven, Conn., 1953) page 423:

> The oldest and most naive version [to explain the business cycle] is that of the allegedly insufficient supply of money. Business is bad, says the grocer, because my customers or prospective customers do not have enough money to expand their purchases. So far he is right. But when he adds that what is needed to render his business more prosperous is to increase the quantity of money in circulation, he is mistaken.

> What he really has in mind is an increase of the amount of money in the pockets of his customers and prospective customers while the amount of money in the hands of other people remains unchanged. He asks for a specific kind of inflation, namely, an inflation in which the additional new money first flows into the cash holdings of a definite group of people, his customers, and thus permits him to reap inflation gains. Of course, everybody who advocates inflation does it because he infers that he will belong to those who are favoured by the fact that the prices of the commodities and services they sell will rise at an earlier date and to a higher point than the prices of those commodities and services they buy. Nobody advocates an inflation in which he would be on the losing side.

Our Canadian lady *unconsciously* had the same *assumption* in her mind: the customers of her husband's business were going to be the *first* to get the fiat credit. By being first they would be gainers *at the expense of all who did not simultaneously get equivalent fiat credit.*

The people who gain from the increase in money are those who buy before sellers generally realize the fact that an increase in money is occurring, and its significance. Those who realize early that money is being increased or who are the direct recipients of that money are gainers at the expense of those who realize only later that money has been increased, or who are not early recipients of that increased money.

It is a fallacy to believe that *all* people gain from inflationism. What one gains another loses. In fact, the losses from inflationism exceed the gains.

Not All "Trouble" Is Caused By Sin

It is an error to ascribe *all* of the "trouble" of the world to sin. Scripture does not teach that all trouble is because of sin. Indeed, a few texts may be selected to "prove" that there is no trouble except that which finds its origin in sin, but the texts are *selected* to prove a point and result in a cosmology as reasonable as the idea that the world is flat.

Men have trouble — a lot of trouble — because the world is finite and is governed by *general* laws. The emphasis here must be on the word *general.* Natural laws operate regularly and do not adjust to human needs or wishes.

Contrarily, men's needs and wishes are innumerable and endlessly variable. They vary with time, place, condition, circumstance. The number of variations are almost beyond mathematical calculation.

It is because man's needs are innumerable and endlessly variable while natural laws are general and invariable that there is a lot of "trouble" in the world.

Imagine a family looking out of their window upon a large yard of green grass. Imagine, further, an argument, in which some members of the family allege that sin is the only cause of any trouble in the world; and imagine others alleging that sin was the cause of some of the troubles of the world, *but not all of them.*

A spokesman for the latter might argue as follows: "That big yard requires a burdensome amount of work. It were much better to live in an apartment. In the 'sweat of my brow' and with 'toil' and in weariness I must mow that lawn. A day is lost every week to mow the lawn and trim the edges. What a lot of trouble! That that grass grows and causes burdensome work is not caused by my sin, nor Adam's sin, nor anybody's sin. That grass grows is a natural phenomena, which unfortunately requires me to mow it."

Then he continues his argument: "But in the northwest corner there is some special grass, which grows only so much, then stops, and which does not have to be mowed. When I seeded that grass and reduced the work of mowing, was that associated with my sinning less? Was my work reduced because I was living a better life, or was merely a natural law involved of seeding in a certain kind of grass?" There is likely to be silence on that argument. What indeed can, in good sense, be said against it?

But the spokesman continues his explanation of his views. He says: "All right, I'll seed the whole yard with this special grass and the lawnmowing 'toil' will practically be over. Shall I be almost sinless?"

"But now my needs and wishes change. I buy a cow, because I need milk. I wish to pasture her in this big yard. I build a fence. But the cow does not get enough to eat. The grass in the pasture is of the wrong kind. For the *present* purpose, I need fast-growing grass, just the opposite of what I have recently seeded. Now, I must 'toil' earning money to buy hay, and transport it to the pasture. The short grass is presently a bane to me. If only I had left the fast-growing grass in that field!"

Clearly, *toil* and *sweat of the brow* is here the result of a man's *varying special purposes.* The general laws of nature could not be expected to dance around and change to every change in every man's need and every man's wish.

Some of the trouble of the world is due to *sin,* in fact the worst trouble by far. But some "trouble" — toil, sweat of the brow, weariness — is caused by the character of creation, to its invariable natural laws which cannot be expected to adjust to the infinitely varying needs of men.

The purposes of men are too many and varied for the general laws of God to be able to provide satisfaction. Therefore work is necessary; sin operates to aggravate the work but it does not "cause" the work.

Two Objections To Fiat Credit

(Any "benefit" is temporary; a later penalty is sure. Also, Fiat Credit is class legislation, that is, it is for some at the expense of others.)

In the preceding issue a sharp distinction was made between *brokeraged credit* and *fiat credit.* The former is beneficial to society, and is in conformity to the generally accepted moral law. The latter is damaging to society, causes business booms and depressions, and is contrary to the moral law; it is *theft.*

Nevertheless, as we illustrated in the earlier issue by citing two examples, respectable business and professional people are enthusiastic about fiat credit. They sincerely believe that fiat credit is profitable to society; but they are wrong in their morals and economics.

The teaching of the ancient Hebrew-Christian religions is that theft is inexcusable, and is *sin.* Further, these religions teach that the consequences of sin are *always* bad. These religions allege that there is a cause and effect relationship — whenever you sin, you will be punished (at least, suffer unwished consequences). When, nevertheless, nearly everybody seems to want fiat credit, there is almost universal confidence that in this case the consequences will be good, not bad. Either the old morality is wrong, or there must be something wrong about the reasoning of men about fiat credit.

Let us consider the argument of the wife of the French-Canadian retail equipment dealer quoted in the preceding issue. As a *French*-Canadian she would naturally vote for Liberal party candidates in Canada, but she testified that at the latest election she had voted Conservative. The reason she gave for this switch was approximately in the following words:

> Under the Conservatives it is easier to help the buyer finance the purchase of industrial equipment; therefore, we can sell more; therefore, we are making more money; we like the increased prosperity. The buyer of the equipment puts it to work, and the equipment increases his earning power so that he can easily pay off the loan. The equipment actually "pays for itself." We voted for the Conservatives because they are increasing prosperity. The key to it all is that they have made more credit available.

The "credit" to which this little lady referred was *fiat credit*, manufactured in accordance with the law, that is, with the full approval of the government.

In the preceding issue we gave a simple illustration of what fiat credit does to business, as follows:

> . . . Assume ten people in a society. They buy $100,000 a year on a non-inflationary (that is, non-fiat credit) basis. Everything is in balance. Each consumes on the basis of what he produces himself, or exchanges freely for what others produce. Nobody is robbing anybody else of goods. In this stable economy, without booms or depressions, the law (let us assume) is changed to permit the injection of $20,000 of new fiat credit. Not one bushel more of wheat, nor one yard more of fabric, nor one pound more of steel has been produced; but two men (of the ten) each have double the old amount to spend; instead of $10,000 they have $20,000. What will they do? They will quietly buy up with their extra $10,000, $20,000 worth of goods that the others otherwise would have bought. They "rob" the other eight. In the process, the others will discover that two of their number, not having produced a whit more, are literally robbing them (because the two are buying with their extra $10,000 each). In order not to "get left out" the others begin bidding up prices. In fact they all begin to bid higher. But in the end, the two have robbed the other eight significantly.
>
> But these two must pay back the fiat credit, say in the second and third years thereafter, at $5,000 a year each. Then the fiat credit, we assume, is cancelled by not being renewed. Now what happens? Buying power declines *below normal* by $10,000 each year. What is produced in goods will not be saleable any more at the current prices. Either merchandise will be unsold, or prices will have to drop. Here are the purchasing power figures by years:

Normal year (without fiat credit)	$100,000 — normal
Fiat credit-extension year	120,000 — boom
First Fiat credit pay-off year	90,000 — depression
Second Fiat credit pay-off year	90,000 — depression

> The $120,000 year is what people call a boom year; the $90,000 years are what people call depression years. This society of ten men would have been better off if they had never had the $20,000 fiat credit. The fiat credit did not enlarge their market; it only made it unstable.

In four years this imaginary community, without fiat credit, would have done $400,000 worth of business (at the steady rate of $100,000 a year). Instead, by employing fiat credit, it did as much as $120,000 in one year, and only $90,000 in two years. But the total is still $400,000 — and not a dollar more.

Nevertheless, our French-Canadian lady alleges that fiat credit creates more prosperity. How does she reason defectively?

In the first place, she is not reasoning "for the long run" — but only for the near future. In the second place, she is not reasoning for everybody in Canada, but only for herself and for others who are granted fiat credit.

In regard to morality, a basic premise should be kept in mind. Morality is neither short-sighted nor nonuniversal. Rules of morality should take the *long view* and should be applicable *to all men* without discrimination.

In our illustration, those who issued the $20,000 of fiat credit did not take the long view. They, obviously, did not take into account the repayment of the credit. If they had done so, they would have said to themselves, *why* put out the fiat credit and make business boom in the near future, but consequently make it correspondingly depressed two and three years hence? The only way that there can be a denial of the certainty of a future depression balancing off the earlier boom is if it is openly or tacitly proposed that the fiat credit *never* be repaid. That may *appear* to be a solution of a depression offsetting a boom, but creates other and even worse problems (to which it is not desirable to digress now). In our illustration then, "prosperity" is apparently promoted while the fiat money is first being spent, namely, in the second year. But the consequences, in our illustration, come as soon as the third and fourth years. In actual life, the depressions come whenever the fiat credit debt is liquidated.

Our Canadian lady, when she reasoned as she did, violated not only rules of morality, which are far-sighted, but she also violated a basic rule of economics, namely that *ultimate* consequences rather than *immediate* consequences should be a major feature of economic analysis and consideration.

In regard to the question who one votes for, voters are constantly presented with the choice of voting for those who seem to help the public today but who definitely hurt it tomorrow, versus those who do not consider it the task of the state to help today at the price of hurting tomorrow. We are not concerning ourselves with Canadian politics, nor are we favoring liberals (St. Laurent's party), nor opposing conservatives (Diefenbaker's party), but if it is a question solely of issuing or not issuing fiat credit — and if this lady was right that the Conservatives were issuing more fiat credit than the Liberals were willing to issue — then *on that issue* she was making a mistake when she shifted from the Liberal to the Conservative party. She was, in ethical terms, merely voting for more sin. She was voting for prosperity this year to be paid for by a depression next year or so. In parallel language she was voting for theft today but with the thought that, because it was *public* theft *approved by the law of men,* the penalty could be escaped. There is no question that certain obvious penalties of misconduct can be escaped by various devices, but then the penalty shows up in some other form. The penalty in this kind of a case is not imprisonment, but a future depression.

The Canadian lady's views, however, are not deficient in regard to *time* only, but also in *extent* or *universality.* There are no grounds for disputing her allegation that *her husband's* business had improved temporarily by the policy of the new party in power in increasing fiat credit. His customers' affairs were also undoubtedly improved. Similarly, the affairs of all others who participated in this increased fiat credit were improved. But was *everybody* in Canada benefited by the more liberal fiat credit policy? Of course not. Every holder of money was hurt, because "counterfeit money" (in the form of fiat credit) came in to compete with the existing stock of money. This is true not only of every holder of money, but of everyone who was a creditor, that is, everyone who was going to be paid back in dollars in that boom year. When such a person received his dollars, and wished to buy, he found himself competing with the equipment dealer's customers who were buying with fiat credit. At that moment there was no more equipment on hand than there would have been had there been no issuance of fiat credit. The would-be buyer who was using fiat credit was therefore an interloper, an illegitimate buyer. He had not *saved* in order to buy.

It will help to clarify the problem if an assumption is made. This lady said that fiat credit is excellent. If it is, then *everybody* ought to get it. Let us assume that fiat credit increased the purchasing power of her husband's customers by 20%. Now assume that everybody in Canada had a corresponding 20% increase in purchasing power, *at the same time.* At that moment there would not be one article more to buy just because the power to buy had been increased 20%. After the first surprise about having 20% more money, everybody would proceed to buy or try to buy what they had wanted but previously did not have the money to buy. But they would quickly become alerted to the realization that with more money, but not more products, the products were too few to go around for all. Immediately, prices in various ways would be increased to balance goods and money. (That does not mean that *all* prices would go up *exactly* 20%.)

Let us think in the terms in which the Canadian lady might have been thinking; let us say, in terms of road scrapers. Because fiat credit was extended to her husband's customers, they would buy (say) six scrapers instead of five, that is, 20% more. But everybody else using scrapers, let us assume, also had 20% more money. At the given moment the supply of scrapers was static; (*later* more scrapers might be built). But *at the moment* "demand" had "increased" by 20%, by fiat-credit creation. *All* buyers would compete on that basis. Their competition would not increase real prosperity, but the price of scrapers would rise (as soon as all knew that all others *also* had 20% more money). Demand would *appear* to be greatly increased. Manufacturers would schedule to produce more. But they would be disillusioned the next year, *unless there was a new dose of fiat credit* injected into purchasing power at that time. If not, and while the present buyers were paying off their debts acquired through these fiat credits, there would be a depression in the scraper business.

What our Canadian lady was saying, if her proposition were accurately formulated, is this: "Because the new government permitted increased fiat credit, therefore (1) our particular business was stimulated temporarily (but we realize that there will be a penalty later when we shall be correspondingly hurt); and (2) we have been benefited because we were *early* beneficiaries of the more-liberal fiat credit policies. Fiat credit benefits the class that first gets the fiat credit. We were in that class. We voted for a party as we did, because we expected that it would pass laws that would help us at the expense of others."

This by no means answers all that the lady was alleging, but sets her claims in the proper light.

The Canadian Lady As A Lawmaker

(as distinguished from being the recipient of "benefits" from immoral legislation)

The Canadian lady will face serious problems if she moves from a country town (as wife of an industrial equipment dealer), to Ottawa, the capitol of Canada, as a lawmaker. In her former capacity she can appraise fiat credit as something that, from her viewpoint as an early recipient of the "benefits," is a profitable thing for her. But if she must become responsible herself for the *policy* in which she hopes for a benefit, from among what policies will she be obliged to make a decision. A lawmaker cannot justifiably pass laws on the basis of surface evidence, or on the basis of failing to take ultimate consequences into account. Nor can a voter vote in favor of a party which does not have a far-sighted policy. The lady whose *fiat credit* views we have presented in the preceding issue (pp. 125ff.) might change her views radically if she became a responsible lawmaker rather than an ordinary citizen. In this article we shall outline some fiat credit problems she would, whether she liked it or not, have to face as a lawmaker. These problems are inescapable for all of us whether we go to Ottawa or Washington or London as lawmakers.

These *inescapable* problems can be stated so that every voter can understand them. To that end, we shall continue to use our imaginary society of ten people with a $100,000 economy. Our illustration involved, first, a normal year of $100,000; then a boom year of $120,000, the result of two of the ten citizens being authorized to buy by means of fiat credit $20,000 extra; then two depression years in which the fiat credit citizens were paying off the fiat credit at the rate of $10,000 a year, causing thereby two depression years of $90,000 each.

Let us assume that our Mrs. Canadian became a Canadian senator during the boom year of $120,000. What problems would she be obliged to face? She would have to decide between several policies, each of which would be accompanied by momentous consequences. Here they are:

1. Is the $20,000 fiat credit to be a one-shot dose, to be liquidated not only by repayment, but also by genuine *cancellation* of the fiat credit? Readers will remember that we ourselves have previously assumed that the fiat credit would be repaid in the third and fourth years. We *assumed* that. But the probabilities are that our Mrs. Canadian would not be sure she wanted the fiat credit to be genuinely liquidated. She would probably think out loud in this manner. "I want the fiat credit. I want the first debtor to make regular payments to repay his *particular* debt. But I do not want the fiat credit to be liquidated. As fast as the first debtor pays on his debt, I wish to re-use the funds for financing another sale to another equipment buyer, a buyer who will be unable to buy unless he can have made available to him this fiat credit. I wish to use the fiat credit over and over." When our lady learns, too, that actual liquidation — cancellation or elimination — of the fiat credit (in the third and fourth years) will entail a depression at that time, she will think long and hard before, as a national senator, she votes in favor of not permitting re-use of the fiat credit after the first time. Almost certainly, being prompted by an unwittingly dishonest rather than a wise self-interest, she will reject policy number (1), namely, a single-dose shot of fiat credit, which is to be withdrawn or cancelled or liquidated — use whatever word you wish — upon repayment by the first user of that fiat credit.

2. This brings her to the second policy she can follow as a lawmaker, namely, a one-shot dose of fiat credit, which once issued is *never* to be withdrawn. Almost certainly she will like it better than a one-shot dose that has to be "paid up," and by being "paid up" will remove the fiat credit from the money situation. She will be greatly influenced by the idea, if it occurs to her, that by re-loaning the fiat credit to a third party as fast as the first debtor pays off, *there will be no depression.* What will happen if *fiat credit* is not to be cancelled? In our regular four year series we then get:

Normal year (without fiat credit)	$100,000 — normal
Fiat credit-extension year	120,000 — boom
Third year; no payment on fiat credit	120,000 — normal
Fourth year; no payment on fiat credit	120,000 — normal

Our lady as a sharp business woman will be making an important distinction, to wit, she knows that the first debtor using fiat credit must repay the loan faster than the equipment wears out, but — and this is a policy she will almost surely come to — she will wish to use and re-use that fiat credit with a whole series of buyers who can buy only if they can borrow the money first with which to buy. We might put it this way: this lady will wish *individual* debts to be paid conscientiously and thereby be liquidated, but she does not want the public use of that fiat credit ever to be terminated. As has been made clear, fiat credit is a substitute for money — and is in a sense money itself — and so our lady wants any money that has been manufactured to be left to exist. If on the other hand, a counterfeiter and his counterfeit money were apprehended, she would vote to have the man put in jail and have his counterfeit bills burned. But in regard to fiat credit, which is no less counterfeit than counterfeit coins and bills, she will probably not want the issuer to be put in jail nor his counterfeit money — fiat credit — to be destroyed. Herein she would be inconsistent.

3. There is a third policy which may look even better to our lady. Just as policy number (2) avoiding cancellation of fiat credit looked better to her than policy number (1) which would mean a single, "one-time" use of fiat credit (*to be cancelled upon the first repayment*), so a third policy will be a great temptation to her, namely, a policy to issue *more and more* fiat credit. This is not a single-shot dose of fiat credit followed by cancellation; nor a single-shot dose to be left permanently in the money system, but this is a policy of steady new doses added to all the old which are to be retained. Such a policy will make our table look as follows:

Normal year (without fiat credit)	\$100,000 — normal
Fiat-credit extension year	120,000 — boom
Second Fiat credit extension year	140,000 — boom
Third Fiat credit extension year	160,000 — boom

Why not do that? Put out each year \$20,000 of new fiat credit and *never* cancel *any* of it. Then we will have a continuous boom! That is what our lady unwittingly wanted as a dealer's wife in a small town. That is what her constituents want now that she is a senator.

In fact, it is almost obligatory to do that. There is hardly an option not to do it, if you think about it. When the program was \$100,000-\$120,000-\$90,000-\$90,000 — who would really be satisfied with one spree followed by a headache! When the program was

$100,000-$120,000-$120,000-$120,000 — then the only real "shot in the arm" was in the second year, when the jump was made from $100,000 to $120,000. But thereafter the stimulus was gone — things settled down to the $120,000 level. If the stimulus was good — and many if not most people agree with our lady senator that a fiat money stimulus is wonderful — then the stimulus must be repeated and repeated. Further, to make a sudden jump from $100,000 to $120,000 and then to continue at $120,000 without further increases would make the second $120,000 year look like an ordinary year. What makes a year look good is its rise above the previous year. Anyway, who wants a normal year, when it is possible to have a boom year. A *level* of $120,000 will soon be taken as a *normal* year. To have booms, gains on gains must be made, and the series must become $100,000-$120,000-$140,000-$160,000 — that is, more and more fiat credit, without ever really "liquidating" any of it out of the money stream.

4. There is a fourth policy which may look still better. The series might be $100,000-$120,000-$150,000-$190,000 — that is, the fiat credit might by augmented each year more than the previous year. The increase in the foregoing series is $20,000 the first year; $30,000 the second year; $40,000 the third year. None of this is ever to be withdrawn. Then, some might say, we have the real basis for a continuous boom! But do we? Every government and every people that has ever tried it has always had a catastrophic collapse.

As a lawmaker the Canadian lady can have any of these alternatives. She must select one or another. She cannot avoid a selection.

Alternative number (1) means an early and small depression. Number (2) mean a slower and longer depression. Number (3) mean continuous inflation to be followed by something worse than a depression, namely, eventual complete economic disorganization. Number (4) means a runaway boom ending in catastrophic collapse.

There cannot *in the long run* be any good that will come from a fiat credit policy.

Henry Thornton

In 1945 a delightful book was published in England entitled *These Remarkable Men,* (Lutterworth Press, London). The author was John A. Patten. Evangelical Christians will find this little book an excellent addition to their libraries.

The book contains sketches of nine men — Wilberforce, Teignmouth, Sharp, Thornton, Stephen, Zachary Macaulay, Grant, Babington and Buxton — nine of the men who founded or were active in the British and Foreign Bible Society.

These men are known in history as "the Clapham Sect." Clapham was, 150 or more years ago, a handsome suburb of London. The men, themselves, were devout evangelicals in the established Church of England. Working more or less as a team, and of course, with the cooperation of others, this group of "remarkable men" made history by (1) organizing and promoting the first English Bible Society, and (2) persuading England to ban the slave trade. Read the fascinating little book, and be inspired to equivalent great deeds in our own day!

The first Treasurer of the English Bible Society was Henry Thornton, one of the sons of John Thornton (1720-90), famous philanthropist, and prominent merchant banker. Henry at age 30 bought Battersea Rise House in Clapham, and this in time became a center for the Clapham team. Henry Thornton was a member of Parliament, a prominent banker, and the most important theorist in his day on banking and monetary problems, on this subject outranking even Ricardo.

In Chapter V entitled "The First Treasurer" Patten wrote as follows:

> "Well, Henry," asked Wilberforce of Henry Thornton on the night of February 23, 1807, after the bill for the abolition of the slave trade had passed the House of Commons by 283 votes to 16, "what shall we abolish next?"
>
> "The lottery, I think," Thornton gravely replied.
>
> The reply was characteristic of the man. Even in the hour of triumph he was looking soberly to the future and planning another reform on which he had set his heart. For him life was a serious business and he wanted others to regard it with equal seriousness. . . .
>
> There was certainly no lack of earnestness among these reformers, and their most hostile critics could never accuse them of levity. On the contrary, criticism charged them with showing a Puritanical strictness and simplicity of life. It is true that they had not only caught the new evangelical enthusiasm but had revived something of the old Puritanism. They lived strictly and denied themselves many ordinary pleasures. Without renouncing the comforts which most of them could easily afford, they set a measure to them, and,

as we shall see, Henry Thornton limited his personal expenditure in order to give away a large part of his income. Sunday was strictly observed at Clapham; daily family prayers were the usual order; and in other ways the appearance of worldliness was avoided. . . .

Yet the Clapham Puritanism was no stern and unlovely manifestation, and Thornton's religion had nothing forbidding about it. On the contrary, he disliked anything ungracious in religion, and in a frank moment confessed that some of the religious people he met in his father's home nearly put him off religion altogether. . . .

Thornton was a famous banker in his day and an authority on high finance. He supported Pitt's financial measures for the formation of the Sinking Fund; he was a leading member of the Bullion Committee of 1811; and he was a Governor of the Bank of England. He wrote a book on "The Nature and Effects of the Paper Credit of Great Britain," which was regarded as an important contribution to a difficult subject. [Page 68ff.]

Thornton's health throughout his maturity was "delicate." In 1815 at the age of 54 he died after a lingering illness.

To describe Henry Thornton as an economic thinker we begin by quoting Joseph A. Schumpeter in his *History of Economic Analysis* (Oxford University Press, New York, 1954) where in Chapter 7 entitled "Money, Credit and Cycles" he wrote (page 689):

. . . But Henry Thornton (1760-1815) must be saluted at once. He was a banker, M.P., philanthropist, and — which he himself and many who knew him would presumably have put first — a leading figure in the influential group of Evangelicals that was known as the Clapham Sect. His *Enquiry into the Nature and Effects of the Paper Credit of Great Britain* (1802)* is an amazing performance. The product, according to Professor von Hayek's estimate, of work that extended over about six years during which the author's energy was largely absorbed by business and political pursuits, not faultless in detail and not fully matured, it anticipated in some points the analytic developments of a century to come. No other performance of the period will bear comparison with it, though several, among them Ricardo's, met with much greater success at the time as well as later. In part this was because the author put no emphasis at all upon his novel results — the book reads as if he himself had not been aware of their novelty. Perhaps he was not, though he paid an almost academic amount of attention to such predecessors as he knew. He was one of those men who see things clearly and who express with unassuming simplicity what they see.

To this Schumpeter adds the following footnote:

[*The Library of Economics reprint (1939) is prefaced by an essay by Professor von Hayek, the scholarship of which is surpassed only by its charm. The reader who misses it deprives himself not only of much valuable information but of an exquisite pleasure.]

Professor Friedrich A. von Hayek edited Thornton's treatise, *An Enquiry Into the Nature and Effects of the Paper Credit of Great Britain* (Rinehart & Company, New York, 1939), and wrote an Introduction of 48 pages, justly praised by Schumpeter. This Introduction contains more data than appears in the chapter on Thornton by Patten. Von Hayek wrote:

> It is quite impossible to make more than a mere mention in this sketch of the more important movements which the Clapham Sect initiated and in which Henry Thornton took a leading part. Their main achievement is, of course, the abolition of the slave trade, and from the beginning of the association of Thornton, and Wilberforce up till the passing of the Act of 1807, the greater part of their energies were devoted to this leading goal. If Wilberforce was the driving spirit, Thornton was the wise and practical counsellor on whom Wilberforce placed absolute reliance. . . . [Pages 21-22.]
>
> It is recorded that till his marriage in 1796 Thornton had made it a rule to give away as charity six-sevenths of his income. His work at the Banking House does not appear to have taken up too much of his time. If we may trust his Diary, to attend there regularly from 11 a.m. to 3 p.m. seems to have been a good intention rarely achieved. And even so, we find occasionally entries as the following: "I did little yesterday at my Banking House except correcting a Sermon on Self Denial." [Pages 25-26.]
>
> This Introduction cannot attempt to summarize the argument of the work or even to point out all its merits. It would take a great deal of space merely to mention all the points in respect to which Thornton's treatment constituted an important advance on earlier discussions, and it must suffice to indicate a few passages which deserve special attention. It may be true, as has often been asserted, that his exposition lacks system and in places is even obscure, but too much can be made of this defect. And there will be few readers who will not be impressed by the acumen and the balance of mind displayed throughout the exposition. [Page 46.]
>
> Great as this achievement is, to many readers Thornton will appear to reach the height of his intellectual power in the penultimate chapter in which he proceeds to meet various objections, and in particular to refute the erroneous argument "that a proper limitation of bank notes may be sufficiently secured by attending merely to the nature of the security for which they are given." It is here that, in summarizing earlier points, he sometimes finds the happiest formulations; he also breaks entirely new ground in an attempt to elucidate the effects of a credit expansion in greater detail. He sees that the expansion of credit will in the first instance lead to the employment of "antecedently idle persons," but adds that as these are limited in number, the increased issue "will set to work labourers, of whom a part will be drawn from other, and perhaps, not less useful occupations." This leads him . . . to one of the earliest

> expositions of what has become known as the doctrine of "forced saving." [Page 49.]
>
> The discussion of the proper limitation of issues leads on to the second point of primary importance in this chapter, the discussion of the role of the rate of interest. The statutory limitation of the rate of interest which the Bank may charge has the effect, he says, that at times this rate will be much lower than the mercantile rate of profits, and will in consequence lead to an undesirable expansion of credit unless the Bank takes other measures to keep down the volume of credit. This is a remarkable anticipation of the distinction between the market rate and the "natural" or "equilibrium" rate of interest which since the work of Knut Wicksell has played such an important role in the discussions of these problems. With this idea, along with the idea of forced saving, Thornton was for the first time in possession of the two main elements which it was left for Wicksell, nearly a hundred years later, successfully to combine into one of the most promising contributions to the theory of credit and industrial fluctuations. [Pages 49-50.]
>
> The points we have mentioned, though they are the most important, do not by any means exhaust Thornton's contributions to knowledge. They may, however, serve as an indication of the character of the work which put the discussion of monetary problems on a new plane. . . [Page 50.]

It may be doubted whether in the history of mankind the character of an evangelical Christian and an excellent economist have been embodied in one person more attractively than in the person of Henry Thornton. (Frederick Bastiat is probably the closest rival.)

Ludwig von Mises

On matters pertaining to money, credit and business cycles, which we are currently discussing, we shall be following the thought of Ludwig von Mises for two reasons. In the first place, the policies which Mises favors are the *only* policies which are reconcilable with the Decalogue, specifically the commandments against theft and fraud; other policies conflict with that moral law. In the second place, the policies which Mises favors are the only policies which are logically consistent.

Mises's ideas are an advance over the thinking of Henry Thornton. But it is almost necessary to *contrast* the thinking of the two men, rather than to indicate there was easy progress from Thornton to Mises.

Thornton, although one of the greatest thinkers on credit and the business cycle, nevertheless did not meet the problem of fiat credit "head on." He did not *fully* understand the problem, and never took a comprehensive logical stand against all forms of fiat credit.

Mises makes an economic rather than a *moral* approach to fiat credit. He is a rationalist in the sense that he reasons persistently to a logical conclusion. The conclusion of his reasoning is this: *that the consequences of ALL fiat credit, no matter how small the quantity granted or the form, is ALWAYS bad.* There is no escape from the undesirable consequences.

In FIRST PRINCIPLES we accept, as authoritarian, the commandments in the Mosaic Law, which forbid theft and fraud. We are therefore against fiat credit, because *all fiat credit is theft and fraud.* We follow Moses in his warning statement, "Your sins will find you out." The reason why Moses was right about that is because the ethical laws in the Mosaic Decalogue are based on cause and effect, on the nature of things, on the character of creation, on phenomena traceable by the human mind by means of the laws of logic.

On questions of money, credit and the business cycle we follow Moses on (so-called) moral grounds, and Mises on economic grounds. The reason why these two authorities agree is because what one teaches on moral grounds and the other on economic grounds are essentially one and the same thing.

We take the following from the preface of Mary Sennholz's *On Freedom and Free Enterprise* (D. Van Nostrand Co., Inc., Princeton, New Jersey, 1956), a book which is a *festschrift* containing nineteen contributions in honor of Dr. Mises on the fiftieth anniversary of his receiving a doctor's degree from the University of Vienna.

> Ludwig von Mises was born on September 29, 1881, in Lemberg in what was then Austria-Hungary. . . . From 1892 to 1900 he attended the "Akademische Gymnasium" in Vienna to prepare himself for the university. Upon graduation he studied law and economics at the University of Vienna. On February 20, 1906, the University conferred upon him the degree of Doctor of Law and Social Sciences, or, as the traditional Latin title goes, of Both Laws, i.e., of Roman and Canon Laws. . . .
>
> After a short occupation with the administration of justice, his increasing interest in social and economic matters induced him to accept the position of economic adviser of the Austrian Chamber of Commerce. For almost thirty

> years he endeavored to stem the tide of interventionism and socialism from this post, until Austria became a part of the German Reich. And for more than two decades he taught the economics of free enterprise at the University of Vienna . . .
>
> In Austria he was fighting a losing battle. In spite of his prodigious labor and relentless counterattacks, the cause of freedom and free enterprise failed to hold its ground. In 1934 he left for Geneva to occupy a chair at the Graduate Institute of International Studies. In the Swiss atmosphere of peace and serenity he observed the rise of nationalist-socialist Germany and the outbreak of World War II. It is here that Professor von Mises wrote his magnum opus, *Nationalökonomie, Theorie des Handelns und Wirtschaftens,* which is a comprehensive treatise on economics. Its revised American edition is known under the title *Human Action.* . . .
>
> In 1940 Ludwig von Mises immigrated to the United States where he had spent some time twice before. In 1926 he was a visiting professor sponsored by the Laura Spellman Rockefeller Foundation, and in 1931 he attended the Congress of the International Chamber of Commerce in Washington, D. C. Now he came to stay and make America his country of choice. . . . Since 1945 he has been lecturing as a visiting professor of economics at the Graduate School of Business Administration of New York University. (Pages ix-xi.)

We also copy the following from what is said about Dr. Mises on the "dust cover" of his book, *Planning For Freedom* (Libertarian Press, South Holland, Illinois, 1952):

> . . . Professor Ludwig von Mises is one of the foremost economists of our age. Inspired in his early career by the work of his teachers, the great Austrian economists Carl Menger and Böhm-Bawerk, he has in a series of scholarly investigations systematically analyzed every important economic problem, critically exploded inveterate errors and substituted sound ideas for discarded fallacies. . . .
>
> In his studies on money and credit Dr. Mises has unmasked the illusiveness of all arguments advanced in favor of a policy of inflation and credit expansion. He has shown how the boom that an "easy money" policy artificially produces, must inevitably lead to a slump. He has demonstrated that the almost regular recurrence of periods of economic depression is not caused by any shortcomings inherent in the very nature of the market economy, the capitalist system, but, on the contrary, the necessary effect of sometimes well-intentioned, but always ill-advised attempts to tamper with the operation of the market. The advocates of inflation and credit expansion have in vain tried to discredit this doctrine, the so-called Austrian theory of the trade cycle. Events — the collapse of the German currency in 1923, the great depression of 1929 and the following years, the troubles brought about by the present American inflation — have clearly proved its correctness.
>
> No less important than Dr. Mises' contributions to the

problems of money, capital and credit are those of his writings that deal with the effects of socialism, communism, planning and all kinds of government interference with the market, e.g., price and wage control.

An economist cannot satisfy himself with pure analysis and scientific interpretation of reality. His teachings imply in themselves an attack upon the political parties whose programs they confute. From the very beginnings of his work as economist Dr. Mises vigorously opposed those tenets and creeds whose application was bound to destroy Europe's civilization and prosperity. He forcibly fought the German Historical School, the forerunners of Hitler's National Socialism, and the Marxians, the harbingers of the most ruthless of all dictatorships the world has even seen. And he fights today in America the ascendancy of the same mentality of all-round regimentation.

It has been said that people do not learn either from historical experience or from theories. It is a sad fact that in most of the American universities the students are today indoctrinated with the counterfeit philosophy that has ruined Europe. Very old fallacies, a hundred times refuted, are flamboyantly advertised under the deceptive label "new economics." Veblenians, Marxians and Keynesians still dominate the scene with their preposterous glorification of "social" control of business, planning, and deficit spending. But their bigoted dogmatism is beginning to lose its hold upon the minds of the rising generation. Says Professor Hayek, the most eminent among the numerous former students of Mises: "Even some of Mises' own pupils were often inclined to consider as *exaggerated* the unfaltering tenacity with which he pursued his reasoning to its utmost conclusion; but the apparent pessimism which he habitually displayed in his judgment of the economic consequences of the policies of his time proved right over and over again, and eventually an ever widening circle came to appreciate the fundamental importance of his writings, which ran counter to the main stream of contemporary thought in nearly every respect."

It is generally recognized that Dr. Ludwig von Mises is today outstanding among those social scientists who advocate economic freedom as the indispensable basis of all other freedoms and valiantly raise their voice against all varieties of totalitarian slavery.

On questions of money and credit, booms and depressions, a long series of ideas come finally to complete and correct formulation through Mises. His great predecessors include men as Hume, Thornton and Wicksell. He has, however, utilized ideas from very diverse sources as, for example, ideas from John Law, whom we shall discuss later. But it is only in Mises that there is a complete and definitive break with a whole mass of fallacies about money, credit, inflation and the business cycle. And unless a man condemns fiat credit as unqualifiedly as Mises does, it is not correct to declare that that man adheres to the Ten Commandments.

Protestantism's Social Gospel As A Substitute Religious Term For Socialism

The National Council of Churches, the United State's segment of the World Council of Churches, appears to be primarily interested in the Social Gospel. The following are extracts from an article by Vernon W. Patterson in the April 22, 1959 issue of *The Southern Presbyterian Journal*, under the title, "The National Council's 'Social Gospel.'"

The National Council's "Social Gospel"

Historically the name "social gospel" and its teachings were promulgated by Dr. Walter Rauschenbusch of Colgate Theological Seminary, later Colgate-Rochester Divinity School, at the time the Federal Council was coming into being. The National Federation of Churches had been organized in 1900 largely through the leadership of Harry F. Ward, professor for 23 years in Union Theological Seminary, New York, . . . [well-known] for his communistic teachings and activities. The Federal Council was organized in 1908. Dr. Rauschenbusch's "Social Gospel" became its guiding principle from its beginning.

Dr. Rauschenbusch had written in his "Christianity and the Social Crisis" in 1906 the following:

> "It would seem, therefore, that one of the greatest services that Christianity could render to humanity in the throes of the present transition would be to aid those social forces which are working for the increase of communism. The church should help public opinion to understand clearly the difference between the moral qualities of the competitive and communistic principle, and enlist religious enthusiasm on behalf of that which is essentially Christian."

Bishop G. Bromley Oxnam in his "personalities in Social Reform," published in 1950, says that this book by Rauschenbusch "changed the thinking of American Christians."

. . . [Rauschenbusch] sees society [as] divided into two fundamental classes, "the one born to toil," the other developed by leisure "with its combination of leisure and wealth . . . conditioned on the power of taking tribute from the labor of many." He decries "the desire for private property" as "antagonistic to public welfare," and advocates "the substitution of cooperation for predatory methods in industry." "The cross," he says, "is a law of social progress," and the goal he sets is a "universal human fraternity," "the perfect social order," "the Kingdom of God."

In his book, "Theology for the Social Gospel," in referring to this "Kingdom of God," he says,

> "This involves the redemption of society from private property in the natural resources of the

earth, and from any condition in industry which makes monopoly profits possible."

Also in this book, he says,

"If we can trust the Bible, God is against capitalism, its methods, spirit, and results" (p. 184).

These teachings are simply Marxism dressed in Christian clothes. They are not the gospel of Christ according to the Scriptures. They are "another gospel." What Karl Marx calls "the solidarity of the race" becomes "the universal brotherhood of man"; his "economic determinism" becomes "social change" and "social planning and control"; and his "classless society" becomes "the Kingdom of God." This "Kingdom of God" — the term popularized by Rauschenbusch — is clearly not the Kingdom taught in the Scriptures, but is *an international, socialistic state.*

The presidents and . . . leaders of the Federal Council, and now of the larger National Council, formed in 1950, have followed and developed these teachings consistently. Volumes could be written, giving quotations from their books and writings, in which they advocate these teachings . . .

Dr. Edwin T. Dahlberg, President of the National Council (1959), was formerly secretary to Dr. Walter Rauschenbusch, and apparently was greatly influenced by him.

* * *

The many publications of the former Federal Council and of the present National Council abundantly confirm this. The National Council has published a "Summary of General Assembly and General Board Action, November 29, 1950 through November 30, 1957." While an exact analysis of these actions is difficult, because undoubtedly there is considerable overlapping of material in their contents, still the following gives an approximate idea of the nature of these actions: 28 were on political activities, 10 on social and moral issues, 9 on labor relationships, 43 on international relations, 7 on economic matters, 18 on racial relations, 12 on religious and spiritual matters, and 10 in the nature of greetings. . . .

. . . leaders of the Federal and National Councils have fought the defense programs of the United States through the years, even when war and destruction were threatening; they have advocated wide-open immigration and unrestricted interchange of travel and trade between America and communist countries; they have aligned themselves with radical labor movements and leaders; they have greatly influenced the advance of socialism and its accompanying inflation; they have sought to curb and abolish the Committee on Un-American Activities; they have created class and racial strife and discord; they have opposed the free enterprise system and advocated collectivism, and have in many ways aided the cause of communism.

The quotations tell their own story. It is difficult to believe that where the Protestant churches preach the social gospel they are teaching anything else than socialism in one of its many variations.

In the first quotation in the foregoing from Rauschenbusch "competition" is designated as the principle contrary to "communism," and communism is indicated to be the "essentially Christian" principle for organizing society. Rauschenbusch was obviously a sentimentalist rather than a rationalist, and apparently did his thinking on the basis of his emotions and without understanding of the "economic order." Competition when harnessed to freedom of buyer and seller has two characteristics — every nerve is strained to give *service* to the fellowman, *according as he chooses;* in short, *competition is rivalry in service to fellowmen* who are pursuing their legitimate self-interests. (See earlier issues of this publication in many places for complete and frequent analyses of this idea.) Now, this "falling over each other" in eagerness to serve the fellowman as *he* decides (not as the producer decides) is clearly indicated by Rauschenbusch as being not "essentially Christian."

What then, according to Rauschenbusch, *is* "brotherly love"? *Communism.* The principle of brotherly love, in this case (that is, in communism), is a combination of humiliating *charity* and violent *coercion.* In this situation, *charity* is the antonym for *service;* and *coercion* is the antonym for *freedom.* Rauschenbusch essentially taught that a society based on *alms* and *coercion* was Christian, and a society based on *service* and *freedom* was un-Christian. This is the social gospel! Rauschenbusch, implying that his foundation was the Bible, wrote: "If we can trust the Bible, God is against capitalism, its methods, spirit and results." Suppose we remove the "if" clause, and leave the proposition stand unqualified: "God is against capitalism, its methods, spirit and results." Here is a good proposition for debate. We shall be glad to take the negative in a public debate with anyone who wishes to advocate the foregoing proposition. Or we shall be glad to take the affirmative on the proposition, "God is against communism, its methods, spirit and results." We shall be glad to conduct the debate solely on Scripture, solely on logic, or on both Scripture and logic.

(The evidence, we believe, is conclusive that Rauschenbusch and those who think similarly were (are) quite uninformed on the subject of economics. They substitute the ideals of a secondary science, sociology, for the realities of a primary science, economics. Consider Ricardo's Law of Association: to our knowledge there has never been in any writing of any social gospeller a reference to it with obvious full understanding what that Law is. But as economic law goes — or as any law of human association of any kind goes — Ricardo's Law is as fundamental and as illuminating as the law of gravity in physics. (See Volume IV, Numbers 7, 8 and 9 of this publication.) If human society is to be organized without knowledge of or conformity to Ricardo's Law of Association, which is fundamental for any understanding of an economic order, then it is as reasonable to say that the science of astronomy should be based on Ptolemaic ideas.)

But our prime purpose in quoting the foregoing is to refer to the fourth paragraph in the quotation, where we read: "Rauschenbusch sees society [as] divided into two fundamental classes

> 'the one born to toil,'
>
> the other developed by leisure
>
> 'with its combination of leisure and wealth . . . conditioned on the power of taking tribute from the labor of many.' "

Rauschenbusch obviously accepted Marx's theory of the explanation of the *income* of capitalists — namely, that it is based on *exploitation* of the laboring man. *That* is socialism's explanation of the income of the capitalist whether it appears in the form of interest on money, rent on land, or profits in business. That income is declared by Marx to be something filched from the worker. Rauschenbusch has apparently been imposed upon by Marx.

It is true that the explanations given by capitalists justifying interest, rent and profits have been vulnerable, and that the socialists have pretty well picked those pro-capitalism arguments apart and shown them to be fallacious; for example, a common argument is that capital gets a return *because* it is *productive*. But that argument is erroneous. It is as erroneous as the socialist argument that capital gets a return *because* it *exploits the laborer*. The *basis* for the return of income to a capitalist is neither of these.

Again if anyone wishes to debate the issue, it can be formulated as follows: "Capital obtains a return because it has the *power* of taking *tribute* from the labor of many." We shall be happy to take the negative in such a debate.

Theologians have neglected economics — a rational, realistic science, soberly analyzing the reality of things; and have instead turned to sociology — a visionary, idealistic "science," unhinged from reality. The social gospel is equivalent to *obscurantism in economics.*

Böhm-Bawerk, the famous Austrian economist, wrote an essay, "*Macht oder Economisch Gesetz,*" which can be translated *Power versus Economic Law.* But that title, to be fully appreciated, would really need a sub-title to the effect: "Can any human power, individual or collective, overwhelm and annul economic *law?*" Böhm-Bawerk answers that question in the negative. No human being nor any government will be able to "abolish" a return on capital, not even by the torture rack, imprisonment nor the death of millions. The return on capital is an economic *law,* based on the *nature of things,* on creation. The equivalent of interest will exist inescapably in any socialist society — under cover, if suppressed *temporarily* by power; and openly, in an *idealistic,* noncoercive socialist society. In regard to the latter, see Böhm-Bawerk's argument in Chapter XII in Volume I of his three-volume work, *Capital and Interest.* Here he poses the problem of five socialists building an engine, and inescapably *in the interest of justice* allowing a return which is the reward of capitalism! Rauschenbusch was an obscurantist in economics when he referred to "the power of taking tribute from the labor of many" and "predatory methods in industry."

(It should be added that Rauschenbusch in one of the foregoing quotations implies that communism is a system of "cooperation," which he contrasts to the "predatory methods" of capitalism. Rauschenbusch's use of the term *cooperation* in this connection is pure question-begging, and false; communism as a system is alms and/or coercion; it can never be *cooperation.*)

Decisions Of The National Council Of Churches Are Reported As Unanimous Unless The Negative Vote Was More Than 25%

The following is an extract from an article in the April 22, 1959 *The Southern Presbyterian Journal,* by Horace H. Hull:

The National Council's "Group Dynamics"

The New York TIMES for November 21, 1958, reported in bold-face headlines that "LEADERS OF AMERICAN PROTESTANTISM VOTED UNANIMOUSLY TODAY IN FAVOR OF U.S. RECOGNITION OF RED CHINA AND

ITS ADMISSION TO THE U.N." Then followed a news story on the four day World Order Study Conference of the National Council of Churches at Cleveland, Ohio. The *unanimous* vote had been taken at the end of the conference.

Ten days later the same paper reported: "CHURCH LEADERS SHUN CHINA STAND." The news item then went on to report that the General Board of the N.C.C.C. had announced that the World Order Study Conference at Cleveland while "it had spoken with a mighty voice had spoken only for itself." I should explain that the General Board is the highest administrative and policy making body of the National Council. It had sponsored and authorized the Cleveland conference. Yet the Cleveland conference which "unanimously" had voted to recognize Communist China "spoke for itself."

This is as patently absurd as telling a man, "My mule did not kick you; it was only his left hind leg which acts for itself." The National Council has employed this . . .[method] before. Some subdivision will hold a conference which was authorized or sponsored by the National Council. It will issue a highly questionable or provocative statement on some social, economic, or political question having absolutely nothing to do with religion, ethics or morals, as a trial balloon. If there is no great protest then the N.C.C.C. advertises it as the "mighty voice of 38 million Protestants." If, however, as is often the case, there is widespread objection and criticism, then the National Council will blandly issue its "My mule did not kick you" statement.

On page 5 of . . . [its] report we learn that "The Fifth World Order Study Conference was planned by the National Council of Churches with the *understanding that it was to be followed with a nationwide educational effort?"* (Emphasis added.) There were two proposals to amend the message with respect to its recognition of Red China section but they "were voted down with less than 25% in their favor."

The Message to the Churches opens with a strictly neutralist position between the communist and non-communist nations. "Revolutionary forces have created new nations featuring a passionate and fractious nationalism; strong and all too justified resentments against the western world — resentment now compounded by the deterioration in race relations in our country" . . . etc. The report does not amplify what the United States has done to earn such "all too justified resentment" except possibly our own "deteriorating race relations."

Next comes the usual Communist and liberal bugaboo of world-wide nuclear annihilation unless the United States and Soviet Russia sit down and become friends — on Communist terms, needless to add. The Conference deplored "the tendency to discredit the motives and proposals for disarmament when made by anyone but ourselves" — in more open and honest terminology "we must trust the Communists."

The National Council's plea for the abolition of universal military training was renewed. Churchmen in this country also need to re-assess their attitudes towards countries "having Communist parties in control of government." The Communist press uses the same language in urging the same appeasement. Now get this — "In Russia and China communist philosophy has endeavored to assimilate the deep traditional sense of national destiny."

Christians are urged to make "stronger efforts to break through the present stalemate and to find ways of living with the communist nations." The Communist press urges the same. We are then lectured that "communist nations have their own legitimate interests and their own reasonable fears. We should avoid the posture of general hostility to them and cease the practice of continual moral lectures to them by our leaders." . . .

The Communists are not expected to "formally renounce what we consider to be their errors." So it is up to us to practice "self-criticism" and find ways and means of accommodating our way of life to co-existence with world Communism. This requires "tireless negotiations with them and imaginative programs of communications, cultural exchange and personal contacts." This . . . appeasement . . . of . . . Communism which openly boasts that it intends to bury us, could only have been written by a deeply buried secret Communist or a craven and spiritually empty fool. Indeed, the Communist press gleefully gave front page coverage to this incredible prescription for surrender by the National Council of Churches. . . .

Yet the National Council's General Board, while . . . "receiving" the World Order Study Conference's statement, . . . inserted the claim that the conference "spoke with a mighty voice." To what mighty voice do they refer? It could be no other than the voice of 38 million Protestants that they claim (erroneously) to represent.

Even more reprehensible was the . . . claim that the vote had been "unanimous." That is what the newspapers said and that naturally was what millions of Americans assumed to be a fact. . . .

Was it unanimous? No, it wasn't. A number of delegates present and voting later claimed they had voted *against* the recognition of Red China statement and were quite indignant about the "unanimous vote" press release. They had learned painfully and at first hand what "group Dynamics" meant as interpreted and used by the N.C.C.C. The ultra-liberal N.C.C.C. has a very illiberal little sleeper clause in its conference rules that minority dissent is registered and made public *only* when it exceeds 25 per cent of the delegates entitled to vote. In other words, if there were 500 delegates voting on the question of recognizing Red China and 124 in opposition, the result nevertheless would be announced as "unanimous." . . .

. . . Secretary of State Dulles, who had spent years of his life building the Federal Council of Churches and in helping found the World Council of Churches, was reported as having privately admitted to a friend that it was "the most devastating experience of my life!"

This . . . incredible pro-Communist propaganda stunt of the National Council naturally aroused nationwide protest from religious leaders and laymen alike. . . .

An Example Of Questions For Which Bureaucrats Spend Tax Money

The following is taken from the *Wall Street Journal,* April 24, 1959. It is an example of degeneration of government under the influence of statisticians and pressure groups. Bureaucracy is a disease that grows and grows unless it is strongly resisted.

How Many Hog Pens Have Running Water? Agricultural Census To Provide The Answer

WASHINGTON. Uncle Sam doesn't care any more how many mules a farmer owns — not to the point of asking him, anyway.

But the Government does intend to find out how much a farmer owes his veterinarian, and whether a new chicken house has a wooden or metal roof, and whether a farmer's hog pen has running water. And it expects straight answers to these suspenseful questions: How much butter is churned by the womenfolk on North Carolina farms? What's the value of cassava output in the Samoan Islands? How many farms have telephones? Home freezers? Electric milk coolers?

All this and much, much more will be sought, and presumably discovered, in the next year and a half during the Federal Government's seventeenth census of agriculture. This exhaustive survey of the nation's rural scene — conducted once every five years — will start next fall. It will cover every state, plus Puerto Rico, American Samoa, Guam and the Virgin Islands. It will be run separately from the 1960 count of the whole U.S. population that starts next April, although farmers will be included in that one, too.

* * *

Most of the suggested questions come from the Agriculture Department's battalion of farm specialists, all interested in getting data for some special project. "There's an awful lot of competition for space on the questionnaire," says Earl Houseman, the Agriculture Department's liaison man on census matters.

* * *

The entire farm census will cost around $24 million, compared with an estimated $118 million needed for the national population census. It will take until September, 1961, to publish the collected findings in some 54 separate volumes totaling 10,000 pages.

The British government beginning with the Labor Government after World War II has also been bureaucratic in character. The following is a news item in the *El Paso Times*:

Britons Coached On Shoveling

LONDON. Britain's nationalized Coal Board solemnly told Britons Sunday how to shovel their own coal. A 46-page manual said shoveling coal is a snap. This is how it is done:

Examine the shovel. Approach the coal. Grasp the shovel. Make a forward stroke. Raise the load. Then don't just stand there — do something. "Swing the shovel in the direction in which the load is to be thrown," the board pamphlet said.

Some people, misinterpreting Romans 13:1-7, believe that everything a government does must be patiently tolerated, because the "powers that be are ordained of God" and that "whosoever . . . resisteth the power . . . shall receive damnation to themselves." Maybe God is speaking to Englishmen through the British government's Coal Board, but we happen to lack the ability to believe it. And we are confident that anyone failing to shovel coal as the Coal Board directs will not "receive damnation unto himself" on *that* account.

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FIRST PRINCIPLES
IN MORALITY AND ECONOMICS
on which depend personal well-being and social health and harmony

VOLUME V | JUNE, 1959 | NUMBER 6

Contents

Russian Interest In American Unemployment

Recently *The Chicago Tribune* published a series of articles on Russia by Max Frankel. He writes:

> . . . the traveler is left with raw particulars in his notebook of things said and asked, overheard or noticed about some Russian people.
>
> Here are some excerpts from that notebook: . . .

After citing various matters Frankel goes on:

> The unemployed. Always the unemployed. [Frankel is referring to the Russian ideas about American unemployment.] It is a horror ever present in the minds and literature of the Soviet Union.
>
> Why can't you plan to have jobs for all? Why don't you do something? What do the unemployed do? Who helps them? Do they lose goods bought on credit?

The most effective propaganda by socialists-communists against capitalism is capitalism's periodic mass unemployment.

We are continuing in FIRST PRINCIPLES our analysis of the *cause* of the business cycle, and its attendant unemployment. The *cause* is not inherent in capitalism, but is a specific evil that capitalism is wilfully cherishing in its bosom to its own destruction.

Further, the present trend of the policies of the United States, although intended to moderate the business cycle and alleviate unemployment, are really aggravating the problem. The situation in total will become worse rather than better, *unless the people of the United States reverse their basic policies.*

An Explanation Of Preference For Security Over Freedom

Political theorists deplore an *alleged* trend on the part of the citizens of the United States toward the preference for security over liberty. If there is such a trend, and there may be, an assumption may be made that there is deterioration in the fibre of the citizens of the United States, that is, that they have lost the fearlessness and initiative that their ancestors possessed. The purpose of this note is to call attention to some changed circumstances, which in our opinion explain to some extent a greater emphasis on security than on liberty. Not that we consider security to be preferable to liberty; we strongly prefer the latter.

There are today in the United States at least two factors which cause greater internal insecurity than before. These two causes are (1) economic instability (the business cycle) and (2) labor immobility. As in this article we intend to point especially to economic instability as a cause for a yearning for security, we shall first dismiss the second factor with a few comments.

Circumstances Making Labor Immobile

By labor *immobility* we refer to the handicaps which a man must surmount before he has another job, if he loses or quits his present employment. Consider the effect of *seniority,* a system by which men are laid off not according to ability or industry, but according to length of service — a man with a short term of serv-

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ice being laid off before a man with a long term of service. Maybe the short-term man is in a weaker position because of a wife and small children, etc. The thing for a man to do is to accumulate seniority in order to be more secure. Hence, men become less mobile in employment than otherwise.

Or consider the requirement of union membership. Many jobs are not available except at the pleasure of those who are managing a union. This *union* power is a rather uncontrollable factor. Men dare not fight it, because the law gives unions *special* privileges, which no other organization has.

And consider pension and profit sharing rights. Many of these are set up so that a man is not benefited until he has a considerable period of service with that company; and further the benefits are not "vested", that is, a man cannot take along his accrued benefits to another location until after 10 years or more, if at all.

In "the good old days" (?), jobs were not so specialized; everything was more variable, there were no restrictions holding a man to a single job, and if he lost it he did not lose valuable *accrued* benefits of various kinds. The *framework* in which men find themselves is more formidable than before. It sobers and often frightens them. Therefore, anything that promises them security appeals mightily to them.

An illustration may make the situation more obvious. Above all a man needs food and clothing and shelter. Imagine a time one hundred years ago when a carpenter could find no work. But he and his family would have to eat and survive somehow. He might rent some land for a big garden and supply food in that manner; in effect, he would become a small, subsistence farmer. With modern industrialization and gigantic cities that is often no longer feasible today. Nor can a carpenter become a *real* farmer today without a capital of say $10,000 for tools and equipment. He may not have that much capital. Further, farming today is more complex than plowing, planting and hoeing. *Alternatives* today for a man who quits or loses his job are probably less available than they were two or more generations ago. Consequently, the average man is naturally and legitimately interested in anything that promises him more security. (We may at a later date discuss factors which will give greater mobility to labor, under modern complex conditions.)

The Cause of the Business Cycle Is Practically Unknown

Economic instability plays an equally great part in the modern search for security, even at the cost of some loss of liberty. This economic instability consists of booms and depressions; mass unemployment; the business cycle.

No man is presently immune to the business cycle. Rich and poor, wise and foolish, the strong and the weak, employer and employe, the big business man and the little business man, manufacturers and retailers, doctors and lawyers — everybody, in fact, is afflicted by this economic instability.

What *causes* this economic instability? All kinds of answers are given. Some say underconsumption; others, overproduction; others, too low wages; others, too little money; the explanations are endless. Some are amusing as that of the newspaper man who declared that the business cycle is caused by "too many people having automobiles." (To what absurdities is the human mind subject!)

The number of those who know the *real* explanation of the business cycle is apparently small. And there appear to be still fewer who are prepared to go to the heart of the problem and correct it; they seem to be so few in number that it is reasonable to be pessimistic.

Let us consider a graduate engineer, excellently educated, in physics, electricity, and electronics; (or take any phase of engineering that you wish). After getting, say, a Ph. D. degree in engineering and going to work for some engineering company, and working there on some specialty — what, indeed, will he probably know about the *cause* of booms and depressions? He has probably never systematically endeavored to analyze the problem. He will probably know as much as he reads in the daily papers or in the magazines which predigest news and manufacture interpretations and subtly induce attitudes. Here is an intelligent man, of good character and a responsible citizen, but quite helpless in regard to his own security in the business cycle. Nor is his position unique; his employer is probably equally helpless, unless he is a business man very much out of the ordinary.

And so the terror which men have of economic instability — booms and *depressions* — is easily understandable, and even excusable because it is a terror of what is not understood. Of course, men then turn toward something which they think will give them security, and any demagogue who promises security finds the average man an eager listener.

The socialists build their appeal essentially on two emotions — covetousness and *fear.* They say (falsely in theory, but truly in fact) that capitalism has a systematic insecurity — regular booms and depressions — which will eventually destroy capitalism. They are right; as presently mal-organized, capitalism has a built-in feature which causes booms and depressions. What capitalism needs to do is to turn from its present evil practice, and purge itself of the cause of booms and depressions.

Unsound Credit Laws and Policies Cause the Business Cycle

The *cause* of booms and depressions is associated with questions of money and credit. The laws of money and credit, in the United States and in other capitalist countries in varying degrees, are inadequate, or evil, whichever word you prefer. Those laws conflict with the moral law. They authorize theft and fraud. Unless and until the law is changed preventing that, booms and depressions will continue in one form or another.

The problem of the business cycle is in a sense simple, but also complex. It is simple in that it is related to theft and fraud; everybody can understand that and ought to be against those evils. But the actual *form* in which such theft and fraud takes place is genuinely complex — practically hidden from ordinary observation.

In these issues of FIRST PRINCIPLES we are endeavoring to make clear the explanation of the business cycle, but not in a formal, textbook manner, because we are writing for nontechnical people. Nor have we organized the material in a systematic manner. To present the explanation in that manner would discourage many readers.

But our efforts will need to be judged charitably and patiently, because the subject is so complex that it is not explainable in a paragraph or two. What is here endeavored is to work through the most difficult subject in economics — money and credit — so that readers will be disposed to use their influence to end booms and depressions — by removing the cause, now imbedded in our Constitution and laws. Further, knowing that all people have a propensity to appeal to morality, we do the same and condemn that cause, in old-fashioned language, as a grievous sin.

In the meanwhile, instead of berating others for wanting security instead of freedom, we are disposed to endeavor to remove the greatest cause of the insecurity, especially because that cause is too great and overwhelming for the average man to cope with.

Attempts to escape this insecurity by *evasion* rather than *correction* will not be a suitable solution, because the mass attempt at evasion would nullify the effort. Some of us may escape the penalties of booms and depressions, because we are in a singularly fortunate position. We may be gaining at the expense of others; their poison may be our meat, but what is needed is a *fundamental removal of the cause for mass economic insecurity.* Current issues of First Principles will continue to struggle with the problem of making that clear.

* * *

If a boy plays a game and the rules are fair to him he will be willing to take a chance on the insecurity of winning. But if the rules are not fair for him, but maybe only for a few initiates, he will seek special security. He will not want freedom but protection. It does not sound unreasonable to us that under such circumstances he demands it. The average employer, employe, professional man, farmer, retailer — the average citizen — is like a boy in a game where the rules are against him.

Freedom is wanted only when there is a sporting chance of profiting from it.

John Law, the Scottish Laird of Lauriston

One of the most fascinating figures in monetary, fiscal and economic history is John Law. All that most people know about him, if they know anything, is that he created a great boom in France in 1716-1719 — for three short years — accompanied however by extreme inflation; and that the boom ended in a terrific collapse, notorious under the name of Mississippi Scheme or Mississippi Bubble. Law was figuratively a financial skyrocket, soaring and exciting on the rise, but coming down quickly as a scorched stick. The whole operation took less than four years.

John Law (1671-1729), Laird of Lauriston in Scotland, is variously described — as a great financier and economist, but also as a gambler, seducer, duelist, speculator and adventurer. His father was a goldsmith in Edinburgh of Jewish extraction. His mother was of the noble Scottish house of Argyle.

When seventeen years old he went to London and lived a life of pleasure and extravagance for nine years. He had a love affair with Elizabeth Villiers, alleged mistress of royalty, and wife of Edward (Beau) Wilson. Law killed Wilson in a duel by shooting him; was sentenced to death; but the sentence was commuted to imprisonment; he fled prison and escaped to Amsterdam, where he studied questions of money and banking.

When 34 years old he returned to Scotland and promoted a scheme for a national bank, which would put out *paper* money (notes) secured by the value of state lands. The Scottish parliament rejected the scheme — *wisely.*

Law then set off on his wanderings; his wife said she was married to the "wandering Jew." He made his living as a gambler. He possessed rare mathematical ability and by computing odds at cards and other games of chance made a good living for himself. He made small progress however at selling his idea of *paper money,* until after the death of Louis XIV of France, the regent, the Duke of Orleans, listened to Law and in 1716, when Law was 45 years old, permitted him to establish the *Banque generale* in France, with a capital of 6,000,000 livres (consisting of 1,200 shares of 5,000 livres each), one-fourth cash and the rest payable over three years in *billets d'etat.* This bank was authorized to issue notes, payable at sight in the weight and value of the money mentioned on the day of issue. On April 10, 1717 the regent decreed that notes of the *Banque generale* would be received in payment of taxes. The operation of the bank had become so "successful" that the rate of interest fell to 4½%! But — and this is illuminating, important and premonitory — *the note issue was increased to 60,000,000 livres,* that is, ten times the original capital of the bank! (The *livre* was worth about twenty cents.)

Let us follow the further steps in Law's career, before describing his policies in economic terms. In 1717 he founded the *Compagnie de la Louisiane ou d'Occident,* in the process absorbing two older companies. Law's company had extensive authority to develop the whole valley drained by the Mississippi, Ohio and Missouri rivers. In 1718 his company acquired a valuable monopoly. Success however stimulated competition, and there was some drop in the shares of Law's company. Nevertheless Law's star continued in the ascendant.

Toward the end of 1718 the name of the bank was changed from *Banque generale* to *Banque royale;* the notes of the latter were guaranted by the king (through his regent, Law's patron).

In 1719 the *Compagnie d'Orient* absorbed the *Compagnie des Indes Orientales et de la Chine* and the merged company was designated the *Compagnie des Indes.* Despite Law's high-powered promotion and despite his overly optimistic expectations, the colonial companies did not expand quickly nor become profitable; (there was not enough time for that, before Law's financial policies were sure to catch up with him).

Law's *Banque royale* obtained the management of the mint and coin issue for nine years; the farming of the national revenues; and it undertook the liquidation of the elephantine national debt of France largely created in the extravagant and warring days of the late Louis XIV.

In the meanwhile this bank, which had begun in 1716 with only one-fourth of it capital of 6 million livres paid in cash, by this time was rapidly approaching a peak in its note issue of 3 billion livres! (The amount of coined metallic money amounted to only 700 million livres.)

In October 1719, the shares of the bank went to 40 times the original value. But the actual climax to the financial orgy came in 1720 when the *Compagnie des Indes* and the *Bank royale* merged.

The smart people, however, for some time already had been observing the hand-writing on the wall. In the preceding fall (1719) shrewd speculators began to sell out their investments in paper securities of any kind, and to replace them with gold, silver, diamonds, lands and *real* property. Eventually, everybody tried feverishly to get rid of *paper* and to own instead *goods.* Tallow, soap and other necessaries rose to fantastic prices. A piece of soap, after all, was a real good, and was worth more than a printed piece of paper. It should have been obvious from the beginning that the public would *eventually* lose confidence in the whole scheme; the only question was *when.*

Law was a man of courage and resource as well as being brilliant (although basically completely unsound). Of course, Gresham's Law, that bad money would drive out good money, was certain to operate. According to that economic law, Law's bad notes would drive out as money good gold and silver; and that is what happened. Drastic measures were taken to endeavor to check the drain of coin out of the country.

On May 21, 1720 a decree was issued by which the value of Law's bank notes was to be reduced gradually to one-half their face value. This action naturally precipitated a panic, which took the form of frantic efforts to get rid of paper bank notes. Law tried to restore confidence by paying out metal as long as he could, but of course the bank could not pay out metal for all the notes for billions of livres which had been issued, and so the bank suspended payments, went broke — in a week.

Law was removed from his position. His system was destroyed by those who had opposed him and seen it operate destructively. In December 1720 Law secretly left France, returned a while to England, resumed his wandering and eight years later in 1729, at the age of 58, died in Venice in *straightened circumstances.* The burnt stick of the skyrocket had come down!

Law himself seems to have believed sincerely in his scheme to the day of his death. He attributed its failure in France (1) not to the basic unsoundness of his economics, (2) nor to the immorality of his monetary ethics, but (3) entirely to the enmity of others and the panic and lack of confidence of the public. Surely, he was a dazzling man of action — a profligate, seducer, duelist, monetary student, banker, politician, the man who created the greatest one-man inflation-boom and crash in history, and a talented economic theoretician and author. Despite all his brilliance, courage and force nevertheless a bedraggled failure in the end.

Those who wish to learn more of John Law might first read, especially if they want entertainment, Raphael Sabatini's *The Gamester* (Houghton Mifflin Company, Boston, 1949). Anything written by Sabatini is enthralling and brilliant, and not too bad history (but, of course, not *history*). The important English biography of Law is by A. W. Wiston-Glynn, *John Law of Lauriston* (1907). Law himself wrote more than one book; the best known carries the title, *Money and Trade Considered, with a Proposal for Supplying the Nation with Money* (1st edition, 1705; republished in Somers' *Tracts,* 1809).

The reputation of Law has fared amazingly well in the appraisal by historians and economists. The reason is not easy to find; maybe the explanation is the fact that *inflation* is so extremely seductive and adorable as a proposed solution to economic problems, similar to a beautiful woman with excessive muliebrity.

Schumpeter in his History of Economic Analysis (Oxford University Press, 1954) page 295f. writes of Law as being in "a class by himself." Schumpeter wrote:

> He worked out the economics of his projects with a brilliance and, yes, profundity, which places him in the front rank of monetary theorists of all times. And this is all that matters for us. Since it is plain, however, that his analysis has been condemned, for about two centuries, primarily on the strength of the failure of his *Banque Royale,* it is pertinent to point out, first, that its predecessor, the Banque Générale, founded 1716, was a perfectly orthodox bank that was to issue notes and to receive deposits payable on demand and to discount commercial paper — no antimetallism about that — and that the *Banque Royale* and the *Compagnie des Indes,* which it absorbed, failed because the colonial ventures combined in the latter did not, for the time being, prove to be the source of anything but losses. If these ventures had been successful, Law's grandiose attempt to control and to reform the economic life of a great nation from the financial angle — for this is what his plan eventually amounted to — would have looked very different to his contemporaries and to historians. Even as it was, that gigantic enterprise was not simply a swindle and it may well be doubted whether France was the worse for it, on balance. However, economists not only fell in with the popular opinion that the scheme was nothing but swindle but also pointed to certain technical defects in it that were in fact important subsidiary causes of its failure. Thus that event acquired considerable influence on the evolution of what eventually became the classic theory of banking. . . .
>
> One of his plans was concerned with a land bank that was to issue legal tender paper money up to a certain proportion of the value of land and to receive as deposits *for placement* money that would otherwise lie idle, so that money would never be either too cheap or too dear. In this he followed the English land-bank projectors . . .

Later in his book, Schumpeter (page 321f.) designates John Law as the "ancestor of the idea of a *managed currency*" (our italics). Schumpeter is probably correct about that, and it is probably equally correct to add that a *managed currency* is the very essence of present-day (1959) monetary theory; and so Law's ideas are the prevailing ideas in the banking world today! Schumpeter wrote:

> *(b) John Law: Ancestor of the Idea of a Managed Currency.* Manufacture of money! Credit as a creator of money! Manifestly, this opens up other than theoretical vistas. The bank projectors of the seventeenth century, especially the English land-bank projectors and Law, . . . fully realized the business potentialities of the discovery that money — and hence capital in the monetary sense of the term — can be manufactured or created. Their reputation, at the time and later, suffered greatly from the failure of their schemes — Law's schemes in particular — just as, in the nineteenth century, the reputation of fundamentally similar ideas suffered from association with wild-cat banking and with the failures of schemes that turned out badly without being fraudulent or nonsensical, such as the *Crédit Mobilier* of the brothers Pereire. But since there is a far cry from an economic principle to a banking project, these failures are not evidence in the court of theory.

The idea of Schumpeter that it was a great "discovery" (rather than a great hallucination) "that money — and hence capital in the monetary sense of the term — can be manufactured or created" is a shocking economic fallacy.

Schumpeter goes on to explain that there is *some* evidence that Law was a "metallist," a hard-money man. However, the evidence is really wholly inconclusive; the *fact* is that Law was just the opposite.

What has especially intrigued later economists is Law's excellent analysis of how certain metals (gold and silver), used for money, acquire their *value*. Obviously these metals have value for industrial uses. The question is: what is the effect on the value of gold that it is also in demand *as money*. All subsequent economists are indebted to Law for that analysis. Law wrote: "Money is not the value for which goods are exchanged, but the value by which they are exchanged. This makes clear that Law did not consider *gold* to be a good monetary unit and a good hedge against inflation, *just because it had value as a commodity in the industrial arts;* contrarily, Law realized that the value of gold depended on its monetary use as well. On this he was entirely and lucidly correct.

But then Law jumps to his fallacious and fatal conclusion, namely, that in order to insure an *adequate money supply* the quantity of money *should be managed.*

Schumpeter describes Law as the "genuine ancestor" of the *managed currency* idea, which came into vogue (as if it were new!) in 1919. Schumpeter considers Law's original *Banque generale* "almost orthodox"; Law's *Compagnie des Indes* "more visionary"; and Law's last measures in 1720 during the crash as the "ultimate resort of a strong swimmer in his agony," but Schumpeter appraises it all as a "great plan" for "controlling, reforming and leading on to new levels the whole of the national economy of France." Schumpeter considers that idea of comprehensive management of an economy as the feature that "glorifies" Law's main treatise on money. It is this very principle of a *managed currency* which is the worst cancer in present-day capitalism.

Others beside Schumpeter are sympathetic to Law's *managed currency* ideas, but despite all the sympathetic acceptance of it a managed currency means uncontrollable inflationism — that is, uncontrollable whether or not the would-be actual managers think they have control of it. The adjective, *managed,* in the term, managed currency, implies or assumes that some demi-god bureaucrat can *manage* or *control* a monetary system, but all history proves that such men have never existed. The monetary system must be "unmanaged" by *individual* men; if it is to be safe and sound it must instead be *managed* by economic law in order to be reliable and conducive to prosperity.

The *Encyclopedia Britannica* article on Law ends with the somewhat contradictory statement: "Though subject to the errors of his time, *he was undoubtedly a financial genius*" (our italics). Collier's *Encyclopedia* ends with the still more erroneous statement: "The credit basis of Law's schemes was sound, but they could not justify the public belief that they would produce untold wealth." This statement should read: "The credit basis of Law's scheme was *wholly unsound* . . ." It was not the belief of the public that Law's scheme would "produce untold wealth" that caused the eventual catastrophe.

The *Encyclopedia of the Social Sciences* does no better. Its article on John Law contains the following:

> . . . "commerce depends on specie" which consists of precious metals. As these are rare, Law conceived the scheme of substituting for metallic currency paper money, which can be created at will and more easily transported, the cost of which is insignificant and the circulation much freer."
>
> * * *
>
> As the value of money does not result from its intrinsic

> nature but from the uses to which it is put, the public would become use to it and accept no other. Then the bank could extend its activities and e.g., redeem the public debt by profitable commercial operation . . .
>
> * * *
>
> The combined bank and company failed owing to paper issues far beyond the necessary security, for which the regent [the Duke of Orleans] appears to have been mainly responsible.

There is also mention in this encyclopedia of lack of confidence engendered by "overexpansion" of the combined activities (of banking and colonial development) and of too much haste.

* * *

In the two preceding issues we gave information on a Canadian lady whose solution of the problem of prosperity in Canada consisted in the simple formula — *more money* — obtained through more credit extension. Basically her idea was identical with John Law's. To this question on how to increase prosperity either of two answers might be given: (1) more production; (2) more money. The Canadian lady and John Law are among those who have held or hold that more money creates more prosperity!

* * *

We have now mentioned three men as representing three different schools of thought on the question of money and about the influence of changes of the quantity of money on prosperity. These men are John Law, a brilliant financial adventurer and monetary theorist; Henry Thornton, devout evangelical and conservative banker; and Ludwig von Mises, the greatest living economist. Law essentially was a man who would *increase* the amount of money; Thornton was a man who would tolerate *variation* in the amount of money by voluntary action of men; Mises is a man who would neither increase nor vary the quantity of money by any action of an individual who considered himself called upon and competent to "manage" the currency supply. Law would *manage* money; Thornton would have the quantity of money *respond* to trade variation; Mises believes neither in *managing* money nor *responding* to changing business conditions, but instead making the quantity of money subject to *economic law* only. All this should become clearer later in this issue and in future issues.

On this money question, as generally in regard to his economics, we adopt the views of Mises. All logic is on his side; and also the moral teachings of the Hebrew-Christian Scriptures.

To Adjust To Economic Reality There Are Two Alternatives, The First Immoral And The Second Moral, Namely, (1) Varying The Quantity Of Money, Or (2) Varying The Prices Of Goods

There is a choice between good and evil in economics as definite as the choice of Adam in the Garden of Eden when he decided whether or not to eat the fruit of the forbidden tree.

That choice concerns the question whether economic objectives of all kinds — matching supply and demand, expanding one industry and contracting another, full employment, hope of prosperity — are to be made by varying the quantity of money, or by adjusting prices. The former, when thoroughly understood, is as definitely unsound as anything can be. The choice then becomes a choice between good and evil.

In the explanations which follow we shall compare and contrast three answers: (1) the answers of men who wish to create or *increase* the quantity of money; (2) the answers of men who wish to *vary* the quantity of money; and (3) the answers of men who do not wish to create money. To make the analyses more interesting we shall use individual men as prototypes of these three programs: *John Law* as a prototype of the money creators; *Henry Thornton* as a type of the money variators; and *Ludwig von Mises* as a type of the men who *seek neither to create nor vary the quantity of money, by fiat action of men (the state).*

In *private* morality all men of honor are with Mises; they are all against counterfeiting. But in *public* morality nearly all men of honor (so-called) are with Henry Thornton, at a minimum; and basically they are often with John Law; the Thornton men are the men who favor the present *variable* credit policy of the United States Federal Reserve Board. The John Law men are all those who talk about reducing gold reserve requirements of Banks, or changing the gold content of the dollar, etc. In First Principles we follow Mises — on questions of both private and public morality. We are against the creation of money — always. It is the path to ruin.

Let us tie in what will be presented in this issue with what was published last month. In that issue attention was called to a peculiar and paradoxical cause for there being a shortage of money, namely, fear that the quantity of money will be increased. The mechanism by which this fear of an increase in the quantity of money creates a shortage is as follows: sellers have anxiety that the prospective increase in the quantity of money will result in a rise in prices of goods before they themselves will be prepared to buy again. Their imagination then goes to work and they try to advance prices even faster than the feared increase in the quantity of money actually occurs. And so there is a "shortage of money." Taking into account such increases in prices there is not enough money to result in all goods and services finding buyers, and so some of these go a-begging, i.e., because of a "money shortage." Obviously, a "money shortage" in this case is caused not by the insufficiency of the actual money supply but by the *expected* increase in the supply, which reflects itself in the too-aggressive pricing policies of sellers.

From the foregoing, an important conclusion can be reached. It is this: *a money shortage is unthinkable, except in relation to pricing goods and services.* If there is a shortage of money, that can be corrected in two ways: (1) increasing the quantity; or (2) lowering prices.

Let us say that there is available $100,000 in money, and that there is a quantity of various kinds of goods and services all properly priced to total $100,000. (Let us assume a turnover of goods of one.) The goods should then all be "turned over," that is, sold, and money and goods are "in balance" because prices are right. There is no shortage of money.

Let us next say that there is a change in the situation with sellers increasing prices to a total amount to $120,000, but that the quantity of money remains the same at $100,000. There is now a "money shortage." Some goods — $20,000 worth — will not be sold. The money quantity has not decreased, and so it is really incorrect to say that there is a money shortage. The real cause of the imbalance is that prices were increased unduly. Still, in popular usage, this situation may be described as a money shortage.

Next, let us say that there is no change in either prices or the quantity of money. Both are constant. But let us vary the physical quantity of goods. Let us say that the physical quantity is increased 20%. The 20% larger quantity at the old price means that $120,000 is needed to move the whole quantity. But the money amounts to only $100,000. Again there appears to be a money shortage. But what ought the correction to be? The price of the individual units should be reduced enough so that the $100,000 would suffice to move the whole quantity.

Let us continue our variations in circumstances. Let us next assume there was an inescapable and unfortunate reduction in physical production. There is now only $80,000 worth of goods. But the money supply is $100,000. At the old prices, $20,000 of the money supply will not be used. Do we then have too much money? Or should prices be increased so that they aggregate $100,000. Anyone taking that view — which is the correct one — espouses the proposition that prices should be increased whenever there is a disturbance between the relation of the supply of goods and the supply of money, with the disturbance being caused by the supply of goods. The alternative is to reduce the supply of money in some manner — maybe arbitrarily — to $80,000. There might be an assessment by which 20% of the money supply was called into a central depot and destroyed. But this is never proposed, nor is it sound.

There is, it will be clear, a choice open to all who are concerned about the *money supply.* They can "solve" the problem in either of two ways: (1) change the money supply; or (2) let prices be flexible, that is, not permit anyone to use coercion *of any kind* to decrease or increase prices.

If prices for everything — goods and services without exception — were genuinely flexible, then for all practical purposes *there would never be a money shortage.* All "money shortages" are really caused by prices not being flexible and/or right.

A fantastic fear — a phobia — has developed among men. That fear consists of anxiety and alarm about price *reductions,* particularly reductions in the price of labor, but also of commodities as, for example, of farm products. It is a fear besetting nearly everyone.

And so men come to the alternative solution: instead of flexible prices — instead of relying on the "market" and being prepared to abide by it — men turn to *varying the quantity of money.* This varying of the quantity of money was at one time considered to be a problem of increasing *and decreasing* the quantity of money, that is, it was a question of *varying* the quantity of money rather than *increasing* it. But the inveterate tendency is to change that to *increasing only*. The former opened the door to the latter. Once it was agreed that the solution was not *variable prices* but *variable quantities of money*, a fatal principle was adopted. What psychology, economics and morality all taught consistently was thereby abandoned.

Now, it is not socialism that perpetrated this abandonment of wisdom and morality in regard to the question of keeping money and goods in balance, but men who were "capitalists" in every popular meaning of the term.

In the early years of the nineteenth century there were two "schools of thought" regarding varying the quantity of money — one the *Banking School* and the other the *Currency School*. Of these two the Currency School was by far the more right, but in principle it was not wholly right either. Both schools of thought were thinking in terms of varying the quantity of money rather than relying fully on varying prices.

Great errors and great sins are not perpetrated heinously by "good" men. When they finally end up in an immoral morass and in practical ruin, they got there by small steps, all designed for "good purposes." From step to step they went the downward path, not realizing to where it would lead.

External dangers may or may not destroy capitalism, but an internal danger gravely threatens it. Unless capitalism reforms — relies solely on flexible prices and abandons the idea of a flexible quantity of money — it will be destroyed.

Matters Of Money Need Not Be Identified With Mammonism

The dictionary defines *Mammonism* as "devotion to the acquisition of wealth; worldliness." The term comes from the name of the Syrian god of riches.

This would be a sorry world if everything pertaining to money would be described as mammonism.

Money (as a tool for facilitating exchange) is one of the greatest blessings men have ever obtained. Where is there a society, and where are there men, who wish to have a moneyless society?

A moneyless society would mean that men could exchange — that is, *cooperate* — only by barter. When business cannot be transacted except as barter, society will be grievously impoverished.

Mammonism really refers to avarice for riches; (we are not here defining avarice.) Money may be a symbol for avarice. But such a metaphorical use of the word *money* in connection with avarice should blind no one to the great utility of money as a *means of exchange*. In this last sense money is an unmixed good.

Some of the interpretations of statements in the Hebrew-Christian scriptures about serving God or Mammon are unrealistic. Such interpetations are usually studies in *motivations*, that is, potential forms of avarice, which are not being discussed here; instead attention is being directed to money as a *means* to an end: to wit, as a tool for facilitating exchange. The question here is whether money *as a tool* can be grossly misused, as well as avarice can be a perversion of the proper, admirable desire for good and fine things. Unfortunately, in the arrangements for using money as a tool for the good end of exchanging goods, as great evils have crept in as avarice is an evil in itself.

Although money as a tool can be wonderful, its fine function can be abused. It is that phase of money that we are considering. Obviously, this has nothing to do with Mammonism, in the sense of avarice.

The Demand For Money, In Economic Science

The *demand for money* is a term that can have many meanings.

It may mean, for example, that we all have desires greater than our means in terms of money; we want more money in order to get more goods than we have; in other words we have some need, wish or covetousness which exceeds our means. We are not using the term *demand for money* in that popular and dubious (maybe covetous) sense. Instead we refer to *demand for money* in the framework of the science of economics.

In economics, the term *demand for money* means quite the opposite of the popular sense just described. In the popular sense, the demand for money is demand for money *to spend*. In economics, the demand for money is money *to hold*. Everybody who has foresight and judgment has a demand for money (*as* money, or *qua* money), to have as a reserve against emergencies and future needs.

If Percy is a clerk for a company and receives his pay every two weeks he has a demand for money, at a minimum, which consists of enough to pay his expenses for surviving for 14 days. If it costs him \$8.00 a day to live, then his demand for money on payday is 14 days x \$8, or \$112; on the next day, 13 days x \$8, or \$104; and so on down to 1 day x \$8, or \$8. Percy's demand for money, then, varies depending on his circumstances; or his estimation of his circumstances; his minimum demand appears to be for the various days in a two-week period, \$112, \$104, \$96, \$88, \$80, \$72, \$64, \$56, \$48, \$40, \$32, \$24, \$16 and \$8, an average of \$60. But the average is meaningless. The demand varies acutely from day to day, and Percy is operating financially in a hazardous manner. He has no reserve whatever on the last day if his employer fails to pay him on payday, or if Percy is sick on that day and cannot get his paycheck. Most people will want more money on hand than merely to squeak by, with just enough to pay the last meal before the next check is received. Percy may, if he is of a more prudent type, have a demand for \$200 as a general reserve plus the daily variations between paydays. Just after receiving his pay his demand for money will then be \$112 plus \$200, or \$312; it will go down by \$8 a day so that just before the next payday he will have a demand for money of \$8 plus \$200, or \$208.

Everybody's demand for money *varies*. If someone has so much that he hardly ever calculates whether he needs more or less, then the situation is not correctly described by saying his demand for money is invariable, but by saying that (for some reason or other) he has such a large demand for money *relative to his actual needs*, that it *seems* his demand does not vary.

In an economic sense, the *demand for money* is the amount a man estimates he needs as money against his requirements, before more money becomes available to him. It is the *store* of money, in one form or another, that people need or at least want, to take care of their known needs and emergencies.

The demand for money will vary not merely according to needs, but also according to temperament. A thrifty, provident man seeing potential dangers of all kinds, will have a bigger demand for money than a careless, optimistic man.

Finally, the same person will not have the same demand for money according to a predictable pattern. If something suddenly scares him, his demand for money will immediately increase — as a protection to himself. If he becomes buoyant in enthusiasm and expects money soon to come rolling in, he will reduce his current demand for money proportionately; why have "idle" money, when it will soon be coming in faster than needed.

The variation in the demand by men for money will have an effect on the business cycle. Suppose everybody becomes optimistic because money seems plentiful, because the banks are liberal in creating new credits — creating fiat credit (see April issue, page 119ff. for the significance of fiat credit). The demand for money *in the economic sense* (i.e., demand for money as a reserve to hold) will then decrease. What does that mean? People will prefer goods and services to money; they will bid for goods and services; prices will go up. But now assume that bankers become apprehensive about the soundness of an economic situation. Instead of putting out more fiat credit they demand payment on the old credit. The psychology of businessmen will then change. Men will try to accumulate money — that is, their demand for money will increase — but the only way that they can accomplish that is by selling more and buying less. For everybody, or at least most people, to try to do that, means that prices of goods will go down. How could it be otherwise when nearly everybody wishes to sell and few wish to buy. Then confidence is disturbed further. More and more people increase their demand for money (in an economic sense). Prices tumble. People become unemployed. We have a depression.

In regard to this demand for money we shall quote Henry Thornton, the great banker, the Christian leader, and monetary theorist, whom we described in the preceding issue. Thornton says the same thing that we have just said. But before quoting Thornton it is desirable to make a few explanatory remarks so that what is quoted will be more readily understandable. Thornton wrote a book which is famous in economic history, entitled, *An Enquiry into the Nature and Effects of the Paper Credit of Great Britain,* originally published in 1802, and republished in 1939 by Rinehart and Company, Inc., New York, with an introduction by Prof. Friedrich A. von Hayek. Thornton begins his book by describing

Commercial Credit, Bills of Exchange, Real Bills and Fictitious Bills, Notes of private banks, and Notes of the Bank of England. He explains which of these kinds of money people will be willing to retain, according to their *demand for money* under various circumstances. Readers of the quotation should keep the general thought in mind which we are discussing, namely, that the demand for money (money to hold as a reserve) increases in times of anxiety, and decreases in times of optimism. The additional point that Thornton makes, to wit, that people will prefer safer money for their fund of money than less-safe money will be obvious to all. And, of course, it will be readily imagined by readers who have not read all that Thornton explains prior to what we are quoting, that the promissory notes of an ordinary merchant may be less acceptable as money, in bad times, than the promissory notes of a big private bank; and that the notes of a big private bank may not be so acceptable as a promissory note from the Bank of England. All this will be considered later, because of its fundamental importance, but at this time we are quoting Thornton only in order to emphasize how public psychology will affect the size of the *demand for money*. We quote from Thornton's book, pages 96 to 98. (The italics have been added.)

> Now a high state of confidence contributes to make men provide less amply against contingencies. *At such a time, they trust, that if the demand upon them for a payment, which is now doubtful and contingent, should actually be made, they shall be able to provide for it at the moment; and they are loth to be at the expence of selling an article, or of getting a bill discounted, in order to make the provision much before the period at which it shall be wanted. When, on the contrary, a season of distrust arises, prudence suggests, that the loss of interest arising from a detention of notes for a few additional days should not be regarded.*
>
> *It is well known that guineas are hoarded, in times of alarm, on this principle.* Notes, it is true, are not hoarded to the same extent; partly because notes are not supposed equally likely, in the event of any general confusion, to find [that is, retain] their value, and partly because the class of persons who are the holders of notes is less subject to weak and extravagant alarms. *In difficult times, however, the disposition to hoard, or rather to be largely provided with Bank of England notes, will, perhaps, prevail in no inconsiderable degree.*
>
> This remark has been applied to Bank of England notes, because these are always in high credit; and it ought, perhaps, to be chiefly confined to these. They constitute the coin in which the great mercantile payments in London, which are payments on account of the whole country, are

effected. If, therefore, a difficulty in converting bills of exchange into notes is apprehended, the effect both on bankers, merchants, tradesmen, is somewhat the same as the effect of an apprehension entertained by the lower class of a difficulty in converting Bank of England notes or bankers' notes into guineas. The apprehension of the approaching difficulty makes men eager to do that to-day, which otherwise they would do to-morrow.

The truth of this observation, as applied to Bank of England notes, as well as the importance of attending to it, may be made manifest by adverting to the events of the year 1793, when, through the failure of many country banks, much general distrust took place. *The alarm, the first material one of the kind which had for a long time happened, was extremely great. It does not appear that the Bank of England notes, at that time in circulation, were fewer than usual. It is certain, however, that the existing number became, at the period of apprehension, insufficient for giving punctuality to the payments of the metropolis;* and it is not to be doubted, that the insufficiency must have arisen, in some measure, from that slowness in the circulation of notes, naturally attending an alarm, which has been just described. *Every one fearing lest he should not have his notes ready when the day of payment should come, would endeavour to provide himself with them somewhat beforehand. A few merchants, from a natural though hurtful timidity, would keep in their own hands some of those notes, which, in other times, they would have lodged with their bankers;* and the effect would be, to cause the same quantity of bank paper to transact fewer payments, or in other words, to lessen the rapidity of the circulation of notes on the whole, and thus to encrease the number of notes wanted. Probably, also, some Bank of England paper would be used as a substitute for country bank notes suppressed.

In times of economic alarm the rate of circulation of money decreases. People wish to get hold of money earlier than otherwise; they want more for apprehended emergencies; they let go of money slower. The *demand for money* is then greater than normal. Then prices *must* fall. If they do not, unemployment *must* ensue. Depression will be here just as sure as the earth rotates, and the sun seems to rise and set.

The Worst — Most Dangerous — Clause In Any Of The Articles In The Constitution Of The United States

Paragraphs 5 and 6 of Section 8 of Article I of the Constitution give the following General Powers to the Congress of the United States:

5. *Money, weights and measures.* To coin Money, regulate the Value thereof, and of foreign Coin, and fix the Standard of Weights and Measures.

> 6. *Counterfeiting.* To provide for the Punishment of counterfeiting the Securities and current Coin of the United States.

The innocent-sounding clause in paragraph 5, which may be the underlying cause of the eventual disintegration of the United States, is the clause "to regulate the Value of Money."

In contrast, Section 10 of the same Article I of the Constitution restrains the individual states on an entirely different basis; Paragraph 1 of Section 10 reads (our italics):

> *No state shall* enter into any Treaty, Alliance or Confederation; grant Letters of Marque and Reprisal; *coin money; emit Bills of Credit; make any Thing but gold and silver Coin a Tender in Payment of Debts;* pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts, or grant any Title of Nobility.

Undoubtedly the restriction is wise which prohibits the individual states from "coining money" or "emitting Bills of Credit;" or of making "any Thing but gold and silver Coin a Tender in Payment of Debts." To have "complexified" the money situation in The United States by permitting the *individual* states to coin money, emit bills of credit, or make anything except gold and silver legal tender in payment of debts has nothing to commend it.

The question is: were the states prohibited from doing those things for the narrow technical reason that they should not "complexify" monetary and credit matters; or were they prohibited from doing those things because one or all of them *are wrong in principle;* that is, should they not have those powers because no government of any kind, high or low, big or small, should have all those powers?

It is noteworthy that the individual states may specify that gold and silver coins are legal tender and may be used for paying debts. *Gold* and *silver coin* are here put in a different class from any other "legal tender" money. The implication is that there cannot be a legitimate objection to gold and silver coins as being legal tender, but that other "legal tender" may be or always is of a more-questionable character, and that therefore the states may not make anything but gold and silver coins legal tender. There is however no restriction of a similar kind on the Federal government: it can "coin money and regulate the value thereof" without *any* restraint whatever. The Federal government may print paper money as Congress wishes, according to its capricious pleasure.

Interestingly, too, the Federal government has decided that gold coins are not to be legal tender in the United States; it has been decreed in fact that no individual may own gold for monetary purposes. Consequently, the right reserved to the states to make gold and silver coins legal tender is now utterly meaningless.

The clause authorizing Congress to regulate the value of money is almost unique in the Constitution, because there are no restrictions or limitations of any kind in this clause. The power is absolute.

The Constitution here adopts a dubious course — it states something positively rather than negatively — a procedure which has little to commend it.

There are other positive powers granted in the Constitution, such as, (in Article I, Section 8, paragraph 12) to "raise and support armies," but immediately there is a limiting clause which reads, "but no Appropriation of Money to that Use shall be for a longer Term than two Years." The power is therefore limited.

Or there is the power (Article I, Section 10, paragraph 2) which reads, "To borrow Money on the credit of the United States." The power here appears absolute, but it is not; it is in fact limited by the "credit of the United States." *Credit* in this case, cannot properly mean any credit other than *voluntary* credit, something which remains with the sovereign people.

Or there is the power (Article I, Section 10, paragraph 6) to "provide for the Punishment of counterfeiting the Securities and current Coin of the United States." The power appears absolute and the authority to do so is in positive language, but the limiting factor is the existence of counterfeiting. If there is no counterfeiting the right to exercise the power to punish counterfeiting is academic and theoretical. In contrast, in a very peculiar fashion, the clause about "coining money and regulating the value thereof" is wide open. There is no limit.

The Constitution of the United States is the ultimate law of the land. No higher authority is acknowledged *in the courts*. But the authority granted by the Constitution of the United States is not the ultimate authority before the bar of human reason, or what is known as morality. There is an ultimate moral law, or a perfectly rational law — whatever it may be — which finally outranks any document such as the Constitution of the United States. Such an ultimate law may not be enforceable in courts, but it is enforceable in reality. Men will eventually always find a way, motivated by legitimate self interest, to circumvent any law or any constitution which is contrary to "ultimate morality," which properly understood is "ultimate reason."

The Constitution of the United States is a marvelous document, maybe the greatest constitutional and legal document ever written by men. But it is not the ultimate law in the United States nor is any other Constitution the ultimate law in its territory. The ultimate "constitution" is the *constitution of constitutions,* towit, the moral law, as expressed in the Decalogue of Moses. This short, simple document completely outclasses any other legislative document written at any time.

An outstanding characteristic of the Decalogue of Moses is that it is cast in a negative formulation: *Thou shalt not* is the customary style. All of the Ten Commandments are negative, from first to last: "Thou shalt have no other Gods before me" to "Thou shalt not covet."

The greatness of the Mosaic *Decalogue,* if correctly appreciated, lies exactly in its negative aspect as in the First Commandment just mentioned, Thou shalt not have any other gods before me. That could never have been effectively phrased affirmatively. Even if rephrased to read, Thou shalt have me only for thy God, the *only* would have been as negative as the formulation actually used by Moses. Similarly, all the negatives in the ethical part of the *Decalogue* — thou shalt not kill, commit adultery, steal, lie, or covet — have singular merit for two reasons: (1) they leave all else free, except what is specifically prohibited; and (2) there is the prohibition of specific evil-doing. The *Decalogue* therefore is a document legislating more freedom than any other code in the world, but it leaves no one with sovereign freedom to do evil (see Volume I of this publication, Nos. 2, 3, 4, and 5).

Now that which is wrong with Article I, Section 10, paragraph 5, clauses 2 and 3 is that they are positive and therefore in this case unlimited, rather than negative and consequently limited, because these clauses set no limit on controlling money, such money need not be gold or silver or any item of value, and any value that Congress wishes to be put on that money can be put on it.

The basic function of a constitution is to restrict the powers of government. The Constitution of the United States does *nothing* to restrict the absolute and arbitrary power of Congress in regard to money. *Our Constitution on this vital subject is defective.*

The consequence of that is that the sorriest aspect of the whole history of the United States is its monetary history, consisting of authorizing fraud and theft in abstruse money matters.

It might be expected that the *sovereign power* of this mighty nation could eliminate the consequences of these sins (despite the Biblical declaration, "Your sins will find you out") but that is a hallucination. The consequences have been there despite the Constitution and all that men can do, towit, depression on depression, and latterly (because of a new phase and a worse one) progressive inflation.

Until the right negative is added to Article I, Section 8, paragraph 5, clause 2 of the Constitution of the United States, the economic stability of this country is in jeopardy; further when there is no confidence in the economic stability of this country, citizens will constantly turn toward tyrannical arbitrary power as a protection against instability; men will seek security rather than freedom, because their basic laws are deficient and do not make freedom a reliable opportunity for all men. When freedom creates insecurity which ordinary men cannot master, they no longer want freedom. It is because there is a pervasive sense of economic insecurity *related to money regulated by Congress* that men in the United States no longer love freedom with enthusiasm.

Applying What Calhoun Wrote About Constitutions To The Specific Case Of Coining Money

In the January 1959 issue of FIRST PRINCIPLES, on pages 22ff., we quoted Calhoun's great treatise on government, entitled *A Disquisition on Government.* We shall repeat a fragment of that quotation.

Readers may remember that Calhoun's treatise has profoundly realistic premises, and that he with perspicuity appraised the true nature of man. From consideration of man as man, Calhoun turns to the nature of government, and from government he advances to the character of constitutions. Constitutions, he declares, are primarily designed *to protect citizens against their own government*; it is *that* which is the purpose of constitutions. Calhoun wrote:

> But government, although intended to protect and preserve society, has itself a strong tendency to disorder and abuse of its powers, as all experience and almost every page of history testify. The cause is to be found in the same constitution of our nature which makes government indispensable. The powers which it is necessary for government to possess in order to repress violence and preserve order cannot execute themselves. They must be administered by men in whom, like others, the individual are stronger than the social feelings. And hence the powers vested in them to prevent injustice and oppression on the part of others will, if left unguarded, be by them converted into instruments to oppress the rest of the community. That by which this is prevented, by whatever name called, is what is meant by *constitution,* in its most comprehensive sense, when applied to *government.* [Pp. 22f.]

These ideas of Calhoun can be applied to clauses one and two, of paragraph 5, Section 8, Article I of the Constitution of the United States. These clauses read: The Congress shall have power to "coin money [and] regulate the value thereof." But the glaring weakness of the United States Constitution consists exactly therein that *it does not even try* to restrain the government in any way in money matters!

We therefore, at this stage of the analysis, propose the following change in the Constitution:

> The Congress shall have powers to coin metals into money of specified weight and fineness; or print paper money as a substitute for metal money, but such paper money shall only be for convenience and shall have full coverage in metal. Metal money only shall be legal tender. Congress shall not have the power to change the weights or fineness of coins in a manner which has the effect of altering the terms of settlements between creditors and debtors. If, because of changed circumstances in regard to metals suitable for use as money, it is desirable to change from one metal to another, then the change shall be made on the basis of the prevailing market relationship of the metals. Congress shall not endeavor to stabilize the value of any metal used as money, nor shall it undertake to make money plentiful. The supply of metal for money which is legal tender is to be left to the world supply and demand situation, for industrial and monetary uses, in that metal market.

Such an article in the Constitution on money will restrain Congress; and consequently protect the people, significantly, to wit, (1) only metal money would be legal tender; (2) the weight and fineness of legal tender coins would not be changed in a manner which breach contracts; (3) paper money, for *convenience*, might be circulated, but would have metal behind it one hundred percent, so that, if there is a demand for metal coins for use as legal tender, they indubitably would be available; (4) the quantity of metal available for monetary uses would be determined by the demand for it at *prevailing market prices*, which in turn would have been set by the demand for *both* industrial and monetary uses; no arbitrary values would be set at the caprice of Congress; (5) no metal market price would be manipulated in order to affect the value of metal for monetary uses; and (6) there would be no power of Congress, at all, to *regulate* the value of money; the value of our money would rest on world supply and demand conditions.

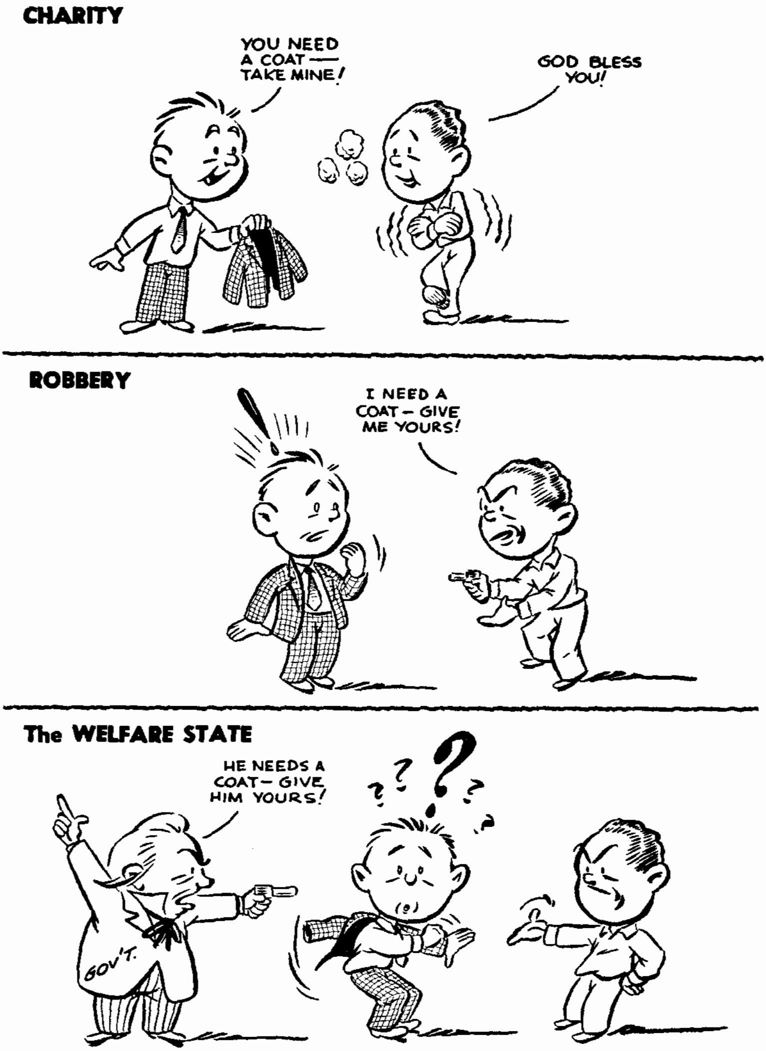
Obviously, the foregoing proposal is metallist in character; and, considering the present money situation in the United States, it is idealistic; it proposes what cannot be accomplished at once, nor except by the use of temporary compromises. In a sense, it is a proposal to return to a gold standard. Doing that entails solving several and difficult problems. However, the proposal outlines a true gold standard, and one which will contribute to stable economic conditions, rather than one which has supplementary features which cause economic instability — the business cycle. This, therefore, is more than a mere return to the gold standard. It will not permit a continuation of planned variation, by monetary authorities, of the quantity of fiat money, something which the old gold standard permitted with disastrous consequences. There will be further discussion of the problem in future issues.

Tale Of A Coat

The following page shows a reprint from *The Freeman*. But we have added a panel of our own, at the bottom. We have labeled it COOPERATION, with the explanatory phrase, "according to Ricardo's Law of Association." Then, not being artists, and lacking design imagination, we have merely inserted the question: "What is this system?"

Our purpose in supplementing the admirable cartoon of *The Freeman* is to enlarge the message. The original message is negative; it needs something positive. The original shows three systems — *charity, robbery,* and the *welfare state.* The chart shows

Tale of a Coat



Reprinted from THE Freeman *May 1955*

COOPERATION, according to Ricardo's Law of Association.

(What is this system?)

that charity is voluntary, and as such is distinguished from compulsory systems. The two compulsory systems are private coercion, labeled *robbery;* and public coercion, labeled *welfare state.* Clearly, coercion is an evil and is not to be preferred in collective form just because it has a deceiving name (welfare). Robbery is robbery whether individual or collective in origin, and whether a good name hides it or not.

Society cannot be organized properly on any of these bases — whether charity, or robbery by individuals, or robbery by a group.

Some additional organizing principle, this time a sound economic principle, is necessary. What is it?

It is *cooperation. That* is the principle on which human association is founded, although the fact may be obscured. *That* is the principle that needs a panel in the cartoon. Then the cartoon will be complete.

The mere word, *cooperation,* will mean nothing significant economically unless Ricardo's Law of Association (or you could call it as well, Ricardo's Law of Cooperation), is understood. What is this Law? The idea can be put this way:

Let us say *A* can produce products worth $3 and *B* products worth $4, a total of $7. But by division of labor *A* can concentrate on what he can do best, and *B* on what he can do best. Men are *never* equal by endowments; each can develop special skills; natural resources make some things less costly to produce in specific locations; investment in special equipment makes one man more productive in one job than in another. What happens then under *division of labor?* We no longer have *A* and *B* aggregatively producing $7 worth of products, but something involving a *seeming* multiplication, like 3 x 4 = $12. That illustrates the "miraculous" character of *cooperation* in the Ricardian sense.

In an earlier issue we presented an example of how Ricardo's Law of Association works. We quote from the July 1958 issue, page 207ff., Volume IV, No. 7:

> . . . we shall take a simple case; we shall imagine a primitive society consisting of two men and their families. Secondly, each man needs a shelter for his family. Thirdly, one of the men is bigger, stronger, wiser, *superior in everything* to the other one. The first man we shall call Mr. Strongman and the second Mr. Feebler.
>
> . . . [We shall assume that both] men have the same size families and need the same space. They are both going to build simple shelters of the same size. All the material that they need is 2,000 logs (or boards) apiece and 9,000 nails.

We shall assume that both men have a hammer and the nails, but that the logs or boards must be cut and the nails pounded.

According to an assumption we have already made, Strongman will exceed Feebler both in sawing logs (or boards) and in pounding nails. Strongman can saw 100 boards an hour and pound 300 nails an hour. Feebler can saw only 25 boards an hour and can pound only 200 nails an hour. . . .

What will it require of Strongman to build his shelter? This is easily computed. If he must saw 2,000 logs or boards at the rate of 100 an hour, it will take 20 hours of sawing. Similarly, if he must pound 9,000 nails at the rate of 300 an hour, that will require 30 hours. The 20 hours of sawing and the 30 hours of pounding make a total of 50 hours.

Feebler's position is different. He can saw 2,000 logs at the rate of only 25 an hour, and so sawing will require 80 hours for him. He can pound his 9,000 nails at the rate of only 200 an hour, and so pounding nails will require 45 hours. It will require 125 hours of work for him to build a shelter compared with only 50 for Strongman.

The 125 hours of work for Feebler plus the 50 hours of work for Strongman total 175 hours as is shown in Table 1.

Table 1

Two Unequally Unequal Men Working Separately

2,000 logs at 100 an hour =	20 hours
9,000 nails at 300 an hour =	30 hours
Total for STRONGMAN	50 hours
2,000 logs at 25 an hour =	80 hours
9,000 nails at 200 an hour =	45 hours
Total for FEEBLER	125 hours
The two together (50 + 125) =	175 hours

On the surface there appears to be only one thing for Strongman to do, namely, to do all his own work and let Feebler struggle alone by himself. Is that, for him, the smartest way to be 'selfish"?

He goes over to the Feebler plot of land and discovers Feebler is at a very serious disadvantage at sawing logs, but that he is not at so serious a disadvantage at pounding nails. And so he suggests to Feebler that they work together building their two shelters. . . . He says, "I will saw all the logs and you will pound all the nails."

But Feebler shakes his head and says that it is impossible to make a deal because he (Feebler) admits that he cannot even pound nails so fast as Strongman can. He says, "It is not possible for me to pound nails for you because you can pound nails 50% faster than I can; I can pound only 200 an hour and you 300 an hour."

To that Strongman answers: "Let us figure this out. If I saw all the logs for both of us, I will have to saw 4,000. If you pound all the nails for both of us, you will have to pound 18,000. Let us see how many hours that will take. First I saw the 4,000 logs at 100 an hour, that is, I work for 40 hours. Then you pound the 18,000 nails at the rate of 200 an hour, that is, in 90 hours. It works out like this:

Table 2
Two Unequally Unequal Men Working Together

4,000 logs at 100 an hour = 40 hours labor for Strongman
18,000 nails at 200 an hour = 90 hours labor for Feebler
The Two Together = 130 hours"

The result is astonishing. The time required to build the two shelters is now only 130 hours compared with the 175 hours shown in Table 1! The saving is 45 hours. In the way we have set up the example, the savings are distributed to both Strongman and Feebler. Previously Strongman spent 50 hours to build his own shelter. Now he has to work 40 hours for exactly the same shelter. He saves 10 hours.

Similarly Feebler makes a saving. Building his own shelter required 125 hours, but now by working with Strongman he will have to work only 90 hours. He has a saving from 125 hours down to 90 hours, or 35 hours.

The foregoing is the *positive* principle underlying society. It is not a positive principle which is *materialistic* only, because men will be seeking to achieve various values and goals, some of which may be wholly immaterial. But this principle of *cooperation,* first worked out most clearly by Ricardo, and carrying his name, is the real cement in society — the factor that makes association of one man with another *mutually* profitable.

The reprint shows two *coercive* systems — robbery and the welfare state. We have balanced these two by two noncoercive systems, charity *and cooperation.* Cooperation is properly about nine-tenths of the combination of charity and cooperation.

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FIRST PRINCIPLES
IN MORALITY AND ECONOMICS
on which depend personal well-being and social health and harmony

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Contents

The Relationship Between Freedom, Utilitarianism And The Mosaic Law

It may appear that there is no relation between freedom and the commandment, *Thou shalt not kill,* but if there is any application of the ideas of the Hebrew-Christian religions to the subject of freedom, it will have to be via the commandment, Thou shalt not kill. There is no other contact point.

In the first place, by common consent and common sense the commandment, Thou shalt not kill, has ever been understood to exclude all violence. The commandment could read then, Thou shalt not commit violence. But "violence" can be accomplished without blood and blows, that is, by non-violent *coercion,* which although non-violent nevertheless does "violence" to the other person. This coercion, by reasonable extension, is also forbidden. Finally, coercion may be legalized by the acts of a legislature or a judge; but the mere fact that it is *public* coercion does not exonerate such acts from the prohibition of employing compulsion against another.

If then the Sixth Commandment forbids *all* coercion (except to employ coercion to protect oneself from coercion), what is this negative prohibition restraining each of us, except to allow *freedom* to others to pursue their inclinations (whatever they may be, except when they violate the reciprocal freedom and rights of others). If I may coerce no one, and if no one may coerce me, what is this other than legislating, *All men shall be left free?*

When the ancient law of Moses with stark simplicity legislates against murder, violence and coercion it not only has the merit of prohibiting those evils, but it has the magnificent positive virtue of legislating freedom.

How does it do that? The essence of the method consists in this: what *A* proposes to do which will affect *B* is not left to *A* to decide unilaterally, but must receive *B*'s uncoerced concurrence, or else it is forbidden. Under Moses's law no man is the *sole* judge of what he proposes to do that will affect another. If *A* wishes to sell, he may not coerce *B* to buy. If *B* wishes to buy, he may not coerce *A* to sell. Obviously, *A* may not get so high a price as he wants, and *B* may not buy so cheaply as he wishes, but whether they make a deal depends on whether each party prefers to make a deal rather than to forego it. The price may be 10% less than *A* prefers, and 10% higher than *B* prefers, but *if they make a deal without coercing each other,* each obviously prefers making the deal to not making it.

There is only one good reason why they will make a deal, and that is that it is preferable to not making it. They choose between the choices available to them. All depends on whether to make a deal gives them more utility than not to make a deal. Utilitarianism teaches that that which yields the greatest utility should be done. Consequently, utilitarianism is based on freedom, and freedom in turn is based on the Mosaic Law.

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The author of the Mosaic law had three options when formulating the law: (1) he could have legislated (a) for freedom, with (b) silence about coercion; (2) he could have legislated explicitly both (a) for freedom and (b) against coercion; or (3) he could have legislated (a) against coercion, with silence about freedom. Number one would have been obscure; number 2 would have been long-winded; number three was adequate and simple. With grim compression of words the author of the decalogue chose the latter, legislating, Thou shalt not kill (commit violence or coerce). But obviously that is legislating for freedom as inescapably as if it had been stretched out in long phrases and complex sentences.

Rightly understood, the commandment, Thou shalt not kill, is the cornerstone of the structure of society and the foundation of freedom. If anyone can formulate the principle of freedom more simply and comprehensively than, *Thou shalt not coerce,* he should speak up.

Morality And Economics Teach The Same Things; But They Present Them Differently

It is not proper to concede that economics and morality may give conflicting answers to problems of human action. When the answers of economics and morality conflict, it is because the economics are wrong or the principles of morality are wrong, or maybe both. In this publication we call attention to the fundamental harmony of the long-accepted principles of morality of the Western world (when not extended sanctimoniously beyond their obvious meaning), and those findings of economics which are not to be challenged on rational grounds.

It is, of course, impossible to harmonize sanctimony and economics. And it is equally impossible to harmonize morality and pseudo-economics.

The principles of morality are simple: (1) the need and legitimacy of self-preservation and self-expression; (2) freedom; but (3) no freedom to do obvious wrong — no coercion, fraud, nor theft.

The principles of economics are equally simple; they trace the course of events from causes to effects. If a proposed action (cause) will not be conducive to the effect wanted, it must be nonsensical or contrary to purpose. Actions which genuinely contribute to the attainment of the desired effects are actions (1) stimulated by the motivation of self-preservation or self-expression, (2) available through freedom, but (3) which avoid coercion, fraud and theft.

Morality teaches authoritatively what economics explains analytically.

With what does morality concern itself except human action? And what should economics analyze except human action? How, then, could they properly give conflicting answers unless either morality or economics is inconsistent with reality.

In current issues we are analyzing some bad economics and bad morality, associated with *money*, to wit, the issuance of *fiat* money, or *fiduciary media,* or *paper money without metal cover* — whatever term you wish to use. This immorality and/or bad economics causes periodic depressions and unemployment under certain situations, and uncontrollable inflationism under other situations.

The Quantity Theory Of Money

In economics there is a theory about money which carries the name, the *quantity theory of money.* Without an understanding of what this theory is, it is not possible to understand money problems in general.

The theory is as follows: an increase in the quantity of money has as its consequence an increase in prices; and vice versa, a decrease in the quantity of money has as its consequence a decrease in prices. There are qualifications and refinements to the law, but this is its essence.

A simple illustration will suffice: imagine an isolated island inhabited by one thousand people. A hundred years ago the people discovered a chest of Spanish coins apparently buried by buccaneers four or five hundred years ago. These coins constitute the only money used on the island. The chest of the buccaneers from which the coins were taken was a big one and there is ample money for the business transactions of the islanders. They buy and sell among themselves using the old coins. Everything remains placid on the economic front. Although *individual* prices rise and fall depending on the amount of merchandise wanted of a particular kind, or the amount offered for sale, *general* prices do not rise or fall from year to year in a significant manner. There is no inflation nor deflation.

But when digging in the sand on the beach one day, two young men on the island discover two additional chests each containing the same quantity of coins as the chest yielded that was found one hundred years ago. They hurriedly cover their find with sand, and during the following night bring all the coins into a shed on their father's farm, a shed which nobody ever visits.

These young men then begin to spend money. They both wish to set themselves up as farmers and marry. They now have enough money, and to spare! They both begin to buy farms. To get exactly what they want they pay relatively high prices. Having a big appetite for owning land they buy more and more farms. But the sellers of the farms and other potential sellers sense that there is something "going on" and they raise their prices. Prices of farms rise more and more rapidly. Each seller, in turn, wants to buy a farm he has long wanted, and so they all go out to buy the desired farms. As prices rise they sell, buy and resell, and there is a big boom in land values. In short, *the first people to "benefit" most at the expense of others, when the supply of money is increased, is the first buyer, then the next, and so on.* In the meanwhile the teachers or preachers have not been benefited at all. Inflation *never* helps *every*body. It hurts the people who are the last to get the money in hand, which occurs after everybody else has used it prior to their use, and bought at prices which did not reflect fully the additional quantity of money. The last buyers were actually hurt because they were able to use the additional purchasing power only after the others had used it to buy merchandise priced nearer the old price. But when the last buy with the new money, it having finally come into their hands, prices are close to the new higher level at which they will settle considering the total supply of money now available.

But the young men who found the two chests go on spending and spending. As they pour new coins into the money stream, these coins stay in the stream. Finally, there is three times as much money in use on the island as before. The question is: where will prices be at that time?

Nobody knows. The easiest answer would be that prices will be three times as high for everything as they were before, simply because people have three times as much money and can be persuaded to pay three times as much for merchandise as before (unless the quantity of merchandise has increased, too; let us assume that the quantity has not increased). But this answer obtained by multiplication is too simple. Certainly, not *all* prices will be three times the old price. Some prices may have quadrupled; others may have doubled. A few may have very small change. Some may even have decreased.

But although the quantity theory of money does not mean that prices will rise exactly as much as money increased, *in a broad general way* it may be asserted as an obvious truth that increasing the quantity of money results in an increase in prices; and vice versa, decreasing the quantity of money results in a decrease in prices. The *general* rule has a number of qualifications, but for a good perspective of the major reality, the quantity theory of money is simply, that as the quantity increases prices increase. The rule as just stated assumes that other factors affecting prices are constant. They *never* are. And so applying the quantity theory of money consists in something more than just knowing how to multiply.

Certainly, in our imaginary island, prices will have risen very greatly within say ten years of the discovery of the two additional chests of Spanish coins. Maybe if a good index number were computed (which is in fact an impossibility), prices might generally be approximately three times what they were before.

What attention do smart people pay to the *quantity theory of money?* They always keep it in mind, as one of their basic considerations in all their plans. They must, if they are sensible, ponder and decide whether they think the money supply will increase, will remain steady, or will decrease. On the basis of their conclusion, they will make all their long term plans, and their current decisions will in turn be affected by the long term thinking.

For example, a man who believes that the people of the United States will continue to increase the supply of money will be reluctant to buy bonds or own mortgages. Why? Because, after ten years when he gets his money back, it will buy much less than it buys now. He will have been robbed by the quantity of money having been increased.

Instead of buying mortgages and bonds which are mere "calls on dollars," he will buy houses and farms and stocks which will have a tendency to rise, because of the increase in the quantity of money. In that case, at the end of ten years he may be able to get much more for farms, houses and stocks than now.

Further, men who think the supply of money will be increased will prefer being debtors rather than creditors, because as debtors they will pay back "small dollars" in the future, whereas as creditors they will be receiving back "smaller dollars" than they loaned.

In short, every mature person should be informed of the following:

1. The principle involved in the quantity theory of money;
2. The prospects on whether the quantity of money will be increased or decreased, and how much;
3. The various qualifications to the quantity theory, which must be taken into account, if a person is to be a careful thinker and anticipate the real course of events, and make money by it.

If you have never given the quantity theory of money careful and organized thought, do so now, and reach some practical conclusions, based on what you think the trend will be in regard to the quantity of money.

The Origin Of "Natural Money"

Money comes into existence in either of two distinct ways, either by planned *natural* action in response to a need, or by planned *arbitrary* action of some counterfeiter or power (state). The terminology here used is nontechnical, but descriptive of what happens in the *development and emergence* of money if it is a "natural" phenomenon, and the *creation* of money if it is an arbitrary action.

Money comes into existence *naturally* by some process as follows:

(1) People wish to exchange goods; the original primitive method is by barter, that is, they trade goods and services. This is cumbersome, because if a man wishes to acquire a horse, he often cannot find someone who owns a horse which is for sale, for the specific miscellaneous products which he as the would-be buyer has available to pay, the miscellaneous products being the only equivalent the buyer can offer because there is no "money."

(2) The man who wishes to buy the horse may have some oats available for exchange, but the seller may not want oats because by selling his horse he no longer needs oats to feed to the horse. The buyer may then try to trade his oats to another who has some wool for trade. But he will do this only provided that there is a more active demand for wool than for oats; the would-be buyer will trade his oats for wool only if it is *more-exchangeable* than oats; after he possesses the wool, it will be easier for him to make a trade than when he had the oats; in a way, wool here functions as a kind of money, that is, it is more-exchangeable than oats; the *more-exchangeable that a commodity is, the better it serves as money;* money is basically that commodity in the community which is *most-exchangeable.*

(3) Although wool may be more exchangeable than oats, let us assume that in this community two other commodities have gradually become more-exchangeable than any other, namely, silver and gold; and so our horse-buyer finally exchanges his wool for some silver; this silver, however, could easily have been alloyed with a base metal and so the silver needs to be melted and assayed so that the horse-buyer gets as much real silver for his wool as he thinks he should get, and as the seller of the silver declares he is getting.

(4) But this weighing and assaying can be simplified if someone will undertake to be reliable in putting out silver of a definite fineness and a specific weight, to be known as coins with a special name, such as dollars, or shillings, or francs. Then these coins, if trustworthy, will develop such exchangeability, that is, such currency, that they will be the money that everybody uses, and it will be called currency. What has happened is that the most exchangeable commodity, in the most usable form, has emerged as the *money* of the community.

(5) Finally, there will be certain problems which develop from having two metals, silver and gold, for money, and it will be found necessary for various reasons, which will not be discussed now, to select either silver or gold; in practice gold has finally become accepted as the money metal of the community.

And so by a logical process the most suitable commodity has become the *natural* money of a community.

In the logical and natural course of events, as just explained, there has been an easily understandable interplay of various conditions and motivations. These are: (1) men's needs differ from those of others or from their own past needs; one man has today too much of one thing and not enough of another; this will be especially true depending on whether there is already considerable division of labor in a community, but it is *always* true in some degree, because men themselves change, as Solomon indicated when he wrote, that "their is a time to be born and a time to die, a time to laugh and a time to weep"; (2) consequently, human beings can greatly improve their lot by exchanging goods and services; (3) such exchange however is often frustrated if the exchange can only take place by barter as, for example, that a horse buyer has only oats as a means of paying for a horse, and that a horse seller wants a house rather than oats; then buyer and seller barter first, if necessary, so that each acquires a product more exchangeable than what he originally owned; (4) the commodity which finally emerges in such a community as the most-exchangeable has become the "money" of that community; (5) certain metals have for various reasons emerged in nearly all communities as the "money" of those communities; (6) the reason why those metals have become money is because (a) the metal had a prior practical value in the community for industry or ornamentation and therefore was in demand; (b) it was divisible into units by weight; (c) it could be assayed for purity; (d) it was not too bulky; (e) it was not highly perishable by wear nor destroyed by the elements (so that what was metal turned to rust); and (f) it could not be manufactured in endless quantity, but, importantly, was relatively fixed in supply; in short, the will of men could not, at low cost, create a lot more of that money; and further, although the demand for money would always be insatiable — everybody would want more of it — nevertheless the supply *never* would permit the demand to be satiated.

If money is to be valuable, it *must* be scarce. To want an unlimited supply of money and expect it to have a value is to be as silly as a baby crying for the moon.

As explained, *natural* money just came naturally, and grew to be *money* just as "Topsy grew."

Endeavor to imagine how you yourself would develop *money,* if you lived in a primitive community trying to emerge from the handicap of a barter economy. Would you not follow the rule to barter where you could; but when you could not barter directly for what you wanted, would you not barter for what would be more-exchangeable; and then for what would be even more exchangeable, until you finally could get what you wanted. *At no time would you be bartering for something valueless, nor on which someone had set an arbitrary value which might disappear as a puff of smoke, but you would always have something of value, with the additional advantage of being more-exchangeable.* Is is not probable that you and all others would finally use the *most-exchangeable* and convenient commodity as money? And is it not probable that everybody would try to have on hand some of that *most-exchangeable commodity* for emergency purposes, and as a reserve. Is it not, in fact, perfectly natural for there to be a *demand for money* of that kind and for that purpose? Such demand for money is not mammonism, but elementary prudence and good judgment.

The important point is that *natural* money is a *commodity* type of money, a money which has value as a commodity as well as it has additional value *as money.*

The Origin Of "Fiat" Money

In contrast to natural or commodity money, there is another type of money, which might be called "unnatural" or "noncommodity" money, that is, money the value of which does not have a relationship to the commodity of which this "unnatural" money is made.

Take, for example, paper money, which is made of paper. A small piece of paper, 2-5/8 inches by 6 inches, may have printed on it *$100.* There is no real relationship between the value of that small piece of paper as paper and an amount of $100. The $100 for which the paper passes is "arbitrary." When that small bill passes from hand to hand for $100, it is because of some reason or convention that it is accepted as such. Certainly that piece of paper is not worth $100 *as a commodity;* it is not worth even one cent. Why then does it pass for $100?

The answer is that originally that piece of paper was exchangeable on demand for $100 in actual gold. The paper $100 was a convenient substitute for a man lugging around $100 in gold coin in his pocket; that $100 would consist of five fairly heavy $20 gold pieces. The *paper* bill for $100 was preferred because it was convenient, and because *originally* it could be converted *on demand* into gold coins. That is no longer true in the United States, because it is a criminal offense for citizens of the United States to own gold coins of the United States. The United States, therefore, is no longer genuinely on a commodity money basis. It no longer has "natural" money, but "arbitrary" money.

If the government of the United States wished to do so, it could pass a decree that its paper money would no longer be "honored" by the government. To put that into effect it might pass a law that it would accept as payment for taxes only gold, that is, a commodity money. There would then be a rush to get rid of paper money and to acquire gold. In the process, the $100 paper bill would eventually be worth what it is worth as a piece of paper, that is, it would be worthless. In the previous issue (page 169) it was reported how on May 21, 1720 a decree was issued in France "by which the value of Law's bank notes was to be reduced gradually to one-half their face value." That signalled the end of Law's paper money boom; his bank was "broke" in one week; everybody wanted to get rid of money that would shrink in value. Similarly, if the United States decides it will not honor its paper money, paper bills will become valueless. The actions of both citizens and foreigners will contribute to that collapse.

Were foreigners to discover that they could not get $100 *in gold* for a United States $100 bill, they would refuse to accept another paper bill at full face value. Foreigners would sell us their merchandise only for gold, or by barter for some other commodity wanted by them.

To the collapse in the foreign demand for paper dollars would be added the collapse of domestic demand. The United States government spends about $70 billion a year, and taxes cover most of that, which means that to pay taxes alone billions of dollars worth of gold would be needed. The demand for gold would be tremendous, and everybody would try to get rid of his paper bills in order to pay his taxes in gold as required. The value of those bills would drop faster than Law's bills when they were to be reduced in value merely one-half, and only *gradually* at that.

How then is it possible for the United States to maintain the value of its paper money?

In the first place, it has prevented a collapse of the value of its paper money by making it convertible into gold on demand in *all foreign transactions.* That maintains the value of United States money in all *international* transactions. But it should be noted that the value of the dollar in international transactions does not depend on the greatness of the United States; it depends, rather, on the value of gold. All the armies, navies, merchants, missionaries, and citizens of the United States are helpless to maintain the value of the dollar in international trade where the United States government declares it to be, *unless the United States is willing and prepared to pay out gold for its paper money.* It is the exchangeability of its paper money for gold which maintains *abroad* the value of the paper bills of the United States.

The value of *paper* money does not go beyond national boundaries. The value of United States money would collapse at the borders of the United States, except that the United States government treats foreigners better than it treats its citizens; the foreigners can get gold for paper; citizens cannot. Because the value of the dollar does not collapse abroad, the citizens of the country have remained unalarmed.

But their confidence is based on genuine quick-sand and the dollar is certainly doomed, if all the previous history of men, in every age, in every society, teaches anything. Never, in all the history of mankind, is there any record of a *money* which was not tied to a commodity value retaining its value. *Money always deteriorates in value when it depends on the mere integrity and firmness of men.*

It is not that men do not endeavor to have the integrity and firmness required in order to keep a money on a stable and reliable basis. That is maybe nearly always their honest resolve. But their resolution is *eventually* always overwhelmed. If temporarily a wise and steadfast man manages the paper currency of a country, he may hold out for a time against the sure and rising clamor for "more money." But sooner or later the question becomes a political issue of the foremost importance. Governments rise or fall on whether they favor sound or unsound money. And the unsound money advocates sooner or later *always* get their chance. In the April issue of FIRST PRINCIPLES on page 124ff., we cited the smart little Canadian lady who said the family had changed its historical party allegiance just because the other party provided more "credit" — which in this case had in principle the same effect as printing more paper money. Neither the Republican Party nor the Democratic Party can win the next election in the United States unless it favors monetary policies which will *eventually destroy* — not merely reduce — the value of the dollar (unless the dollar is again hitched to gold). It is not a question *whether* that will happen, but only a question of *when*. Of course, nobody knows when that time will come, but it is undoubtedly "later than we think."

In a sense, dead gold is far more reliable as a basis for money than the judgment and character of living men. The latter are corruptible and weak. It is not the inertness or deadness of gold that makes it so valuable as a basis for money; the reason lies rather in the fact that the quantity of gold cannot easily be varied. Gold is good as a commodity money, primarily because the quantity is relatively invariable by the wills of men. But paper money can be varied easily enough. All that is necessary is to add zeros to the figures on paper bills, and the quantity of money is varied 10 or a 100 or a 1,000 fold!

When in 1934 the United States went off the gold standard it took the most momentous decision in its history to date. It shifted from the only base for money that has ever proved reliable (a commodity base) to the alternative base which has always proved eventually to be unreliable (printed paper). It shifted, in principle, from commodity money to fiat money.

Why has fiat money never yet been a success and why will it not be a success in the United States? There are several reasons: (1) because people confuse their personal shortage of money as being a shortage of *money*, whereas it is in fact a shortage of real goods and of their own production; they see the token for goods and for production — money — and think that when they grasp for the token they will be getting the real things they want; but, as the quantity theory of money teaches, increasing the quantity of money increases prices but it does not increase the quantity of real goods; (alleged exceptions to this statement will be considered later). Increasing the quantity of money, even if the increase were permanently controllable, would not increase the well-being of a society; (2) but the other reason is that rulers, or those delegated to manage money, are never strong enough themselves to resist the pressure to increase the quantity of money without limit which comes from the masses. A demagogue will always come along who will promise prosperity by increasing the quantity of money, in one form or another.

Of the several forms that an increase in the quantity of money can take, the *disguised* forms are the most dangerous. The disguised forms have been corrupting the monetary system of the United States even long before it went off the gold standard in 1934.

Intellectual Confusion About The Dollar Being "Safe"

In 1934 when the United States went off the gold standard everybody, (1) who knew the important facts about monetary history during the whole recorded history of man, or (2) if he did not know that but who knew how to reason from the indisputable premise of human frailty (and depravity), should have known that the dollar was doomed as a reliable monetary unit.

Today, twenty-five years later, in time of peace and high prosperity, the value of the dollar is shrinking daily. The government is not able to balance its budget. The quantity of fiat money is increasing steadily. The dollar is on the superhighway toward steadily decreasing purchasing power.

Individuals no longer wish to buy bonds or mortgages. In this little town where thirty years ago there was an active market for mortgages among individuals, that market has practically disappeared. There are a few old men left who live in the past and who buy mortgages as investments, but they have become the exception. There are, of course, always some relatives who will take a mortgage, as a father taking a mortgage on the house of a son or daughter; but such transactions are not purely business. The same lender will probably refuse to take a mortgage on anybody else's property.

But intellectual confusion and uncertainty continues. What people would not or could not foresee in 1934 regarding what 25 years would do to the American *paper* dollar, has not taught them much, now that it has already come to pass. Very few people, business men and bankers too, really believe that the present trend will continue *permanently,* and that consequently the dollar will eventually be worthless. They all vaguely hope that the decline will be arrested somehow, sometime, by somebody.

But this vague hope is unrealistic. These people failed to reason lucidly in 1934, and they do not reason lucidly today.

The only people who give evidence of reasoning correctly are *those who wish to undo what was done in 1934;* and *further, who wish to undo the bad features of the system prior to 1934.* Such people are practically nonexistent. Such being the case — nearly everybody being in a frame of mind to continue the present fiat money situation in the United States — anyone who thinks the dollar will be safe — or at least is not "too unsafe" — must be classed as an intellectual bumpkin.

If one of the big parties proposed that this country would go back to the old gold standard (which was only *partially* on a commodity money basis) it would undoubtedly lose votes for that very reason. Presently there is not the ghost of a chance that the United States will put its money on a *sounder basis* than it has been since 1934, let alone the hope that it will put its money on a *genuinely sound base,* eliminating the bad features of the old system prior to 1934.

Whoever really understands the situation will engage in a "flight from the dollar," to be accomplished by owning goods, not dollars; and by being a substantial debtor (but not so large a debtor as to be easily embarrassed by temporary declines). This policy, *as long as the United States monetary structure is built on sand,* is good for widows, orphans, pensioners, employes, employers — in short, is good for everybody.

Unsound Money Breeds Socialism

People who are excellently informed about problems of government, international dangers, economics and business, when they see others uninformed or misinformed, often regret that they themselves have only one vote to cast when influencing the policy of their country, and they toy with the idea of restricting the right to vote and to influence the policy of their country to wise people only, the "wise" of course being those who agree with them. This is day-dreaming. The right to vote is not likely to be taken away from anyone who possesses it today. If the voter is uninformed, or a fool, or a scoundrel, there is only one practical program to follow — to inform and improve him by education and persuasion. Otherwise, we shall all be dragged down in a common destruction.

Improvement in the financial and monetary program of the United States must come, in the first place, through educational efforts addressed to all voters in terms which they can understand. All voters should know the consequences of voting for certain policies or for voting for certain people who favor certain policies.

It is also romantic to hope that voters will vote for policies theoretically sound, but which they think will hurt them personally. To make a voter interested in favoring what is *right,* it is also necessary to show him that if he does not vote right, then he himself will suffer some injury. Men, despite sanctimonious babbling about looking out for other people more than themselves, will follow "truth and righteousness" only when "truth and righteousness" will do them some good. Fortunately, the rewards of "truth and righteousness" are definite and observable, because the rewards of morality are obvious for all to see. The Hebrew Scripture reiterates on almost every page that wisdom consists in observing the Law of God, and that it does not consist in cleverness or taking advantage of the neighbor in any way. Wisdom then becomes relatively simple moral rules. All public and private policy can and should be based on those rules.

Money problems are complex, and many people are confused. They do not understand the problem well enough to apply the simple rules of morality to monetary questions. They want fiat money without knowing that that means bald theft. Further, they do not clearly see how they themselves will be hurt: they, in fact, think they are helping themselves by favoring fiat money.

But in a vague and confused way they do realize that there is something wrong. They think they want more credit — which means more money — and that that helps them themselves. But they also realize that prices continue to rise steadily and that there is something frustrating for themselves about such credit expansion. And then they are also aware of the business cycle, something they do not understand, but which *periodically* hurts them and *perpetually* terrifies them.

Let us think in terms of modest but steady creation of fiat money. That is the present policy of the United States government — steady but controlled credit expansion. What are the consequences of that for the "common man." By "common man" we mean a large majority of the businessmen; nearly all doctors, lawyers, preachers, teachers, engineers; the overwhelming majority of farmers, employes, wives, pensioners, adolescents; and all children. What do they know about money and banking? What do they understand about the effects of constantly expanding the amount of fiat money? Naturally, practically nothing. Nevertheless they are practically all being hurt by present policies, for which whoever is entitled to vote may be held responsible.

Most people do not have a lot of money, or at least not at the beginning of their career as responsible adults. The first savings come hard, and are almost sweat and blood. Not too many people have the grim firmness to self-deny themselves present goods when they are poor, in order to make savings for the future. But that is the original foundation on which practically all wealth is based. Suppose a man has that fortitude. He saves, let us say, $20 a month, or $240 a year. What can he do with it? For one, he can put it under his mattress or under a corner of the carpet, that is, hoard it. Or he can put it in a savings account, or a building and loan association; if he does this, he will get 2 to 4% interest. But in the meanwhile those dollars (because of public inflation of the money supply which makes prices rise) are shrinking in purchasing power at the same rate — say 3% a year. If he hoards the money, his capital is shrinking 3% a year; if he puts his small sums to work via the banking and loan route he "treads water" presently; the interest about equals the simultaneous shrinkage in purchasing power. There is under such circumstances really no reward for saving.

Further, this steady and controlled inflation may get out of hand. Instead of being steady and controlled it may become wild and uncontrolled. Eventually, every inflation scheme has become that. That wild and uncontrolled phase may be called the "runaway boom." Then, what are the typical man's savings worth?

Practically nothing, because the end of a run-away boom is a crisis and complete collapse. The savings of the common man are practically wiped out by the process.

What are the alternatives for the common man? If he saves long enough, he will have enough to make a down-payment on a house, or maybe to buy a farm, or some stocks. The house purchase may be something which will not prove foolish, but what do people — the average folk — know about investments in farms, commercial real estate, or in stocks. These latter are the "best" but by no means perfect investments in an inflationary market. Only the experts, in these fields, can hope to come out well, simply because they know more or less what they are doing, whereas the average man would be buying and selling in substantial ignorance. It is the initiated who are likely to do well. If they are rich, they are likely to become richer.

But the future of the struggling poor is different. *Under inflation,* there is a strong tendency for the poor to become poorer, *because they do not have a really suitable avenue for investing their savings.* What the poor need is a dollar which is not inflating, but if anything deflating. (This will be explained later.) Under an "honest" capitalist system the dollar would be steadily deflating, which would basically help the poor man as a saver. Under this situation, a young man could put his savings into a savings account or into a mortgage — where there would be safety in the purchasing power of the money saved — and those investments would intrinsically be good. The future purchasing power of the principal that he put in would be greater than the purchasing power at the time he put in the money. His capital would be safe, the interest return would be genuine, and when he took it all out, he could buy more with it than when he put it in or when it first accumulated. What poor people need is not inflation but deflation! What young people need is the same.

It would be like this: Each year he would put in $240; at the end of 40 years that would amount (at compound interest) to more than $30,000 possessing *unimpaired purchasing power.* In fact, the purchasing power would be higher than when he put in the money. He would feel "safe." He would have an inducement to save. He would not think he was being cheated. He would, in fact, be getting what he needs, a stable unit in which to save, and his savings would go into the safer (less risky) investments, namely, bonds and mortgages, the natural vehicle for those unskilled in business and investments, because of lack of training or youth.

It is, however, a fallacy on the part of many who consider themselves clever in their investments to think that, because they know something about risky investments (stocks, real estate, etc.) they will gain at the expense of the ignorant and small investor. In genuine inflation, those who have been clever enough to fatten themselves on other peoples' losses, will find that *eventually* stocks are not a hedge against inflation — and the clever people will go broke, too. If not, popular clamor against the really skillful investors who did finally come out all right will be so great that they will be expropriated. At any rate that has always happened in the past.

The clever investors who survived the disastrous German inflation after World War I had means available to survive which do not exist today, namely, they could transfer their assets to a stable economy elsewhere, especially to the United States. After the German boom was over, and the crash had prostrated everything, they brought their money (which had been kept safe in gold or its equivalent abroad) back home, and brought up large assets cheaply. No large part of the private wealth in the United States can be managed that way. Nowhere else abroad is there a large, genuinely stable place for investments. All the great nations are "off gold." Consequently, the principal means of survival — to export assets to a safe economy and later bring it back — is not available to citizens of the United States. We are all *eventually* (with very few exceptions) going to pay the piper.

But even the few who really succeed, and cheat the ambush into which the country is running, will not fare well. Those people who out-smarted the German inflation experienced a grave penalty in the form of impaired public relations. They were thereafter hated, and persecuted by the victims. Mankind is not "built" to be happy about the enrichment of others at the expense of the rest. Men make a distinction between wealth obtained by performing genuine services, and wealth obtained *at the expense of others;* the former they tolerate; the latter they expropriate.

What inevitably happens when there is skullduggery about money even if the people "did it" themselves? The poor, who have the right to vote as well as the rich, vote for a system different from capitalism. They say to themselves: "We were cheated under that system. We do not want capitalism and popular government. Instead we want wealth, too. If we cannot get it ourselves, individually, we will get it collectively. We will vote for socialism and not capitalism. And we will not have popular government either. We will have a dictator, instead, somebody to protect us from the capitalists — those few who have become richer and richer while we were tricked out of the benefits from our savings."

And so the best seed bed for socialism is an unsound money system. We have such an unsound money system presently in the United States. One does not *need* to be an especially endowed prophet — one does not need charismatic powers — to be able to forecast in what direction the course of events in the United States will be.

A New Lord God Almighty

People who favor fiat money rather than commodity money cannot possibly accept the first commandment in the Decalogue of Moses. The first commandment reads: Thou shalt have no other gods before me. To have another god means to acknowledge another *creator*. Fiat money advocates have such another god, namely, the state, *the creator of fiat money.*

Anyone who favors a *commodity* money is, at least in regard to money matters, not an idolator of the state. The value of that commodity money came about in the natural course of events. The state may "accommodate" itself to that situation, and endeavor to formalize it. For example, let it be assumed that gold is the commodity money which, in the natural course of events, has become the money of a society. What is needed is the most widespread uniformity in regard to the weight and fineness of gold coins. This can be left to individuals or private corporations. Probably there would eventually be remarkable uniformity in both weight and fineness if competition were permitted to run its course. That is probably the most desirable way of determining the weight and quality of currency.

But it has become customary for states to intervene to set the weight and fineness of coins to be used within their borders. No great wrong is done by that, although a bad precedent is established by it. In such actions, the state conforms to reality, and selects a weight and fineness that agrees as closely as possible with the existing market. The state merely "validates" what exists. It really creates nothing. The values were already there.

But when the state puts out fiat money it undertakes to be a creator. By fiat money it creates purchasing power for itself or someone else. This purchasing power was not some other good, available through prior work or production of some sort. It is *new* purchasing power arbitrarily *created* by the fiat money. Something is established which was not there before. It is an arrogant and vicious act of creation. The state when it does that qualifies under the fanatic statement of Ferdinand Lassalle, the socialist, who declared, "The State is God."

The viciousness of this act of creation consists in it being theft authorized and organized and accomplished through the state.

Whoever favors fiat money favors theft, and has a false god. He sins at least against the first and eighth commandments.

No Fiat Money Will Ever Be The Universal Money Unless The World Has Only One Government

Gold is today the *one* world-wide money that exists.

Gold is the universal money in the world, because it is a *commodity* money, and not a fiat money. *Commodity* money has value independent of the declaration of value by the state.

Fiat money is never genuinely more than local money. If it is more than local money, that is solely because that government *will redeem its paper money, on demand, in gold.* It is the assured *redemption in gold* which makes that money valuable beyond a nation's border. Such money is not yet completely fiat money.

Of course, on the basis of two fiat monies in two separate states goods can be exchanged; but the exchanges between those two countries are never "stable" over any period of time, unless the monetary policies of the two countries are genuinely dependent on each other. Such exchanges accomplished by fiat money really remain barter, facilitated by fiat money.

In the case of gold, the situation is different. If prices in Country *A* get out of line, say too high, it cannot ship so much of its high-priced products any more to Country *B* where prices are lower. But vice versa, Country *B* can easily ship to Country *A*. because Country *B* has lower prices and presumably lower costs. More merchandise then moves from *B* to *A*, than from *A* to *B*. The question is: how settle for the extra shipments from *B* to *A*? The answer is: *A* ships gold to *B* to pay for the extra merchandise, in gold.

Then what happens? Because of the operation of the quantity theory of money, prices in Country *A* drop, and in Country *B* rise. The reason is that the smaller quantity of money in *A* lowers prices, and the greater quantity of money in *B* raises prices — according to the quantity theory.

Gold, then, a commodity money and not a fiat money, keeps prices between countries in line. Or rather, it is the shipment of gold which restores price relationships between countries. No fiat money can do that.

And so when people, who are idolators, look upon their government as a creator of money, their "god" is not a universal god after all. At most, he is a territorial god — who is a "creator" of fiat money only within his own boundaries.

But a genuine *commodity* money (it does not necessarily need to be gold) can be a universal money, without the government of the world being *one* power — a one-world government.

Dismay About A Friend Taking To Bible Reading

Dismay

Some years ago a banker told a group of friends engaged in casual business conversation that he had begun a project consisting of "reading the Bible from beginning to end." I endeavored to prevent my face from betraying dismay. But why dismay?

The speaker was one of the ablest bankers in the United States. He had been educated without religion and was without religious affiliation. It was highly improbable that he was a "seeker" of religion or salvation. This project of his — to read the Bible from beginning to end — was a research study, somewhat in this vein: — "thousands of people appeal to the Bible and live and die professing faith in it and declaring they conduct themselves according to it, or they allege that they at least are endeavoring to do so; now, what is there to it? Is it what it is advertised to be?

The quality of this banker is such that his reading of the Bible although not predisposed to be genuinely sympathetic, would at least be "objective;" this is the kind of man who reads (say in regard to money and banking) the writings of men whom he considers unsound, just to know what force there may be to their ideas. In short, a man with an "open mind" and consequently most extraordinary.

Reason For Dismay

The Bible is full of contradictions, as some would say; or apparent contradictions, as others would say. Just because of that, no organized church, with extensive history, has neglected to take a position on those "contradictions." They have all developed a creed or a dogma. The creed tells what is to be emphasized as important in the teachings of the Bible. The dogma tells which interpretations are approved when there are "contradictory" passages. The churches by creed and dogma have told their members *how* to read (interpret) the Bible. Dogma exists in order to "rationalize" the teachings of Scripture. The Christian religion would have difficulty surviving if the church did not "assist" its readers by supplying the key — by means of dogma — to interpretation of its Scriptures.

This banker was reading the Bible without such assistance. He would probably reject such assistance with some remark to the effect: "I read all other documents on my own without a key or guide. I can *read*. Why should I need somebody to help me read the Bible. If it is a good book, it ought to be readable, and it ought to be consistent. If it is not, I shall make up my own mind about that."

There can be no doubt that the Bible is a wonderful book. Its effect on many men and women throughout history testifies to that. But its quality *appears* to be mixed. The authors are a heterogeneous group. The contents purport to be pre-history, history, poetry, theology, ethics, prophecy, eschatology.

The Bible is a book containing spectacular promises. A "troubled and seeking soul" might select out of the mass of material in the Bible those parts which give consolation and guidance. His *need* might result in the right "dogmatization" of what Scripture teaches. But this banker was hardly a "seeking soul" and would feel no urgent need for it to be a guide to help him grasp firmly the promises in Scripture. In this respect, our banker is typical of his age and his nation. Life is being good to him. While death and disaster are delayed, he is in an undisturbed frame of mind.

Several examples will be considered of problems which Scripture does not answer unequivocally. In a sense, a man can take whichever interpretation of these cases he likes, and ignore the others, or he can in confusion reject them all.

Differences About The Sacraments

The sacraments are an important aspect of the Christian religion and a subject of lively contention. Catholics say that there are seven sacraments; Protestants declare that there are only two. In the sacrament of the Eucharist or Holy Communion there is an irreconcilable difference between Catholics and Protestants about the change in the character of the bread and wine upon their being blessed. Catholics declare that the bread and wine are completely changed; Protestants dispute that, as being contrary to fact.

But the Protestants are in irreconcilable disagreement themselves. After the Reformation one of the German princes decided that it was important that the two main bodies of Protestants, the Lutherans and the Calvinists, should be reconciled and should merge. A conference was held at Marburg, Germany, between Lutherans, Zwinglians and Calvinists, known as the Colloquy of Marburg. The Colloquy was wrecked over disagreements between the Lutherans and Calvinists about Holy Communion.

Similarly, there are differences between the churches about baptism, which separates some denominations from all others; consider those who demand immersion and apply baptism only to adults, in contrast to those who sprinkle and apply baptism to infants as well as adults.

On these questions pertaining to the sacraments, which have been bitterly disputed for centuries, Scripture either does not unequivocally teach one clear doctrine, or else the several denominations are reading something into Scripture which is not there.

What conclusion would a banker, knowing about these controversies, reach in regard to the bitter differences between Christians about the sacraments — on the basis of a single research reading?

The Doctrine Not To Resist Evil

It is commonly recognized that the Sermon on the Mount in the New Testament is the high water mark in the ethical teaching of the Christian religion. *Rightly understood,* the Sermon on the Mount is a spectacular advance over the previous prevailing teaching. Nevertheless, it must remain a highly controversial document as it stands. There are in it many radical statements which are easily misunderstood or can easily be misinterpreted. Consequently, the interpretation of the Sermon on the Mount has divided Christians on practically every subject taught in it.

The general tenor of the teaching of Scripture is that evil deeds should be (and are) punished. Nevertheless, the astonishing statement appears in the Sermon on the Mount, *Resist not evil* (Matthew 5:39). This sounds like a perfect denial of the most elementary morality. Leo Tolstoy, the Russian novelist, actually took this text as the key text to all Scripture! He completely ignored that there might be an omission or ellipsis in the report on the Sermon on the Mount, which it was assumed the reader would assume when he read the statement, namely, Resist not evil *with evil means,* or with *retaliatory motivations,* rather than utilitarian motivations. There is a basic difference between saying, *Resist not evil* and *Resist not evil with evil.* But would this banker read the Scripture carefully enough — *could* he on *one* reading read it carefully enough — to supply the words omitted by the ellipsis in the expression?

To Obey Or Not To Obey The State

Scripture teaches, or seems to teach, three contradictory doctrines regarding the state:

1. The state is a divine institution, and must be obeyed.

2. The state is a devilish institution, the "great beast" of the Apocalypse;

3. The state may be (a) good *or* evil; (b) is not always divine *nor* always bestial; but (c) should be obeyed when it is good and resisted when it is bad.

For the first attitude toward the state, see Romans 13:1-7 where one may read:

> (1) Let every soul be in subjection to the higher powers: for there is no power but of God; and the *powers* that be are ordained of God. (2) Therefore he that resisteth the power, withstandeth the ordinance of God: and they that withstand shall receive to themselves judgment. (3) For rulers are not a terror to the good work, but to the evil. [And so forth in the same vein through paragraph 7.]

Paul was a privileged person *because* he was a Roman citizen. He could travel where he wished. The Roman state was of great assistance to *him,* compared with what his problems would be under petty states with inferior laws. Paul felt constrained undoubtedly (and rightly so) to accept and recommend obedience to the Roman state. Paul's statement here may not be completely parochial and conditional, but it cannot be considered (in our view) to be universal. What Paul wrote was valid (1) for Paul, (2) in his time, (3) under the Roman state, (4) in a letter addressed to Romans. What he wrote was not (1) for all men, (2) in all times, (3) in every state, nor (4) was it valid for some German on the fringes of the Roman empire.

So much for what the Apostle Paul taught.

2. For the second attitude toward the Roman state consider the practically contemporaneous writing of the Apostle John, exiled to the Island of Patmos in the Aegean Sea. In the last book in the Bible, *Revelation,* John writes as follows (Revelation 13:1-18):

> (1) And I saw a beast coming up out of the sea, having ten horns and seven heads, and on his horns ten diadems, and upon his heads names of blasphemy . . . (7) And it was given unto him to make war with the saints, and to overcome them . . . (16) And he causeth all, the small and the great, and the rich and the poor, and the free and the bond, that there be given them a mark on their right hand, and upon their forehead, (17) and that no man should be able to buy or to sell, save he that hath the mark. . . .

The "beast" referred to is obviously some state or dictator.

This abbreviated quotation also has some "parochial" earmarks. It pertains to a specific future time, under specific future conditions. It does not purport to be universal in time although it seems to be universal in area. In any event it does not justify the conclusion that all obedience is forbidden to all governments, any more than that the quotation from Romans required obedience by all men to any government.

3. For the third attitude consider what a third apostle, Peter, said in Acts 4:19 and Acts 5:29. We quote the latter:

> But Peter and the apostles answered and said,
> We must obey God rather than men.

Here priority is given to whatever a man regards as the commandments of God. This statement is not the least parochial in time or place, as a principle governing the relations between men and the state. (However, see also I Peter 2:13-25.)

Here are three principles: (1) always obey the state; (2) consider the state the "great beast," the anti-Christ, and never bow before it for your soul's salvation sake; or (3) obey the state when it conforms to the commandments of God, but not otherwise.

What would our banker friend make out of these three principles. Would he accept Paul's doctrine, and reject John's and Peter's; or would he prefer one of the others? Or would he conclude that Scripture contains lamentable disagreements, and that at best one must pick and choose?

The Attitude Of God Toward Men

If there is any teaching in Scripture which would seem to be significant for this life, it would appear to be its teaching regarding the attitude of God toward men — is it (1) generally favorable; (2) generally unfavorable; or (3) is it discriminatory? Let us quote three views again:

1. God loves the sinner more than the righteous;
2. God loves those who are good, but not those who are evil; and
3. God loves good and bad men equally.

Here is enough disagreement to confuse even a sagacious banker.

1. Let us first consider the statements about God's preferential love for the sinner. There are conspicuous examples, the parable of the Prodigal Son, the Lost Sheep whom the Shepherd went out to save at the cost of temporary separation from the "Ninety and Nine." Then there were the publicans and sinners preferred to the Pharisees, who at least *outwardly* were not such grievous sinners. Or if they were all equal sinners, why was such preferential time and attention given to the "publicans and sinners"?

2. In contrast, Scripture repeatedly promises rewards for the good, and punishment for evil-doers. Consider the First Psalm:

> Blessed is the man that walketh not in the counsel of the wicked, Nor standeth in the way of sinners, Nor sitteth in the seat of scoffers. . . . The wicked are not so, But are like chaff which the wind driveth away. Therefore the wicked shall not stand in the judgment. . . . the way of the wicked shall perish.

The idea is simple: the good are rewarded and the evil punished.

3. Finally, there is the third idea, found in the celebrated Sermon on the Mount, namely, that God does not treat the righteous better than the unrighteous, but that (Matthew 5:43-48):

> Ye have heard that it was said, Thou shalt love thy neighbor, and hate thine enemy: but I say unto you, Love your enemies, and pray for them that persecute you; that ye may be sons of your Father who is in heaven: *for he maketh his sun to rise on the evil and the good, and sendeth rain on the just and the unjust.* For if ye love them that love you, what reward [merit] have ye? do not the publicans the same? And if ye salute your brethren only, what do ye more *than others?* do not even the Gentiles the same? Ye therefore shall be perfect, as your heavenly Father is perfect.

Here good and evil men are treated equally without discrimination.

A banker, by a single, first-time, objective reading will probably lay the Bible aside, and say, "There are some fine statements and grand stories in the book, but it is self-contradictory. As a book, the Bible is just about what you want to make out of it. In regard to being (1) indifferent to good and evil, versus (2) rewarding merit and penalizing evil, the latter looks like the better policy to me. As a banker I have no intention whatever to make loans to the unwise and dishonest in the same way as I make them to the prudent and honorable, nor am I going to take a natural phenomena, as rain and sunshine, for my guide in business." If our banker friend reasoned that way, we would be in perfect agreement with him.

Of the three propositions here listed regarding God's attitude toward good men and evil men, the only one that states a comprehensive rule is the second, God rewards the good and punishes the evil. But then the other two propositions: that God favors sinners, or that He is a nondiscriminator, need careful exegesis — if the Christian religion is not to be ridiculous.

If the experts in interpreting Scripture, after much study, are often at loggerheads on the most elemental and fundamental subjects, what is one to expect from mere *casual* Bible reading even when the reader is a highly intelligent person, or *just because* he is a highly intelligent person.

An Erotic Poem?

Or, consider the "Song of Solomon," also known as the "Canticles of Canticles," which appears in the Old Testament. On simple reading — by our banker or anyone else — this Bible book will probably leave a man with two conclusions, (1) this is an erotic poem catering to sexual instincts, and (2) it is an extremely confusing poem, if not meaningless. Neither conclusion will do the Christian religion any good, nor enhance the Bible in the estimates of its readers.

Recently a friend gave us a new Catholic edition of the Holy Bible (known as the Confraternity Edition). This edition supplies some genuine helps for understanding the "Song of Solomon." First, there are some helpful footnotes. Secondly, this edition indicates that there are *three* "characters" in the Song, and it is further indicated in this edition what is to be ascribed to each of the three. Who, indeed, would know that there are *three;* most people think there is only *one* character speaking in the "Song?" The three are, the bridegroom, the bride, and a chorus (probably of girls). With this assistance, the Song of Solomon takes on an altogether different aspect; it "makes sense" and has "propriety." But without that assistance, not improbably the Song of Solomon would not enhance our banker's estimate of the Scriptures.

* * *

There is, indeed, an interesting problem about *how* to read Scripture. There are at least three different approaches that can be made to it: (1) the Catholic, (2) that of the organized Protestant Churches, and (3) that of the undenominational churches. The first favors the thought that Scripture should be interpreted through the church, and this is emphasized to such an extent that Catholic layfolk are not encouraged to explore Scripture by themselves; if they have questions, ask the priest. The second favors free study of the Scriptures by everyone, but adds the restrictive discipline — you may not belong to this denomination unless you do indeed read (interpret) the Scriptures as we do; accept our creeds, or stay out. The last group rejects the other two positions, and apparently sees no problem and seeks no harmonization or rationalization of Scripture; if there are problems, the undenominational churches do not appear to work at solving them.

The history of the Church indicates a tireless effort at "rationalizing" Scripture. People today do not read it as they did one thousand years ago. The "framework" in which they see Scripture is different. The "frame of reference," in Einstein's sense, has been altered greatly. It is probably correct that the creeds need further substantial rationalization. The process will always be "behind the times," which is probably inevitable and as it should be.

But a mature individual, with no real Christian background, under no great emotional strain, philosophic in temperament, reading the Hebrew-Christian scriptures as a research project, in our estimation, needs help in two ways, one of which is available. The two aids that he needs are:

(1) What creeds and dogmas the churches have already worked out to "harmonize" the varieties of ideas in Scripture; in other words, he should read not only Scripture but the creeds as well; maybe simultaneously, maybe *after* reading scripture; but the analytic work which has resulted in the creeds should not be ignored.

(2) He might wish to work at further harmonization of Scripture himself. He — if a superior reader of Scripture — should think beyond the creeds, should bring them up to date, and should interpret the (apparently) conflicting statements in Scripture more skillfully than the slow-moving creeds have yet done.

Lord Charnwood somewhere in his biography of Lincoln quotes Lincoln (who did not read the Scriptures once but often and repeatedly and Lincoln was a most excellent reader), as saying something to the effect: "Take all of Scripture that you can understand on its merits, and the rest on faith, and you will not go far wrong." That would be a profitable attitude for all men to take.

* * *

Not many mature, prosperous people who have not been educated to the Christian religion are converted to it in their full maturity. A single research reading will not develop many Christians. For Scripture to be accepted it is usually necessary to be educated in it from childhood. This is probably the reason that denominations with parochial schools appear to be the most prosperous and virile. The graduates of their grade and higher schools already have the assistance of a creed in reading Scripture, and the approach to the reading is not pure research, but is often accompanied by genuine devotion.

If Christianity is to survive, it will be necessary to "assist" the Bible with some dogmas, systematically taught, and intelligently interpreted. Churches without their own schools, (or the equivalent of parochial schools,) will probably dry up as a river running into desert wasteland. Whoever does not hold to that will be obliged to place his reliance on the kind of reading of this banker.

Joe Doakes At The Gate

The following is taken from an article by Leonard E. Read entitled "On That Day Began Lies" in *The Freeman,* April, 1956, published by the Foundation for Economic Education, Irvington-on-Hudson, New York. Readers of First Principles should read this entire article because it pertains to a dispute within the National Council of Churches, an organization with a program which is strongly interventionistic if not socialistic.

> Imagine this: Joe Doakes passed away and [appeared at the gates of heaven]. He [rapped at] the Gates and St. Peter appeared.
>
> "Who are you, may I ask?"
>
> "My name is Joe Doakes, sir."
>
> "Where are you from?"
>
> "I am from Updale, U.S.A."
>
> "Why are you here?"
>
> "I plead admittance."
>
> St. Peter scanned his scroll and said, "Yes, Joe, you are on my list. Sorry I can't let you in. You stole money from others, including widows and orphans."
>
> "Mr. St. Peter, I had the reputation of being an honest man. What do you mean, I stole money from widows and orphans?"
>
> "Joe, you were a member, a financial supporter, and once on the Board of Directors of The Updale Do-Good Association. It advocated a municipal golf course in Updale which took money from widows and orphans in order to benefit you and a hundred other golfers."
>
> "Mr. St. Peter, that was The Updale Do-Good Association that took that action, not your humble applicant, Joe Doakes."
>
> St. Peter scanned his scroll again, slowly raised his head, and said somewhat sadly, "Joe, The Updale Do-Good Association is not on my list, nor any foundation, nor any chamber of commerce, nor any trade association, nor any

labor union, nor any P.T.A., nor any church. All I have listed here are persons, *just persons.*"

Individualism and Christianity are not "social." They keep their eye on persons; not on "*corporate* responsibility."

The Consequence Of A Market Economy

For the purpose of *organizing* society, there is a choice between only two systems: a free-market system associated with private ownership of capital; or a socialist-communist-interventionist system in which bureaucrats control distribution and production, because there is no private ownership of capital but only public ownership.

What is the principal economic consequence of a *free-market-private ownership* type of economic organization of society? This is Ludwig von Mises' answer: (see page 413, *The Theory of Money and Credit,* Yale University Press, 1953)

> Private ownership of the means of production tends to shift control of production to the hands of those best fitted for this job and thus to secure for all members of society the fullest possible satisfaction of their needs. It assigns to the consumers the power to choose those purveyors who supply them in the cheapest way with the articles they are most urgently asking for and thus subjects the entrepreneurs and the owners of the means of production, viz. the capitalists and the landowners, to the sovereignty of the buying public.

The consumer is "boss." Contrarily, under a socialist-communist-interventionist system the "boss" is not the consumer interested in his own welfare, but a bureaucrat, who does not urgently see to it that the control of capital comes into possession of the most efficient users of capital.

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FIRST PRINCIPLES
IN MORALITY AND ECONOMICS
on which depend personal well-being and social health and harmony

VOLUME V | AUGUST, 1959 | NUMBER 8

Contents

A Man Who Taught That Business Is Solely For Profit

An associate, who was also a professor at a famous midwestern university, was accustomed to tell, as a fit subject of amusement, the various answers his students gave to his questions: "Why is a man or a company in business? What is the purpose?"

The answers, he would relate, were of all kinds: (1) to increase production; (2) to supply men with what they needed to survive and to be comfortable; (3) to provide employment for those who needed work; (4) to provide for self and have a surplus for charity; (5) to devote one's life to service for others; and a surprising number of additional reasons for being in business.

The questioner was a self-made man and rugged individualist. He was born on an unproductive farm in the south-central part of the United States. As a boy he had rebelled against farm work and the living conditions in his home. In defiance of parents he had packed his few belongings and left for the "city". Hard years followed — of poverty, privation, disappointments. But these had all been surmounted by hard labor, driving ambition and an iron will. He was now a business "tycoon" with a large income and great influence. If, as was often the case, he had worked far into the night at his regular business, it was nevertheless his invariable practice to be at the university at seven the next morning on his lecture days to teach a class in business problems. This teaching activity was in a sense a labor of love. The money he received for it was a small part of his income. But he had a "compulsion" to teach to others what he had learned himself. And so he continued to teach, despite the steady drain that it was on his strength; he died before he was 50 years old. Obviously, he was a man of mixed make-up; aggressive, but with a strong streak of idealism in him, making him willing to exhaust himself to teach others whatever he had learned that he considered of value.

This was the man who was asking the question: "What is the purpose of business?" This was the man who was relating with ridicule the type of answers which he was given. Then he would bring his story to a climax by saying that he always told his class of students: "The sole and only purpose for being in business is to make a profit."

How be reconciled to the fact that good business men concentrate intensely on making a profit, and without compunction express

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their objectives in those terms. Is there a connection here between selfishness (the wish for profits) and success; and is there no connection between idealism and success? Especially, if a man has idealism about *serving his neighbor,* and thereby presumably showing "brotherly love", does that mean he is likely to be a failure in business? Can a man, in fact, have his goal set solely on making large profits, and still be serving his neighbor?

The problem can be stated in this manner: how reconcile the objective of serving one's neighbors with the objective of making a profit?

It Is Maladroit To Say That The Sole Purpose Of Business Is To Earn A Profit

Although the expression, *The sole purpose of business is to earn a profit,* is an admirable and to-the-point formulation, it is nevertheless an unfortunate one. We agree wholeheartedly with the idea, but deplore the words in which it is expressd. It is very maladroit, considering the way most people will interpret the statement.

It will sound to them as if the speaker is shamefully selfish. Many people will suspect that he aims to be successful *at the expense of other people.* It sounds almost as if a man who says, the sole purpose of business is profit, is also in effect saying, the devil take the hindmost, and what do I care about how anybody else gets along. Actually, the expression, when used by a business man who has a comprehension of the real business structure, does not mean that he intends to get a profit from his business activities by means of exploiting other people, or by being indifferent to their welfare. There will *never* be a profit, in a free economy, for a business man who is indifferent about serving his fellow men. In a free economy, the only road to profit is exclusively via the road of service.

How then should the "idea" encased in the expression, the sole purpose of business is to earn a profit, be better formulated? This is the way we would express the identical idea: *the purpose of business is to serve independent customers so well that they voluntarily and actively will wish to buy from you, which will be evidence that they consider it is beneficial to them to do so, which in turn means that your selling prices are in-line or low, that your* *quality is good, and that your product functions as well or better than competitive products. Further, if after serving your customers so well, you still make a profit, then that is evidence, in a free market for labor, that you are an efficient operator who knows how to muster labor and material so well that there was a profit left to you after paying the full market for material and labor. Your profit was the evidence, assuming free markets, that you were legitimately in business, that is, that you were genuinely efficient, because only those efficient enough to survive under free competition are legitimately in business. People simply rewarded you with a profit, because you were efficient in service to your fellow men; and they rewarded you in proportion to that efficiency.*

Surely, a business man wants a profit, for more than one reason. He wants a profit from his personal self-regarding viewpoint, just as everybody wants what he can honestly get. There is nothing wrong about that. He wants a profit, too, because it sustains his morale. He knows that if he does not make a profit, he is, and will be known as, a blunderer in business. He does not wish to have that reputation. The blunderers miscalculate, lose money, go out of business.

Of course, none of the foregoing is true if there is not a *free* market. The phenomenon of profit is not evidence of service and efficiency when a society is either socialistic, communistic, or interventionistic; the "profits" of a business in such cases are controlled by bureaucrats; *they* are sovereign, and not the consumer. But where the free consumer is sovereign, and in a society where coercion is prohibited (according to the Sixth Commandment of the Decalogue), there *profit* is synonymous with *superior service to one's fellows.*

If anyone insists that that statement be qualified, then it might be thus: profit in a free society is equivalent to service to fellow-men, except in so far as fellow-men do not know their real interests or lack vigor to act in a manner to attain them.

But, in any event, "consumers are sovereign." They determine, by buying from you or abstaining from buying from you, whether you will be able to make a profit.

If there is anything in this world that is a reward for obeying the Sixth Commandment (which broadly means, Thou shalt not coerce), then it is profit.

Ludwig von Mises On The Present-Day Significance Of Knowing Something About Economics

In an article in *The Freeman* (published by the Foundation for Economic Education, August 1959) Ludwig von Mises has the following to say about the present-day importance of reading economic books and studying economic problems:

> . . . what about the general reader, the man who does not plan to specialize in economics because his strenuous involvment in his business or in his profession does not leave him the leisure to plunge into detailed economic analysis? . . .
>
> To answer this question we have to take into account the role that economic problems play in present-day politics. All the political antagonisms and conflicts of our age turn on economic issues.
>
> It has not always been so. In the sixteenth and seventeenth centuries the controversies that split the peoples of Western civilization into feuding parties were religious. Protestantism stood against Catholicism, and within the Protestant camp various interpretations of the Gospels begot discord. In the eighteenth century and in a great part of the nineteenth century constitutional conflicts prevailed in politics. The principles of royal absolutism and oligarchic government were resisted by liberalism (in the classical European meaning of the term) that advocated representative government. In those days a man who wanted to take an active part in the great issues of his age had to study seriously the matter of these controversies. The sermons and the books of the theologians of the age of the Reformation were not reserved to esoteric circles of specialists. They were eagerly absorbed by the whole educated public. Later the writings of the foremost advocates of freedom were read by all those who were not fully engrossed in the petty affairs of their daily routine. Only boors neglected to inform themselves about the great problems that agitated the minds of their contemporaries.
>
> In our age the conflict between economic freedom as represented in the market economy and totalitarian government omnipotence as realized by socialism is the paramount matter. All political controversies refer to these economic problems. Only the study of economics can tell a man what all these conflicts mean. Nothing can be known about such matters as inflation, economic crises, unemployment, unionism, protectionism, taxation, economic controls, and all similar issues, that does not involve and presuppose economic analysis. All the arguments advanced in favor of or against the market economy and its opposites, interventionism or socialism (communism), are of an economic character. A man who talks about these problems without having acquainted himself with the fundamental ideas of economic theory is simply a babbler who parrot-like repeats what he has picked up incidentally from other fellows who are not better informed than he himself. A citizen who casts his ballot without having to the best of his abilities studied as much econo-

mics as he can fails in his civic duties. He neglects using in the appropriate way the power conferred upon him in giving him the right to vote.

Unreasonable Requests Addressed To Union Leaders That They Be Reasonable

Presently (August, 1959) there is a steel strike in the United States. Negotiators for the employers, and many people — some of whom speak for themselves and others who speak and write as if they were authorized spokesmen for the "public" — call on the negotiators representing the United Steelworkers of America to be "reasonable", that is, not to demand large wage increases and not to strike, all for the alleged reason that the union should not contribute further to the inflationism which has been continuing steadily in the United States.

This request to be "reasonable", addressed to the negotiators and the members of United Steelworkers of America does not appear, upon careful thought, to have real merit and it is hard to see why the Union and its leadership should heed it.

Recently three men were riding back from lunch to an afternoon meeting. The sales vice president of a heavy machinery company which consumes annually thousands of tons of steel was sitting in the back seat, and he was talking about the strike. This is what, in effect, he said: "I don't see how anybody can expect a favorable response from MacDonald [head of the United Steelworkers of America] to a plea that he be 'reasonable.' How long could any labor leader expect to survive who does not fight hard, using all means that the law allows, to get for his members everything that he can? Every union head who expects to keep his job must fight for all he can get, without paying any attention to general conversation about inflationism. If he does not follow the policy of getting what he can get, strike or no strike, he won't last long. Somebody else will get his job. When I imagine myself in MacDonald's position, I can't think of myself doing anything differently from what MacDonald is doing."

These were approximately the words of a business man adversely affected by the strike, and not the words of a union partisan. This man was sincere in his thinking and speaking. What he said appears to be sensible; it gets down to this: *if the law permits something to free men, they will surely do it if it is good for* *them or their group, even though it hurts society generally. If the law permits men to do what is wrong, but one man resists the temptation to exercise the power which he has to do wrong, he will be succeeded by someone who does not exercise that voluntary self-restraint to be "reasonable". When the law permits something, competition among men will insure that whatever is permitted will surely be done. If* A *will not do it because he is "reasonable", then* B *or* C *or* D *will be crowding hard to do whatever the law allows, completely disrespectful of whether it is "reasonable".* It has always been that way, and it will always be that way.

MacDonald is a foolish man, if he does anything less than the law allows. If there is something wrong, it may not be the "reasonableness" of MacDonald or his United Steelworkers of America union, but it may be the law of the land which says what unions may or may not do; or, finally, it is poor enforcement of laws which MacDonald and the union might be breaking. The real trouble is not the lack of sweet reasonableness, but (1) the law of the land or (2) its enforcement. The citizens of this country should address themselves to that, and omit ridiculous preachment to MacDonald about "reasonableness."

Similar Unreasonable Propositions Addressed To Bankers By Themselves

When reading this article, the several things previously written in *First Principles* about money and banking should be kept in mind. To assist the reader we shall restate a few of them so that what follows will be more easily understandable.

There are various kinds of money, namely, metal money, paper money, token money, fiat money, credit money. If a bank extends *credit* to a customer, that means it supplies purchasing power to customers; credit is therefore an obvious substitute for money and has the same effect as regular money.

Secondly, under United States law (for the unwise purpose of making money more plentiful), banks are permitted to put out as much as five times as much new credit as their gold reserves increase. This special privilege of the banks, permitting them to "create" five times as much money as they increase their gold supply, means that there is a terrific leverage from changes in the gold supply, either up or down.

This five-fold leverage, which is "organized" into the United States banking system, is the source of that systematic disorganization of business, which is known as the business cycle, or booms and depressions. We are describing phases of the process, as simply as possible, in a general analysis which indicates that there should be changes in the money and banking laws of the country.

Bankers have sometimes admonished themselves, just as moralists sometimes admonish labor union leaders. Such bankers admonish themselves in this vein:

> We should, of course, make all the loans to business that we can. That is our function. The money to make these loans comes in part (1) from our capital and from savings deposited with us or from balances left by depositors in their checking accounts; and in part (2) from fiat credit — credit which we "create" as out of thin air — resulting from our special privilege which permits us to manufacture credits in the amount of five times any increase in our gold reserves; if we get $1,000 more of gold (which we will deposit as additional reserve with our Federal Reserve Bank), then we may — if we wish — increase our loans $5,000.
>
> Our problem is to make as much money as we *safely* can. We, therefore, want to loan pretty freely. If we get more gold, we must put that resource to work as soon as possible by loaning (or investing) five times as much. If we do not do that, then the business will go to competitors. They will expand their loans — credits which they make available to borrowers — more than we will. They will make a bigger profit than we will make. We will appear to be unsuccessful bankers and they will appear to be much more competent. But we must be careful not to increase our loans *too much*. We should not increase them so that we *overdo* it. We must exercise self-restraint, too.

This is exactly the same kind of "solution" to banking problems as would be applied to labor problems today, if we permit proposed labor reforms to be nothing more than to tell labor union leaders to be better men and to let the labor laws stand unchanged —labor laws which permit labor leaders to do these very things that are bad.

The trouble with the banking situation is that the laws governing banking are as deficient as the laws governing labor unions. They are both, in fact, intolerable.

The Remorse Of Big Bankers In 1908

As we have reported earlier (in the November 1957 issue), many years ago the writer had occasion to go to the local Federal Reserve Bank, to ask permission to examine certain old financial magazines. He wished to read them as far back as the year 1900. He had tried other libraries first and had been told that the magazines, if available at all, would be in the library of the Federal Reserve Bank. Upon inquiry at the bank, he was readily accommodated, except that none of the publications were available prior to 1908.

The year 1908 was the year following the banking panic of 1907, a year in which the banks had been unable to meet their obligations and many of them had failed. Those who survived had done so by creating a temporary money, known as Clearing House Certificates.

The magazines in question were in 1908 full of honest and upright self-examinations, confessions and self-incriminations, by bankers. Some of the articles in the magazines were written by outstanding bankers of that day. Or the articles told about some conference of bankers at which several had made speeches analyzing why the financial disaster of 1907 had occurred. With obvious sincerity they all *blamed themselves.* This in effect is what they said:

> We loaned *too much.* We extended *too much* credit. We should have exercised more self-control. If only we had not loaned so much, there would not have been a depression, much less a crisis, and certainly no panic. We made a mistake. We ought never to make the same mistake again.

Their sincerity about all this was obvious, and they were as contrite as a sinner coming down "the sawdust trail."

But they did not, in the articles we read, condemn the *system* under which they had operated. They condemned themselves only. That was good as far as it went, but it did not go far enough. They should have been more fundamental in their condemnation, namely, they should have condemned the basic premises of the banking system under which they had been operating.

The Problems Of Banks: To Be Profitable And Liquid

A description of *everything* that would take place if a person engaged in the banking business in the United States would be difficult to understand, especially if the description outlined all of the features and details of present-day banking law. What follows is instead a schematic description designed to reflect the monetary and banking *principles* involved, so that the average layman will obtain a general understanding of them, rather that a precise and complete technical description.

Imagine deciding for yourself that you will be a banker. If that would be your goal, these might be the steps in the program that you would take.

Step I

As a banker, you would invest, say, $100,000 of your own money in a commercial bank.

Next, you would ask others to deposit their money in your bank. Maybe they would put in $500,000 and open checking accounts. You have then $600,000 with which to work. Your bank will have expenses, as rent for banking quarters, salary for a teller, light, taxes, remuneration for yourself, etc. Further, you ought to get a 5% return on your investment of $100,000, or $5,000, because income from capital is in the nature of things. Rent would be, say, $5,000 a year; teller, $5,000; salary for yourself, $6,000; miscellaneous expenses, $4,000; and a $5,000 return on your investment. The total of that is $25,000.

Step II

You will wish to put the $600,000 to work quickly. The thing to do is to loan it. If you loan every dollar of it at 5%, you will have a return of 5% on $600,000, or $30,000. Your "costs" (including a 5% return on your investment) are only $25,000. You have, under this assumption, an *extra* profit of $5,000. If this was the real character of the banking business, then it would be a nice business to be in.

Step III

But the assumption in Step II is unrealistic. People do not have checking accounts in banks, except to have money available *whenever they want it.* You, as a banker, cannot loan the money to third parties, if your depositors have placed their money in your bank for the sole purpose of having it reliably available to draw on whenever they need money. They wish to have their money available *on demand.*

If that is the case, it might seem to follow that it is not safe to loan any of the money to third parties, unless it is loaned to third parties who will make a contract to pay back immediately on your demand. Few borrowers will want loans which must be repaid *on demand,* that is, whenever the lender (in this case your bank) must have the money back, so that the depositors of the bank can use it themselves. Gone then is most of the $30,000 of theoretical earnings figured in Step II. If *all* the $500,000 of deposits must be kept on hand, you can loan only your capital of $100,000 at 5%, or earn $5,000.

Compared to the $25,000 of costs which you should be able to cover, according to Step I, you are short $20,000. Who would want to be in the banking business, and lose money at that rate? Would you not give some thought to returning to your depositors the money which they had deposited, to cancelling your lease, and to putting your own $100,000 to work somewhere else?

Step IV

But after being in the banking business for a while, you do discover one thing, namely, although all your depositors want their money to be available *on demand,* and although now one and now another does draw out all of his funds, nevertheless *it seems* that *it never happens that all the depositors want their money at the same time.* You notice that although deposits fluctuate — sometimes over, sometimes under $500,000 — the amount of deposits never seems to go below $300,000. When you think it over, this appears natural and even probable. If *A* buys a house and must pay to *B* $5,000 for it, *A* may draw $5,000 out of his account, but *B* adds it to his account. One man's disposal of money means another man's acquisition of money. Money is never "idle" in a real sense. People wish to have money as their cash reserves against emergencies. Money can be looked upon as resting always in someone's possession. There is, indeed, a "circulation" of money, or a "turnover" of money, but money *always* belongs to somebody. It is either in *A*'s possession or *B*'s possession. The moment of transfer between the two is infinitesimal, and from this viewpoint can be looked upon as nonexistent in time. And so, there it is, always in your bank, unless (1) a depositor withdraws money in order to carry more in his pocket; or (2) he transfers funds to another bank; or (3) someone to whom he makes payment keeps the money in his pocket or deposits it in another bank. But the money is always "resting" somewhere.

Having discovered that your deposits appear never to go below $300,000, you reach a major conclusion, namely, not only can you loan the $100,000 which is your own capital, but you can loan another $300,000 of depositors' money. You can now loan a total of $400,000. At 5% your income as a banker is now $20,000. That compares with your costs of $25,000. There is still no profit in your banking venture, but a loss of $5,000. Nevertheless, by "taking a chance" on loaning $300,000 of depositors' money, which they *seem* always to leave in their balances, you have cut your loss from $20,000 to $5,000. But, who knows, they *might* demand all their money some day!

It should, of course, be kept in mind that people can become frightened. The first thing they then do is they try to protect themselves by getting or holding tightly to emergency funds, that is, by having more cash. If a terrifically frightening event occurs, your depositors might make an unprecedented withdrawal. They might reduce their deposits to nothing, or rather *try* to do so. They could not, under the circumstances assumed, do that. The cash would not be there, because you have loaned out $300,000 of their money. When they begin to draw out and continue to draw out cash, you will be sitting anxiously in your bank office hoping that the special withdrawal will end. But there are still depositors who want $200,000 more. What can you do? You could go out on your bank floor and talk to each of them like this: "Mr. Smith, I have loaned out $300,000 of the depositors' money to borrowers who needed money. They will pay me back soon, at varying dates, depending on when their notes are due. Would you please wait another 60 days or a half-year?" But Smith and the other depositors may be frightened. They may say: "Mr. Banker, we understood we could *always* get our money when we wanted it. If we had not expected that, we never would have put our money in your bank. We *must* have our money, *right now.*" If the borrowers, whose notes come due from time to time, pay their notes on time, you will be able *finally* to pay out your depositors.

At the moment that you are unable to pay you are at least *nonliquid,* and if many of your borrowers do not pay you, your bank may be *insolvent.*

To make the distinctions between being nonliquid, insolvent and bankrupt will be helpful in explaining the problem.

To be *nonliquid,* and nothing worse than that, means that what you own is worth more than what you owe, but nevertheless you are unable to pay because your debts come due sooner than you can convert your assets into cash with which to pay your debts. To be nonliquid is always distressing to honorable people, and very frequently brings on bankruptcy. The reason is that alarmed creditors do not wish to wait for an orderly and maybe slow conversion of your assets into cash. Because they need the money, or because they are alarmed, they may insist on so fast a sale of your assets that the prices you get for them are less than their real worth. At first, you may have been merely nonliquid, but you may end being insolvent and bankrupt. To be nonliquid is always to be suspect, and consequently a nonliquid condition is very dangerous.

To be insolvent means that your debts really exceed your assets; you have *no net assets.* Nevertheless, it can happen that you will not, although insolvent, go through bankruptcy. Your creditors may give you time, and by hard work and thrift you may be able to accumulate an amount equal to as much as your debts exceeded your assets, and so pay off the debts.

To be *bankrupt* means more than that you are insolvent; you may see no hope to pay your creditors fully, and/or they mistrust it; you ask for bankruptcy proceedings and/or they demand it; your creditors are then all paid proportionately, but not the full amount (unless they are secured creditors in which case they get more); and you are then declared free of obligation to pay the remainder. Your name has, however, a stain on it. You have been a bankrupt.

A bank, to do well, must retain the reputation of being liquid, as well as being solvent. The mere fact that your bank might not be able to pay one depositor his money, *on demand,* will be disastrous for your bank. That depositor will surely talk about it.

For a bank to retain its reputation, it is as necessary to be "liquid," as it is for a woman to be virtuous. The breath of suspicion is ruinous. Depositors who do not need the money and had not intended to take it out will at once demand their money if they come to have doubts. There will be a "run" on your bank.

To restrain banks from following policies which will result in their being *nonliquid,* laws have been passed prohibiting commercial banks from making certain kinds of loans, that is, loans not due for repayment until a long time in the future. Obviously, the longer the time the loans made by a bank are not due to be repaid, the less liquid that bank is. Bankers, too, pay attention to "spacing" the maturity dates of loans they make, so that regularly some loans come due. By spacing and by being restricted to *short-term* loans, commercial banks are kept *relatively* liquid.

But in a sense, every bank is in part unsafe, namely, in so far as its obligations to pay are *demand* liabilities, that is, are depositors' claims due *on demand,* while simultaneously assets are invested in loans which are not all due and collectable *on demand* of the bank. Every commercial bank which has all its liabilities due on demand, but not all its assets are due on demand (or if due on demand in theory are not collectible on demand in fact) is vulnerable, and is in a sense courting trouble in times of emergency. (Banks have some "reserve", of course, in the form of capital, undivided profits, and surplus.)

Step V

But, as if your problems as a banker were not great enough, in emergencies, in the form of the potential demand for immediate repayment of *all* of the deposits, what would you think of increasing the risk still more?

Suppose the law permitted you to put out five times as much money as you have gold in your bank (or, more accurately, in your Federal Reserve Bank). Let us assume that you have taken your $100,000 of capital and put $80,000 into gold and $20,000 into bank fixtures. On the $80,000 of gold, according to the laws of the United States, you could make $80,000 x 5, or $400,000 of loans. The law does permit you to do that, and let us assume that you acted according to that permission. Your situation in regard to income-producing assets would then be:

1. Your own assets ($100,000-$20,000) x 5, equal to	$400,000
2. Depositors' money in the amount of $500,000, less $200,000 for "fluctuations in their balances," which means you can "safely" (?) put to work only	$300,000
Total potential working assets	$700,000

Now, if you get 5% interest on the $700,000, your gross earnings will be $35,000. Subtract from that the $25,000 "costs" as previously computed and you have an *extra* profit of $10,000. Finally, your bank has become profitable.

Let us proceed with the analysis. Originally, you as banker "contributed" $100,000 to the supply of funds. You must have obtained that in some way — by inheritance, by work, by saving, by borrowing from a friend — at least somehow. You parted with $20,000 of it for furniture and fixtures. That left you the $80,000, which you invested in gold. Then you "created" $400,000 of deposits. That was done something like this: Mr. Andrews comes in and wishes to borrow $20,000. You agree to loan him that amount. Where does the $20,000 come from? Your own capital is "tied up" in furniture and fixtures, and in gold. You simply ask Andrews to sign a note of $20,000 and you take Andrews' bank passbook and post there-in a deposit credit of $20,000; you give him a check book; he can draw out the $20,000 as he needs and wishes. To "balance" the $20,000 on your books you show on your books an "asset", consisting of $20,000 owed to you by Andrews and evidenced by a note. This loan to Andrews is in the form of a *deposit credit.* It is equivalent to money in the markets in your community.

Andrews can spend any or all of the $20,000. Usually, he is expected to "keep a balance" of one-fifth the amount of his loan; in this case that is $4,000. If he observes that rule, he can spend $16,000 of the $20,000 he has borrowed. That "money" is "new" money for all practical purposes. Andrews buys like any other buyer, and when he does so, he affects business as other buyers do. But there is nevertheless a fundamental difference. There was *no production on Andrews' part antecedent to his buying.* He is a "new" buyer, a man who comes in with the exact equivalent of counterfeit money (except that the law allows it, and that the public believes that this kind of counterfeit money makes for general prosperity, whereas nobody believes that the practices of regular counterfeiters contribute to prosperity).

Counterfeiters have not found the way to produce counterfeit money half so easily as the banking system, as just explained, permits counterfeit money to enter the buying stream. Counterfeiters must laboriously (and secretly) print counterfeit bills. But, in the case just explained, all that is necessary is for a user of the banking type of counterfeit money to sign a note for $20,000 and for the banker then to give the man a bank passbook, post the date in it, and the figure of $20,000. Presto! There is $20,000 of "counterfeit" purchasing power, created so easily, so legally, and blessed with so much community approval and praise, that everyone who understands what has really happened should be astonished. The world is really upside down!

Step VI

What you do for Andrews you can do for others until your total of $400,000 of "counterfeit money" is exhausted.

In a sense your $400,000 is not all "counterfeit." There is behind it $80,000 worth of gold. That gold could have been used for money and so the counterfeit amount is really $320,000, as far it affects business. The amount, however, that you as banker have available for disposal is the full $400,000. How far you go in loaning it depends on your discretion. You know there is that limit in the total — $400,000. Once you have loaned out the $400,000 you must stop. Any late comers for some of the purchasing power which you have "created" will have to be told regretfully that there are no funds available anymore, (unless some of the older loans made by you come due, and are paid off, and you can re-loan that amount). The *surge* of loans that you could make is over as soon as you have utilized the whole amount obtained by multiplying your reserve of gold by five.

That surge had an effect on business of significant proportions. There was $400,000 of purchasing power in the form of new bank deposits added to the $500,000 that the townspeople had already put into your bank. They originally had $500,000 in the form of bank deposits, with which to buy. If your $400,000 is added to it, the amount is $900,000 of monetary purchasing power. Such an increase will have some big effects in your city.

There is no reason whatever to expect that there will be an increase in prosperity from this increase in money. A country does not become rich by borrowers signing notes at a bank, and the banker posting $20,000 (or whatever the amount of the loan is) in the passbook of the borrower. It would be ridiculous to think that prosperity could be created in that manner.

The borrower can go out and use the $20,000 to buy capital goods, consumer goods, or go on a wild spree of debauchery. But society is not richer by his *consumption,* and he becomes a consumer of something, by the use of your money, before he can become a producer. (Whether the borrower uses the $20,000 for one purpose or another will have an effect on the welfare of society; a wise expenditure will give better consequences than an unwise expenditure, but some of the remote consequences of that are beyond the present analysis.)

The fact of importance at this time is that the borrower himself benefits from getting this purchasing power, and that during the current situation his *fellows are correspondingly injured.* That has been explained in earlier issues. When fiat money of whatever kind is made available, the *first* users are the principal beneficiaries of that new money, because they intrude into the buying of existing merchandise, at the old prices, which do not reflect the enlarged money supply. There is, as Hume recorded long ago, only one sure effect from increasing the quantity of purchasing power — not increased prosperity or wealth — *but only higher prices.* Those higher prices do not occur equally and concurrently but variably and in sequence. The *second* users also gain from the new money, albeit less. And so on. The later and especially the last users of the new money are unqualified losers. They do not get the *extra* quantity of purchasing power which has been made available until everybody else has preceded them. These last users, in the meanwhile, have been selling their products and their services at the old prices or at laggard prices. They have been buying more dearly all the time because the early users of the new money were bidding for goods, but they themselves did not yet get hold of some of the extra or new money to enable them themselves to bid higher. In short, what the early users of the new money obtained as an advantage, the later users lost.

The over-all consequence of the new fiat money, in the form of *deposit credits as explained,* is that some gain at the expense of others, *temporarily.* Eventually, the consequences permeate through the whole economic structure. All prices are then higher. But *in the meantime there have been great inequities perpetrated between individuals.*

The outstanding conclusions that can be reached are that you as a banker have increased the quantity of money in your community, have benefited your direct borrowers and other early users of your money, have hurt all the later users, and that prices are generally higher, but that the community has no more real prosperity than it would have had if you had not created new money in the form of deposit credits. By your new money, you have *altered* but *not improved* the economic aspects of your community. Further, you have made a profit for yourself by "creating" money in your banking operations. You and your borrowers were the gainers to the hurt of the rest.

(Some may argue that the fiat money you created will turn out to be a form of "forced savings", from which society will benefit. But so-called "forced savings" are only one of several potential consequences of your putting out new money. But in any event, it is not correct that "forced savings" have certain effects as some people think. It is not feasible to digress here to consider the merits or demerits of "forced savings".)

Step VII

But you yourself will have some special problems as a banker, which derive directly from your practice of putting out new money in the form of *deposit credits.*

If some disaster happens and your depositors suddenly want their $900,000, you will be unable to pay them. According to our assumptions, you would have $20,000 in furniture and fixtures; $80,000 in gold in the vault of your Federal Reserve Bank; $200,000 in cash in your bank quarters; $300,000 of loans made with depositors' funds; and another $400,000 of loans with " created" funds. (A phase not covered here is that some of the loan amounts would be left in cash balances.)

You would pay out your $200,000 which is in cash to those first in line to take out their money, but what about the remaining $700,000 you would need? You could not pay that out to your depositors except over a period of time — namely, the time that must elapse before the last borrower's note comes due. If you loaned some man $10,000 which will not be due until two years hence, the last of your depositors may have to wait for *two* years. (In this calculation no allowance was made for your own $100,000 of capital.)

* * *

What conclusion can be reached? There is almost never a *wholly liquid* bank in existence. Nevertheless, people expect banks to be liquid. And in normal times, under reasonably good management, banks are "liquid." But in abnormal times, the banks as a whole — the system of banks — have *always* been found not to be liquid enough.

Somebody must then come to the relief or rescue of the banks; a moratorium is openly declared; or the banks are temporarily actually closed down; or "temporary money" is created in the form of Clearing House Certificates; or a Central Bank is authorized to manufacture new money for the emergency (maybe without a burdensome charge, or maybe with it).

This not-adequate-liquidity of banks derives from two factors:

1. Checking accounts are on the basis of being able to withdraw money *on demand;* but the assets, into which a bank is under inducement to invest deposit money, are *not* equally convertible into cash *on demand;* and

2. This is aggravated by banks being authorized to loan as much as five times the gold they have deposited with their Federal Reserve Banks.

* * *

What causes a depression?

1. The demand of depositors to have their money so that you as a banker are obliged to reduce your loans for that reason. Your borrowers must then pinch in their operations. They are unable to operate on the scale that they have been operating.

2. The consequence of the foregoing is a change in the climate of thought, so that you as a banker want Andrews to pay back the $20,000 he borrowed in the form of a deposit credit; and your further reluctance to loan it out to anyone else right away. And so, the credit which you manufactured and which was at that time an artificially favorable factor increasing "demand" for products, has now become a grievously unfavorable factor reducing such demand. Once there was a boom, created by the creation of manufactured credit; now there is a depression correspondingly caused by the liquidation of manufactured credit.

Commodity Credit Versus Circulation Credit

If a person seeks to understand the effect of certain modern banking practices on the money situation, and consequently its effect on the business cycle, then it is necessary to distinguish between:

> 1. On the one hand, the credits (or loans) which a bank extends (a) *by using its own capital, or* (b) *by re-loaning money which depositors have put into the bank;* and
>
> 2. On the other hand, the credits (or loans) which a bank extends because it is in possession, according to United States Banking Law, *of the special privilege to loan five times as much as the amount of gold in the so-called Reserves which it has placed in the vaults of the local Federal Reserve Bank, under which it resorts.*

In other words, it is necessary to distinguish between: credits, that is, loans granted, which your bank makes out of the $500,000 of actual deposits, in our illustration in the foregoing article; and credits in the amount of $400,000 which are "manufactured" by the bank, as also explained in that article. All thinking about money and banking is confused unless these two kinds of credits or loans have different names and are carefully distinguished.

What does not have a name cannot be understood. An evil that does not have a name, cannot be fought against. If different types of loans have only one name as loans; if different types of money are never differentiated and are nothing more than money in general — then no thinking of money, banking, or the business cycle can be highly profitable. It is therefore necessary to distinguish between kinds of credit and between kinds of money. Only then can the cause of the business cycle be understood, and can the cause be removed, or at least reduced to proportions so that public policy is no longer dominated by terror that there will be a depression.

To distinguish between the two kinds of credit that we have described, which are fundamentally different, we shall employ the terminology of Ludwig von Mises, as given in his earliest book on money and credit, entitled *The Theory of Money and Credit* (Yale University Press, New Haven, Connecticut). Mises applies to those loans by banks, which consist of the use of their own capital and the deposits of customers, the term, *Commodity Credit;* and he applies to loans by banks, which consist in exercising their special privilege of manufacturing loans equal to five times their gold reserve, the term *Circulation Credit;* it is the *Five Times Privilege* which is the origin of Circulation Credit.

We quote Mises briefly:

> Credit transactions fall into two groups, the separation of which must form the starting point for every theory of credit and especially for every investigation into the connection between money and credit and into the influence of credit on the money prices of goods. On the one hand are those credit transactions which are characterized by the fact that they impose a sacrifice on that party who performs his part of the bargain before the other does — the foregoing of the immediate power of disposal over the exchanged good, . . . This sacrifice is balanced by a corresponding gain on the part of the other party to the contract, [who gets an] earlier disposal over the good acquired in exchange. (Page 264.)

The reason why Mises calls such loans a *commodity credit* is clear from his analysis, namely, the money used represents capital, and the *reality* of the transaction consists herein that the lender temporarily forgoes the use of his own capital so that another can use it temporarily. The capital that the borrower acquires is an offset to the capital which the lender relinquishes. In total there is no increase or decrease in disposal power over existing goods, merely a transfer. There is the reality of commodities behind this transaction, and consequently the term *commodity credit* is apropos.

Mises continues:

> The second group of credit transactions is characterized by the fact that in them the gain of the party who receives before he pays is balanced by no sacrifice on the part of the other party . . . In the kind of credit transactions [which have been designated as *commodity credits*] what is surrendered consists of money or goods, disposal over which is a source of satisfaction, and renunciation of which a source of dissatisfaction. In the credit transactions of the second group [which will be called *circulation credit*], the granter of the credit renounces for the time being the ownership of a sum of money, but this renunciation (given certain assumptions that in this case are justifiable) results for him in no reduction of satisfaction. (Pages 264 and 265.)

When the bank was loaning its own capital or part of its depositors' deposits which the depositors themselves were not actively using, the borrowers could become *substitute* buyers of goods but not really *new* buyers. But when the bank is also loaning what it "creates" because it has the *Five Times Privilege,* then all original owners who have power to buy will continue to do so, but the new borrowers are additional claimants for goods that exist. The loaner of the new purchasing power, namely, the bank, has not surrendered a legitimate existing purchasing power to the borrower; it has granted new purchasing power which did not exist before.

The real "villain" in the monetary and credit situation is *circulation credit*. In a sense, there is nothing new about that idea that circulation credit is the villain. The idea that it is a "villain" in more than one hundred years old. Critique, therefore, of circulation credit is not critique by a "money crank."

Peel's Bank Act In 1844 In Great Britain

In earlier articles in this issue attention has been given to those deposit credits which are based on the Five Times Principle. The reason for singling out deposit credits *of that kind* is because it is this type of deposit credits which is unsound but prevalent today in the United States and elsewhere.

By *deposit credits* we refer to the transaction by which a borrower goes to a bank for a loan, and although the bank has no money of its own to lend or unused depositors' money, it nevertheless makes the loan because it has the right to grant credits equal to five times its gold reserve. We have used the illustration of a man borrowing $20,000 by signing a note, and the banker posting on the borrower's passbook a credit of $20,000, against which the owner of the passbook could draw checks as long as the money lasted. Today such deposit credits are the principal device by which banks in the United States grant circulation credit.

In England, in the early part of the nineteenth century the device by which to accomplish the objective of circulation credit was different. The device then consisted of issuing *bank notes*, rather than posting a credit in a passbook. In those days the borrower might enter the bank, ask for a loan, be granted the loan although there were no funds there in a commodity credit sense; the banker would take the man's note for $20,000, and give him in place thereof a kind of money (in appearance like ordinary paper money), printed by the bank and known as *bank notes*. In those days, borrowing was principally conducted by means of such bank notes, rather than deposit credits and checks. The deposit-check system was, it is true, beginning to be developed at that time, but was of trifling importance compared with the bank note system. It will be obvious that bank notes and deposit credits are merely two different manifestations of one and the same thing, circulation credit.

In the early part of the nineteenth century the merits and demerits of *circulation credit* were actively debated. This great debate is known as the controversy between two schools of thought, one known as the Currency School and the other the Banking School. In this controversy the currency school was essentially right and it won out. It was able to get its views incorporated in that famous piece of banking legislation known as Peel's Bank Act, enacted by the Parliament of Great Britain in 1844. (The official name is Bank Charter Act.)

The enactment of Peel's Bank Act was an event of major significance in monetary history. The Act prohibited the further issuance in Great Britain of the then prominent type of circulation credit, namely *bank notes.*

What did Peel's Bank Act do and fail to do in regard to circulation credit (1) in the form of bank notes, and (2) in the form of deposit credit against which a customer could write checks?

The Act prohibited further increase of circulation credit in the form of bank notes. It froze the amount of bank notes already outstanding. It did not deflate the existing circulation credit in the form of notes by demanding their withdrawal. The mischief had already been done, and there would be acute problems, if the existing circulation credit in the form of bank notes would be reduced. But it banned *additional* circulation credit by the issuance of *more* bank notes.

Obviously a circulation credit in the form of a deposit credit against which the borrower can draw by writing checks, rather than by using bank notes, is just as much a circulation credit as bank notes. To have been consistent Peel's Bank Act should have prohibited an increase in circulation credit in the form of deposit credits just as definitely as it prohibited an increase in circulation credit in the form of bank notes. But Peel's Bank Act did nothing of the kind. It left the further increase of circulation credit in the form of deposit credits unrestricted. This was a glaring inconsistency and weakness in the Act.

The consequences were as follows:

1. The British banking and credit structure was relieved of a great weakness, the improper privilege of creating circulation credit by means of the issuance of additional bank notes.

2. Nevertheless, in order to grant and to obtain circulation credit, but in a different form from bank notes, the bankers and borrowers respectively turned to deposit credits as a substitute for

bank notes, because such deposit credits were not prohibited.

The evil of circulation credit in one form was arrested by Peel's Bank Act, but in another form was left unmolested. Naturally, the evil took the road which was still open to it and the increase in circulation credit was thereafter in the form of deposit credits.

Peel's Bank Act was therefore an Act of great strength, like as by a Sampson. But, like Sampson, it had a great weakness, which undid its strength.

The victory of the principles of the Currency School was not a decisive victory. It did not end the proper war against circulation credit. It was merely a successful battle on one front. An advocate of the Currency School who thought that the ban on further expansion of bank notes would end the expansion of circulation credit was a dangerous somnambulist in questions of money and banking. Having won the battle on one front of current importance, Peel's Bank Act proceeded to lose the battle on a front which at that time was of minor importance, but which was to become of overshadowing importance.

A Bank Law For The United States Patterned After The Famous Peel Bank Act

There are many "cranks" or "screwballs" in the world, on all kinds of subjects.

People who are critical of the established order in some way or other, are widely suspected of being cranks or screwballs. One way to dismiss the critique of such people is to sneer at them and "smear" them as cranks and screwballs. But the practice of "solving" problems by calling someone a crank or screwball requires discrimination, or else valid critique will be neglected.

The world has a goodly number of *money* cranks. One might be persuaded to believe that most of the people of the United States are today monetary cranks and screwballs, for various reasons, of which an important one consists in their favoring the continued issuance of more and more *circulation credit.*

If the game becomes one of name-calling, we, too, are as exposed as others are to being called money or credit cranks. What is our position?

We are against circulation credit, regardless whether it is in the form of bank notes or of deposit credits. We, therefore, favor for the United States the equivalent of the Peel Bank Act, that is, a modernized version for this country of the real import of the Peel Bank Act in Great Britain 111 years ago. To accomplish that end, we would be pleased if a law were passed which:

1. Froze existing *circulation credit* in the United States, whether in the form of bank notes or deposit credits, at the present level, and prohibited any *further extension* of either form of circulation credit (except with temporary exceptions recorded in number 2).

2. We would make this exception, namely, we would first compute the *average increase* in circulation credit in the latest two years, and then we would permit:

   a. An increase of circulation credit of 85% of that average in the first year following;
   b. 65%, in the second year;
   c. 40%, in the third year; and
   d. 15%, in the fourth year.
   e. But thereafter none: the "freeze" would be absolute, and presumably in perpetuity.

In other words, we would "shock absorb" the proposed cessation of the issuance of circulation credit over a four-year period. (See the next article.)

Is this proposal a "screwball" proposal? Not unless the basic idea underlying Peel's Bank Act is basically a "screwball" idea. Peel's Bank Act, however, is a highly respected piece of monetary legislation. What is here being done is no more than applying to the American banking situation presently what the Peel Bank Act applied to the British situation more than a century ago (although it is admitted that the Peel Act was partially ineffective, because it was not *foresighted* in seeing that *deposit credits* were potentially of far greater importance as forms of undesirable circulation credit than bank notes).

In one respect, the proposal here made is more compromising than Peel's Bank Act, namely, in the paragraph numbered 2 there is a suggestion to permit the issuance of *additional* circulating credit, but in rapidly decreasing amounts. This is, maybe, a dangerous suggestion, but it is submitted for consideration.

An Endeavor To Escape The Moral Law

The world is full of people who think that they can escape the consequences of the "moral law." Maybe suggestion number 2 in the preceding article is a case in point.

Moses taught differently. He said, "Your sins will find you out." Or, in other words, you can *never* escape the consequences of your sins (which are always follies) but will experience them in one form *or another*. You may be clever enough to escape the obvious and usual penalty, but a penalty will show up sooner or later in another form. You cannot "beat the game."

There is also a tendency to be complacent about violating the moral law, because we know there is often a *time lag* of the penalty, considerably after the deed. It is fundamental in human psychology to *discount* future good and future evil. One of the most profound ideas in modern economics is the so-called "discounting of the future." You can safely offer a man $1,000,000 a thousand years from now. It is valueless to him, because he will not be here to collect it. It is quite different if you put your hand in your pocket and give him $100 *now*. One hundred dollars today is worth much more to him than $1,000,000 a thousand years from now. There is, therefore, always a "discounting" of the future. Similarly, the consequences of sin are discounted depending on how far the consequences of those sins are estimated to be in the future.

If a man believes that smoking will cause his death tomorrow unless he desists from smoking at once, he will not smoke at all until the danger is passed. But the same man may be almost indifferent about certainly dying, at some unknown date in the vague future, because of his smoking.

This idea of discounting the future, which is so important an idea in modern economics, is an old idea in Scripture. Solomon long ago wrote:

> Because sentence against an evil work is not executed speedily, therefore the heart of the sons of men is fully set in them to do evil. Ecclesiastes 8:11.

The expression sounds somewhat archaic in modern ears, but the idea is that, if the penalty for violating the rules that make social life advantageous were instantaneous, there would soon be very little of such violation, but (unfortunately or fortunately?) the penalties are delayed, and so, because men discount future penalties as well as future pleasures, men are pretty bad today and now; they "discount" the future retribution.

Now, although most of us know what Moses and Solomon taught, and which experience reveals every day to observant people, nevertheless we are beguiled by the idea that we may be able to cheat the moral law of its consequences. We cannot resist the temptation to be unrealistic.

And so, we are tentatively proposing some temporary wrong-doing, in the form of *additional* circulation credits: 85% of the recent average, for the first year; then 65%; then 40%; then 15%; but thereafter no more such wrong-doing.

And what is our justification for this, in principle, malpractice? We think that the *gradual* progress from evil to good, from dishonesty to honesty, will reduce the consequences, that is, in this case will reduce the shock to prosperity, much more than if we cut off monetary folly abruptly.

This country cannot genuinely escape the consequences of having been putting out more and more circulation credit over many years. Everything is "geared" to continuing that malpractice. (We may be able to develop this important idea at a later date.) Some people are actually prospering by that malpractice, because they understand the game that is being played. But change the rules of the game, and then the players will change their policies at a rate dependent on their astuteness. There will be turmoil, confusion, faltering, miscalculation — *and a depression* of some kind. The reaction to that will be bad, because people will feel justified in being deterred from reforming, because the transition from evil to good is painful, and has some penalties which appear to come from becoming good, but which are really the *belated* consequences of the earlier evil.

The United States will *not* be able to make the transition from the dishonesty of circulation credit to the honesty of a stable and sound money supply without serious transition difficulties.

And so, hopefully and optimistically, but against better judgment, we propose a *gradual* adjustment to the discontinuance of putting out circulation credit. We are proposing giving men four years in which to adjust.

The Quick, Abortive End Of A Sound Eisenhower Credit Policy

In the United States the Democrats were in control of the administration from 1932 to 1952 — for twenty years. The Democrats do not have the best record in regard to favoring sound money policies.

Eisenhower, when he came into office in 1953 was the first Republican president in twenty years. It is implied in the nature of the case that a party out of power is critical of what the party in power is doing. And so Eisenhower was elected on a "sounder" or less-unsound money policy than the Democrats had been following.

The policy originally adopted by the Eisenhower administration was not a completely sound policy, to wit, an announced, fixed policy *of no further extension of circulation credit at all,* but rather a slowing up of the extension of circulation credit.

Eisenhower appointed an experienced business man as Secretary of the Treasury, and as Assistant Secretary appointed a veteran banker, who undoubtedly realized fully the ultimate consequences of a continuation, without a terminal point, of the issuing of more and more circulation credit. The technical steps necessary to slow down and end the issuance of more and more circulation credit are outside the bounds of this discussion, but those technical steps were promptly and effectively applied by competent people in the new administration.

In essence, the policy was nothing more than bringing to an end the persistent increase in circulation credit which the Democrats had fostered, or at least tolerated. Here was a new administration moving away from monetary malpractice and dishonesty. The consequences should *immediately* have been *salutary.*

But the actual *early* consequences appeared to be just the contrary. The steady business blood transfusions of new money in the form of circulation credit no longer being forthcoming, the "patient" began to feel distressed and ill. The "money market" (that is, the *loan money* market) tightened at once. All plans of business men had for long been basically adjusted to continuing monetary blood transfusions. The economic leaders were *accustomed* to count on more and more circulation credit. Those expectations were deeply incorporated in all their plans. Now that expectation was not being fulfilled, and funds were not available to complete plans already "in the works"; and funds were still less available for initiating new programs which could only be executed on the assumption of a continued increase in circulation credit.

The New York Stock Exchange is the greatest *market* in the history of mankind. It is the meeting place of smart money and also of not-so-smart money. Astute buyers and sellers on the New York stock market immediately sensed the significance of the new financial policy of the Republican administration, and they discontinued buying and began selling, realizing that there would be deflationary consequences merely from no longer issuing additional circulation credit. By March the stock market was in full retreat. By April the alarm had spread widely to business. An anxious hue and cry began to come from the newspapers. There was fear of a severe depression with unemployment and distress.

Pressure on the very new admintsration to change its policy was steadily increased. By mid-May its fortitude was gone and it began to abandon its program. It has since that time never endeavored unfalteringly to reinstate it.

It was imprudent to adopt the policy of discontinuing the issuance of more circulation credit *without pre-advising everybody thoroughly about the immediate consequences which would be disturbing, and the long-term consequences which would be salutary.* If the administration had

(1) Explained its own policy, and the reason for it;
(2) Warned of the need of everybody rationally to adjust their own policies accordingly;
(3) Forecast, without evidence of anxiety, the disturbing *short-term effects;* and
(4) Assured, with confidence born of knowledge of economic law and moral law, that the *longer-term* consequences would be helpful to everybody, especially the "common man",

then public opinion would probably have supported the continuation of the new policy over the transition period long enough so that the eventual favorable results would have mustered public opinion solidly behind it. On all the foregoing counts, those who had an improved policy in mind failed to operate as *political* leaders who know how to reassure their followers and retain their active support.

The initial program of the monetary leaders in the early days of the Eisenhower administration was not so definite nor inflexible as the program herein proposed. The financial policy in the early months of 1953 was the policy of a few men who "knew the score." It was not the policy of a whole party of well-informed citizens. It was not a policy which was proposed to be incorporated in statutory law, but merely a sound policy operated by a few individuals. To get a law passed making the policy the official and relatively permanent law of the land would have required a declaration of the policy, explanations of it, public discussion of it, and all the other requisites that go along with a sound government based on popular suffrage.

It is not possible for a few, well-informed men to set the monetary course of the United States soundly and keep it that way. They require the support of public opinion behind their program.

The program in 1953, although good as far as it went, was defective in being merely the program of experts unsupported by educational efforts and popular opinion, and deficient in not being incorporated in legislative law which would positively end the issuance of more circulation credit, as Peel's Bank Act ended the issuance of additional bank notes.

Nor is the evidence conclusive that the directors of the early Eisenhower administration financial program were *completely* convinced about *all* the objections to *additional* circulation credit. They may only have been opposed to the *too-rapid* issuance of additional circulation credit rather than the complete cessation of the issuance of additional circulation credit.

It is regrettable that the noble attempt in 1953 was abortive — because not clearly enough enunciated, not adequately justified to the public, not accomplishable because of a lack of supporting public opinion, and not definitely stabilized by being incorporated in statutory law.

Four Things Morally The Same - Circulation Credit, Fictitious Bills, Counterfeit Money, And Theft

Four different terms can be used for what, *in principle,* is the same thing:

1. Circulation credit
2. Fictitious bills
3. Counterfeit money
4. Theft

1. *Circulation credit* is the term selected by Mises. Mises hints that his term may not be ideal. As a term, it is weakest in the foregoing list. It definitely fails to indicate the moral turpitude of circulation credit. The term, theft, by its connotation, expresses an adverse moral judgment. Circulation credit, as a term, fails completely to indicate that there is theft involved.

2. A better term is *Fictitious bills.* This is the term that Henry Thornton accepted from popular usage to designate bills which merchants put out without the transaction being a response to a real transaction in commodities. (See Volume V, number 5, pages 144f. Further details on what Thornton writes about fictitious bills may be presented later. See page 87 in his book.) These fictitious bills were as much theft as circulation credit is theft. Whereas the term, *circulation credit,* does not warn a user that it refers to something evil, the word *fictitious* in Fictitious Bills performs that function fairly well, but not perfectly. *Fictitious* can mean that something is no worse than fancy or imagination; it does not necessarily mean that something is dishonest. What is needed is a vigorous term that unmistakably indicates moral turpitude.

3. *Counterfeit money* is a term that pretty much has a meaning which designates that moral turpitude is involved in putting it out and using it deliberately. *Counterfeit* is not a neutral nor a mild term. Still, it is vague in a sense in the minds of many people, because it does not indicate specifically in what the turpitude exists.

4. *Theft* is a wholly unequivocal term. Nearly everybody accepts it as being wrong. Circulation credit, fictitious bills and counterfeit money are all forms of theft. Circulation credit is legalized, and is by most people considered to be a source of prosperity, or a necessary prop to prosperity. Fictitious bills have been defended as a great aid in supplying the "necessary" funds with which to do business. Some of the most respectable people in the world have defended (or do defend) circulation credit and fictitious bills. But counterfeit money is generally condemned.

We shall use the four terms interchangeably whenever we refer to the *theft* which is accomplished by issuing circulation credit in one form or another. A man is a thief when he thieves from others. He is also a thief if he accepts in exchange from others goods which represent real value, but gives in return something counterfeit in the sense that it does not represent his having performed a reciprocal act of providing real goods or services.

Maybe the best term to replace *circulation credit* would be *counterfeit credit. Circulation credit* is to *commodity credit* what counterfeit money is to real money. It appears justified to use the term *counterfeit credit* in place of *circulation credit.*

Morally, there is no difference between circulation credit (which is installed in the monetary and banking structure of the United States as if it were honorable and desirable) and counterfeit bills or coins. Because circulation credit is not *open and obvious* theft, because of the lack of understanding of it by most people, and because they do not openly resist it, its consequences are indirect, and its penalties are not understood. Its penalties, by the way, show up in the form of booms and depressions, and not in jail sentences.

In the elementary and fundamental categories of the Decalogue of Moses, circulation credit and fictitious bills and counterfeit money are all forms of theft, and are forbidden.

★ ★ ★

"Of all the contrivances for cheating the laboring classes of mankind, none has been more effective than that which deludes them with paper money."

—Daniel Webster

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FIRST PRINCIPLES
IN MORALITY AND ECONOMICS
on which depend personal well-being and social health and harmony

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Inflationism Designed To Help The Poor Really Helps The Rich

The late J. Laurence Laughlin, at one time professor at the University of Chicago, wrote a book *The Principles of Money* (Charles Scribner's Sons, New York, 1921) which is of considerable interest as monetary history. On pages 43-4 he asked:

But who compose the debtor class?

To that question his answer was:

> Large capitalists . . . have . . . obligations . . . in excess of their . . . capital. Merchants are constantly doing business . . . far beyond their own capital. They borrow . . . and create the greater proportion of general indebtedness. The largest part of the obligations of a country, so far as amounts are concerned, necessarily arises from those who engage in the more extensive transactions. . . . A poor man may be in debt, but the total [debts] of the poorer class is but a fraction of the obligations of a few large institutions, and legislation giving preference to debtors will serve the poor man infinitely less than it does the large producer.

Many of the people of the United States today favor inflationary policies: (1) they have abandoned the gold standard, whereas it is only by having an inert metal standard that inflation of prices can be prevented; (2) they have legislated to authorize *circulation credit,* which raises prices; (3) they are, in general, complacent or semi-complacent about increases in government debts; and (4) they think that by inflation they are filching the rich and helping themselves.

But in regard to number (4), as Laughlin indicates, they are deceiving themselves, and doing just the opposite of what they intend; they are indeed following policies contrary to purpose. In the process, presumably of helping themselves (and hurting others), they are really hurting themselves.

Inflationism is basically wrong because it is theft. It is not justified for the purpose of enriching the poor (which means injuring the rich); nor is it justified for the purpose of further enriching the rich (which means injuring the poor). Inflationism is *always* wrong.

The poor man usually saves in the form of insurance, savings accounts, purchases of bonds or of mortgages. Where does all this money go? To finance the big *debtors.* The *poor* man, through these institutions of insurance etc., becomes a creditor. Big corporations are almost always big debtors. A few, large modern corporations have no debts and apparently pride themselves in

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that. Their pride is misplaced. The managements of these companies are "living in the past."

Latterly, as a semi-conscious defense against inflationism, many poor people (usually *young,* because the young are naturally poor, not having had time to accumulate capital) have taken to buying a residence for themselves *on time,* rather than renting. This is significant, but is relatively not yet of great importance in the general situation. Big corporations are pursuing the same policy even more strongly; they are steadily doing more and more of their financing *by means of borrowing,* rather than by stock financing, which is known as "equity financing." There are limits beyond which a corporation should not borrow. Many corporations are pressing against those limits.

The *tax* laws of the United States also encourage corporations to borrow rather than to seek money from stockholders. If a corporation finances by means of 5% preferred stock, it must earn more than 10% on that money in order to benefit the stockholders by this expansion. The reason is that the Federal Corporation Income tax rate is 52%. But a 5% debenture or bond (that is, borrowed money) is profitable to stockholders whenever the use of such funds yields to the corporation more than the 5%.

Two Public Evils In The United States — Bad Laws Governing Unions And Banks

Two of the bigger evils in the United States today are: (1) unions, as they operate; and (2) banks, as they operate; or better said, two of the bigger evils in the United States are the laws giving unions and banks special privileges.

Bad laws permit union members to do what an ordinary private individual would be sued for doing or for which he could be thrown into jail. This is aggravated by a lax enforcement of laws in those cases where the law still protects partially against unionism. The consequence is that unionism is rife with gangsterism, of a mild or virulent type. Unionism itself does not make men bad; it is the bad laws giving special privileges to unions which make bad men of union leaders and members.

The bad bank situation is equally because of bad laws, which permit banks to put out *circulation credit,* that is, a "counterfeit" credit, up to five times the amount of gold reserves which the bank has deposited with its Federal Reserve Bank. The law authorizes bankers to manufacture "money." Exactly as in the case of the unions, the trouble is not the absence of "law," but the existence of a law permitting a "special privilege."

We do not need any new laws prohibiting union violence. All that we need to do is to rescind laws which in actual practice permit union violence. Similarly, we do not need a law to prohibit banks from putting out circulation credit. All that we need to do is to rescind the law which permits banks to do that. Repeal the present bad laws! Do not pile law on law!

There are certain *elementary* laws for society. Two of these are (1) the law against violence and (2) the law against theft. The laws pertaining to unions are bad because they do not prohibit union violence, but grant opportunities for violence to be perpetrated with impunity. The banking laws are bad because they do not prohibit banks from perpetrating theft in the form of circulation credit, but deliberately authorize it.

The laws on unions violate the Sixth Commandment, Thou shalt not coerce (kill).

The laws on banking violate the Eighth Commandment, Thou shalt not steal.

A return in *public* law to the elementary Ten Commandments will greatly benefit society.

Menger On "The Nature And Origin Of Money"

Carl Menger (1840-1921), the Austrian economist, was the fountainhead of that great "revolution" in economics which resulted from the formulation of the proposition that *value* does not ultimately derive from the factor of supply but from the factor of demand. *Costs* (a supply factor) do not in an originary sense determine value, but *utility* (a demand factor) does.

The old slogan that price is determined by "supply and demand" only finally obtained real meaning when Menger and his associates (and others) developed the idea of *marginal utility.* In his book *Principles of Economics* (The Free Press, Glencoe, Illinois, 1950), in Chapter VIII on "The Theory of Money," Menger presents his simple and convincing explanation of the origin of money. (Menger's writings generally have the characteristics of simplicity and cogency.)

He begins by referring to the discovery, by people, of the advantages of division of labor. But division of labor entailed exchange of the product which each specialist produced. The first exchanges, he notes, must have been barter, and were based on *use value.* He wrote:

> . . . economizing individuals have goods in their possession that have a smaller use value to them than goods in the possession of other economizing individuals who value the same goods in reverse fashion.

He cites the case of *A* having a sword of smaller use value to himself than a plough owned by *B,* but that for *B* the use value of the sword is greater than of the plough he owns — and so an exchange can and will be made (page 258).

Menger then expands on the idea that although *A* wishes to exchange his sword for something else, that *B* usually does not have exactly what *A* wants. The consequence is that no deal can be made.

The next step then, according to Menger, is that each man, who wishes to exchange whatever he has in surplus or no longer needs but who cannot by barter get specifically what he wants, will attempt to make a trade to get something that has *greater marketability than his own commodity.* A sword or a copper armour may be less marketable or less exchangeable than a cow or cattle. And so a man might *as his first move* sell his sword or armour for one or more head of cattle even though he has no direct use for the cattle. Then he might exchange his cattle for something still more in general demand, and consequently still more exchangeable. Menger wrote (his italics):

> As each economizing individual becomes increasingly more aware of his economic interest, he is led by this *interest, without any agreement, without legislative compulsion, and even without regard to the public interest,* to give his commodities in exchange for other, more saleable, commodities, even if he does not need them for any immediate consumption purpose. With economic progress, therefore, we can everywhere observe the phenomenon of a certain number of goods, especially those that are most easily saleable at a given time and place, becoming, under the powerful influence of *custom,* acceptable to everyone in trade, and thus capable of being given in exchange for any other commodity. [Page 260.]

Money, therefore, *does not find its origin in legislation,* but in what Menger calls *custom.* The everyday decisions of ordinary men make money to be money, and not the stamp of a government. The German Weimar Republic, which was socialistic in character, stamped pieces of paper as being of 1 mark, 10 marks, 100 marks, 1000 marks, or more, but such paper became worthless. A government can neither create nor sustain the value of the money within its borders *by legislation or decree.* The decisions of individual citizens determine the value of money.

Finally, the commodity which was found to be "more exchangeable" than all others was gold. That is why gold is the foundation of the monies in the world, whether or not a particular government recognizes that.

The reason why gold is "most exchangeable" is because it has the characteristics of "portability, indestructibility, homogeneity, divisibility and cognizability" as Laughlin wrote (page 41), but far more importantly, (1) because it possesses the quality of *not being manufacturable or augmentable (greatly) in supply,* and (2) because it already had and retains a value independent of its utility for monetary purposes; (gold always will retain some value in the arts and for decorative purposes).

The worst kind of money is money supposedly "sustained" by, or even influenced by, a legislature, or the director of a central bank, or a dictator. For something to be money requires that it be beyond the arts of an alchemist with chemicals and mystic rites, and beyond the arts of a monetary expert of any kind or calibre, who has a printing press, or its equivalent, at his disposal.

Roscher, On False Theories Of Money

Schumpeter in his book, *History of Economic Analysis* (Oxford University Press, New York, 1954) wrote (on page 699):

> Roscher expressed dominant opinion when he said that the false theories of money may be divided into two groups: those that hold that money is more, and those that hold that money is less, than the most salable commodity.

Money, in a *general* sense, is simply that which is the *most exchangeable item.* There are, it should be noted, various kinds of money. The problem pertains partly to variations in the total quantity of money, and partly to the fact that there are different kinds.

A Note On Menger And The Other Austrians, As The Best Primary Source Of Economic Information

As admirable an *introduction* to economics of any treatise known to us is Menger's *Principles of Economics.* That is preferable compared to beginning by reading the classic writings of Adam Smith or David Ricardo. The major conclusions of these men have been so drastically revised by the work of the Austrians (Menger, Böhm-Bawerk, Wieser, Mises) that it is confusing, and also a serious error in method — wholly anachronistic — to begin with the outdated English classicists. After a reader has gained a sound base from the Austrians, then the works of the old English classicists, which deserve imperishable renown, can be read with great profit — but they will then be read discriminatingly. As Böhm-Bawerk wrote:

> The most important and most famous doctrines of the classical economists are either no longer tenable at all, or are tenable only after essential alterations and additions. [From his article on "The Austrian Economists" in the *Annals of the American Academy of Political and Social Science*, January 1891.]

* * *

This applies to the difficult subject of money, too. Even Menger, as late as 1892 wrote:

> The enigmatic phenomenon of money is even at this day without an explanation that satisfies; nor is there yet agreement on the most fundamental questions of its nature and functions. Even at this day we have no satisfactory theory of money. [Quoted by Laughlin, page 225.]

Menger is comparatively recent in economic history. But "much water has gone under the bridge" even since Menger's time, and there is today a "satisfactory money theory." But the trouble is that people do not like it, because that satisfactory theory is based on the premise that theft is wrong.

To rely on the old economists in regard to money matters is like relying on a Galileo in the age of an Einstein.

The Profit Problem Of Banks

In the previous issue a simplified illustration was employed to show that there are problems to be solved before a bank can make a profit. The contribution which the privilege of putting out *circulation credit* together with the exercise of the privilege can make to profits was also demonstrated in a schematic way. Then it was proposed that a law (patterned on the famous British law on banking, officially known as the Bank Charter Act of 1844, but also known by the name of the British Prime Minister who put it through, as Peel's Bank Act) be passed which would prohibit the banks in the United States from putting out any *additional* circulation credit.

That proposal might be opposed on the ground that there will be a serious consequence in the form of a loss of legitimate bank profits. Will the banks be injured seriously or dangerously by losing their privilege to issue circulation credit? Or will the banking industry easily and quickly adjust?

Fortunately, the banking business in this country is genuinely competitive. A bank managed with average efficiency will earn an average return on its net worth; if managed with less than average efficiency, the return on net worth will be less than average and may disappear entirely; and vice versa, unusual efficiency will result in extraordinary profits.

If the banking business on the average were more profitable than other businesses, that fact would quickly be noted by shrewd men, and they would enter the banking business in order to participate. But before long there would be so many in the banking business that the profits would decline to the average for all industries (or temporarily maybe even to less than average).

Banks in the United States possess a special privilege, which in the preceding issue we called the *Five Times Principle,* and which consists in being permitted to loan about *five* times as much as the bank has reserves of gold on deposit with its regional Federal Reserve Bank. This privilege gives the banks a special opportunity for profit. That was shown by assuming a bank would be organized with $100,000 of capital, of which $80,000 would be put into gold. The bank could loan as much as $400,000 on that gold reserve of $80,000. With an interest rate of 5% the gross income of the bank on the $400,000 would be $20,000. This gross income relative to the $100,000 of capital is attractive; it is 20% of the principal.

However, this special source of profit — from issuing circulation credit — has long ago been distributed or "dissipated" to others by the banks in various ways, and it is a misconception to think that bank stockholders obtain *in total* a better than average return on their investment.

The ultimate *origin* of the special source of profit for the banks (i.e., to issue circulation credit) is the banking law of the land. Nobody other than bankers may put out five times as much credit — which credit gives purchasing power, and which is equivalent to money — as they have gold reserves. A banker obtains this privilege at a heavy price, namely, he must submit to detailed government regulation. In fact, as an individual, no one is permitted to own gold; the law of the land provides a heavy penalty for violation of that prohibition.

Although banks have a special privilege (in principle, privileges granted by law are suspect and almost always bad), they are not able to continue to "cash in" on that. The reason for this is that there is free entry into the banking business, provided one abides by the rules and regulations laid down by the government. In order to take advantage of the special privileges, *so many people have gone into the banking business that the special advantages have been transferred to customers.*

Mr. *A*, who hitherto may not have been a banker, may observe that Mr. *B*, who is already a banker, is very prosperous. *A* may then enter the banking business, too. Both may continue to be prosperous. Then *C* and *D* may enter the banking business, but let us assume that the community did not need four banks. *C* and *D* then do not prosper as bankers. The bulk of the banking business may be retained by *B* and *A*. The interest rate in the community has been in the past, let us say, 5% on commercial loans. In order to get more business, *C* and *D* may reduce the interest rate to 4%. That reduction in the rate will reduce the gross income from loans by one-fifth, or 20%. The cream is now "off" the business. If *C* and *D* continue dissatisfied with their share of the business, they may even drop their interest rate to 3%. A 3% rate means a 40% reduction in gross income from the 5% originally prevailing. Customers will leave the banks of *A* and of *B*, unless they also reduce their rate to 3%. Competition will continue to operate so that the *special advantages* derived from the privilege of issuing circulation credit, given by the government, *will be diffused to the customers of the bank* in the form of lower interest rates than would otherwise prevail. Eventually, the owners of the bank will retain not the slightest residue of special advantage from their special privilege. Their customers will reap the full harvest, and competition will have done it. (The foregoing pertains to a temporary situation in which competitive banks are trying to take business from each other. The eventual interest rate depends on other factors.)

If it is now proposed to take away from the banks the special privilege which in itself was originally profitable, the banks will *temporarily* earn a less than average rate of return on their investment. If they have charged customers too little for the various other services they perform (because they had been making an extra profit on their Five Times Principle), then they will be obliged, when their special privilege is taken away from them, to increase their charges for those other services that they perform, and put them where they belong.

Bankers will probably be disposed to fight for retention of their Five Times Principle, because it is natural for people to wish to retain what they possess. But bankers do not really need the Five Times Principle in order to be prosperous.

Six Different Approaches To The Problem Of Money

The "money problem" ought to be approached as a *money problem only,* and not as something that should be decided, or even be influenced, by any secondary or collateral interest. The money problem should never be determined on some basis such as efficiency, national interest, full employment or price stability. To inject these other factors into the attempted solution results in a genuine degeneration of the solution, whatever it may be.

The following disturbing, non-germane considerations have bedeviled the pure money problem:

Considerations of:	The Special Interest Involved
1. Profitability	"Efficiency" in the use of money, to enhance the profitableness of the *banks,* and to lower the overall cost of money for society.
2. Liquidity	The needs and wishes of *depositors* to have access to their money *on demand.*
3. International Exchange	Control of the inflow and outflow of gold and of goods, for *national* reasons.
4. Full Employment	The apprehension of *employes,* and the *mass of people* in a country, about unemployment.

5. Price Stability — The wishes of *politicians, bureaucrats, business men and others* that prices do not decline.

Finally, there is an unadulterated, single interest which will be called

6. The Pure money problem, — which has one and only one consideration in mind, namely, honesty in the medium of exchange, or Thou shalt not steal. This consideration is not special nor for any class, but is for *all men.*

Problems of money, as has been noted before, are as difficult as any in economics, or, as some would say, as any problem in matters of human action or human behavior. The most unsettled economic controversies among experts, and the most serious anxieties among the mass of mankind, pertain to questions of money. The problem must seem to nearly all to be intolerably complex and to be something that we have to live with, without being able to understand it.

To endeavor to simplify the money problem it is proposed that purposes, class goals and all considerations *except honesty* be removed from it. Modern society "lives" by exchange. Money is used in modern society in nearly every exchange. The media for exchange is money of some sort. If money is not "honest" almost no single transaction between men can be honest, because if the media has been corrupted then there will be a taint to the transaction itself, despite honest intentions of the participants.

It is planned to strip away the considerations which have caused the wrong solutions to be found to the money problem.

The sequence that will be followed in this endeavor is:

1. The harmful effects of letting the ideal of "efficiency" of money unduly influence the attempted solution of the money problem;

2. The unsettling and morale-destroying consequences of tampering with the money situation, by deceiving ourselves that we have money available on demand which is not really available on demand. In regard to money, we want it to be both "fish and fowl" at the same time; to be *liquid* and to be *earning* at one and

the same time. In this matter, men want to "keep their cake" but "eat it" at the same time.

3. The inevitable injury to society that will result from a specific *so-called* full employment policy. Everybody, without exception, is of course *for* full employment, but reference is here made to what is a *synthetic* full employment policy, which is not to be tolerated if honesty is the criterion.

4. The special and dangerous influence of politicians, bureaucrats and industrialists in favoring certain monetary programs designed to avoid price declines, and tampering with money for that purpose.

5. Next, a nationalistic and sometimes chauvinistic interest, concerning itself about the importation or exportation of gold, and the related problem of the importation or exportation of goods, of national self-sufficiency and national defense, and of the impact on foreign nations of a domestic money policy. The motivation usually has been one of enmity — to hurt the foreigner rather than to help the self.

6. Finally, there is left what is here designated as the *pure problem of money,* and consideration is given to what should be done to attend to that problem as is best possible.

Probably the thought should be expressed that there is no single, *perfect* solution available (at least to the writer's knowledge) for the money problem. But there is certainly a very tolerable solution that can give men peace of mind. That solution is to be *honest* in regard to problems of money.

The five factors mentioned in the foregoing which are intended to be stripped away from the basic problem, thereby to assist in the finding of the most desirable solution, are not completely distinct. They are intermingled in a disconcerting manner.

Consideration will first be given to the "complexifying" effects of letting considerations of *money efficiency* affect the money situation in a dominating manner.

"Efficiency" In The Use Of Money — By A Banker, And By His Defalcating Teller

Maybe excessive attention to the idea of *efficiency* in the use of money has done as much damage to monetary theory and monetary practice as any other factor.

In the example presented in the previous issue (page 234) depositors put $500,000 into your bank, into checking accounts.

You discovered that some of this money was always "idle," resting in one or another of the depositors' accounts. The arbitrary figure used in the illustration was $300,000.

And what did you as banker do? You said to yourself, "That money is *always* there. It is never removed. It is *idle*. I will put it to work by loaning it to *A* and *B* and *C*, etc."

Your argument was one of "money efficiency." The proposition was that money should not be "idle." Admittedly, you will "profit" from the use of that money; and you justify *your* taking that profit *for yourself* originally (although eventually you cannot retain it), on the ground of efficiency, namely, money ought to be employed to the maximum; this money is not being used; therefore, you will put it to work.

The law of the land has sanctioned that *efficiency argument*. You as a banker are permitted to loan to third parties your depositors' money. There are certain restrictions which are imposed upon you to reduce the hazard of the operation, but the privilege exists and is assiduously exercised by bankers.

Suppose that you have a big bank and many tellers. Suppose one of your tellers discovers that the account of a certain depositor always carries large balances, but that the owner apparently does not check his exact balance situation except at long intervals and maybe almost never. He probably has, for many years, found the bank to be more correct than his own additions and subtractions on his checkbook stubs. And so your teller takes out $10,000 of unused funds.

If you as owner of the bank may use — loan out — unused funds of depositors, why should not this poor teller put $10,000 to work to buy a house for himself? Suppose he does buy a house, and uses the defalcated $10,000 for the downpayment, and suppose that he has a firm intention to repay. He may say to himself: "I will work and save and pay off $2,000 a year. My relatives will contribute several thousand dollars to the house. I will eventually repay the whole sum. I am only temporarily using *unused money*."

But if the bank's own auditor or if the public bank examiner discovers what has happened, the poor teller will go to jail for having tried to be *efficient* in the use of money.

There is something wrong with any law that says a banker may loan unused funds but that his teller may not. Of course, the two cases are not exactly parallel, but the principle of using unused depositors' funds is parallel.

The Conflict Between Efficiency In The Use Of Money And The Demand For Money

The term, *demand for money,* has been defined previously (page 178, Volume V, Number 6), but the term continues to be elusive to most people and to have several meanings. Two common meanings should be contrasted.

The real *demand for money* does not consist in the demand to have money for the transaction of regular purchases. If *that* meaning is accepted, then demand for money is merely a disguised and indirect demand for goods. Your demand is not a demand *for money,* but for the things you wish to buy and consume or in which you wish to invest.

The *real* demand for money consists in the demand you have for a *store of money,* or a *stock* of money on which you can rely in emergencies, and which you need in order not to be embarrassed financially in your regular transactions. Your demand for money is evidenced by the money that you carefully *keep on hand* in one form or another, maybe in the form of cash in pocket, or amounts in checking accounts.

There is a "conflict" between (1) this latter concept of *demand for money,* which is the true concept and (2) the idea of *efficiency in the use of money in the form of loaning unused checking balances to borrowers.* What real sense can there be in your having a protective stock of money in a checking account at your bank (which evidences your *demand for money*), and which is really your stock or your *reserve* that your judgment tells you that you need, but your banker proceeds to loan what you consider to be necessary cash for yourself to a borrower who will not be able to repay, say, in less than 60 or 90 days, or a half year, or a year, or even longer?

The banker may be "efficient" in using your "idle" funds in his bank, but *he has genuinely undermined your cash position.* His hope is that if you suddenly demand your money somebody else will put in a comparable amount.

The phenomenon, *demand for money,* really does not tolerate a banker loaning out any part of the funds of depositors *on time.* The reason is that the depositors understand that they can get their deposit money *on demand,* but their banker has loaned out the money *on time.* There is here an innate contradiction.

How The Zeal For Efficiency In The Use Of Money Manifests Itself In The Way That The Seasonal Demand For Money Is Taken Care Of

The demand for money (in the economic sense, as defined) varies not only by persons but also for the same person. He will deliberately increase his money on hand to anticipate extra needs, and reduce his money on hand when he anticipates less-than-usual needs. These variations do not all offset each other, and so there is a variable *seasonal* demand for money. It is higher at the ends of months, than between month ends; it is even higher at quarterly dates. It is exceptionally high at year ends.

One way to take care of the high seasonal demand for money is for a merchant to carry the whole year long a balance in his checking account big enough for his maximum demand for money in the fall, or whenever his maximum demand will occur. But that means a kind of "inefficiency." He will have "idle" funds for a large part of the year. To have "idle" funds means to suffer the loss of interest that might be earned on those funds. Business considers itself too competitive to tolerate that waste or "inefficiency." Businesses, therefore, have often become accustomed to having a *demand for money* in the economic sense which is no more than their demand in their lowest season. What they need above that in their busy seasons they obtain by borrowing for short periods, maybe only a few months, from the banks. Bank loans regularly increase in the fall, because of that phenomenon. The *loan money* market (*ceteris paribus*) always tightens up beginning in September and continues into January.

How do the banks meet the situation? Elaborate financial machinery has been developed to enable the banks to make greater loans *seasonally.* The reason for this elaborate organization is "efficiency" or "economy" in the use of money.

It is in times especially of high seasonal demands for loan money that what we have called the *Five Times Principle* comes into play in order to provide funds. Furthermore, the Federal Reserve Banking system in the United States is especially designed to take care of the seasonal needs of business. A prime device, ordinarily not easily understood, in such situations is for the Reserve Banks to increase their holding of government bonds by purchases. They pay out money for the bonds to commercial banks and their customers and that money takes care of the seasonal needs of business. When the seasonal needs for money of business are diminished then the Reserve Banks re-sell the bonds and receive back the extra money which they had pumped into the money supply. The details of this are irrelevant at this time.

The fundamental fact is this: the banking system which we have is authorized to manufacture *circulation credit* (see preceding issue, page 243ff.) to take care of peak seasonal needs for money. Then, as the seasonal demand diminishes, this *circulation credit* is or at least can be withdrawn. Temporary money has been temporarily manufactured and temporarily kept in circulation in the interest of "efficiency" in the use of money.

The alternative would have been to have "less efficiency" in the use of money, namely, there would be in seasonally slack periods excess idle funds which would not be earning interest; that would occasion a loss in potential income. Furthermore, because there would be less money, therefore, according to the quantity theory of money (see page 196), prices would generally be lower, if for no other reason, because money was "turning over" less frequently.

Some of the unsound ideas about money have, in a sense, sneaked into the money and banking system, via the plausible idea that there should be no inefficiencies in meeting the seasonal demand for money; that is, the high demand for money should be taken care of by *circulation credit,* or as we have also designated it, "counterfeit" *credit* (see page 254ff).

It is no great jump from the idea of the merit of manufacturing *seasonal* funds for the sake of economy, to the idea of manufacturing *all* funds needed at any time — also for the sake of "economy" or to achieve a hoped-for "efficiency" in the use of money.

The Currency School Versus The Banking School On The Question Of Efficiency In The Use Of Money

It is seductively plausible to consent to being "efficient" in the use of money, in order to meet with ease the rhythmic seasonal variations in business. Clearly, too, although *circulation credit* (which in principle is plain theft) may have been issued to finance seasonal business, but if it is withdrawn when the season is over, then it appears that the harm from the theft has been undone (similar to the case of the teller who defalcated $10,000). Who, however, could really be at ease about either case, if they are in principle the same, which they are.

But with *seasonal* circulation credits as a wedge, it becomes possible to reason in this manner: generally, *circulation credit* will never be issued unless there is a genuine demand for it, just as there is for seasonal *circulation credit;* and as there is from time to time a natural demand for it, will there not also be a natural retirement of it? And so there need be no fear that an "excessive" amount of circulation credit will ever be issued, because if an excess is issued, it will naturally return to the issuer, and so no harm will be done. The proposition, in other words, is this: there is *never* really any *danger* from an *excess* of circulation credit, because it will, if no longer needed, automatically be returned to the issuer for redemption. Consequently, so the argument goes, there is no need to be opposed to circulation credit, because the system under which it is issued is self-corrective. Why, then, all the furore against circulation credit? Is it not obviously a good thing as far as it is needed? It is certainly a low cost, "efficient" way of having the required money supply; and beyond its natural and proper use it will not continue to exist. Such is the "argument" in favor of circulation credit.

That is the basic proposition of the school of thought on money and banking known as the *Banking School* which flourished in the first half of the nineteenth century in Great Britain. The school of thought opposed to that idea is known as the *Currency School.* (The Currency School was successor to the Classical School of Smith and Ricardo.) The Currency School argued, contrarily, that more circulation credit could and would be issued than was "needed," and that circulation credit should be prohibited, or more accurately, that no *further increase* should be permitted. In so far as circulation credit already existed, the Currency School argued that the best thing to do was to leave that amount undisturbed, because there would be injury from decreasing circulation credit as well as from increasing it, and that the damage had already been done by any increase in the past.

The complex issues between the Banking School and the Currency School are not easy to understand, but for our purposes the issue will be understood if the following ideas of the Banking School are grasped: business needs more and more money as its volume increases; credits will naturally be created to finance such business increases; the quantity of money, in the form of credits, safely responds to the needs of business; if too much in credits is given to finance business, the credit will be paid off and thereby be cancelled. There is no real danger in circulation credit. It is the most "efficient" and "cheapest" way to provide additional money, as business needs it.

The Currency School dissented: it denied that there was a natural limit restricting the amount of circulation credit. It declared there could and would be over-issue of circulation credit, with the consequences of rising prices, boom, strain, export of gold, and depression.

The principal leader of the Banking School was Thomas Tooke. He was supported generally by John Fullerton, James Wilson, Bonamy Price, and (in France) by Courcelle-Seneuil.

The principal leader of the Currency School was Mr. S. Jones Lloyd (Lord Overstone). He was supported by G. W. Norman, Colonel Torrens, and Sir Robert Peel who was mentioned in the previous issue, and who was the British Prime minister who put through the famous Bank Charter Act in 1844. This Act put into effect the ideas of the Currency School, as was related last month.

Professor J. Laurence Laughlin, who, strangely enough, favored the principles of the Banking School more than the Currency School, stated the issues between the two schools as follows (page 264):

> According to the currency school:
>
> 1. Prices rise and fall with the increase or diminution of the amount of the circulation.

2. Banks have it in their power to increase at pleasure the quantity of paper money.

3. The efflux and influx of gold are to be regulated by regulating [the amount of the circulation credit issued by] the banks.

As opposed to these declarations, the banking principle included the ideas that:

1. Prices do not depend upon the quantity of the circulation.

2. Banks cannot increase their issues at pleasure; since, if convertible, any excess will be returned for redemption. Banks only follow the attitude of their customers.

3. Consequently, the issues of the banks need not be regulated according to the price of bullion in the foreign exchanges.

Laughlin then goes on to say:

> Some writers have assumed that the two schools differed principally on the second proposition, and that the controversy pivoted on the question whether convertible paper could be issued to excess. It will be found, I think, that the fundamental differences existed in regard to the first proposition.

There have been many quibblers about the quantity theory of money, and Laughlin appears to have been one of them. Logic and experience both indicate that the quibbling is absurd. The peasants throughout the world know that money — that is, *paper* money, the quantity of which is being increased — is unsafe to keep. In so far as the Banking School was attacking the quantity theory, they were arguing foolishly against the obvious. (Various inexactnesses in the specific formulation of the Quantity Theory do not subvert the theory itself; in economics, too, there are many who "strain at a gnat, but swallow a camel.")

The specific controversy between the Currency and the Banking Schools was (to use Laughlin's expression), "whether convertible paper could be issued to excess." When thus phrased, a simple *yes* or *no* can hardly be given. The reason is that there are really two propositions in the single phrase quoted. The submerged proposition pertains to the word *convertible*. What does *convertible* mean? does it mean absolute capability of conversion? or does it mean that paper money is (partially) convertible as long as there is no alarm about it, or awareness of its increasing quantity? If paper money is always absolutely convertible into gold, then it cannot have been issued to excess. There is then no problem. The question really should be phrased thus: "whether *potentially un-*

convertible paper can be issued to success," because that is in fact what this circulation credit or paper money situation is. The paper money in the United States today and in every country in the world today is NOT convertible in fact. It is an absolute impossibility! By inserting the word *convertible* Laughlin has implied something contrary to fact and he has perpetrated the fallacy of "begging the question."

The fact is that the Currency School was entirely correct in its propositions, as formulated in the foregoing by Laughlin. It is a grievous mistake to let the Banking School or economists today, more than a hundred years later, confuse the people.

Our interest, however, is at this point primarily restricted to considering the "efficiency" of paper money, that is, that it should be used because it is cheaper than metal money. Laughlin wrote (page 267-8); (our italics, and note its significance from our present viewpoint of *efficiency*):

> The contention, however, that convertible notes could not be issued in excess, depends upon what "excess" means. Probably no one would deny the correctness of this position, if it were understood that convertibility carried with it efficient and ready means for immediate as well as for ultimate redemption. Instant convertibility, on demand, at various points throughout the districts wherein the notes are circulating, must, in the light of modern banking experience, permit to circulate no more of the medium of exchange than is required by the needs of business. But this should not be taken to imply that such notes, on entering the circulation, would not drive out a portion of the specie currency. To the extent that gold might have been used as a medium of exchange in aiding the movement of goods, a new issue of convertible notes would certainly take the place of this quantity of coin, *and save to the community that amount of the cost of the machinery of exchange.* The convertible paper and coin together might equal the sum of the original coin required; but it might very properly result that almost the whole of this medium might be made up of paper, coin being almost entirely retired to reserves. This is consistent with *modern devices for saving the use of the valuable standard commodity from being passed about as a medium of exchange.* In Great Britain, above the strata of small denominations of gold and silver coins, the Bank of England notes serve all the purposes of a medium of exchange instead of gold; while the deposit currency since 1844 appears also, as a medium of exchange, to have clearly *relieved even the bank notes of such duty* in the vast mass of transactions.
>
> Therefore, when the currency school contended that by excess they meant that "the whole money of the country, paper and gold, undistinguishably, is depreciated in comparison with the money of other countries," they could have referred only to the temporary processes, while in operation, by which the *superfluous specie, made such by economizing*

devices like bank notes, was disposed of in the international distribution of the precious metals. But, assuming by "excess" that they meant they did not wish gold to be displaced by bank notes, and hence that bank notes should not be issued because, even if convertible, they would drive out gold (as evidenced by the course of the exchanges) they were correct in their anaylsis of the operation; but *their assumption was against the interests of the commercial public, because the substitution of an expensive gold circulation by paper was a saving to the community, . . .*

We quote the foregoing only for one purpose — to show how the *cost of money* influenced the view. The *motivation* behind the idea of the Banking School, and that motivation is pervasive among all advocates of circulation credit and other counterfeit money, is that *it is cheaper for the community to have paper money than to have metal money which is expensive to mine, heavy to transfer, etc.*

On the question of the cheapness — the unrivalled cheapness of circulation credit, whether deposit credits or bank notes — there should be no dispute at all. The answer is obvious. Substitute money is *always* cheaper to supply than metal money, or otherwise why would it be substituted. *But the cheaper that substitute money is, and the easier that it is to supply, the greater is the danger that the public will be robbed and impoverished by over-issue of circulation credit.*

The ideals of "efficiency" or low cost of money versus "retention of its value" are not *necessarily* contradictory, but there is a very great danger that they will be just that, unless exceedingly careful and important distinctions are made.

For money to retain its value, it must be of a kind so that it is expensive, rather than cheap, to supply. When in the previous issue it was proposed (on pages 248-9) to discontinue all *further* issue of circulation credit, then it was in effect proposed that the idea of having an artificially *low cost* media of exchange *be completely and permanently abandoned.* The principle of efficiency in money can be as seductive, and eventually as destructive, as a Cleopatra.

But it is an injustice to the members of the Banking School to imply that they alone were unduly afflicted with the idea of "efficiency" (low cost) in provision for money. Men such as Henry Thornton, a practical banker, held some questionable ideas on money, which indicated the tremendous impact of the efficiency argument on his thinking. And, as previously indicated, Adam Smith and David Ricardo, highly superior reasoners, were also led astray by economy, or low cost, or efficiency considerations, in their thinking about what kind of money to employ in a community.

Ricardo, On The Value Of Gold And Economizing The Use Of Gold

David Ricardo wrote:

> Any improvement in the facility of working the mines, by which the precious metals may be produced with a less quantity of labour, will sink the value of money generally.
> — *The Principles Of Political Economy and Taxation,* (Everyman's Library edition, page 90)

This is Ricardo's reasoning: (1) A lowered cost of mining gold will result in greater profits to the mine owners. (2) The mine owners will then see to it that more gold is mined. (3) The availability of more gold will (according to the quantity theory of money) result in higher prices of other commodities, or, what is saying the same thing, will result in a lower value (purchasing power) of gold as money.

All other things being the same (*ceteris paribus*), Ricardo's statement is undoubtedly true. And it is, of course, wholly irrelevant to quibble whether *all* other things do or ever can remain unchanged. What of it? That does not qualify this proposition, but only what happens in a particular case, whatever that may be. It is improper to confuse principles and facts in such manner.

(1) If paper money were strictly a substitute for heavy gold lying in vaults; (2) if there were a dollar's worth of gold behind every dollar of paper money, then the "economy" or "efficiency" of substituting paper for gold would be unexceptional. But if paper money is an *addition* to the money supply over the amount of gold available, and if the quantity of paper money is not restricted by effective legal prohibitions, then the quantity of paper money will undoubtedly increase indefinitely, and the "value of money" will sink indefinitely. *Money, to be safe, must not be increasable except at a cost about equal to the present value of gold.*

But if the first step of a process consists in making the manufacture of additional money cheap (by issuing paper money of all kinds, including circulation credit), then Ricardo's statement can be paraphrased:

> If paper money is the real money of a community, completely unhinged from gold, then the eventual value of that money will not be determined by the numbers printed on it, but by the value of the paper, the printing of it, and the overhead costs from putting it out. In other words, it will be practically worthless.

That all the monies of the world still have some value is solely due to the fact that they are still *partially* tied to gold. Remove that tie and then the value of the paper will (as it always has in the past) eventually sink to its cost of manufacture which is practically nothing, just as gold money will sink to its cost of mining.

Later (page 241) Ricardo wrote:

> Experience, however, shows that neither a state nor a bank ever have had the unrestricted power of issuing paper money without abusing that power; in all states, therefore, the issue of paper money ought to be under some check and control; and none seems so proper for that purpose as that of subjecting the issuers of paper money to the obligation of paying their notes either in gold coin or bullion.
>
> To secure the public against any other variations in the value of currency than those to which the standard itself is subject, and at the same time, to carry on the circulation with a medium the least expensive, is to attain the most perfect state to which a currency can be brought, . . .

With these statements of Ricardo we agree perfectly.

Fortunes can be made today by understanding and adjusting to the principles stated by Ricardo in the first paragraph.

And in regard to the question of a *sound* currency (namely, one based on metal) with *economies strictly limited to the substitution for existing gold,* we also agree perfectly. Economies should always be limited to substituting for *existing* gold, and "economies" should never be extended to provide additions to the gold.

(We shall return to these ideas later in order to note an exception from Ricardo which can be designated as minor but which is really important. He left a "crack in the door" by which much mischief could and did enter.)

Mises's Summary Of Smith's And Ricardo's Views On Economizing On Money

> As the naive Midas-like trust in the usefulness of a large stock of precious metals disappeared and was replaced by sober consideration of the monetary problem, so the opinion gained strength that a reduction of the national demand for money in the narrower sense constituted an outstanding economic interest. Adam Smith suggested

that the expulsion of gold and silver by paper, that is to say notes, would substitute for an expensive means of exchange a less expensive, which, however, would perform the same service. He compares gold and silver which is circulating in a country with a road over which all the corn has to be brought to market but on which nevertheless nothing grows. The issue of notes, he says, creates, as it were, a path through the air and makes it possible to turn a large part of the roads into fields and meadows and in this way considerably to increase the annual yield of land and labour. Similar views are entertained by community of the apparatus of circulation. His ideal monetary system is one which would ensure to the community with the minimum cost the use of a money of Ricardo. He also sees the most fundamental advantage of the use of notes in the diminution of the cost to the invariable value. Starting from this point of view, he formulates his recommendations, which aim at expelling money composed of the precious metal from actual domestic circulation. [*Theory of Money and Credit,* Yale University Press, 1953, pages 297-298.]

Hugo Grotius On "Natural Law"

Hugo Grotius (1583-1645), whose regular Dutch name was De Groot, was of a respected family in Delft, The Netherlands. In religion, he was an Arminian; in politics, he was opposed to the princely Orange family. In the time of Count Maurice of the House of Orange, Grotius was imprisoned for life, but his wife shipped to him while in prison trunkloads of books, in and out. On one of the shipments going out, De Groot was in the trunk, and not the books he had read. He fled to Paris. For the ten last years of his life he was Sweden's ambassador to France. Grotius was a modern ecumenist in religion; and a "one-worlder" in politics, if that is defined as being for universal peace. His best known books are against war, generally, and once there is war, to make it less barbarous.

Hugo Grotius, the Dutch political theorist, diplomat and theologian, in his famous book *The Law of War and Peace,* published in 1625, based his theories on the idea of *Natural Law.* (We are using the translation of W. S. M. Knight, Peace Book Company, London.)

Grotius's idea of *Natural Law* is an excellent illustration of the unattractive intellectual consequences resulting from the unnecessary multiplication of terms.

Grotius was looking for a *universal law of nations,* a law higher than man-made law, which latter (a *human* origin) would be fallible and maybe be prejudiced. That *law of laws* he called *Natural Law.* He wrote:

> Natural Law is the dictate of right reason . . . It indicates whether an act is morally right or wrong, according as it complies or disagrees with rational nature itself. Such an act is consequently either prescribed or forbidden, as the case may be, by God the Author of Nature. . . . Natural law is so immutable that even God Himself cannot change it. For though the power of God be boundless, yet it may be said that there are some things to which it does not extend . . . as it is impossible even for God so to make it that twice two are not four, so He cannot make that which is intrinsically bad not to be bad; . . .

Every thinking man, in a sense, seeks for a supreme law, something greater than the statutes or court decisions of a particular nation. For *world* peace it is natural to seek a *world-wide* law, a so-called "natural" law, a law resting on the very nature of things, or even in God as Grotius endeavors to ascribe his Natural Law. Grotius was interested in *peace,* and to promote that he "manufactured" his idea of Natural Law. There are many noble ideas in his, *The Law of War and Peace.*

But it appears that his ideas on what Natural Law is has some serious defects. These "defects" (assuming that they are defects) are worth examining.

1. First, Grotius's Natural Law tolerates slavery. He wrote:

> Another unjust cause of war is the desire for liberty, whether that of individuals or that — autonomy or self-government — of States, as if it were a natural and constant right of every man or State. For when liberty is claimed as the natural heritage of men and peoples it must be understood only as a natural right as it existed before any human action in derogation of it, and as an exemption from slavery, but not an absolute incompatibility with slavery. So, though a man is not a slave by nature, yet there is no natural right which prevents him ever being a slave. For in the latter sense no one is free. "No one is born either free man or slave," says Albutius, "but fortune gives these names to them afterwards." [Pages 60-61.]

This may be Natural Law, or God's Law (whatever one may wish to call it,) but, if so, there are reasons for dissenting.

2. Secondly, Grotius disputes that "law [is] . . . insti-

tuted for the sake of utility alone," and he declares it is untrue what Carneades wrote, that "Utility is the mother of the Just and the Right" (pages 34 and 32). Grotius, living before the real development of economic science, ascribed society largely to "a desire for *mutual society* even though our necessities should have no actual need of it." But almost two centuries later Ricardo (1772-1823) worked out mathematically, in a demonstration that cannot be discredited, his famous *Law of Association*, which shows that the overwhelming reason for men to associate together is not "mutual society" but individual and personal benefit. (See Volume IV, Numbers 7 to 10, beginning on page 200.) If Grotius had lived three centuries later he might have written differently.

3. Thirdly, Grotius considers the Mosaic Law (the Decalogue) to be mere local or national law, and not universal Natural Law. He defines (page 43) Voluntary Divine Law, that is, law having its origin in the Divine will, and he adds the comment, quoting with approval Anaxarchus, that "God does not will a thing because it is just; but it is just, that is legally obligatory, because He wills it." This is a statement which will be unacceptable to many of us. Then Grotius goes on to say (page 43):

> XV. . . . This law was given either to all mankind or to one people only. And we find that it was given by God to all mankind on three occasions — the first, immediately after the creation of man; the second, upon the reinstatement of mankind after the Flood; and the third, on man's more sublime reinstatement through Christ. Without doubt these three laws oblige all men, as and when they acquire a sufficient knowledge of them.
>
> XVI. To only one people, the Hebrews, did God especially give laws, . . . the Mosaic Law, which binds only those to whom it was given, and not strangers . . . Hence, we may conclude that we are bound by no part of that law.
>
> XVII. Since, therefore, the Mosaic Law cannot, as we have just shown, impose any direct obligation upon us, let us see if it can have any other use — first, in this matter of the laws of war, and next, in other like questions. This is important in regard to many matters. First, then, the Mosaic Law shows that its commands are not contrary to Natural Law. And because that law is eternal and immutable, as we have already said, it is impossible that God, Who is never unjust, should command anything contrary to it. Add to this that the Mosaic Law is called pure and right in several places in the Scriptures.

It is clear from the foregoing that Grotius held to the idea that what he called Natural Law, or "right reason" was the ultimate standard by which to judge the Decalogue. The Decalogue, contrarily, was not, in Grotius's estimation, itself the ultimate standard. In FIRST PRINCIPLES we hold to the idea that the Decalogue is indeed the ultimate standard, the Law of laws, the Constitution of constitutions, the Law of Nations, or to use a term of the Romans, the *jus gentium*. We consider all people, in any time, in any circumstance, to be under the Decalogue. For us the Decalogue is itself the Natural Law.

* * *

Not only do we disagree with Grotius (1) concerning which outranks the other, his Natural Law or the Decalogue; and (2) concerning what the proper content of his Natural Law should be; but we also disagree in a very broad way with his basic approach. There is good reason to believe that Grotius unintentionally fell into a serious fallacy, viz., that of "manufacturing" a term (1) with a vague meaning, (2) mostly derived from the past, (3) put together in an eclectic or patchwork manner, and (4) that he added little of value to the "concept of law" by utilizing the term *Natural* Law, and glorifying that as the ultimate law of laws.

Grotius's approach, was, we believe, ancient and medieval. He was not really a modern, although he could have been. The modern intellectual age can be said to begin with William of Occam (or Ockham) (1270-1349), a Franciscan friar, who made an approach to the wordy discussions of the philosophers of the Middle Ages which was a death blow — a *coup de grace* — to scholasticism. The scholasticism of the medieval era was, in a sense, a facade of Christianity attached to the framework of Greek philosophy. This Greek influence had come in especially through Augustine. In this system, words and ideas were greater than specific things. The great ideas (using Plato's term) outranked everyday specific reality. The soil in which these so-called "*great ideas*" grew was the soil that consisted in quibbling endlessly about terms and talking about abstractions. That approach resulted in the *multiplication of terms*, or of words. Occam, who became known as the Invincible Doctor (presumably because in dialectics he could "pull the rug out from under" any of his opponents), developed apparently a remarkable technique to unmask the fact that his opponents were mouthing words, which sounded learned but meant little, or at least not what they were intended to mean. He showed that the other man's argument was little more than a new term for some old idea or some confusion of ideas. He phrased his critique in the famous slogan known as Occam's Razor, namely, *Entia non sunt multiplicandum praetor necessitatem,* that is, terms must not be unnecessarily multiplied or proliferated.

What, upon sober inspection, is Grotius's famous Natural Law? It is nothing more than a combination of the ideas in Scripture and in the writings of Seneca, Plato, Aristotle, Cicero and many others. His Natural Law is not anything new or something created or discovered by Grotius. Whatever merit Grotius's ideas have do not depend on their being glorified as Natural Law, but they stand or fall on what they are *specifically. Specific* rules of conduct have more real meaning than *general* ideas such as Natural Law.

* * *

Occam's Razor did not make a really new approach to *law,* or ultimate law, or supreme law, or natural law, or divine law, whatever you call it. In the field of laws for human behavior or human action, Occam's Razor was a "throw-back" to Moses. In an anachronistic sense, it can be said that Moses was the first Occamite.

There is nothing *general* about the Decalogue. It is as specific as anything can be. In the field of human behavior it talks about murder, adultery, theft, falsehood, covetousness. There are no "great ideas" here, *in the Platonic sense.* In the Decalogue the abstract does not take the place of the specific.

In First Principles we are not Occamites *in method,* because Moses agrees with Occam. We are, instead, Occamites *in method,* because we follow the teaching of the Decalogue. What Grotius called mere tribal and Hebrew law, we call universal law.

* * *

A pitifully narrow view can be taken of the ethical rules in the Decalogue, namely, they forbid coercion, adultery, theft, fraud, and the motivations that induce such *specific* acts; so much, and no more. But the Decalogue, as we read it, has three parts, two of which are implicit and one of which is explicit. The three parts of the Decalogue are:

1. Acts injuring a neighbor are forbidden; this is the explicit part; everybody can "see" that; no assumptions are necessary.

2. All else is *free;* you can do all that is not forbidden. The world is, therefore, really intended to be a realm of pervasive freedom. You may do anything except hurt your neighbor, and in what that hurting him consists is plainly stated. This part of the Decalogue is not explicit, but only implicit. It is there, but it is not always seen. Failure to see this is a very great and dangerous failing.

3. If your neighbor injures you, you may not vindictively retaliate by in turn injuring him. *Forbearance and utility must govern your reaction to the evils others inflict on you.* This also was always implicit in the Law of Moses. But because it was not explicit it was lost sight of. The teachings of Christ made this part of the Decalogue explicit, rather than merely implicit. Read the Sermon on the Mount; "Resist not evil *with evil.*" Do not be vengeful, but be helpful to your neighbor, despite his prior acts. The Sermon on the Mount explicitly adds utilitarianism to what was always implicit in the Mosaic law. The Decalogue is always intended to be helpful to all men and is never intended to be hurtful.

In Old and New Testament times, scriptural thinking on ethical questions was individualistic, not general; specific, not scholastic; "modern," not medieval; Occamish and not Platonic. The foundation of the ethics in this publication is Hebrew in character and not Greek.

* * *

If, finally, it is rebutted that there was deterioration in New Testament times, away from what was specific, in the form of the *general* statement, Thou shalt love God above all, and thy neighbor as thyself, then a completely satisfactory rejoinder can be given, namely, (1) this formulation pertains to an objective rather than a method; and (2) the method (for the purpose of showing love to God above all and to the neighbor as to the self) is always explicitly *identified with* the Decalogue.

There is *nothing new* in the idea of loving the neighbor as thyself. The exact statement occurs in the Old Testament in Leviticus 19:18b, where one can read: "Thou shalt love thy neighbor as thyself."

The statement meant no more in the New Testament than what it meant in the Old Testament; see Matthew 19:17b-19, where one can read:

> . . . if thou wouldest enter into life, keep the commandments. He [a young man] saith unto him, which? And Jesus said, Thou shalt not kill, Thou shalt not commit adultery, Thou shalt not steal, Thou shalt not bear false witness, Honor thy father and thy mother; and, [then and thereby] Thou shalt love thy neighbor as thyself.

Here is a perfect linking of the "specific" of the Old Testament with the "general" of the New Testament.

* * *

The groping of philosophers and political thinkers for a "natural law," or a "universal law," for an "unbreakable law," for a *real* law of human action is understandable. What might that "ultimate law" be?

To that question, an excellent answer is, *self-love*. Scripture teaches this plainly when it instructs a man to "love thy neighbor *as thyself*." *Self*-love is the standard. Obviously, you cannot, by this rule, love the neighbor much, unless you first love yourself much.

By a process of pejoration *self-love* can be down-graded by the use of the terms *self-interest* and, in an even more pejorative way, by the use of *selfishness*. But what is selfishness *rightly* understood, and what can be wrong with it? Is it more than preferring what one likes more over what one likes less? And what is wrong with preferring that? Simple *selfishness* is therefore not to be criticized. (There are, of course, bad types of selfishness.)

But *self-love* can be upgraded as well as downgraded. This upgrading can consist in substituting *self-preservation* for self-love. What is self-preservation but a vigorous form of self-love? Are we not entitled to self-preservation? What are the commandments against murder, adultery, theft and fraud but specific defences in order to promote "self-preservation." Again, Scripture is not philosophical or scholastic but practical and Occamish; it mentions the specific acts that endanger self-preservation, and condemns those *specific* acts. How good would the Decalogue be, as a practical guide, if it merely legislated, Thou art entitled to self-preservation? The Decalogue is therefore *universal* law because it legislates specifically against what endangers self-preservation. Under every vicissitude of life a human being strives for self-preservation; it is the last thing a man abandons; therefore, self-preservation is the quintessence of Natural Law, that is, of the Natural Law which Grotius was trying to discover. So much for the defensive phase of the Decalogue.

The *freedom* phase of the Decalogue can be designated as an opportunity for self-development. If everything is indeed free, except to injure others, for what more could a man properly want that freedom than for self-development? This freedom may, unfortunately, be abused or not be well utilized, but self-development obviously depends wholly on the existence of freedom. The demand for opportunity for self-development exists everywhere, and in all times and circumstances. This *phase* of the Decalogue is, therefore, also universal, and should be satisfactory for meeting the test of Grotius's Natural Law.

Finally, forbearance and goodwill toward even those who injure us — as required by the teaching in the Sermon on The Mount — is a necessary adjunct to the prohibitions against evil acts and to the exercise of freedom. Machiavelli was a great political and social thinker, in many ways a most admirable author. But there is a grave lack, which everybody senses, in Machiavelli. The lack is exactly in the absence in his teachings of forbearance, generosity, kindness, goodwill. The greatness of Abraham Lincoln consisted contrarily therein, that he incorporated in his program noble forbearance and goodwill:

> "With malice toward none; with charity for all; with firmness in the right, as God gives us to see the right, let us strive on to finish the work we are in; to bind up the nation's wounds; to care for him who shall have borne the battle, and for his widow, and his orphan — to do all which may achieve and cherish a just and lasting peace among ourselves, and with all nations.
>
> — Second Inaugural Address, last paragraph.

Grotius himself finishes his book with some noble. secular quotations, teaching what the Sermon on the Mount teaches. He quotes Tacitus as follows:

> Excellent are the conclusions of those wars where pardons are the characteristic of the final terms.

And he also quotes from a letter of the not-so-admirable "dictator" Caesar:

> Let this be a new way of conquering: *to protect ourselves by mercy and generosity.*

The Right To Work

According to a report issued by Fortune magazine, Europe has strong labor unions but, with a few exceptions, has avoided labor contracts requiring workers to belong to a union before they are employed or forcing them to join shortly thereafter.

Even in labor-dominated Britain, the vast majority of workers are free to join a union or not, according to their own choice. Sir Charles Geddes, former president of Britain's Trade Union Congress has said:

> "I do not believe in a closed shop. . . . There is a fundamental issue here of the right of the individual to say whether or not he would become associated with other people. . . . I want the right to exclude people from my union, but that cannot be done on the basis that everyone must belong or starve."

France has a strong group of labor unions but contracts are not written between labor and management requiring the former to join unions or lose their jobs.

Germany and Italy also have powerful trade-union movements but the principle of the open-shop is recognized and practiced everywhere. This would seem to discredit the voices in America that proclaim right-to-work laws are "union-busting" measures.

—Dr. Howard Kershner
in *Christian Economics*

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FIRST PRINCIPLES
IN MORALITY AND ECONOMICS
on which depend personal well-being and social health and harmony

VOLUME V | OCTOBER, 1959 | NUMBER 10

Contents

Why Socialists Do Not Appreciate Constructive Critique of Capitalism

FIRST PRINCIPLES is devoted to promoting capitalism, that is, in simple language, free markets and private property. But it is a critic of capitalism *as it operates.*

Socialism favors controlled markets and condemns private property. It is a mortal enemy of capitalism.

FIRST PRINCIPLES is a critic which endeavors to be helpful to capitalism and which bases its critique on the ethics taught in the Law of God. The socialists are critics who mean to destroy capitalism, and who base their critique on ethics contrary to that Law.

Although the socialists and FIRST PRINCIPLES are both critics of capitalism as it exists, there is no harmony in their criticism. Socialism rejects FIRST PRINCIPLES' critique of capitalism; socialism resents that anyone criticizes capitalism *except from a socialist* *viewpoint.* FIRST PRINCIPLES, in turn, rejects the socialist critique of capitalism.

The difference is this: The socialists condemn the merits of capitalism. FIRST PRINCIPLES, instead, condemns the unnecessary deficiencies of capitalism, its deviation from its own intrinsic principles of noncoercion, truth and safety of persons and their possessions. In FIRST PRINCIPLES, the critique is different *in motivation and in content* from the criticism of socialists-communists.

Readers will recognize three positions:

1. Capitalists who have no significant criticism of capitalism as it manifests itself today; these are not the best friends of capitalism;

2. Capitalists who criticize certain moral (and consequently operating) deficiencies in capitalism, which deficiencies are unjustifiable accretions to capitalism; and

3. Socialists-communists who criticize capitalism with the purpose of destroying it.

FIRST PRINCIPLES belongs to class two.

To which class do *you* belong?

Morality Depends Substantially On The Existence Of Private Property

Private property is not an institution that men can abandon without penalty. The possession of private property gives to the owners a sense of responsibility, and a wish to retain what they have, which means that they *conserve* and become *less wasteful.* What men do not own, or do not have to pay for in accordance with their consumption, they *always* waste more or less.

The water supply of the world will probably be the ultimate barricade at which the increase in population will be halted. Nearly everywhere the demand for water is increasing relative to the supply, and the trend is that water will progressively need to be more carefully conserved than it is today.

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The following is a paragraph taken from a commercial advertisement:

> One proved way to stretch dwindling water supplies is to discourage water waste through universal metering. Water consumption in the United States averages 150 gallons per day, per person. When water meters are installed in a previously unmetered community, per capita water consumption decreases by about 50%.

What people do not have to pay for in proportion to their consumption, and what is not their own possession, *they waste.* It is always that way. Even the most conscientious persons are less careful with what belongs to others, and especially to the public, than with what belongs to themselves.

Socialism-communism always impoverishes a people because it does not utilize the *motivation to conserve,* which becomes operative only with private ownership and charges in accordance with use.

Socialism teaches, from each according to his ability to each according to his need. What is the *need* of people? Is it one hundred fifty gallons of water per day per person? Nobody knows what each person needs. He alone can appraise that. One person needs more and another needs less. No government decree can take care of *variable* needs for water by different persons, or the same person at different times. The only effective way to conserve water is to charge for it, and let people determine their own consumption. But what they must pay for will certainly be less wasted than what they do not need to pay for.

Because socialism-communism does not stimulate human effort, by incentive in the form of ownership; and because it does not curb so effectively as capitalism does the *universal propensity to be wasteful* unless something must be paid for; therefore, there is an inherent tendency for socialist-communist societies to be poor. History substantiates that.

"In Forty Days Nineveh Shall Be Overthrown"

The story of Jonah is well known. He was instructed by God to go from Palestine to Nineveh, some 300 miles northeast, and warn the inhabitants of the imminent overthrow of Nineveh because of its sins. In what the overthrow was to consist no information is given.

Jonah demurred. He was unwilling to go because he was afraid that the inhabitants of Nineveh would repent, and that God would then not destroy Nineveh. Jonah apparently felt that under such circumstances, he would look rather silly.

From the foregoing data some tentative inferences can be made. Jonah may have been a well-travelled man. At one time he may have lived in Nineveh. He may personally have known of its sins. He may have deduced clearly that the bad situation created by those sins would soon come to a head. He was probably a linguist who could speak the language prevalent in Nineveh, or at least a language understandable there. And he was probably a powerful speaker. He must have had so much confidence in his message, in his oratory, and the force of his logic, that he was afraid the Ninevites would repent. In his own distant native land this man was under such compulsion from God to go to Nineveh, that he could not rest or have peace of mind. He fled to obtain distraction, and get farther away from Palestine and Nineveh. The storm at sea, his being tossed overboard, and his being swallowed by a fish and later vomited on land are known to everyone.

He then set out for Nineveh, one of the mighty cities of that time. Its exact site is now known by archeological excavations. The city was on the north side of the Tigris river, below where the Khoser river enters the Tigris, and across from the modern city of Mosul.

Jonah entered the city as a street preacher with his ominous message, "After forty days Nineveh will be overthrown." This can be no more than the gist of what he preached. Undoubtedly the reasons why were outlined by Jonah with clarity and force. Jonah covered one-third of the city by his preaching and by that time the Ninevites, as he had feared, repented. He then went outside the city and camped there to wait and see what would happen. But there was no destruction of the city. Jonah was disgusted.

What Jonah preached about Nineveh can be preached about modern capitalism, without being specific about the time, something like this: *In four years, or forty years, or, at some time, capitalism will be overthrown.* Why? Because as a system it has departed from basic principles; for example, Thou shall not coerce (kill), in the case of unions; or Thou shall not steal, in the case of the authorized banking and monetary structure. Of course, the people living under the present semi-capitalist system may repent, and then capitalism may not be overthrown.

It may genuinely be doubted that Jonah preached against individual private sin. He almost certainly preached against the *public* sins of Nineveh, that is, sins systematically incorporated in its laws. Similarly, a modern society is vulnerable to destruction when certain sins are officially authorized by the law of the land.

Who has been a modern Jonah relative to capitalism? The name of Karl Marx might be mentioned. He prophesied the destruction of capitalism by progressive aggravation of booms and depressions. Booms and depressions are caused by a specific evil which is authorized by prevailing law, of issuing *circulation* credit. As a modern Jonah, Karl Marx might be right.

But there was a great difference between Jonah and Marx as preachers. Jonah undoubtedly called attention to the *real causes* of the evils in Nineveh, their essential character. Marx, superficially, saw only the consequences of one sin of capitalism, namely, depressions. He did not have real understanding of the true causes of the business cycle. He was no real Jonah.

Capitalism needs not unreasoning defenders or patriots, but genuine critics, who will call attention to capitalistic evils which should be purged. And those critics should be more kindly disposed to capitalism than Jonah personally was to Nineveh. Capitalism needs critics who will preach a return to sound practices with the hope that the message will be heeded, that amendment will take place, and that capitalism will not be overthrown.

But sooner or later capitalism will be overthrown *unless it abandons its public sins,* that is, sins incorporated in its laws.

"The Church In Germany Is Dead"

A friend who has travelled over Europe this summer made the statement given above — "The church in Germany is dead." The only testimony he gave in support of his conclusion consisted in the declaration that the churches on Sunday are practically empty. (His statement referred to Protestant churches.) Empty churches indicated, apparently to him, a profound aloofness or indifference on the part of the people to the church and the religion it teaches.

A year or two ago a family physician who had toured Europe made a similar observation, to the effect: "The churches are full (of tourists) on week days, but are empty (of worshippers) on Sundays."

Whether the conclusion at the head of this article is accepted on the basis of such evidence is a matter on which everyone can have his own opinion.

* * *

If the "church is dead" in large sections of the world, then why? To this question, the following answer is suggested: the churches no longer always teach realities. They often teach, instead, extravagances and foolishness. ("Foolishness" here does not mean the foolishness to which Paul referred in I Corinthians 1.)

Aspects of the Christian religion can be listed under three headings: (1) theology, (2) ethics and (3) cosmology.

1. Much of the *theology* of modern Christianity has become this-worldly and denies supranaturalism. It departs from the historical position of the church. There can be no real Christianity without supranaturalism.

2. The *ethics* of modern Christianity have become sanctimonious — radical extravagances. What is taught in ethics in many churches is unattainable, undesirable, hypocritical, contrary to the nature of things. Ethical demands on Christians have been puffed up to elephantine size. (See Volume I, p. 26ff., especially p. 113ff.) Such *extension* of Christian ethics can be reacted to by ignoring it. Most people do.

3. The *cosmology* associated with Christianity is, alas, very out-of-date. By cosmology is meant ideas concerning the character of the world in which the drama of human action is played. Unless its cosmology — which is the backdrop for its ethics and theology — is brought up-to-date, Christianity can be expected to become progressively less influential. The specific cosmology taught has never been a genuinely *scriptural* matter. It has always had extensive supplements based on current experience, observation, and understanding. The experiences and observations which have become fossilized in religion are anachronistic to most modern people. People neglect the true theology and the true ethics of Scripture, because they (more or less unconsciously) have such a low opinion of the cosmology associated with Christianity.

An example will illustrate the problem. A typical view among devout Christians is that *all* pain, or distress or trouble is the result of sin. Pain is an "evil" they say. Evil entered the world with Adam's Fall. If there had been no sin, there would have been no pain whatever. A friend argued this matter recently with another. He said: "If I suffered no pain, my arm might be ground to pieces in a machine — without my knowing it — by my standing too close to it. Pain is a warning signal. It is a good and not an evil. Yes, pain may be a genuine and direct consequence of sin and evil. But not *all* pain is a consequence of evil or sin."

Some of the basic doctrinal standards of some churches have incorporated throughout their whole texture indefensible ideas in the field of cosmology (as the idea that *all* the trouble in the world is *solely* the result of sin). The denomination to which the writer belongs has such out-dated standards. (This denomination, does, however, permit individuals to have views *privately* which permit radically modernizing out-dated ideas in *cosmology*. But although an individual may *privately* hold such views and be without the taint of heresy, it is forbidden to teach a modern cosmology from the pulpits of this denomination! See J. L. Shaver, *The Polity of the Churches,* Volume II, pp. 34-35. A dynamic application of supralapsarianism to cosmology permits a relatively modern view of cosmological questions.)

But in the present circumstances it is natural that to a wide extent "the church is dead."

Modern economics could make a considerable contribution to bringing up-to-date the outmoded cosmology of Christianity.

"Cheaper By The Dozen"

One of the pioneers in "industrial engineering" — a so-called efficiency expert — was the late John Gilbreth.

Mr. and Mrs. Gilbreth were the parents of twelve children. Gilbreth himself coined the phrase (referring to the having of children): "They come cheaper by the dozen." After his death Mrs. Gilbreth took over the management of her husband's professional practice, and operated it successfully for several years. Husband and wife were each, in their own right, remarkable persons. Two of the twelve children in 1948 wrote a charming biography of their father, under the title *Cheaper By The Dozen* (Thomas Y. Crowell Company, New York). The book has already had a thirty-third printing.

Gilbreth was an insatiable *driver for lower costs in business.* He was the most important originator of "time and motion studies." His goal was to eliminate every unnecessary motion made by a man (or by a machine). The purpose was to reduce the amount of labor and other costs required to attain a given result. His children report that he would confidently walk into a factory as "Zeiss . . . in Germany or Pierce Arrow in this country and declare he could increase production 25 percent — and do it." He taught his children how to bathe to cut off minutes and seconds from the time. He cut down the time of lathering his face by using two brushes, and for a while tried to shave with two razors. He found out that he could reduce the time to button his vest from the bottom up to three seconds whereas from the top down it took seven seconds! It all sounds fantastic. But this man, by his idea, made an enormous contribution to the welfare of this country. He did far more for the common man than most of our presidents.

An individual worker usually develops a certain way of doing his task. It is seldom the easiest, fastest or lowest cost way of doing it. An expert on "time and motion" problems, by studying the work and the movements of the man, can often show ways to make it easier for the man; economize on his motions; speed up the action; lower the cost; and thereby eventually increase the income of the man, because real income must and always does depend on productivity. These time and motion studies do not pertain merely to the man; they include the situation in regard to the raw material with which the man works; the performance of the machine he operates; the handling of material generally; and all related problems.

The men who cover this field of activity are usually graduate engineers, and are described as *industrial engineers.* Gilbreth himself was originally a brick layer, with a keen and original mind. He helped discover and pioneer the whole "idea" of increased efficiency, today known as industrial engineering.

At the end of the book already referred to, an incident is related which basically challenges the idea of *efficiency* and *industrial engineering.* Some person skeptically asked Gilbreth what the purpose was of all this furore about productivity.

"But what do you want to save time *for?* What are you going to do with it?" "For work, if you love that best" Gilbreth is reported to have replied. "For education, for beauty, for art, for pleasure . . . for mumblety-peg, if that is where your heart lies."

Clearly the character of the question asked of Gilbreth revealed the psychological background of a person who was hostile to the whole idea of efficiency. In short: "What's the use; what does efficiency do for society? Is it not in a sense futile?"

Maybe the question caught Gilbreth by surprise so that he did not go into a complete rationalization of the benefits of efficiency obtained through industrial engineering. He probably found it hard to understand that there are people in the world who would contrast efficiency with joy of living. Such an antithesis is false, and the implied conclusion is erroneous.

What indeed is the result of *efficiency* via the route of industrial engineering? Here is what happens:

1. Each worker becomes more productive. It takes less men to produce the quantity which the market will absorb. This increase of productivity comes potentially from several sources: (a) more and better equipment (that is, more capital per worker): (b) a reduction in his physical exhaustion, by eliminating unnecessary motions and improving necessary motions; (c) by showing him how to accelerate his speed; etc.

2. The result is that some men are thrown out of work. The first consequence of increased efficiency appears bad; but the observation is superficial. The unemployment may be severe or mild. It may only be that no new workers are employed to replace those who naturally retire. But it may be that suddenly five men do the work of ten. Then five become unexpectedly unemployed. What happens to them?

3. In a *free* economy they are unemployed *only a short time*. This requires an explanation. The individual members of society universally have a *welfare-shortage*. You have; I have; your family has; my family has; your friends have; my friends have. We all would be glad to get some things which we now do not have. Make up a list and you will discover how big your welfare-shortage is. We all work, because that *welfare-shortage*

besets us all the time. No matter how prosperous we are, there are some things which we cannot yet afford. (There may be a few exceptions among the *very* wealthy, but they are so few that the generality of the foregoing statement is not really assailable.) *We do not suffer that welfare-shortage, because of lack of money, but because there is in society a lack of productive power by labor. It is not money that is in short supply; it is product that is in short supply.*

4. Now, because men have been "freed" from labor by a new efficiency, a "new" labor power has become available to produce what formerly could not be produced. Just what new jobs those five men in the example will get cannot be forecast. It depends on which shrewd entrepreneur is first to find out what consumers want most over and above what they now can have. The man who correctly "senses" where the new, real extension in demand will occur, which will satisfy what has hitherto been an unsatisfiable welfare-shortage, is the man who will develop new and profitable business which can and will re-employ the men who were disemployed. The standard of living in society will be proportionately higher.

We can now answer the skeptic who was wondering about the utility of what Gilbreth was endeavoring to accomplish: *The purpose of efficiency is to give men more and better goods, more services, and greater comfort in living,* by lowering the amount of labor that must go to produce the old goods.

Real gains in material welfare depend largely on men with the type of mind of Gilbreth. Men of this type, in our estimation, do more for society than almost any class. They *basically* attack the poverty problem of the whole world, rather than trying to ameliorate it by alms from one to another. The good economic situation in the United States versus, say, the bad economic situation in India is in large part because the United States has had men such as Gilbreth, and that business men generally have adopted his psychology.

In a sense the talk about how wonderful *charity* is, is poor blather compared to Gilbrethian efficiency. However, both have their place. But charity alone without a Gilbrethian type of efficiency dooms mankind genuinely to wretched poverty.

Why Standards Of Living In Europe Are Lower Than In The United States

Standards of living in Europe, in a *material* sense, are lower than in the United States. The European civilization is older; therefore, it "ought" to be richer. But it is not.

The explanation is that labor in Europe is less productive than in America. That does not mean that labor works less-hard in Europe than America, although the pace is obviously slower in some cases. The reason why labor is less productive in Europe, and consequently that the standard of living is lower, is that the *amount of capital employed to enhance the productivity of labor is less,* that is, the amount of *capital per capita* is less, or in the common language of America, the amount of *capital per person* is less.

If a visitor looks out of a hotel window in a big European city, what will he see?

For one, he may see a street sweeper with an old-fashioned broom of a primitive sort and with a cart for leaves, paper and rubbish. The process is slow, dusty and not thorough. There are many of these sweepers. In the United States a relatively large, white-painted truck operated by one man, moves down the street at a rapid rate. The machine sprays out water, spins a big modern brush which whirls the trash into a container in the body of the truck. *One* man and *one* machine in the United States do the work of ten or twenty men in Europe. The nine or nineteen men freed from street sweeping can then go to the production of other goods or the performance of other services, previously not accomplishable because the required labor was not yet allocated to it; but now, such really new production can be accomplished. That freeing of much labor from old tasks, to be available for new tasks, is what has already progressed extensively in America; it has not yet developed so extensively in Europe. In other words, the *capital per person* in Europe is less than in the United States.

Or, a view out of a hotel window in Europe may show some construction workers, let us say, those who lay sidewalks. Instead of building a solid and smooth concrete walk — by means of liquid cement brought from a central cement mixing plant in "truck mixers" with rotating drums, and dumping several cubic yards of concrete at a time, and in this manner quickly laying a smooth concrete walk — a man will be seen on his knees laying square concrete slabs about 10 x 10 inches, or 12 x 12 inches, on a sand base. He will tamp them down one by one. One man in a whole day will do less than what in America would be done in an hour or two. Further, the end product as sidewalk is less satisfactory, especially for women wearing high heels, because it is not level and smooth. Again the answer is, Europe does not have the construction equipment (that is, the capital) to make its construction labor equally productive with American construction labor.

The contrast in the availability of capital in the form of construction equipment between West Berlin and East Berlin is conspicuous. As is well known, West Berlin has been rebuilt much more rapidly than East Berlin. Much of East Berlin is still a depressing ruin. But where in West Berlin reconstruction is going forward with steel scaffolding and extensive construction equipment, in East Berlin the scaffolding is of make-shift lumber and much of the labor is by hand rather than by machine. Poverty in East Berlin is worse than in West Berlin *in proportion* as there is less *capital.*

Or, consider the railroads. In the United States there has been heavy investment in the form of elevating the tracks and making underpasses and overpasses. Europe, despite its dense population, has not done so much of that. Many men are employed as gatemen to raise and lower gates. The labor of such gatemen is "lost labor" in the judgment of an American. His greater capital formation has saved labor, and the saved labor has gone into the production of more and more consumer goods and more and more elaborate capital goods.

In the case of housewives, there is a corresponding loss of labor power in Europe. A stroll down a residential street on a weekday morning will permit observing many women who are engaged in sunning themselves and simultaneously doing *hand* knitting or preparing foods. Home *hand* labor is obviously more prevalent than in America where prior processing has been done on a *mass* basis, at much lower cost, *with the cooperation of capital.*

Or, the constant stream of women going to food markets to shop for small quantities is conspicuous. In Europe they lack large home refrigerators or have none; women therefore shop for *one* day's food requirements; they go to the grocery store six days in the week! In America, many women shop not oftener than once a week. They buy in large quantities, because they have (1) the *capital* to get to the store and carry the groceries home, namely, an automobile which is "capital" in this case; (2) the *capital* to store the perishables, namely, a refrigerator and a freezer. This relieves American women so that they can use their labor power at home for other purposes, or can use their labor power in industry or commerce.

In Europe a milkman, with an unrefrigerated cart maybe attached to a bicycle, brings milk to the door. He cannot deliver one-fourth the amount of milk that an American milkman delivers in his specially built refrigerated milk truck. Similarly in Europe the breadman or bakery man also delivers from door to door. He usually first takes an order; goes back to his cart, then delivers the order! All this is "lost" labor power, to anyone whose standard of comparison is one in which more capital is applied to enhance productivity.

In the judgment of an American there is enormous wastage of labor in Europe; but that is only because he judges on the basis that capital might be available (as in America). But the capital is not available.

Of course what is true in Europe compared to America is many times more true for the so-called "under-developed nations."

What will enable the nations of the world to "develop" a higher standard of living in the foregoing sense? The answer is *more capital per person.* But will they obtain that? Not unless they have laws which make capital *safe,* and not unless they consider it a virtuous act to *save* and to *invest in capital.* Even in the United States some intellectuals and some moralists look upon *saving* and *investment* as anti-social and as of the devil! This is so grievous an error that if the idea becomes general it will destroy the prosperity of the western world. Unfortunately the ideas of

1. safety of capital, of
2. stimuli to saving, and of
3. investment in real capital

are inadequately appreciated in large parts of the world, and are specifically *rejected* by the governments and populace of many of the under-developed countries. "As a man thinketh in his heart so he is"; and similarly, as the people of a nation think so they are; which in modern language is nothing else than saying that you must think soundly before you can act soundly. And throughout the world, even in the richest countries, savings and investments are often decried as mean, selfish, worldly, materialistic, wicked and un-Christian! If that is true and is acted on, then men are properly — and inevitably — doomed to poverty and distress.

"High mindedness" does not consist in treating good living with contempt. The Founder of the Christian religion wore some fine clothes and was accused (undoubtedly with some malice) of being a "glutton and a wine-bibber." He did not live austerely just for the sake of austerity. Solomon repeatedly recommends enjoying the good things of this life (see Ecclesiastes 3:24; and 9:7-10). Riches are repeatedly described in Scripture as blessings (although there are frequent and proper warnings against riches becoming a snare).

In contrasting the capital situation in Europe and America there is no intention to minimize the great capital formation which has taken place in Europe. Consider the great capital accumulation in a country as Switzerland with its electric power generating stations, its railroad tunnels, its terraced fields, and its banked lakes. Similarly in Germany, The Netherlands, England, France, etc. But much of the effort which from the beginning went to create productive capital (factories, machines. etc.) in the United States, has in Europe, in ages now past, gone into the construction of what was ornamental, such as elaborate and ornate churches and art museums. This was a development mostly for the upper classes. In the United States the real capital development has been "pitched" to serve the common man, thank God. And in the process of thereby developing a broad material base to a high standard of living, a broad base was also laid for the *subsequent* development of the artistic, the gracious and the intellectual. As evidence of that it can be mentioned that America — largely inhabited by descendants of the lower classes in Europe — is today the intellectual center of the world. Material prosperity is not a hindrance but a base, a foundation, to intellectual and cultural progress.

And what is the essential nature of *capital?* How learn to understand what it really is? The best answer to this question can probably be given by making reference to what Eugen von Böhm-Bawerk (1851-1914), the Austrian economist, wrote in his three volume work, *Capital and Interest,* Volume II, Book I, Chapter 2 (Libertarian Press, South Holland, Illinois, 1959).

The Misesian Explanation Of The Business Cycle

There are many theories which declare that they explain the business cycle — the booms and depressions which frighten everybody. Reference is here made to three of them.

General Overproduction

There is, first, the theory of *general overproduction,* which is so much in conflict with reality that everybody on careful reflection will know that it is inadequate. Everybody realizes that he himself is suffering from a comprehensive *welfareshortage;* there are many things which people *want* — that is, they wish to have them but they lack them. If people lack many things how can there be *general* overproduction? There can be specific overproduction, but *never general overproduction.* But the overproduction bugaboo frightens grown-ups, as a man with a sheet over his head frightens children by shouting "bugaboo" in a disguised voice. Jean Baptiste Say (1767-1832) long ago blew this theory "out of the water" for good, but nevertheless people hold to this illogical theory of general overproduction.

Shortage of Money

Then there is, secondly, the theory of a *shortage of money,* which is equally unacceptable. Adam Smith blew that fallacy "out of the water" in his *The Wealth of Nations* (Modern Library edition, page 406 f.). "Money" in fact is, because of the great issue of circulation credit at the time, in greatest supply at the peak of a boom; the supply of money, the greatest, but nevertheless a simultaneous shortage! This is an obvious contradiction. There is no profound mystery nor profound answer necessary to realize that there must be some confusion in the theory.

The so-called money shortage is a *loan* money *shortage;* it is not a "real money" shortage. The supply of "real money" remains relatively invariable. What is called a loan money *shortage* is really a *too-big demand for money,* which excessive demand is in turn the result of a gross miscalculation of real resources. (See foregoing reference to *The Wealth of Nations.*)

The gross miscalculation results from the unrealized misinformation caused by the earlier issuance of circulation credit — the issuance of, in effect, counterfeit money. But there have been limits to the issue of this counterfeit money, which limits have been set by law (and experience); then, suddenly, people become painfully aware that they do not have enough real resources to complete their programs. The inability to complete the seriously miscalculated programs, and the discovery of the nonprofitability of those programs brings on the depression.

In principle, the *money shortage* explanation of the business cycle is nothing more than a mild version of the idea that printing presses which print money can bring prosperity. Even the peasants in the world know that printing paper does not make them prosperous. Why then should learned folk believe it?

Mises's Monetary Theory

There is a third major theory explaining the business cycle, and this is the *Monetary Theory.* It is also known as the Austrian Theory, because the author of this theory, Dr. Ludwig von Mises, presently visiting professor at New York University, has for the latest thirty years been the outstanding representative of the famous Austrian school of thought in the field of economics. If a distinctive name is to be given to the theory, it should be called the Misesian Theory of the Business Cycle. Say destroyed the false theory of the business cycle which consisted in alleged *general* overproduction; Adam Smith destroyed the false theory of the business cycle which consisted in an *alleged shortage of money;* Mises has supplemented these negative contributions, by a *positive theory which actually explains the business cycle.*

What is presented in FIRST PRINCIPLES is our understanding of the Misesian theory, without thereby, of course, making the author of the theory responsible for our version of it.

There is nothing new or different in our version of the Misesian theory, except maybe *emphasis on an underlying immorality as the real cause of the business cycle.* What Mises as economist condemns as bad economics (namely the emission of circulation credit, that is, illegitimate money), we condemn not only because it is bad economics, but also because it violates two of the commandments of God, to wit, Thou shalt not steal, and Thou shalt not bear false witness. Putting out circulation credit is (1) disguised theft and (2) involves such misrepresentation of the real economic situation that even the sharpest observers and reasoners are tragically deceived.

We are continuing in current issues our analysis of the monetary factors causing the business cycle. The problem is a difficult one. But the "common man" should aim to understand it, and know the correct solution, or else Western civilization will probably eventually collapse; the issue possesses an importance of that magnitude. The four or five issues of FIRST PRINCIPLES prior to this one should be available and known to readers of what follows; also the issues of November and December 1957.

Last month we suggested that the money problem should be considered only from the viewpoint of strict *honesty,* and that considerations of (1) *efficiency,* (2) *liquidity,* (3) *international exchange,* (4) *full employment,* and (5) *price stability* should not be permitted to becloud the real issue. At that time the *efficiency* motivation was given attention. Attention will be given in what follows to these other extraneous and harmful considerations.

When this analysis is completed, it should be apparent that by the whole process which has been followed the residual program left is that of Mises, to wit, the program to prohibit the issuance of *circulation credit,* which circulation credit is a form of counterfeit money, and which FIRST PRINCIPLES opposes on moral as well as economic grounds.

Uncle Frank, A Walking Bank

Before World War I, during the war and especially immediately after the war, a man in the midwest of the United States who had extensive farm lands, and whom everybody trusted, accepted money from others on his note, and in turn used that money in his land deals and to loan to others. The transactions were informal. Everybody trusted Frank. The reason why they trusted him so completely was because whenever they wanted any money they had loaned to him, he would pull out his check book, figure the amount due, and write out a check. Money deposited with Uncle Frank (he was a distant relative) was *perfectly liquid;* it was available *on demand.* He was a "walking bank," as well as a farm operator and real estate dealer.

Frank had come rather naturally to being an unincorporated bank. His father before him had been a pioneer in the territory. The father had been a man of considerable vision who had "financed" many new immigrants who moved into the territory. He made it a practice to loan them enough so that they could buy a team of horses, some cows and hogs, and farm implements. The father, known as Whispering George, had lived and died as a benefactor of the community. The difference between the operations of father and son was in the fact that the father did not "accept deposits," that is, he did not use other people's money. Frank, the son, extended his operations beyond anything his father had attempted.

A thoughtful review of how Frank was operating would have resulted in the conclusion that it was unsafe to loan money to Frank. What *obviously* did he do with the money? He was buying and selling farms, and financing the buying of farms by others. His operations grew to considerable proportions during World War I and especially during the big farm land boom in 1919 and 1920. If Frank was genuinely *using* the money to buy land for himself, and to loan it to other buyers of farm lands who were buying through Frank as a broker, what would happen if all, or even a goodly number of those who had deposited money with Frank requested the return of their money? Frank had it pretty much invested in real estate. Real estate is generally not a liquid investment, but at the time (1914-1919) farm lands themselves were very liquid; speculation was rife; prices were rising rapidly; confidence was "in the air." Frank had no trouble to pay out *on demand* requests made by depositors. If he needed money he probably "took his profit" on some farm, and then again had the ready money he needed.

Further, Frank had undoubtedly discovered that, if *A* bought a farm and needed money, then *B* as seller would have as much more cash as *A* had less. If *B* left his money with Frank, then what *A* withdrew was balanced out. (See Volume III, page 331ff.)

(1) A real estate dealer is an agent; (2) a man who lends his own money is a capitalist; (3) a man who lends the money of others is a banker. Frank had graduated to the status of a banker, with his own capitalist and agency operations inextricably intertwined with his banking operations.

Frank had only *informally* entered the banking business. He had his own capital, more or less liquid, with which to operate. He had, in addition, the originally wholly liquid funds of his depositors. As the ancient silversmiths had learned and the commercial bankers after them, Frank had learned that it was improbable that all his depositors would want their money at one time. As time went on he operated on a steadily expanding scale, without personal apprehensions and with complete community confidence.

In a rising market and in a genuinely expansionist economy, *liquidity* is never a problem, unless a man is grossly incompetent. Frank was not grossly incompetent. He operated successfully for years.

But the great midwest land boom during and immediately following World War I did not last. The rise in prices petered out. The curve of farm product prices, and consequently of farm land prices, first flattened out and began to move horizontally. This was an ominous phenomenon, because Frank's scheme of operation depended on farm lands being highly salable — really liquid. Indeed, why buy and sell farm lands if prices are steady. During the big rise in prices, a farm might change hands three times in six months — each time at a new high price. But as prices steadied, the turnover and the liquidity of farm lands decreased. The walking bank, in the person of Frank, would then not really be so liquid anymore.

The real trouble lay ahead. It hit catastrophically in 1921. There had previously been much speculation in farm products. That meant that inventories had been accumulated. Sooner or later they would have to be sold. Surely, market prices would then become soft.

Calf skins, the raw material for sturdy shoe leather, might be taken as an example. Prices averaged 20 cents a pound in 1913. By 1919 they temporarily rose to more than 90 cents a pound. The following incident is actual history. The calf skin trader of one of the big American packers accumulated calf skins steadily — at rising prices. When they were more than 90 cents a pound he gleefully and confidently asserted to his employers that he would hold his huge inventory of calf skins until he could get more than a dollar a pound. There was danger in this because others were doing the same. Very soon calf skin prices began to decline. And then they crashed in one of the most terrible agricultural commodity price declines in history. The owners of the packing company, whose calf skin trader had been holding skins to get more than one dollar a pound, had their accountants compute their "losses" on calf skins. They were more than one million dollars! One of the owners said: "Fire him; pay him off; he makes me sick every time I see him. I keep thinking of my million dollars."

What was bad for the calf skin trader was also bad for the farmer, and what was bad for the farmer was bad for Frank as a farm owner himself, as a real estate agent, and as a "banker."

What happened to him as a banker? He discovered, to his dismay, that his depositors now wanted their money. They really needed it, or became frightened that they would need it, or they may have come to doubt Frank's *liquidity,* even though they may not have used that word.

But simultaneously, new depositors disappeared. They previously may have bought land at $400 an acre. Now the price was maybe $300. There may have been a mortgage against the farm of $150 or $200 an acre. But land was not "moving." Those who had losses were loath to sell. Those who might have bought kept saying to themselves: "Let's wait, maybe next month prices will be still lower."

Frank, therefore, got no new deposits. But he continued to lose his old deposits.

The price of land in that territory dropped eventually to less than $100 an acre!

The end of Frank as a "walking bank" hardly needs to be reported. He "went broke," lost everything he had, failed to repay his creditors, fell into dishonor, and died not long afterwards, as he was no longer a young man.

Liquidity! What is it? It appears to be something that is beyond question, and nonsensical to worry about, *in a rising market.* It is indeed in such times almost absurd to discuss it or to worry about it. But in a declining market it is a controlling consideration; it just does not exist any more as earlier, that is, it does not exist unless all loans may be "called" on *demand,* and if the borrowers have the ability to repay *on demand;* this they can *never* all do in a declining market. Bankers do not make only loans payable *on demand.* They make mostly time loans — loans not due until one month hence, or three months, or six months, or for a year; or even longer as so-called term loans.

No bank is really *liquid* unless it has *only* loans payable on its demand which loans are to debtors who *can* (that is, are genuinely able to) repay on demand. No bank exists with such a portfolio of loans.

But, it may be urged, loans can so be "staggered" that they will come due ahead of demands by depositors for their funds. This is well and good *if* the depositors do not have demand deposits, but only time deposits which need to be repaid only after ample prior notice of intended withdrawal has been given.

Liquidity of banks is a relative term. There is no perfect liquidity, for the following reasons:

1. The bank's own capital is mostly tied up in its building, its equipment, and in reserves in the Federal Reserve Bank. Its capital is not "liquid" in a perfect sense.

2. The bulk of the depositors' money in the bank on deposit has been reloaned to borrowers *on time,* although the depositors' claims are *on demand.*

3. The bank has, in addition, put out loans or made investments equal to *five* times its reserves at the Federal Reserve Bank. This is like having a building whose top floor area is five times the size of the foundation. Such a building is precarious, and so is such a loan structure.

Admittedly, in a rising market there will not be trouble. But, *inevitably,* in a declining market there will not only be trouble but catastrophy.

Loaning depositors' liquid assets — assets that depositors consider their *liquid* reserve — to third parties who will put them into assets not fully liquid, is on the face of it a dangerous action. A child could reason to the correct conclusion that periodically such a policy will lead to difficulties. Loaning out depositors' demand money *on time* is like being careless with a warehouse full of gunpowder.

But when to that is added the issuance of *circulation credit* on the *Five Times Principle* it is like lighting a big bonfire near the gunpowder warehouse. Trouble is as sure as anything can be in this world.

Economic Definitions Of Various Kinds Of People

The following are rough definitions of people classified according to certain economic characteristics. The definitions are oversimplified in order to facilitate easy understanding. In no case are the terms used meant to indicate criticism or disrespect.

Every man can classify himself as (1) a spender, (2) a hoarder, (3) a peasant capitalist, or (4) a real capitalist. These classifications are arbitrary. The lines of differentiation are not absolute. Many people fall in more than one category, particularly at different times.

In regard to the limited group of real capitalists, there is a subgroup of bankers. There are three main types of bankers; savings bankers, commercial bankers and investment bankers. Again the categories are not watertight compartments. Nor is the description here given of each class complete, but only indicative.

Spenders: All those whose economic program does not involve *saving*, and consequently do not acquire capital. There are two kinds of spenders, namely, (1) those who spend all their income practically *daily* on small purchases and so dispose of their resources, and (2) those who do collect funds *temporarily* in order to make larger purchases, but these purchases are for consumption and not for investing; for example, a man might "save" two thousand dollars in order to take a trip abroad. This is not *savings* in the real sense of the term. It is a temporary accumulation in order to finance a large consumption item.

Hoarders: All those who do indeed save, but who do *not use* the savings for investment nor put the savings to work directly or indirectly, but sequester the savings in a mattress, a jar buried in a hole in the garden, a safety vault, or sewn into the lining of a coat. Hoards do not yield any income, because they are not put to work. Hoarders save, but because of their psychology, do not invest their savings. This may be because they are aware that they do not really know how to invest, and are fearful of the consequences of trying to invest. Hoarders are often timid, or uninformed, or have a mental quirk, but they are not necessarily stupid or queer. They are not necessarily penny-pinchers or extreme savers, who deny themselves the necessaries of life in order to gloat over their coins. They are simply savers who do not invest nor let others use their funds for investment.

Capitalists: All who not only save but who invest their savings in order to obtain an income. Capitalists are one of the two major groups under savers, hoarders being the other.

Capitalists are of two types, peasant capitalists and real capitalists.

A *peasant capitalist* is one who does not know how or in what to invest directly, or who has too little to invest to make direct investment practical. He deposits his money with someone who invests for him. The major groups of peasant capitalists are those who deposit money in savings associations or in savings banks, who buy insurance, or who buy a house primarily for their own residence needs. They are people who may be extremely intelligent in some profession or business, and do very well in obtaining a good income and in saving a prudent proportion of it, but *they do not themselves know how or in what to invest and by that process themselves determine the direction of investment by society in real capital goods.* A peasant capitalist is one who saves for obtaining an income, but who does not himself know how to invest directly in a business venture. Savers who never study to become direct, wise investors remain a peasant type of capitalists.

A *real capitalist* is one who saves and invests directly in order to obtain an income. Real capitalists are individuals who themselves decide what farms, houses, or businesses to buy for income; or what bonds and of what maturity and of what interest rate; or what stocks, in what companies, in what industries and at what yields and prices. These people are *real* capitalists. They earn, they save, *they invest directly.* If they invest unwisely they lose their capital and are not capitalists any more. Being real capitalists does not make them wise or permanent capitalists by any means. They are real capitalists not because they are successful but because of the function they undertake to exercise.

Savings Bankers: Savings bankers are real capitalists who have put some of their own money into the organization of a savings bank, and who accept *time* deposits which come mostly from peasant capitalists. These deposits are not demand deposits which can be withdrawn on demand. The legal terms controlling the acceptance of savings deposits are such that the savings banker can, if he wishes, require prior notice before he is required to pay out to a savings depositor what he has deposited. The savings banker reloans the deposited funds to borrowers. These loans are seldom demand loans, that is, the savings banker seldom makes loans which he can recall on his own demand. He makes instead time loans, due in thirty days or sixty days, or three months, or a half year, or a year, or longer. Presumably he selects his investments so that he can be rather liquid, that is, so that he can make payments to depositors at the due date after proper notice from them. A savings banker is an agent between lenders and borrowers, especially lenders who are peasant capitalists and borrowers who are small borrowers. But the activities of savings bankers are not limited to this. Some of their depositors may be highly sophisticated "real capitalists" using a savings account in a savings bank for a special purpose, in a shrewd manner.

Commercial Banker: Commercial bankers are real capitalists, (1) who have put some of their own money into the organization of a commercial bank, (2) who accept *demand* deposits from peasant and real capitalists; (3) who loan out part of their own capital and part of the sums deposited, mostly, on a short-term basis, and (4) who possess the special privilege of manufacturing money in the form of *circulation credit,* in an amount five times the reserves which they have deposited in their Federal Reserve Bank. Commercial banks are more vulnerable than savings banks, because their deposits are almost all demand deposits and much the greater part of their loans are time loans. A commercial bank is never liquid in the full sense of the word. But the unique feature about an American commercial banker is that he is granted by law a special privilege, which, if he did not possess it but nevertheless employed it, would be known as counterfeiting money. A commercial banker is not a counterfeiter in the full sense of the term. A counterfeiter produces false money *to benefit himself.* A commercial banker produces circulation credit (false money) *to benefit society! That* is the theory!

Stock broker: A stock broker is an agent, who for a commission, sells or buys stocks for real capitalists, whether wise or foolish. A stock broker does not raise new capital but is an agent in the exchange of existing capital. What a real estate agent is in regard to real estate, a stock broker is in regard to stocks.

Investment Banker: An investment banker is primarily an agent between *long-term* borrowers and *long-term* investors. This contrasts with commercial bankers who are primarily agents between short-term borrowers and depositors who can demand their money at any time. An investment banker *underwrites,* that is he undertakes to assure a big borrower (usually a corporation) that he will raise a certain amount of money for such borrower permanently or for a relatively long term — five, ten, twenty, fifty or more years. If he cannot sell the securities to the public, he undertakes to put up the money himself. An investment banker is an agent; he does not have the right to manufacture money in the form of circulation credit. An investment banker sells either stocks or bonds. He does not accept deposits. He uses his own capital or is a borrower at a commercial bank. An investment banker is a very real *real capitalist.* He determines the direction of long-term investment.

Circulation Credit vs Commodity Credit Again

If you seek credit, the purpose is to buy something, or to pay for something, bought earlier but not yet paid for; (there are various secondary reasons such as to restore your buying power, if you have suffered losses, etc., but these are of no great consequence). To get credit means that you get purchasing power.

Someone grants you credit, say, a banker. He gives you currency (paper bills), or he credits your checking account and you write checks against the credit.

The crucial question is: *where* did the banker get the money? There are two possibilities.

1. He may have got the money from someone else, who did not wish to use it or at least was not using it. In this case, the banker was not the real creditor; the banker was only the agent between you and another; the real creditor was the man who deposited money in the bank, which he himself was not using. He was buying less; now you can buy more. As much less as he can buy you can buy more. Total purchasing power has not been increased. Because total purchasing power has not been increased, therefore, your borrowing this kind of credit could not increase prices generally. Credit of this kind is called *commodity credit,* as previously explained in the August issue, p. 243ff. (We are using the terminology of Ludwig von Mises.) This kind of credit does not cause booms.

2. But the banker may have "manufactured" the money. If an ordinary citizen manufactures money, he is called a counterfeiter. He manufactures money *for himself*. A banker is authorized by law to manufacture money far more easily than a counterfeiter. All he usually does is: (a) he asks you to sign a note, and (b) he then credits your account in your pass book for the amount, and then you can draw checks and use up the credit. The banker manufactures money — "counterfeits" — for you and others, that is, for "society." This kind of "counterfeiting" by some queer quirk of reasoning is supposed to stimulate business. If true, a regular counterfeiter's money will stimulate business and welfare just as much. Whereas nobody encourages the lone counterfeiter, everybody encourages the banker. Credit and purchasing power of this kind is *circulation credit*. (Again, we are using Mises's nomenclature and terminology.) *Circulation credit* is *the* cause of booms, and is (through creating booms) *the* cause of depressions. Circulation credit is subtle and social theft. In Hebrew-Christian ethics it is designated *sin*, the word that sounds so odd in modern ears.

Why is counterfeiting evil, and why is circulation credit also evil?

The counterfeiter is a buyer without having first been a producer. All buyers who come by money in regular business (except in the case of fraud or error) are first producers of goods or services. They brought something to market. They gave *quid pro quo*. They robbed nobody. Now, just as a counterfeiter is an illegitimate buyer with money he manufactured himself, so a person getting circulation credit is an illegitimate buyer. He does not give "society" *quid pro quo* any more than the counterfeiter does.

The counterfeiter is a *deliberate* thief. The successful applicant for circulation credit is an *unwitting* thief. He is unwitting, because he does not know whether the credit he is getting from his banker is commodity credit or circulation credit.

(The foregoing is a repetition of what has been written earlier, but material in the current issues will not be understood unless the character of *circulation credit* is thoroughly realized.)

How Circulation Credit Ruined Frank As A Walking Bank

Frank, the walking bank, did not put out any circulation credit. He could not, because he was not authorized to do so. He was not permitted to issue bank notes (paper money) nor open deposit accounts based on circulation credit. Frank dealt only in commodity credit.

Frank's ultimate problem — which caused him to "go broke" — was caused by others putting out circulation credit. It should be interesting to trace how his disaster developed.

As far as Frank was concerned, his only problem was *liquidity*, that is, his ability to repay those who had placed money with him *when they wanted it.* All Frank had to do was use the money in a way so that he could get it back quickly. But Frank did not really do that. He *seemed* to do it, but nevertheless he did not.

Frank invested the money directly in farms for himself, or helped to finance others to buy farms through him as agent. The question is: are farms "liquid"? Can you get your money out of farms quickly?

A quarter section of farm land (160 acres), the usual unit in Frank's territory, at $200 an acre, amounts to $32,000; at $400 an acre, $64,000. Buyers of units of that amount are not numerous. Right away the conclusion can be reached that farms of that kind are not easily and quickly sold. Try to sell such a farm on short notice (without a big discount in the price), and you will discover that farms are not (ordinarily) liquid. Bankers and banking law have, in fact, never considered farms to be "liquid assets." Frank, therefore, was going against experience, and rules based on experience.

Something must have deceived him. What might it have been?

Beginning around 1900 the territory in which Frank was operating had prospered greatly. Urban population was growing; transportation facilities to get products to markets had steadily been improved. Farm income in the territory had risen gradually from 1900 to 1915. Then, during World War I, and thereafter, farm prices rose very rapidly.

The rise in farm land prices from 1900 to 1915 could be largely ascribed to the economics of the territory. There had not been significant *general* inflation of prices, but locally the price changes had been caused by nonmonetary factors. But beginning in 1915 the situation became different. The Allies in Europe (England and France) urgently needed foodstuffs as their own production turned more and more to war materials. Demand for United States farm products became *abnormal.* That was obviously *temporary,* that is, would last only during the war and long enough afterward until normal conditions could be restored. In 1917 the United States entered the war.

What did the government do? It could have financed the war without inflation, namely, by severe taxation. What *could* have been done was not done, because it was considered politically inexpedient. The war was therefore partly financed by selling more government bonds than the people saved and bought. If government bonds had been issued only for as much as people cut down their consumption — that is as much as they really saved — then the bonds could not have been inflationary. But the government put out bonds which entered the money stream.

The method, despite complexities, is relatively simple. The government did not print paper money directly — "run the paper presses," as the expression goes — but did it indirectly. It did run the presses to *print bonds.* Then it "sold" the bonds to the banks who "paid" the government for the bonds by crediting the government's deposit accounts by creating circulation credit. And so, when that happens, printing bonds is *in effect* identical with printing money directly. What has happened is that the government has made itself the recipient of circulation credit, in big amounts.

More money, according to the quantity theory, always means some effect in the form of higher prices, and that is what happened in a big way in 1918 and 1919. The consequence was a big rise in prices of nearly all products, and especially of farm product prices, *and finally of farm land prices.*

What *seemed* to make farm lands liquid assets? Rising prices. Why? Because when the prevailing psychology was that six months later you could get twenty dollars an acre more for the land, people became eager buyers. A farm might be sold by *A* to *B* at $200 an acre; six months later it might be sold by *B* to *C* for $230 an acre; *C* in four months might sell the farm to *D* for $275 an acre; *D* might in a half year sell it to *E* for $330 an acre; *E* might resell it to *F* for $400 an acre.

The *turnover* of any commodity, including farm lands, increases far above normal when prices are rising. The more rapidly that prices rise, the faster the turnover.

But this "liquidity" disappears when the price rise ends. In fact, the *turnover* decreases to less than normal when prices decline.

Liquidity, in a boom, which depends on the issuance of circulation credit, always disappears when there is a stop to issuing circulation credit.

The average man thinks that price rises in a boom are normal and will continue. Only the *most exceptional* men know that the price rises are abnormal and temporary, and cannot continue indefinitely.

And so, the media through which the sure consequences of the immorality of circulation credit wreaks itself is through confusing and befuddling men *so that all their calculations are made erroneous and too optimistic.* The reality in the economic situation is no longer correctly appraised.

A return to a correct appraisal means a grave adjustment, known as a depression, before things can get back to "normal" again. The cause of the boom is the ultimate cause of the depression.

All liquidity which essentially depends on rising prices is a pseudo-liquidity.

The only kinds of loans bankers should make by using depositors' money is to borrowers whose ability to repay, whose liquidity, does not essentially depend on rising prices, but on uses where the turnover is naturally rapid and the need temporary. A liquidity which disappears with the ending of rising prices is a treacherous and not a real liquidity.

The Credit Jam In The Great Depression Of 1931-1934

A friend returned to the office one day during the Great Depression and told of a problem he had heard discussed at lunch.

A owed *B* $20,000; *B* owed *C* $20,000; similarly *C* owed *D; D* owed *E; E* owed *F; F* owed *G;* and *G* owed *H*. The total of these debts amounted to $140,000. And not one of these debtors could pay. *G* could pay *H,* only if *F* could pay *G; F,* however, could pay only if *E* could pay him, and so on back to *A*. If *A* could pay, then all could pay. Here was a jam of debts amounting to a considerable sum, just because the first man could not pay.

If, however, *A* could obtain $20,000, then presto, within an hour of time $140,000 of debt could be liquidated.

The question posed was this: why not get rid of this mountain of debt — $140,000 — by helping the first man in some way pay his $20,000 debt? But how do so? *Who* would provide him with $20,000?

Well, if *A* could not or should not be helped, how about washing out all the intermediate debtors and creditors, everybody from *B* to *G* inclusive, leaving only one debt left, namely *A*'s $20,000 debt which he would now owe *H*? However, *H* might not agree. He might not wish to relieve G of his debt to himself (*H*). *H* might consider himself left with the least-able-to-pay debtor in the series, the first man *A*. *H* will say to himself: "One of the rest in the series may some day be able to raise the $20,000, and then I can be paid. I do not wish to rely on *A* only."

But in any event, so the argument went, is it not folly to force seven men through bankruptcy when there is only one "culprit"? Why not help the first man in the series and save the other six from the same fate?

Then the situation was generalized in this manner: "It is because there are a lot of cases like this that the country is currently debt-ridden, and we are frightened about it; if only we could get rid of the 'multiplication' of the debt by dealing only with the ultimate debtor and the ultimate creditor, then we could solve our problem."

By this type of reasoning, it was believed, that a major contribution could be made to solving the depression problem of the early part of the 1930 decade.

The proper answer to these proposals is left to readers, who may prefer to work in their own way to "solve" this hypothetical problem. Let us here consider only the *origin* of the problem.

What probably was the origin? Almost certainly a series of debts of this kind would be the result of inflationism. Consider, as an example, the rising prices of farm lands in the inflation of 1915-1920: a farm may have carried a mortgage of $20,000; *A*, let us assume, owned the farm and owed the amount of the mortgage. How, probably, would a series of debts of $20,000 each arise as in the example posed? One way would be by the farm changing hands seven times, and each buyer assuming the mortgage. Each new owner, getting in his turn a higher price, would probably quickly reinvest his "profit" in still more land, or at least higher-priced land.

Maybe the farm had originally been worth $40,000. Recognize definitely that the price had gone up to $120,000. The difference between the $120,000 and the original mortgage had almost certainly been "used" and "re-used" by these investors (speculators?) in farm land. In rising markets people are reluctant to leave money idle. They rush into new investments.

But something had happened. The rise in farm land prices had stopped, and then a rapid decline had set in. All the "profits" had been wiped out by declining prices. The wealth each of these men thought he possessed had disappeared as vapor in the air.

And what was finally left to pay the $20,000 due on the mortgage on the land? Nothing but the farm itself, and just at that time the farm could not be sold to anyone for $20,000. Everybody might concur that the farm looked very cheap at $20,000, but nobody had the money, or at least nobody had the inclination just then to pay $20,000 to get the farm. In addition, all the men in the series were probably reluctant to have a general "settlement" at the prevailing depressed level of prices. They probably said to themselves, "Before that boom started the farm was worth $40,000. Sombody once thought it was worth even $120,000. Surely, it is worth more than $20,000." And so everything remained "paralyzed" without any settlement being made.

One thing is certain: the debt jam described was caused by falling prices; and equally certain, the debt mountain was originally piled up on the basis of rising prices.

Those rising prices, in turn, were caused essentially by *circulation credit.*

Are Bankers The Men Who Cause Depressions?

In a sense, bankers do cause depressions. They "cause" a depression when they become "alarmed" or "prudent" about the business situation, and, as their first reaction, cease putting out more circulation credit; and then, when still more alarmed, insisting on a reduction in outstanding circulation credit.

The earlier increased circulation credit which they had put out had operated like additional money, and had caused rising prices (according to the quantity theory of money). As certainly as more credit stimulates price increases, just as certainly a reduction in credit induces a price decline.

And so, bankers are the "cause" of booms and depressions, because they vary the amount of circulation credit. But really it is a grave injustice to bankers to make the charge against them that *they* cause booms and depressions. Everyone admits that bankers, as a group, are as honorable as any group in the country. They are most highly respected and properly so.

If bankers are not to be blamed for varying the quantity of circulation credit, who *is* to be blamed? The public, the citizens of the United States.

The banking laws of the land are the laws that the citizens want. Bankers merely react as anyone would react to the laws under which banking must be conducted. Change the law and then bankers will operate differently.

Bankers, however, should acknowledge a special responsibility. They ought to educate the public to the folly of the present banking law of the country. This is the "field" in which bankers are experts. They ought, therefore, to be in the front ranks of those who are endeavoring to end the issuance of circulation credit.

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IN MORALITY AND ECONOMICS
on which depend personal well-being and social health and harmony

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Banks Probably Do Not Charge Enough For Some Services Which They Perform

People, when they put money in a bank, consult their own interest — that is, they expect to get some advantages from having a bank account; but they often do not expect to pay much or anything for the service they get.

People do not like bank "service" charges, that is, special charges which banks make for the number of deposits and withdrawals, unless there is a cash balance in the account big enough so that the account is "profitable" to the bank. They say to themselves and others, "Why should the bank make a service charge? It has the use of my money." But what use? The depositor retains the privilege to draw all his money out *without notice*. How can a bank pay for the use of money which is withdrawable any day? Suppose the banker does "use" the money, and, when you want it, says to you: "We are *using* your money; sorry; you cannot have it today, nor for some time." Most depositors would not be pleased with such an answer and such a situation. The fact is that a bank cannot *use* all of your deposit, and it really exposes itself to danger when it uses *any* of your deposit.

Here are some of the advantages of opening a checking account:

(1) Your cash is *safe,* in the sense that it is not subject to loss by theft, fire, flood or disaster. This is a significant service, whether fully realized or not.

(2) The bank does a large amount of bookkeeping for you. For every action you take which affects your deposit, the bank must make its own corresponding record. At present-day costs of labor and overhead, the banks must incur considerable accounting expense to give you checking service.

(3) By providing you with checking account service, the bank saves you time otherwise required to pay bills personally by performing the errand. If you have a checking account, you merely mail the check. Checks are particularly labor-saving in regard to bills payable at some distance. The bank "clearing system" for cancelling out checks payable elsewhere is a large economy. You get the benefit of that when you have a checking account.

(4) Automatically, your cancelled check constitutes a receipt. There is less prospect of dispute whether or not you have paid a bill.

Unfortunately, the partial loss to banks on their inadequately-paid-for checking account service is made good by earnings on the unsound (but legalized) practice of issuing circulation credit.

The Quantity Theory Of Money Is Easily Understood

Problems of money are not the easiest in the world, and thinking about such problems may be disturbed by emotions of envy, covetousness and fear. But people can think their way through money problems, if they are reasonably thorough. In this little article on the quantity theory of money it is shown that no mystery is involved. Let us consider a farmer, a person usually without special training in money matters, and neither sharper nor duller than the rest of mankind.

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A farmer knows that if a crop is large, then the price per unit (all other things being equal) will be lower; and vice versa, if a crop is small, the price per unit will be higher. A farmer has a *quantity theory* of the price, say, of wheat.

A farmer will apply this rule to what he buys as well as to what he sells. He will always want the highest price he can get for what he sells, and the lowest price for what he buys — and consequently he will argue about price and be "unhappy" about it — but he will not fail to understand, nor will he dispute, the existence of the general rule itself.

Now, can such a farmer reason correctly about the *quantity of money,* about the effect of increasing its supply? Undoubtedly; and his conclusion will be: the greater the quantity of money, the lower its "price" must be.

What was the "price" of wheat? The answer is: whatever it will exchange for, either in the form of money or *other commodities.* "Price" does not need to be measured *only* in money; it can be measured in terms of other goods.

Now, the "price" of money itself cannot be measured in terms of money, anymore than the price of wheat can be measured in terms of wheat. Such an idea is nonsensical — to measure something by itself. The "price" of money must be measured in terms of other things, namely, how much of those other things it will buy. If the number of dollars is greatly increased, each individual dollar will buy less of other goods; just as each bushel of wheat buys less if there is a greater quantity of wheat. The quantity theory of money — that the more money there is, the lower its value — should be and undoubtedly is as understandable to a farmer as is the quantity theory of wheat in regard to wheat prices.

The difference between wheat and money is that everybody is familiar with measuring wheat *in terms of money.* But if money is to be measured, it must be in terms of wheat, or better, *in terms of all other commodities and services.* The price of money is measured against *all* commodities and services, rather than against wheat only (because there might be something special affecting the wheat situation).

The price of wheat is affected not only by the *supply* of wheat itself, but also by factors on the *demand* side; for some reason or other, people may wish to acquire less wheat because, say, they are eating potatoes instead. Similarly, other factors than the *supply* of money will influence the price of money. Suppose that the supply of goods suddenly is cut in half, but the quantity of money itself remains the same. Immediately, the price of goods will go up because the same quantity of money is being used to bid for a supply of goods only half of what it formerly was. This is the same thing as saying that the value of the existing money has gone down. In this case, the value of money has gone down *because the quantity of all other commodities changed.*

Price of anything is always a *ratio.* The ratio can be affected on either side, supply or demand. The quantity theory of the price of wheat looks at the problem of wheat prices from the supply side; the quantity theory of money likewise looks at the problem of the price (or value) of money from the supply side.

1. Whoever favors more money in total must, all other things being equal, be reconciled to less purchasing power per unit of money, that is, he can expect higher prices generally.

2. Whoever favors less money in total must, all other things being equal, be reconciled to more purchasing power per unit of money, that is, he can expect lower prices generally.

3. Whoever wants steady prices in total must undertake to vary the quantity of money in proportion that total goods and services offered vary in quantity — a task which unfortunately requires omniscience.

The foregoing three are all "managed" money systems. They rely on the judgment, caprice and cupidity of men. This is building a money structure on quicksand.

4. There is a fourth system for money, which in type is just the opposite of the foregoing three, individually and collectively. This fourth system is an attitude of not trying to increase the quantity of money to raise prices, nor to decrease the quantity of money to lower prices, nor omnisciently to increase and decrease the quantity of money to keep prices steady, *but to let prices be determined by the gold supply of the world.*

Presently, the people of the United States are pursuing — or rather they think they are pursuing — the course numbered three. By *people* is meant nearly everybody — merchants, industrialists, bankers, the country's money managers, congressmen, unions, wage earners, farmers, retired people. The "climate of thought" on money is to manage the quantity so that goods prices are steady. But what appears to be course three turns out in practice to be course one — inflation of the quantity of money, which results in inflation of prices.

In FIRST PRINCIPLES this third course is rejected categorically because the *management* of the quantity of money has NEVER yet been successful in the history of mankind. FIRST PRINCIPLES does not believe that the management of money will ever be successful. It favors instead the course numbered four. The most prosperous eras in the history of mankind have occurred when money was not "managed."

The consequences of the "management" of money are not revealed in a year, or ten years or even thirty years. It takes time for that supposedly wonderful management to deteriorate under the influence of pressure, cupidity and stupidity.

Rejection Of The Quantity Theory Of Money

What the common sense of the common man teaches him about the quantity theory of money, the technical knowledge of experts sometimes apparently obscures. There are wheat-price experts who suffer from the hallucination that they can modify the quantity theory of wheat prices. Similarly, there have been and are money experts who reject the quantity theory of money.

The greatest economists England has produced developed a school of thought known as Classical economics. The two most famous representatives of this school were Adam Smith (1723-1790) and David Ricardo (1772-1823). They accepted the quantity theory of money.

The men who came after them in succeeding generations split, in regard to questions of money, into two contending schools of thought — known as the Currency school and the Banking school. What divided them? One of the best historians of the history of ideas on money is the late J. Laurence Laughlin of the University of Chicago; see his *The Principles of Money* (Charles Scribner's Sons, New York, 1921). Laughlin declares that what divided these two schools of thought was the acceptance or nonacceptance of the quantity theory of money (page 264). The Currency school basically accepted the quantity theory, the Banking school basically rejected the quantity theory.

When chatting with a successful banker one day, the writer made a statement based on the quantity theory of money. The banker interrupted to say with some evidence of impatience and rejection: "Why that is nothing except the *old* quantity theory of money." He obviously did not accept it.

The quantity theory of money has, of course, qualifications and refinements. A crude statement of the theory can be objected to. But the objection to inexact formulation of the theory does not constitute a good ground for rejecting the basic idea of the theory.

There is no pretense that the simple formulation of the quantity theory here presented takes into account all the facets of the problem. To do so would make this analysis too technical.

But in regard to the fundamental idea underlying the quantity theory it is believed that there are no valid grounds whatever for disputing it.

In the great fight with the Banking school, the Currency school won in principle, upon the passage in Great Britain of the Bank Charter Act of 1844; but it lost in practice (see pages 246ff. in the August issue). The reason is that the Currency school was stupid about one thing, and left a loophole which wrecked the accomplishment of its purpose, and which has plagued the Western world since. The Currency school successfully attacked circulation credit in the form of bank notes, but *failed to include bank deposits in circulation credit,* an egregious blunder. Consequently, although the Act stopped putting out more circulation credit in the form of bank notes, it left wide open the putting out of more circulation credit in the form of bank deposits.

On what premise do bankers and the people of the United States generally reason today, the correct premises of the Currency school or the incorrect premises of the Banking school? Astonishingly, the premises really underlying American monetary theory and banking policy *today* are the false premises of the Banking school. And so the Currency school in 1844 won a battle, but lost a war, not only in England, but practically around the world. It successfully "sold" a sound idea, but flubbed the application of it.

The essence of the battle that the Currency school fought and seemed to win was that circulation credit is bad, really bad; there is no good in it; and no justification for it in practice or theory. But who in the United States is *in principle* against circulation credit? Practically nobody resists circulation credit except that *too much* should not be issued. The moral and economically sound answer is: *none* should be issued.

Money, In A Narrower Sense, And In A Broader Sense

Without being technical, let us look at money in two senses — in a narrower sense, and in a broader sense.*

In a narrower sense, money consists only of gold, or a metal suitable for money and used as money.

In a broader sense, money consists not only of gold but also of credit granted by those who presumably have the means to grant credit, or at least the authority to do so.

The dispute about money, in this age, is the credit part of it. But in order to understand what the modern trouble is, it is necessary to recognize that there are two kinds of credit rather than only one. One kind of credit, commodity credit, is inevitable and justifiable; the other, circulation credit, is unneccessary and inexcusable.

Our money, in the broader sense, then, consists of the following:

1. Metal, usually gold, but not necessarily gold;
2. Credit, (a) commodity credit; and/or (b) circulation credit.

Because commodity credit is inevitable, impossible to stop, and undesirable to stop, everybody with judgment approves it. But, although circulation credit is unnecessary, easy to stop and disastrous in its effects, nearly everybody nevertheless approves it.

Why is *commodity credit* good? Because it helps business. A farmer may have wheat, which he wishes to sell to the town miller. The miller shakes his head. He says, "I have no money with which to buy. I could not pay you until I sell the flour. I am 'paralyzed' to act. I would like to, but I cannot." To that the farmer may say, "I shall sell you the wheat *on credit;* I shall

*These expressions are borrowed from Ludwig von Mises' *The Theory of Money and Credit* (Yale University Press, 1953).

deliver it; you grind it; you sell the flour; and after two months you pay me, because you should be able to pay me by that time." On that basis the farmer delivers the wheat and the miller mills.

The farmer trusted the miller. His trust was manifested in the credit he granted the miller. The credit was "collateralized" by the commodity, wheat, or later, flour.

The miller may give the farmer a note, due in two months. The farmer may need the money before the two months has elapsed. He may then go to the town bank and say, "I need this money *now*. I will take less than the face value of the note, by an amount equal to five percent interest. I will endorse the note on the back so that you can collect from me, if the miller does not pay." The banker may have a deposit *received from a saver* with which he pays the money to the farmer. In that case the saver, through the banker as agent, is the real extender of the credit.

In any phase of this transaction there is no real *creation* of money or credit, but a *transfer*. Behind the credit is the wheat or the flour; or the savings of the bank depositor. This is genuine *commodity credit*. Upon payment of the note, the credit is retired or eliminated, whether extended by the farmer or through a banker.

Commodity credit, when limited to goods which are easily salable and which will probably be quickly sold, in general is safe. The credit transfer has a short life. Such credits do not get into the money stream *or stay there*.

There can be abuses of commodity credit, just as there can be abuses of many good things, as marriage, private property, liberty. The miller may be incompetent or dishonest. He may mill the wheat, sell the flour, spend the proceeds, and then be unable to pay the farmer. Is there then more money in the world, because that credit is outstanding? Indeed not; people do not unrealistically count assets twice. The farmer's possession of the miller's note will be considered of no value if the miller cannot or will not pay. What the miller spent, the farmer must abstain from spending. Such credits do *not* cumulate. They are staked down to reality.

The situation is different in the case of *circulation credit*. There is *nothing* behind circulation credit than the expectation or at least the hope that nobody will suspect it, and consequently that people will accept it and pass it on from one to another.

Suppose the miller wishes to buy 1,000 bushels of wheat. Suppose, instead of signing a few big notes, he makes a large number of smaller notes, say of one dollar each. Let us assume, also, that the miller is respected and trusted. He tells those who sell him wheat, supplies, etc., that the smaller notes will be more convenient for them. Further, he promises to pay cash on his notes, whenever his creditors need their money. He vaguely waves his arm to the groaning mill behind him, and says, "I have a lot of wheat, you know, in my elevator and silos and mill. You do not need to worry." And so, in order to buy 1,000 bushels of wheat and a modest amount of supplies, he may finally put out enough of his notes to equal the value of 5,000 bushels of wheat! And he may have little trouble doing so, because people do not present so many of his notes to him for real-money payment that he cannot cash them. Our miller friend has a "float" of notes not covered by real wheat, let us say, in value equal to 4,000 bushels worth of wheat.

Because people have trusted this miller on his receipts, they have enabled him to be an unsuspected and uncaught counterfeiter. He has bought merchandise equal in value to 4,000 bushels of wheat that he did not possess. This credit, which is not "covered" by a commodity, is called *circulation credit*. The law of the land permits — authorizes — encourages — bankers to do exactly what this miller has done, with, however, a certain limit. They are supposed to be public benefactors when they do that. They are acting in accordance with the *Five Times Principle* previously described; see the August 1959 issue, pages 238ff.

The law of the land does not permit a miller to engage in the malpractice just described. That it is malpractice everybody will recognize who considers counterfeiting money to be bad. The miller has manufactured "credit" as a counterfeiter manufactures bills. The miller has implied and pretended that there are ample commodities behind his notes. He pretends his notes represent commodity credit. Actually, he has only $1,000 worth of commodity credit, which he was once worthy to have; and he has $4,000 worth of circulation credit which he is not worthy to have.

The cause of confusion among those who favor circulation credit is their not distinguishing between circulation credit and commodity credit. They begin by defending commodity credit, which is easy enough to do, but end up finally in defending circulation credit under the good flag of commodity credit. Whoever is unable to distinguish between commodity credit and circulation credit will be unable to understand the problem.

Some correspondence on circulation credit recently came to our attention. One writer favored both commodity and circulation credit. But he did not keep the two separate. He defended circulation credit on the basis of the character of commodity credit. This is an inexcusable confusion or may be a very willful unwillingness to recognize a vital difference.

In the U. S., the total supply of money in the broader sense is not only gold and commodity credit but also circulation credit.

How Gold Exports And Imports Tell Which Country Is Putting Out The Greater Quantity Of Circulation Credit

Putting out more circulation credit means that there is more money (in a broader sense), and that will result, all other things being equal, in increased prices. This is another way of saying that the purchasing power per unit of money has decreased, just as more wheat makes the purchasing power per unit of wheat go down.

Thomas Tooke (1774-1858) one of the most famous of the representatives of the Banking School, was co-author with William Newmarch of a monumental study of prices, under the title, *History of Prices and of the State of the Circulation from 1792 to 1856,* which was designed to prove that the increased issue of circulation credit had not raised prices in England in the early part of the nineteenth century.

Both Schumpeter in his *History of Economic Analysis* (Oxford University Press, New York, 1955, pages 520ff.) and Laughlin in his *The Principles of Money* (page 265ff.) indicate that Tooke and Newmarch set out to prove that circulation credit in England had not tended to raise prices. Laughlin quotes from Tooke and Newmarch what they said in summary of their study of prices for the years 1793 to 1837:

> "The whole tenour of the facts and reasonings adduced has been to establish the conclusion that the great alterations of prices originated, and mainly proceeded, from alterations

in circumstances distinctly affecting the commodities, and not in the quantity of money, in relation to its functions.*

They also wrote:

> "As far as trustworthy evidence can be obtained, there are no facts in the experience of the last Nine Years (1848-1856) which justify the conclusion, that in this country the fluctuations of Prices . . . were immediately preceded by, or connected with, changes in the amount of the aggregate outstanding circulation of Bank Notes.**

Tooke's whole *approach* to the problem was wrong. He *set out to prove by statistics* that the quantity of money had not influenced prices. So many factors influence prices that the idea of statistical proof of the kind that Tooke and Newmarch mustered is absurd. The result is confusion. Schumpeter, who is in general a gentle critic, admits that Tooke was "woolly" in this thinking. No statistics that anyone ever musters will discredit the theory that the supply (quantity) will affect the price (all other things, of course, being equal).

It is possible, by statistical studies such as by Tooke and Newmarch, and by interpretations of such figures, to prove about anything you wish to prove; the wish is usually father to the thought.

It is not to be disputed that prices are the result of many factors. It is not disputed that an increase in the price of one commodity only does not prove that there is money inflation. It is not disputed that an index number of many commodities may give a rough indication of what has happened, although no general index number can be a really reliable index of what has happened and is happening to prices. Tooke and Newmarch may therefore have written an impressive book, and still have failed altogether to prove their case.

Whether prices in England were being influenced according to the quantity theory of money, by the issuance of circulation credit, could be ascertained with greater accuracy from *circumstantial evidence* than from statistical material. The proper manner to look at the text of Tooke and Newmarch is that it contained "much testimony but no evidence."

* History of Prices, II, pp. 350. [To this Laughlin adds this footnote:] Of course he admits that during the paper-money period the price level was raised to the extent of its depreciation as compared with gold (cf. II, 349); but this is the inevitable consequence of a fall in the value of the standard in which prices are expressed, and not necessarily of the increased quantity of the paper money."

** *Ibid.*, V, p. 344."

The conclusive evidence of the effect of issuing or withdrawing circulation credit in Great Britain, in the nineteenth century and until World War I, lies elsewhere, namely, in the movement of gold in and out of England. This mechanism, as proof of whether circulation credit is being increased or decreased, is worthy of examination and understanding.

Imagine two countries, say England and France, which trade together. If these countries are putting out circulation credit, as did the flour miller referred to in an earlier article in this issue, then the people in these two countries will not accept each other's paper money. They will want real money, *gold*. Let us assume then that England and France are both on a gold basis, and that both also put out circulation credit. When it comes to final settlement between the merchants of the two countries, then they will demand gold and refuse to accept paper money (circulation credit) of the other country.

Let us imagine that each country has one billion dollars in gold and five billion dollars in circulation credit; each then has a total of six billion dollars in money in the broader sense. That is the status of affairs at the beginning of our illustration.

Merchants do not trade within a country, nor with merchants outside a country unless there is mutual advantage to be derived from trading. Prices between countries for comparable merchandise are therefore never permanently significantly different, if there is free trade. Goods always move to where they can be sold most advantageously, which inevitably results in a tendency toward an equalization of prices. We shall assume there was free trade between England and France; therefore, prices would "tend" to equalize between the two countries.

Trade between France and England will have to be a "two-way" street. English merchants will sell some things to France and buy others from France. Similarly, French merchants will sell French wares to England and buy English wares.

Let us assume, now, that in a given period English merchants buy more French goods than they sell to France, and (consequently) that French merchants sell more French goods than they buy English goods. If the flows both ways were equal, the credits and debits would balance off. But they will not do so in the case here assumed. English merchants, because they have bought more than they sold, will have to pay for the surplus in money. As the French will not be willing to accept English *paper* money (money in the broader sense), the English will have to ship some of their billion dollars worth of gold (money in the narrower sense).

Why would there be this imbalance in sales and purchases? For one reason only — French goods were temporarily cheaper than British, which is why the English bought eagerly and the French were happy to sell. For the French, the price on the foreign sale to the British probably exceeded the price on the domestic sale in France.

Let us assume the English shipped $200 million of their gold to pay for the excess purchases from France. That would leave England with only $800 million in gold; but France would have $1.2 billion in gold.

The ratio of circulation credit to gold in England was assumed to be 5 to 1: or five billion to one billion. Now that one-fifth of the gold has been shipped out, the banks will feel obliged to reduce their circulation credit from five billion to four billion. British money will then be reduced in quantity from a total of 6.0 billion to a total of 4.8 billion. According to the quantity theory, British money would become more valuable, that is, prices of commodities will surely drop. When British commodity prices drop, British costs will drop (if there are free market conditions). Merchandise in England will now be lower priced — because there is less money.

Simultaneously, the contrary will be true in France. On the basis of 1.2 billion of gold the French will, if the old ratio is to be retained, expand their circulation credit to 6.0 billion, which added to the 1.2 billion of gold would provide a total of 7.2 billion of money. As a result of this increase in the quantity of money, French commodity prices will rise, and French costs will surely advance.

Now, the trade movement will be reversed. Whereas because French prices had previously been low, English merchants had bought more French goods than they had sold English goods to France, under the new situation the French will buy more British goods because they are cheaper, and the French will ship less goods because what they have to sell is dearer.

Now the movement of gold will be reversed. The French will be shipping back the gold which they had received from the English earlier.

Readers will become aware that it is not necessary to have Tooke's *statistics* to determine whether, relatively, prices for goods had increased or decreased in England. The movement of gold in-and-out of England was conclusive proof whether English prices were higher or lower than elsewhere. (Gold movements, temporarily, also have causes other than commodity price differences, but for simplicity sake, such details are here omitted.) When England was obliged to ship gold, that was evidence her prices were higher than prices elsewhere. When England contrarily gained gold, that was evidence her prices were lower than elsewhere.

The movement of gold tells more conclusively than anything else whether prices between countries have changed ratios, and which country, by means of circulation credit or otherwise, has increased its quantity of money more than other countries. (Again, other phases of international gold movements are not being considered here.)

For a hundred years after the Napoleonic wars the movement of gold was the agency by which international prices were kept in line. When gold drained out of a country, it was proof that that country had issued too much circulation credit relative to the circulation credit other countries had put out; and vice versa, when a country gained gold, it was proof that her prices were low, which in turn was proof that credit had been more severely rationed in that country than in other countries.

Gold movements, and not the statistics of Tooke or anybody else, tell whether circulation credit (or some other factor) has influenced prices in one country differently from another.

George Winder's, A Short History Of Money

A valuable book on money has been published this year in England entitled, *A Short History Of Money*. The author is George Winder, an attorney and economist from New Zealand, now retired and farming in Sussex, England. The book has only 188 pages and is of small format, but contains much valuable information. It is available in this country through the Foundation for Economic Education, Irvington-on-Hudson, New York, for $2.50.

In what follows, this remarkable book is used as a foil to permit contrasting what is proposed in FIRST PRINCIPLES with what appears in *A Short History of Money*.

* * *

There is a fundamental difference between what Winder thinks about money and what is presented in FIRST PRINCIPLES. In FIRST PRINCIPLES *all* circulation credit is condemned; it is against the further *creation* of money, and believes only in money that has been *produced*. Winder, contrarily, is against circulation credit *if its origin is a government deficit;* and he is also against circulation credit if it is based on nonliquid assets, such as land; but he does not condemn circulation credit originating as short-term advances to commercial borrowers. (That is his position, if we understand him.) He really fails to distinguish between commodity and circulation credit.

* * *

Winder's first chapter has the title, "Do Banks Create Money?" He begins with the basic observation that in ordinary business no one properly has money *unless he has first produced something or performed a service,* by which he obtained the money, and by which he therefore has legitimate purchasing power to get something else. This is the ultimate underlying *moral* distinction between those who honestly have money and those who do not, and Winder is admirably explicit about that. He thereby has condemned the counterfeiter who has not performed a prior service, and who is a *thief* when he uses his counterfeit money. But if banks create money in the form of circulation credit (just as a counterfeiter creates money in the form of bills) is that creation theft? To this Winder's somewhat surprising answer is *No*.

In his first chapter he quotes various authorities, who do declare that money is *created* by banks, but he does not quote with approval, but dissent. He disagrees with Marinner S. Eccles, formerly chairman of the Federal Reserve Board, who is reported to have said:

> The banks can create and destroy money. Bank credit is money. It is the money we do most of our business with — not with the currency which we usually think of as money.

Winder also quotes the well-known English economist R. G.

Hawtrey to the effect, "When a bank lends, it creates money out of nothing." But again Winder dissents. His reason is (so he declares) that it is not the bank which creates money, but the commercial customers of the bank. He insists that the banker is only an agent and not the originator of the credit. And so, he argues, the banks *themselves* do not create credit.

The fact remains, of course, that there *is* a credit granted. How does Winder resolve that? Consider a transaction between a wholesaler and a retailer. The wholesaler has some clothing to sell; he actually possesses the goods; he owns the merchandise. Of course, he wishes to sell the clothing. But the retailer does not have the money to buy; he can only pay *after* he has sold some or all of the clothing to consumers. What does the wholesaler do? He ships the clothing to the retailer *on credit,* that is, the retailer does not have to pay until (say) four months later; in that interval, he will presumably have sold enough of the clothing at the retail price to pay off the wholesaler at the wholesale price.

Let us assume that the retailer does pay off the wholesaler. What has happened: first, credit has been created; and second, credit has been destroyed (liquidated). The creator of the credit was the wholesaler; the "destroyer" of the credit was the retailer. If a bank were to enter into the picture, it would only be as an agent. Therefore, so Winder presents the matter, it is the *credit-worthy customer* (in this case, the wholesaler) who really extends the credit, *and not a bank,* if a bank participates. Therefore, Eccles, Hawtrey, The *Encyclopedia Britannica* and many (in fact, all) others must be wrong when they say that it is *banks who create credit. That* is how Winder negates the idea that banks create *circulation credit.* The *origin* of the credit, he says, lies elsewhere — with the business man.

But somewhere the reasoning must be awry, and despite the other extraordinary merits of his book, Winder has here overlooked something.

Surely, he is correct that the wholesaler in our illustration has extended credit. He has transferred a *commodity* credit, which is certainly legitimate and unchallengeable. The commodity credit is related to the commodity, *clothing.* It is an error to call the transfer of such credit *creation* of credit. The wholesaler has not really created purchasing power; he has let the retailer have the clothing; the receipt he gets for the clothing is not money *creation*.

The real money problem is not such *commodity* credits (which are economically and morally to be approved), but *circulation* credits (which are not economically and morally to be approved). What should Winder have done? He should have considered instead the *Five Times Principle* — under which there *is* creation of credit *by banks*. (Incidentally, in England the principle is the *Twelve-and-a-Half Times Principle,* because in England the custom is for banks to create 12½ times as much credit as their reserves. See Winder's book, page 139.)

Winder appears to do the same thing that Henry Thornton did (see his *The Paper Credit of Great Britain*), and begins with obvious cases of credit extension *on commodities*. Who can argue that a man who owns a commodity may not put it into the possession of someone who cannot immediately pay for it himself but who can sell it, and upon such sale get the money to pay the creditor. Such a loan is destroyed (liquidated) upon sale to a consumer and repayment to the lender, just as definitely as it came into existence when the clothing was transferred by the wholesaler to the retailer. Commodity credit is not immoral, because he who extends the credit does not *create* purchasing power. The retailer has more clothing, and the wholesaler has as much less. This is not *creation* but a *transfer*. That some papers have been created to evidence the transfers does not mean that there is "more money" in the world. Such commodity credit, although maybe sometimes imprudently extended, and maybe sometimes uncollectible, does not raise the price level in an unstable manner. As the Banking school (despite being wrong on the real issue) correctly insisted, such credits if wisely extended are self-liquidating, either upon payment by the debtor, or by the creator writing off his loss if the debtor cannot pay.

But all the foregoing has nothing to do with that quite different kind of transaction — the *Five Times Principle*. In this case, there is a genuine "creation" of credit. Winder has not met this real issue.

* * *

Winder's position is a sagacious, but nevertheless inadequate, "reversion to type." He apparently wishes to go back to the gold standard; on that issue he is eminently right. He is against government deficits, on which he is equally right. He is against government domination of a central bank, or the banks generally on which all experience in human history gives evidence that he is right. He is against monetizing government debts, on which many will agree with him, even those who are unfortunately not in agreement on the subjects previously mentioned.

What Winder is for is a return to the situation before World War I, before 1914. He in effect proposes a return to an *international gold standard,* and practices in conformity with that standard. Compared with what Winder proposes, what the world has today is a wretched deterioration. He argues powerfully and conclusively for a return to a far better past. But he proposes no amendments to the pre-World War I gold standard; FIRST PRINCIPLES does, namely, the elimination of *further increases* in circulation credit. We are for the old gold standard with that amendment; Winder, if we understand him correctly, is for the old gold standard without that amendment.

How does this difference show up? For Winder the *one* great problem today is *inflation.* If today the nations go back to the pre-World War I gold standard, inflation must inescapably end. For FIRST PRINCIPLES there are instead *two* main problems today, namely, (1) inflation *and* (2) *booms and depressions.* To solve those *two* problems, two things are necessary: (1) the world must go back to a gold standard (as Winder indicates); and (2) the world in addition *must discontinue the practice of authorizing circulation credit.* Winder's program will solve the inflation problem, but not the depression problem. FIRST PRINCIPLES' proposals will resolve both the inflation problem and the depression problem.

Toward the end of his book Winder makes some references to depressions, but they are incidental. The book does not seriously relate monetary policies to depressions. To anyone sensitive to the problem of depressions, Winder's smallish treatment of it is a conspicuous omission.

Not that *every* fluctuation in business can be completely leveled out by a sound monetary policy. Fortuitous events affect business, and it is unreasonable to expect a completely even course, at any time. But the business cycle, resulting from circulation credit extension and contraction, as experienced in 1907, 1921 and 1930-1934, can be eradicated by a sounder monetary system than this country or the world has ever had.

* * *

Winder thinks and writes as an Englishman. His sources of information are English, to wit, (1) the Classical school of Smith and Ricardo; (2) the men of the so-called Banking school; (3) Walter Bagehot, the famous financial essayist of a generation ago; (4) more-modern classicists as Edwin Cannan; and finally, (5) the various "moderns" of all persuasions (including even John Maynard Keynes!). See the bibliography which the author presents on pages 173 and 174.

The ideas which apparently have influenced Winder are limited to England and are therefore, in a sense, parochial; he quotes no German authors. In his bibliography he does not mention, for example, the work of Knut Wicksell who made a conspicuous contribution to the theory of money and money rates. And even more surprising, he makes no mention of the writings of Ludwig von Mises, particularly his earliest major work, published as long ago as 1914, with the significant title, *The Theory of Money and Credit* (English translation by H. E. Batson, published by Jonathon Cape, London, 1934; republished by Yale University Press, 1953, with a new Part Four, entitled "Monetary Reconstruction"). It is Mises who has reasoned with final cogency against circulation credit, because it is *the* cause of the business cycle. This most admirable source has apparently not influenced Winder, and may even be unknown to him. FIRST PRINCIPLES, in contrast, has been decisively influenced by Mises.

Winder is heir to the Classicists and the Banking school. We are heirs of the Classicists, then of the Currency school who were the real heirs of the Classicists, and finally decisively of the Neo-Classicists (Jevons, Menger, Böhm-Bawerk, Mises). In order to have an adequate theory about money, the easiest (and best) sequence of reading (we believe) is: Menger's *Principles of Economics;* Böhm-Bawerk's *Capital and Interest;* Adam Smith's *Wealth of Nations;* Ricardo's *Principles of Political Economy;* and Mises's *Human Action* and *The Theory of Money and Credit.* We accept that part of the writings of the Classicists (Smith and Ricardo) as is reconcilable with the Neo-Classicists.

Despite his reading apparently being limited to English writters, Winder's book is fascinating reading. Its great merit will be conspicuously apparent; and also where it falls short. None, except an extraordinary economist, could have said so much, so well, so simply, and in such small space.

* * *

The goldsmiths, long ago when they discovered that they could put out more receipts than they had gold, took to putting out false receipts. They *counterfeited* "money." Winder does not condemn it; this may be because he is too-familiar with it and because the practice was thoroughly incorporated into the English banking structure before World War I; see pages 36-39. Winder writes:

> But few doubt today that the goldsmith, in giving the world the forerunner of the bank note, performed a beneficial service to mankind.

We find it impossible to agree. This circulating credit of the goldsmith's, it should be noted, relied not on a *commodity* behind it, but merely on the receipts continuing to circulate (whence the name, *circulation* credit) *because* people trusted them; there was NOTHING behind some of the receipts except the foolish trust of the people who trusted the receipts.

* * *

That Winder, unfortunately, belongs to the Banking school of thought on money is evident from page 57. He argues in favor of circulation credit in the form of *deposit credits*. He writes about the Bank Charter Act of 1844 and the trend of economic events in the nineteenth century, as follows (our italics):

> The great increase in the supply of goods coming on to the market [in the burgeoning nineteenth century] would have met a too-slowly expanding supply of money, and the Quantity Law would inevitably have manifested itself in lower prices. That this fall in prices did not occur . . . is due to the fact that the Bank Charter Act of 1844 completely failed in its objects [namely, to end the issuance of circulation credit].
>
> It was based on the assumption that only two kinds of money existed — metal money and bank notes — whereas, . . . a third type was already acting as a medium of exchange for a very large part of Britain's trade. *Very fortunately, as we may suppose*, this third type of money [deposit credits] completely escaped the legislative net.

The ground that the author advances for favoring circulation credit is that putting out this *extra* money helped prevent prices going down. Here, for a moment, Winder seems to share the incomprehensible fear, which pervades the world, concerning *falling prices*. Elsewhere in his book he argues most excellently for fluctuating prices rather than fluctuating money; and when he does that he is most right. But here he lapses.

The *falling prices* to which he refers are not *disastrously* falling prices. The decline, if it had occurred, would have been steady, not irregular; maybe one or two percent a year. Further, every well-informed person would have expected it. Long-term contracts would have taken it into account; both borrower and lender would have adjusted interest rates accordingly. And so — just so people know what to expect — a drift of prices upward or downward is neutralized by the terms of contracts when contracts are made.

Slow trends in prices when dependent upon a natural phenomenon (such as the availability of gold) are far to be preferred over well-intentioned but unstable variations in the money supply *according to the judgment of fallible and weak men*. Nature is more stable than the judgment of men.

A long-term slow drift of prices is not a reasonable ground for tampering with the money supply. Business men are accustomed to radical changes in the prices of individual commodities. Interest rates may fluctuate 20 to 100 percent a year; stock prices on the New York Stock Exchange usually fluctuate *within one year* as much as 30 percent above and 30 percent below the average for the year; individual commodity prices fluctuate similarly. Business men, and everybody, adjust facilely to those *violent* fluctuations; it is not logical therefore to become apprehensive about slow, steady trends in prices.

* * *

Winder is complacent about booms. On page 99 he indicates that booms may be the result of unwise credits — in our language, too much *circulating* credit. He writes:

> However, the optimism of the business man is contagious, and sometimes this infection is caught by the banker. Too much money is lent, prices rise, and a boom eventuates. This susceptibility of banks has its advantages. It enables the business man to sieze a new market at the right time.

Here the author accepts the proposition that granting of unwise credit — "*too much* money is lent" — causes booms. The "too much" is always circulation credit. But the inevitable consequence of a boom is a depression, unless the alternative, namely, permanent inflation, is adopted (which is even worse, and to which Winder is adamantly opposed).

Unless capitalism rids itself of booms and depressions, caused by variation in circulation credit, it will probably be more and more surrendered in the direction of socialism and tyranny, by citizens who are alarmed by and irreconcilable to booms and depressions.

* * *

Winder says that the British Treasury controls the policies of the Bank of England. The Bank of England in turn dominates the commercial banks. British banks, he writes, are no longer free and virile.

A parallel statement can be made for America. The exigencies of the government of the United States determine the issuance of bills and bonds of the United States. The Federal Reserve Board cannot effectively resist such action by the United States Treasury. The Federal Reserve Board dominates the regional Federal Reserve Banks and through them or directly the commercial banks. The banks here are no longer free either, any more than they are in England.

What the public in England and in the United States knows as *banks* are merely branches, in the final analysis, of the central bank, and the central bank is a finance tool of the government.

* * *

The book has many striking and accurate statements, for example, page 145:

> The power of Governments to control the quantity of bank loans may be described as an attempt to substitute a flexible supply of money for a flexible price-and-wage structure.

That, indeed, is the choice: free markets versus a flexible money supply, which latter always means at least bad booms *and* depressions; or even worse, inflation. FIRST PRINCIPLES is for free markets and opposed to a flexible money supply managed by mortal men.

* * *

Chapters toward the end of the book, beginning with the twentieth, entitled "The Cause of Inflation" are written with extraordinary clarity and force.

Withal, a most remarkable book. Read it. Whoever does not understand money does not understand the problems of the age. This book will be very helpful — *with the one exception that it fails to condemn circulation credit, the cause of booms and depressions.*

"Love" In Christian Ethics Should Not Be Used To Designate A Sentiment

In Hebrew-Christian ethics the term, *love,* refers to an unsentimental, profound policy for conduct, rather than to an affection of any kind.

Love, in a legislated ethical sense in the Scriptures, does not refer to *affections* as between husband and wife; or parents and children; or between friends. It refers instead to *rules of conduct* between *all* people — those fond of each other as well as those not fond of each other; friends and enemies; lovers; parents and children; white and negro — everybody.

Love in the Scriptures does not mean to *like* and does not depend on *liking,* because liking is a relative term, and the minute *love* (as a term describing policy) is debased into *liking,* then the issue arises of liking *equally,* which is sure to become a preposterous demand and sanctimony.

A difficulty is that the word *love* means so many things, even in Scripture, such as, (1) unlicensed sex and infatuation, (2) liking, (3) preferential treatment, and (4) profound policy.

As an example of *love* in the first sense, namely, unlicensed sex, consider II Samuel 13:1:

> And it came to pass after this, that Absalom the son of David had a fair sister, whose name was Tamar, and Amnon the son of David *loved* her.

After feigning illness and getting everybody else out of the way, Amnon proceeded to ravish Tamar. Nobody will call this act of Amnon *scriptural love,* or declare that love in this case means something that is in conformity with the Law of God.

As an example of love as *liking* consider the relation between David and Absalom, (I Samuel 18:1):

> And it came to pass, when David had made an end of speaking unto Saul, that the soul of Jonathan was knit with the soul of David, and Jonathan *loved* him as his own soul.

This is a case of one person genuinely *liking* another. The *affection* in this case does not refer to a profound, universal policy, but a sentiment, a free act of the will, in a field where the will should remain unbound, namely, whom to like; and also whom to like more and whom to like less.

As an example of love as *preferential treatment,* consider Elkanah, the father of Samuel, and how he treated his two wives, Peninnah and Hannah. Peninnah bore Elkanah children, but Hannah did not. When going up annually to Jerusalem Elkanah gave "portions" to Peninnah and her children, (I Samuel 1:5a):

> But unto Hannah he gave a double portion; for he loved Hannah.

Elkanah apparently found it impossible to have *equal* affection for his two wives. His *preferential* sentiment toward Hannah is called "love." But preferential sentiment is not *love,* in its ethical, legislated meaning in the scriptural Law of Love.

In the New Testament, *affection* is enjoined upon the members of the church *among themselves.* This, too, is called *love,* but it is not the same thing as the profound policy derived from the Mosaic Law, correctly interpreted. Christ declared, in the Gospel of John, Chapter 13:34-35:

> A new commandment I give unto you, that ye *love* one another; even as I have loved you that ye also love one another. By this shall all men know that ye are my disciples, if ye have love one to another.

This is not universal legislation either, but group legislation, and the meaning of *love* here refers to favorable sentiment *among the brethren;* the quotation obviously *segregates Christ's followers from those who are not.*

* * *

In contrast, it should be noted that in the Sermon on the Mount Christ required that men *love* their enemies, but that does not refer to an affection for them but a policy toward them, namely, the universal policy taught in the Mosaic law. The content of that universal policy for conduct has five basic ingredients:

(1) Complete freedom in all inter-relations according to a man's own judgment, indeed according to his sovereign caprice, EXCEPT

(2) No freedom to coerce, debauch, steal or deceive anyone; PLUS

(3) A limited amount of charity, according to the judgment of the giver and not according to an enforceable claim on the part of a potential recipient; PLUS

(4) Patient and steadfast forbearance, that is, an adherence by you to number (2) foregoing, despite any other person doing to you those same forbidden things and thereby harming you; no revenge; no ill intent; and no action by you *except to help and correct him;* PLUS

(5) Educating the neighbor in the full import of the gospel, namely, endeavoring to persuade him to get *all* of his thinking straight on life and death, creator and creature, justice and mercy; but this gospel to be strictly education and no more — never any coercion to get it accepted.

Those are the constituent elements of *love* in the ethical legislation about *love* in Scripture. Such love pertains to *policy,* not sentiment.

* * *

The *great* elucidation of the Mosaic Law of Love by Christ in the Sermon on the Mount pertained to the item numbered (4) in the foregoing. Whenever Christ uses the word *love* in the Sermon on the Mount, He means by the term everything that the Law stood for historically plus something wholly distinct from affection, to wit, patience, forbearance, absence of revenge and existence of good will, that is, *a utilitarian approach to the "enemy" in order to help him to reform.* The word *love* is used in *that* sense only in Matthew 5 and 6. Again, it refers to *policy;* not to *affection.* (Contrarily, in John 13, love refers to affection among the brethren, and self-sacrificing conduct between them.)

* * *

The Law of God requires you to "love" me, but it does not require you to like me. And it certainly does not demand that you like me *equally* with all others. It will be a messy world if the *love* required in Matthew 5 and 6 is extended to include the emotion referred to elsewhere in Scripture as love; imagine your neighbor extending the meaning of love in Matthew 5 and 6 to the meaning in II Samuel 13:1, and treating your sister according to Amnon's demonstration of "love."

When there is reference in FIRST PRINCIPLES to *love,* it refers to a *universal policy for conduct* and not any sentiment of liking, whether noble or ignoble, sexual or preferential.

Th Hebrew-Christian religion is too wise to command that all men *like* each other, or worse still that they like each other *equally* — a proposition that is ridiculous and that properly breeds contempt for any religion which teaches it.

The Mess In Corinth

The Apostle Paul, in the first century of the Christian church, established a congregation in Corinth, Greece, and he subsequently wrote them two letters, known in the Christian scriptures as the First and Second Epistles to the Corinthians. In I Corinthians 13 there is an apparent paeon, or glorification of *love.* Two aspects of this paeon will be discussed: (1) Why was it interjected into the epistle? and (2) What is meant by the term *love* in this chapter; does it refer to a sentiment of affection or a policy of conduct?

The Unwarranted Insulation Of The Thirteenth Chapter

Unfortunately, the First Epistle to the Corinthians has been subdivided by editors into chapters and verses, thereby obscuring its coherence and *divorcing the chapter from the context.* The context includes, in this case, two long chapters surrounding chapter 13, namely, the 12th and the 14th. Without realizing the significance of the context, people read chapter 13 *in abstracto,* as if it were an unattached and universal idea. Whenever that is done, the chapter is inescapably misread and becomes irrational.

Chapter 12 describes a bad situation in Corinth. Chapter 14 contains a reprimand. Chapter 13 is sandwiched between for two reasons; first, the lamentable situation at Corinth was a violation of a sound idea of *love,* as a profound policy for conduct; and second, Chapter 13 sugar-coated the bitter pill which Paul administered in what is chapter 14.

The Corinthian Mess

Paul covers many subjects fast in his Epistle. Ignoring the earlier subjects, in what is chapter 11 in present-day Bibles, he writes about the hair-do of women (a not too profound subject for a widower or bachelor to discuss); and he deplores very bad practices, including drunkenness, at their communion celebrations.

Then he comes to what is known today as chapter 12, and he there describes the turbulent meetings of the Corinthians. One person, believing himself to be a prophet, shouted prophecies; another, considering himself inspired, muttered gibberish — a phenomenon which was known in Corinth as "speaking in tongues"; Paul makes it unmistakably clear that this "speaking in tongues" was not understandable, a chaos of sounds; then there were faith healers, who had the "gift of healing"; others who taught "wisdom" and "knowledge." However marvelous — or imaginary (everybody is entitled to his own opinion) — these "gifts" were, they apparently had a common characteristic, they did not do other people much good; or, if they did not, the possessor of the gift apparently did not care much about it. He apparently went on teaching "knowledge," healing in his style, prophesying, uttering ununderstandable sounds — all on his hown. There was a lack of proper order, edification or coordination.

The 12th chapter (which must be read with the 13th in order to understand the latter) *teaches cooperation* by means of a homely and appropriate illustration. Corinth obviously lacked real cooperation, and Paul urged genuine cooperation. To make his point, he comments on the *cooperation* between the parts of the human body. He says that each part of a human body needs the other part; they must *cooperate:*

> *I Corinthians 12:12-25:* For as the body is one, and hath many members, and all the members of the body, being many, are one body; so also is Christ. For in one Spirit were we all baptized into one body, whether Jews or Greeks, whether bond or free; and were all made to drink of one Spirit. For the body is not one member, but many. If the foot shall say, Because I am not the hand, I am not of the body; it is not therefore not of the body. And if the ear shall say, Because I am not the eye, I am not of the body; it is not therefore not of the body. If the whole body were an eye, where were the hearing? If the whole were hearing, where were the smelling? But now hath God set the members each one of them in the body, even as it pleased him. And if they were all one member, where were the body? But now they are many members, but one body. And the eye cannot say to the hand, I have no need of thee: or again the head to the feet, I have no need of you. Nay, much rather,

those members of the body which seem to be more feeble are necessary: and those parts of the body, which we think to be less honorable, upon these we bestow more abundant honor; and our uncomely parts have more abundant comeliness; whereas our comely parts have no need: but God tempered the body together, giving more abundant honor to that part which lacked; that there should be no schism in the body; but that the members should have the same care one for another.

Paul calls attention to what all good observers note sooner or later, and what Socrates and Plato had also noted, that people differ in talents. There is *no equality* in creation. To the contrary, an outstanding characteristic of the world is diversification of abilities. Such diversification can enrich life, *if each person becomes an expert in the field where his interests and talents lie, and leaves other fields to others with other talents, and if the various experts then exchange their surplus production obtained from their own specialization.* There was specialization in Corinth, but inadequate cooperation. The activities were semi-useless and the subjective attitude was apparently such that an *exchange of real services* was not possible. This was especially true of the Corinthian gift of "tongue" which consisted purely in emitting meaningless sounds. Chapter 14 makes that clear:

I Corinthians 14:1-9: Follow after love; yet desire earnestly spiritual gifts, but rather that ye may prophesy. For he that speaketh in a tongue speaketh not unto men, but unto God; for no man understandeth; but in the spirit he speaketh mysteries. But he that prophesieth speaketh unto men edification, and exhortation, and consolation. He that speaketh in a tongue edifieth himself; but he that prophesieth edifieth the church. Now I would have you all speak with tongues, but rather that ye should prophesy: and greater is he that prophesieth than he that speaketh with tongues, except he interpret, that the church may receive edifying. But now, brethren, if I come unto you speaking with tongues, what shall I profit you, unless I speak to you either by way of revelation, or of knowledge, or of prophesying, or of teaching? Even things without life, giving a voice, whether pipe or harp, if they give not a distinction in the sounds, how shall it be known what is piped or harped? For if the trumpet give an uncertain voice, who shall prepare himself for war? So also ye, unless ye utter by the tongue speech easy to be understood, how shall it be known what is spoken? For ye will be speaking into the air.

Then Paul admonishes them to be less puerile, less childish, and urges them to grow up (verse 20):

Brethren, be not children in mind: . . . but in mind be men.

Later, in chapter 14, Paul writes (verse 23):

> If therefore the whole church be assembled together and all speak with tongues, and there come in men unlearned or unbelieving, will they not say that ye are mad?

In order to hold down the extent of the disorder he writes (verses 27 and 28):

> If any man speaketh in a tongue, let it be by two. or at the most three, and that in turn; and let one interpret: but if there be no interpreter, let him keep silence in the church; and let him speak to himself, and to God.

In verses 18-19 of chapter 14 Paul delivered himself of strong words of thanks to God:

> I thank God, I speak with tongues, more than you all: howbeit *in the church* I had rather speak five words with my understanding, that I might instruct others also, than ten thousands words in a tongue.

Apparently, Paul himself did not speak in "tongues" in public. Finally, his toleration shows up again, in what are the two last verses in chapter 14 (our italics):

> Wherefore, my brethren, desire earnestly to prophesy, and *forbid not to speak with tongues.* But let all things be done decently and in order.

An ordinary missionary would probably have thrown up his hands in disgust about the situation in Corinth, and turned it loose to its own end. Drunkenness at communion, incest tolerated among members, chaotic disorder at meetings — none of these things daunted the great Apostle.

Whereas chapter 12 outlined the problem and in a metaphor stated the solution, namely, *genuine cooperation,* chapter 13 describes the character of the cooperation — and it is that practical *cooperation,* not sentiment, which is called love (or *charity*); further, chapter 13 follows the universal practice of talking about something nice before the truth is plainly told, and so chapter 13 cushions the heavy blow to their pride that Paul was intending to administer to the Corinithians in what is chapter 14. In short, chapters 12, 13 and 14 are an *inseparable* unit. What is taught refers to a specific situation, and should not brashly and indiscriminatingly be generalized.

Love (or Charity)
In I Corinthians 13

Chapter 13 contains 13 verses. The first thing to do is to remove the verses which do not describe what love is.

The first three verses are not description but refer to that Corinthian extravagance, known as "speaking in tongues," and hence they begin as follows:

> If I speak with the [meaningless sounds] of men and angels, but have not love [cooperation], I am become sounding brass, or a clanging cymbal.

This is a shocking way to put it, but it fits the context. The idea that *tongues* here refers to sound sense or grand oratory, or celestial music, does not fit, although that *is* the way it is usually interpreted.

At the end of the chapter, verses 8-13 do not define either. The basic idea in these verses is the same as in chapter 14: please grow up, and get rid of ridiculous and childish actions.

That leaves the inbetween verses, from 4-7 which describe aspects of love (or charity), the aspects that should be learned and heeded in Corinth. (There is no evidence that this was a *general* definition of love.) These verses read as follows:

The Text:	The Virtue Referred To:
LOVE:	
suffereth long	patience (not an affection)
is kind	not vengeful (not an affection)
envieth not	good will
vaunteth not itself	modesty
is not puffed up	modesty
doth not behave unseemly	good order
seeketh not its own	modesty (not outshouting another)
is not provoked	patience and forbearance
taketh not account of evil	forbearing
rejoiceth not in unrighteousness, but rejoiceth with the truth	appreciation of good sense and morality
beareth all things	patience
believeth all things	kind interpretation of the failings of fellow Corinthians
hopeth all things	optimism that things will improve
endureth all things	forbearance
never faileth	perseverance in well-wishing and well-doing

The emphasis throughout is on *objective virtues* rather than subjective sentiment.

No part of the foregoing can be interpreted as living *for* others as distinguished from *bearing up under the shortcomings* of others. In an earlier *negative* statement the Apostle had said (I Corinthians 13:3):

> And if I bestow *all* my goods to feed the poor, and if I give my body to be burned, but have not love, it profiteth me nothing.

Giving up life and property for others is here described as not being the *love* to which Paul refers.

In the context, what Paul means by love is *cooperation* among men, which consists in two elements (1) it must be useful, so that (2) it can be exchanged. As the hand is useful to a body, or an eye, so the activities of individuals must be useful to each other.

This exchangeability, resting ultimately on the natural diversification of talents among people, becomes profitable in proportion to the *proper* exercise of special talents by each. This is nothing else than a nontechnical statement of what was later formulated as an economic law by David Ricardo, and which is known by the name of Ricardo's Law of Association (see Volume IV, page 200ff.). Underlying this law are the basic elements of the Hebrew-Christian Law of Love which were summarized in the preceding article.

There is in I Corinthians 13 no reference to violence, theft, or fraud. There *is* reference to envy. There *is* reference to charity, in the sense of alms. There *is* reference to giving evidence of good will and getting thinking straight; consider the Apostle's admonitions in the preceding and succeeding chapters.

But is chapter 13 a paeon of praise of an emotional sentiment of affection? Not as we read it. The *subjective* element that would constitute an attitude is here reduced to *objective* significance by recommending cooperation, consisting (1) of being useful rather than a fool, (2) of judging all action in a pragmatic way — is it any good to others? (3) of being patient and forbearing with those who fail to live up to (1) and (2); and (4) by kind admonition urging them to grow up, be less childish, and be men.

I Corinthians 13 contains a very limited definition of *love,* and boundless generalizations about love based on this chapter are unwarranted.

The Testimony Of St. Augustine On Miracles

Montaigne wrote the following about St. Augustine:

> When we read in Bouchet the miracles of St. Hilary's relics, away with them: his authority is not sufficient to deprive us of the liberty of contradicting him; but generally and offhand to condemn all such like stories, seems to me a singular impudence. That great St. Augustine testifies to have seen a blind child recover sight upon the relics of St. Gervaise and St. Protasius at Milan; a woman at Carthage cured of a cancer, by the sign of the cross made upon her by a woman newly baptized; Hesperius, a familiar friend of his, to have driven away the spirits that haunted his house, with a little earth of the sepulcher of our Lord; which earth, being also transported thence into the church, a paralytic to have there been suddenly cured by it; a woman in a procession, having touched St. Stephen's shrine with a nosegay, and rubbing her eyes with it, to have recovered her sight, lost many years before; with several other miracles of which he professes himself to have been an eyewitness; . . .
>
> — Montaigne, *That It Is Folly To Measure Truth And Error By Our Own Capacity*

Catholics and Protestants alike lean heavily on St. Augustine. Montaigne elected to accept the testimony of St. Augustine on miracles, but to reject that of St. Hilary. In effect, Montaigne here argues for liberty of judgment on these matters.

"The only purpose for which power can be rightfully exercised over any member of a civilized community, against his will, is to prevent harm to others. His own good, either physical, or moral, is not a sufficient warrant."

— John Stuart Mill

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FIRST PRINCIPLES
IN MORALITY AND ECONOMICS
on which depend personal well-being and social health and harmony

VOLUME V DECEMBER, 1959 NUMBER 12

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The Cause Of Depressions

If neither *general overproduction* nor *shortage of money* causes depressions, then what does?

The *cause* of depressions is remote from observation; therefore, the explanation must begin some distance from the observed effect. An illustration can be drawn from physiology. There are various causes for kidney stones. The natural thing is to seek the cause in the kidneys themselves. But *one* cause of kidney stones is known to be a pea-size tumor on one of the four thin parathyroid glands in the throat, which are no bigger than finger nails. The cause of depressions and depressions themselves are as remote as the throat is remote from the kidneys.

In this explanation the following questions will be considered:

1. What is *interest on money?*
2. What is *interest* in a broader sense?
3. Do the Hebrew-Christian Scriptures forbid interest?
4. What determines the interest rate?
5. How does lowering the interest rate cause booms?
6. How do booms, *inevitably*, end in depressions, or in something even worse?
7. A summary, answering the question: Who and/or what causes depressions?

I. WHAT IS INTEREST ON MONEY?

If you have $1,000, and if you let another use that $1,000 for one year, he will be willing to pay you say 5% on that amount, or $50, for the *use* of the $1,000. At the end of the year he will pay back to you $1,050.

It *appears* then that interest is a reward for the *use* of money, but "things are not what they seem." The root cause of interest is not *use*.

Many people erroneously think that interest is intrinsically a monetary phenomenon. They apply illogically the "quantity theory" of money to interest rates. They reason as follows: (1) increasing the quantity of anything lowers the price; (2) the "price of money" is the interest rate on money; (3) increasing the quantity of money will therefore lower the interest rate; and (4) consequently, in order to lower the interest rate, the thing to do (so they say) is to increase the quantity of money.

This reasoning is *logically* false, and it is (consequently) also *historically* false. A modern example will make the point clear. In Brazil the quantity of money is being increased rapidly. That being true, the interest rate should be very low in Brazil. The fact is that in Brazil banks have been charging 20% interest per year on *cruzeiro* loans. There *must* therefore be something wrong with the idea that increasing the money supply lowers the interest rate. (The *cruzeiro* is the Brazilian money unit.)

Nevertheless, the idea is so plausible that it is difficult to disabuse oneself entirely of the thought that increasing the quantity of money will lower the interest rate. It is necessary to remember that (1) according to the quantity theory of money, prices of goods increase when the supply of money is increased (other things being unchanged); but (2) it is an altogether different proposition to say (by a misapplication of the quantity theory of money) that interest rates will decline when the supply of money is increased.

The quantity theory of money does not have *two* propositions in it, namely, (1) that increasing the quantity of money raises the prices of goods and services, and (2) that it cheapens the cost of money in the form of lower interest rates. Instead, it should be reiterated: the quantity theory of money has one and only one clause in it, to wit, increasing the quantity of money increases the prices of goods and services — that, and that *only;* it does *not* lower the interest rate.

We are here talking about the total money supply and the over-all rate of interest. In some *narrow* segment of the total

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market the rate of interest may be affected, or the total market may be *temporarily* affected. If in San Francisco for some special reason half of its loan money supply is shipped to Pittsburgh, then the bankers in San Francisco will be obliged to ration their remaining loan funds and they will do so by loaning only to those able and willing to pay higher rates. Contrarily, in Pittsburgh, the bankers who have the increased supply of loan money will wish to put it to work, and in order to do so they will lower interest rates. But the lower rate in Pittsburgh is offset by the higher rate in San Francisco. A rate at *a time,* and at *a place,* may be affected by the supply of loan money. But then there must be an offsetting situation elsewhere.

It might be argued that the illustration has been slanted; what, it might be asked, will be the situation if the loan money supply is increased in *both* San Francisco and Pittsburgh? But again the question must be asked, where did the extra money come from? If from elsewhere, then the rates will be as much higher elsewhere as they are lower in San Francisco and Pittsburgh.

If it is assumed that the increased supply of loan money in San Francisco and Pittsburgh came from nowhere else, but was newly mined or "manufactured," the eventual consequence in those two cities will be that prices will rise, according to the quantity theory of money. The additional supply of money will not do better work than the old supply, but will create a *temporary* illusion of prosperity. *When the increases in the prices of goods and services fully reflect the increased supply of money (according to the quantity theory), then the subsequent demand for loan money will be as intense as formerly, and the artificially lowered interest rate will be replaced by the old interest rate.* Prices will be higher, but interest rates will not be lower. Increasing the supply of money cannot do more than lower the interest rate *temporarily.*

There is nothing new in the foregoing. David Hume (1711-1776) long ago clearly stated what the situation is. In his essay "On Interest" (*Essays Moral, Political and Literary,* Grant Richards, London, 1903 edition, pages 303ff.) he wrote:

> Lowness of interest is generally ascribed to plenty of money. But money, however plentiful, has no other effect, *if fixed,* than to raise the price of labour. Silver is more common than gold, and therefore you receive a greater quantity of

> it for the same commodities. But do you pay less interest for it? Interest in Batavia and Jamaica is at 10 *per cent*, in Portugal at 6, though these places, as we may learn from the prices of every thing, abound more in gold and silver than either London or Amsterdam.
>
> Were all the gold in England annihilated at once, and one and twenty shillings [of silver] substituted in the place of every guinea [of gold], would money be more plentiful, or interest lower? No, surely: we should only use silver, instead of gold. Were gold rendered as common as silver, and silver as common as copper, would money be more plentiful, or interest lower? We may assuredly give the same answer.
>
> * * *
>
> All augmentation has no other effect than to heighten the price of labour and commodities; and even this variation is little more than that of a name. In the progress towards these changes, the augmentation may have some influence, by exciting industry; but after the prices are settled, suitably to the new abundance of gold and silver, it has no manner of influence.
>
> An effect always hold proportion with its cause. Prices have risen near four times since the discovery of the Indies; and it is probable gold and silver have multiplied much more: but interest has not fallen much above half. *The rate of interest, therefore, is not derived from the quantity of the precious metals* [that is, money]. [Our italics.]

Interest rates are not made high or low by varying the quantity of money. Although we shall not follow Hume exactly, this is what he wrote (page 305):

> High interest arises from *three* circumstances: a great demand for borrowing, little riches to supply that demand, and great profits arising from commerce: and [those] circumstances are a clear proof of the small advance of commerce and industry, not of the scarcity of gold and silver. Low interest, on the other hand, proceeds from the three opposite circumstances: a small demand for borrowing; great riches to supply that demand; and small profits arising from commerce: and these circumstances are all connected together, and proceed from the increase of industry and commerce, not of gold and silver.

Men in general determine the interest rate. They do that by a simple (for most people, unconscious) method. What this is, is easily explained and understood.

Men "discount" time. By that is meant that they value present goods higher than future goods. Material goods which are *very* remote-in-time men consider valueless.

If one man undertook to promise a friend $1,000,000 one thousand years hence, the friend would treat it as a joke. What good would the $1,000,000 be to him, if he was already 950 years in his grave, and his grave maybe unknown? And his Santa

Claus friend just as dead physically as he would be? In this case "time" has "discounted" the $1,000,000 down to zero.

Suppose, however, that a father promises a son $10,000 ten years hence and, in order to "guarantee" that, he gives his son a note for $10,000, due in ten years. Let us assume the father's assets are so substantial that the note is indubitably good. Let us assume that the father wishes the son to get the money only after ten years, but that the son is undutiful and as soon as he gets the note, he goes to the bank and asks the bank to "buy" the note. Will the bank pay him $10,000? Indeed not. If it did, it would be giving the young man $10,000 *now*, but it would have to *wait ten years* before it could get the $10,000 from the father. No one, possessing judgment, would evaluate $10,000 ten years hence to be worth $10,000 now. It is because the understanding of that idea is not limited to bankers, that bankers do not control the interest rate. They are merely a part of the machinery by which the interest rate is determined, but the people who determine the interest rate are a combination of the thrifty and the spendthrifty; those who save, and those who want funds to invest either in capital goods, or to spend before they themselves have earned it.

What will a banker pay for this note of $10,000?

Let us first assume two things: (1) that the prevailing interest rate is 5%, and (2) that the note is only for *one* year. Then the bank will pay the young man the quotient obtained by dividing $10,000 by 1.05, or $9,523.81, a difference of $476.19 which is the *discount*, or in more inaccurate terms, the *interest*. If the interest rate is 4% or 6%, the divisor would be 1.04 or 1.06.

If the note was for two years, the next step would be to divide the $9,523.81 by 1.05 again, to which the quotient would be $9,070.29. If the note was for three years, the $9,070.29 would again be divided by 1.05, or $8,638.37.

Similarly, back to the tenth year. The figure would be $8,227.02 for the fourth; $7,835.26 for the fifth; $7,462.15 for the sixth; $7,106.81 for the seventh; $6,768.39 for the eighth; $6,446.09 for the ninth; and finally $6,139.13 for the tenth year.

The shrinkage from $10,000 to $6,139.13 is $3,860.87, which is the *discount* — the lower valuation — because of the lapse of time, on $10,000 due only after ten years, at a 5% discount rate per year.

Interest is not a reward for productivity, direct or indirect. John Calvin, although an acute thinker on interest, made that mistake. He said that interest on money was paid *because* the money could have been put to use to buy land which would yield a rent (that is, would be productive), and so there would have to be interest paid on money, or otherwise people would invest only in land and would refuse to loan money itself. The argument is good as far as it goes, but finally explains nothing, because rent itself needs to be explained, something which Calvin did not think of undertaking.

If an acre will produce 40 bushels of wheat, which will sell at 50c per bushel more than the cost (except rent) to produce it, or $20 net per acre, why should not that one acre sell for 10,000 years x $20 = $200,000 an acre? Or why not price that acre on the basis of its yield in 1,000,000 years (1,000,000 x $20 an acre), or $20,000,000 for that one acre of land? Why not go further, into infinity by using infinity as the multiplier? If yield times the profit from producing wheat — *without discount for time* — will produce that much money, why does land not sell for such fantastic figures? Obviously, there must be a *discount* for something somewhere in the calculation.

The fact obviously is that land is not *priced* on its yield only. It *appears* that way, but it is not. Let us lower the years to a more modest figure. Why should not land sell at least at what it will yield in one man's lifetime of 80 years? In 80 years it will yield 80 x $20, or $1,600. Shall we then price this acre of ordinary farm land at $1,600? If so, then the yield in percentage will be the quotient of $20 divided by $1,600, or 1.25%. Land does not sell to yield only 1.25%. And so yield, or productivity does NOT alone determine the rent on land, and consequently *cannot* be the basis of money interest, as Calvin erroneously reasoned.

Something else determines the rate of interest — and that something else is the *discounting, by men in general, of future values to a present basis.*

By *how much* men estimate the value of future goods to be lower, they *discount* the value; that is the *discount rate,* or as it is also called, the interest rate. *Discount* is the *descriptive* word.

Despite that fact, many business men consider interest to be a manifestation of *productivity,* or a reward for *abstinence,* or a payment for *use.* These are fallacies. Labor union leaders, contrarily but almost equally universally (following Marx), believe that interest (and rent and profit) is something filched from the working man, and so is *exploitation* of the employee. This explanation is equally erroneous. It also is a fallacy.

That interest is related to time is evident from the fact that interest is *noncomputable except on a time basis. Time* is of the *essence.*

II. WHAT IS INTEREST IN A BROADER SENSE?

The simplest return, or income, that a man can think of is a reward for labor. Even Adam had to work to get an income. The fruits — apples, pears, berries — on which he subsisted did not fall into his mouth. He *had* to *work.*

Men can be in any of three categories:

1. A man can be a wandering hunter for game, a wandering fisher for fish, or a wandering berry picker in season. *This is the poorest living that there is.* It is the hardest work; and the most precarious living. Adam was in that class during his early life. Moses makes that clear in Genesis.

2. A man can be a tiller of the soil, or a caretaker of flocks. Then he no longer wanders. He has some elementary tools. He can survive better than as a non-tiller. Cain and Abel advanced to this higher level of subsistence. Cain was a farmer and Abel a shepherd. In the cases where a man is a mere hunter, fisher or berry picker, he depends really on what raw nature provides.

3. The third step, from tillage to capitalism, is greater than from hunting to tillage. *Prosperity* for men, as distinguished from hazardous survival (hunting), and poverty (mere tillage), depends on something God did not create — namely, capital. *Capital* is natural forces, harnessed or guided or converted by men, so that the strength of those natural forces works *for* men. A simple example is the work of a steam engine. The *power* depends on natural law — the conversion of water into steam, and the use of steam pressure to do *work.* (See Volume III, pp. 266-297.) Capital is, therefore, extremely valuable to man. In a

figurative sense *an eighth day of "creation"* might be declared to exist, namely, that on the eighth day man (not God) began to *"create"* capital. (See Volume III, pp. 266-288.) When *capital per capita* increased, then human material prosperity increased.

On what then does production and income depend? Apparently, on several things: (1) labor, remunerated as wages; (2) natural resources, remunerated as rent; (3) capital, remunerated as profit; or (4) use of money, remunerated as interest. This list, although pat in form, is deceptive. Rent is *not remuneration* to natural resources; profit is *not remuneration* to capital; nor is interest a *return on money* — in the sense that most people understand that.

Profit, rent and interest (in an economic sense) are the same thing under different forms. (The most ambiguous of these terms is *profit*, but it will be unwarranted digression to go into detail.) The origin of all three rests in *time* — that discounting of future values to a present basis.

This often appears in an inverse form, not so much in the pricing of a future good lower (as in the *discounting* of the $10,000 note just explained) because of the time factor, but in the form of adding something to the present value in the form of an "interest" charge. Instead of working back from the future to the present *by discounting,* it is also possible to work forward from the present to the future *by addition.* For example, a man loans you $1,000 now and you pay him back at the end of the year $1,000 plus $50, or $1,050. To make the future value equal to the present standard, something had to be *added* to the present base. It is "six of one" or a "half-dozen of the other" whether (in the previous illustration) $3,860.87 is added as ten years' compound interest on $6,139.13; or the future value of $10,000 is discounted by $3,860.87 to $6,139.13.

Instead, then, of four kinds of rewards: (1) wages, (2) interest, (3) profit, (4) rent, there are in *principle* really two — (1) wages and (2) all other forms of income which are all of a *discounting* character, and are the *so-called* remuneration of natural resources as rent, of capital as profit, and of money as interest. In economics, the "reward" to these three (land, capital and money) has a common generic name, *interest.* In other words, *interest* has a narrow meaning as a return on money only, but it also has a broader meaning as a return not only on money, but also on natural resources and on capital.

That "return" is in dispute between those who favor socialism-communism and those who favor capitalism. The socialists-communists say that this return — this discounting of the "yield" from natural resources, capital and money to allow for time delay — is an unwarranted and immoral return. The theorists for capitalism, contrarily, say that this return is "in the nature of things" and is unalterable, inescapable — even in a socialist-communist economy — *because men discount future values when converting them to a present basis.*

This whole question of *interest* in the broad sense is one of the most fundamental in society. Disturbance in regard to *interest* can, therefore, gravely undermine the stability of society. In communist countries, the attempted elimination of *interest* (in a broad sense, as defined) changes the whole character of that society. If bringing interest, say, from an average rate of 5% to zero (as in communist countries) results in revolution and convulsion, the variation of the rate within capitalist societies between 2% and 7% (also a 5% range) could obviously result in grave convulsions known as booms and depressions. That is what happens.

III. DO THE HEBREW-CHRISTIAN SCRIPTURES FORBID INTEREST?

The Hebrew-Christian Scriptures prohibit neither interest nor even usury *in business.*

Interest, as just explained, is a generic term, covering rent and profits as well as a return on money. There is *nothing* in Scripture which declares that rent on land is immoral, nor profits in a business. Only one small segment of interest, namely, interest *on money,* seems to come under the ban of Hebrew legislation. (See Exodus 22:25; Leviticus 25:35-37; Psalm 15:5.) Contrarily, the whole Hebrew-Christian moral law *assumes without question* the existence of private property, the collection and payment of rent, profits on trade and investment, and the collection of interest on funds loaned *in business* (as, for example, business with foreigners).

But there is a *limited* ban in Scripture on interest. Some people, although in distress, should not get a loan. A creditor by making a loan may contribute to the injury of a borrower. There ought to be a penalty on such loans, which are not business loans, and Hebrew law provided such a penalty — no interest might be collected on them. In the Hebrew Scriptures it is not the interest itself which is in dispute (if it was, the Hebrew law was based on confusion), but the moral validity of a loan *to innocents or desperate folk — the very poor.* Neither innocents nor the desperate should fall into the hands of a business-like, and much less, an exploitive, lender. His rates will be high. The innocent and the desperate ought either to stay out of business or be helped *in other ways.*

Modern secular *usury* laws — laws saying what is legitimate interest and what is exorbitant interest — have the same base as has just been outlined. To prevent loan sharks from taking advantage of fools and unfortunates, a maximum rate is set today, say 7%. The Mosaic rate is 0%. The idea is the same, and the difference is only in the figure.

Usury laws *for business* are undesirable and morally invalid. If a smart man without money sees a way to make 30% on a new investment, why should whoever might lend him money charge only 7%? It is far better that the would-be borrower obtain an 8% or 10% loan, than no loan at all. High profits are often hazardous. If a smart man is prepared to pay a high rate and a lender wants a compensatory participation, then the anti-usury rate (of a Mosaic character) is not properly applicable.

There is *nothing* in Scripture that legislates about *business* rates of interest. How could Scripture wisely set a rate which is the inescapable but variable discount between present and future values? Those discounts properly change with circumstances. A big discount (which means *apparently* usurious rates) is desirable in business at times.

Interest in the business sense is not under the ban but the blessing of Scripture.

IV. WHAT DETERMINES THE INTEREST RATE?

If the question is asked, *What determines the interest rate,* it is not possible to answer it before designating first what interest rate is being talked about. Here is a list of the *kinds of interest* which can be subsumed under "interest" in the foregoing question:

A. Interest rates, in the universal sense

1. The *natural rate* of interest.

B. Interest rates, in a narrow sense
   1. The *long-term rate* of interest, on bonds and mortgages.
   2. The *short-term rate of* interest, on commercial loans made by banks.
   3. The *rediscount rate* of the Federal Reserve Banks in the United States, or of central banks elsewhere. (A *discount* or *rediscount* rate, as has previously been explained, is an inverted form of interest, but is in reality the same thing; the base for the calculation of the discount is different from the base for the calculation of interest; *interest* is added to the present value to make the lower future value equal to the present; *discount* is subtracted from the future value to show what it amounts to presently. The base *only* is different.)

C. Interest rates, in a broad sense. These include, in addition to money rates:
   1. Yields on common stocks, as dividends and as retained earnings.
   2. Yields on natural resources, as rents from farm lands and real estate generally.

D. Pure interest, versus other factors added to the pure interest rate; these other factors are such as disguised insurance premiums for potential losses from hazardous risks; or as a disguised compensation for that subtle loss of principal known as inflation; etc.

In the compass of this article only the briefest consideration can be given to these different types of interest.

There being so many kinds of interest, it is nonsensical to think that there will be a uniform interest rate; the variations will be infinite.

The Natural Rate Of Interest

Let us begin with the *natural rate* of interest. This is the *prevailing* discount of future goods to bring them to the present basis. Who is the individual who would have the temerity to declare exactly what it is? This rate will have a few characteristics which are hardly disputable.

One of these characteristics is that the rate is *fairly stable.* It is a figure arrived at in a massive market of hundreds of millions of people. All make their contribution, although many do so unwittingly, to the rate. How much or how little they look to the future, and how much or how little they themselves "discount" a future value to bring it to a present basis, determines the rate.

Another characteristic is that the natural rate of interest is probably *in the neighborhood of 5% annually,* certainly at least 3% and hardly 7%. (Many might say that the rate is between 4% and 6%.) For simplicity's sake, we accept 5% as the *natural rate of interest;* let anyone else choose his own.

At that rate, at compound interest, money at 5% will double itself in about 14 years. Another way of saying the same thing is that at 5% \$10,000 available only after 14 years is worth only \$5,000 now.

It is not a question whether natural interest is right or wrong as a principle, nor at this specific rate. We submit, merely, that it is an approximately correct description of facts. People as a mass simply will not evaluate future goods as worth so much as present goods. (*Individuals* can be found who will, in *specific* cases, value a future good even higher than a present good, but they are exceptions. There are other minor exceptions.)

The *natural rate of interest* is not recorded anywhere. You will not be able to find quotations in magazines or newspapers.

Interest Rates in A Narrow Sense

Interest rates in a narrow sense are all definite *money* rates of interest, and we have divided them into three classes, (1) long-term rates, (2) short-term rates, and (3) rates charged by central banks (that is, the government banks, as the Bank of England in England, or the Federal Reserve Banks in America).

Four charts are presented to show: (1) prime commercial loan rates, which are the rates of interest that the companies which are most respected in the financial community have had to pay for short-term money since 1952; (2) the New Corporate AAA bond rates, which are the rates that the best companies have had to pay for long-term money (repayable only after several years); and (3) the rediscount rate of the Federal Reserve Bank of New York, the bellwether of the 12 Federal Reserve

Banks. (These charts are replicas of those shown in the October 1959 issue of the admirable *Monthly Letter* of the First National City Bank of New York.)

CHART I

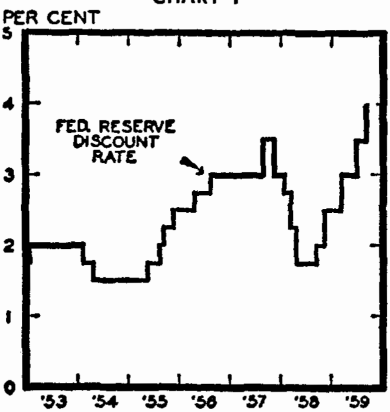


CHART II

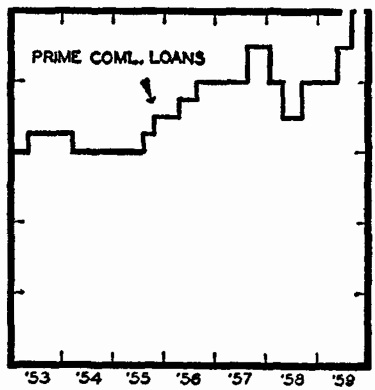


CHART III

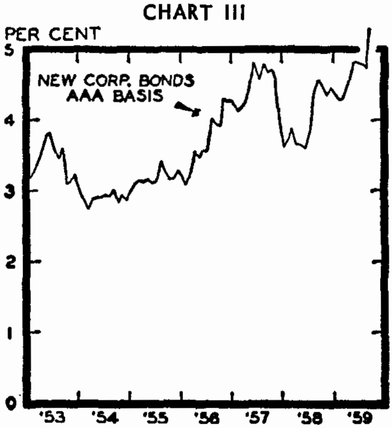
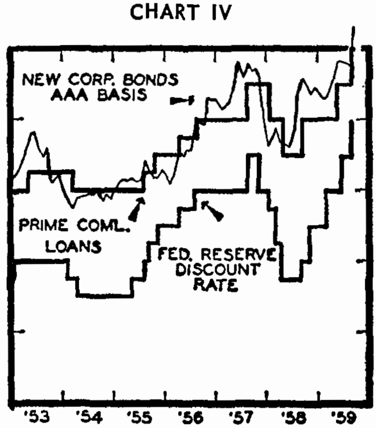


CHART IV



The years from 1953-1959 inclusive are shown on the horizontal scale; and the interest rate on the vertical.

Chart I: The New York Federal Reserve Discount Rate has these characteristics: the rate is lower than that of prime commercial loans or bonds; further, the fluctuations are relatively more violent. The figures on three recent dates are:

September 1957	3.50%
June 1958	1.75%
October 1959	4.00%

In the nine months from September 1957 to June 1958 the rate was *halved* — from 3.50% to 1.75%. Then in the following 17 months the increase is from 1.75% to 4.00%, an increase of 129%.

Chart II: Certain characteristics of this graph of commercial loan rates immediately draw attention, for one, the *lowness* of the line; it has prevailingly been under 5%, which percentage has earlier herein been estimated to be the *natural rate.* The lowness may be ascribed to the fact that these are the most-preferred loans, and consequently will have the lowest rate. It may also be held that the financial policy followed by monetary authorities, *under pressure of public opinion and political parties,* has made money rates abnormally low. This significant factor cannot be measured; every man can have his own opinion. The trend of the rates has been upward. The rates in the early 1950s were *abnormally low,* because of political policy and pressure. There is little reason to believe that rates will go down significantly unless an easier money policy is again adopted.

Chart III: The variations in the yield on bonds has been similar to the variations in prime commercial loan rates. The two markets are related. Bond yields tend to be a little higher than commercial rates, because *long-term* loans are, in a sense, less attractive than short-term paper. Further, the range of fluctuation of bond yields is a little wider than the fluctuation in commercial rates.

Chart IV repeats the graphs appearing in the preceding three, so that comparisons may more easily be made.

Interest Rates, In A Broad Sense

The "interest" (that is, the earnings on the market value) on shares in corporations, and on land (that is, rent), are seldom, if ever, computed in a comprehensive manner.

The First National City Bank of New York publishes annually a figure described as "percent return on the net assets" of some 3,500 leading corporations. The figures are as follows: for the year 1956, 11.3%; for 1957, 10.6%; for 1958, 9.0%. But in a sense these figures lack significance. They are calculated on the basis of "book values." These book values do not allow fully for the inflationism which has occurred. On present-day *market* prices, the yield is much less than shown in the foregoing. The reason is that market prices are in general above the partly uninflated book asset figures. If well-regarded stocks are (on the average) selling at 60% above book values, then the yields shown in the foregoing should be recomputed by dividing by 1.60, or, be for 1956, 7.1%; for 1957, 6.6%; for 1958, 5.6%.

These data refer to the largest and the most-profitable companies. If *all active* corporations are included, the percentages decrease. In an earlier study covering 19 years, the figure was 4.5% of *book* values.

All these figures on "interest" are "corrupted" on the high side by the systematic inflationism which has been continuing since the United States went off the gold standard.

"Interest" on the market price of stocks is less than some people seem to think. It may be doubted that the real return on common stocks for *all active* corporations equals 5% — the figure previously somewhat arbitrarily selected as the "natural rate of interest."

Data are not available on the "interest," that is, yield, on investments in land.

Pure Interest

Really, pure interest is the same as natural interest but the term *pure* is useful to designate that other factors than those determining the natural rate are included in published interest rates.

Pure interest is in a sense an abstraction, because other factors than the "discount for the time factor" always enter in. Consider the interest rate on cruzeiro loans in Brazil of 20%. What puts the rate so high? The expected *further depreciation* of the value of the cruzeiro. If at the end of a year, a cruzeiro is expected to buy 15% less than at the beginning, it is not unnatural that the interest rate is as high as 20%, which should be collected to allow for (1) a 15% inflation of prices (that is, a 15% depreciation of money), plus (2) 5% as "pure" interest.

In 1959, interest rates rose in the United States. Does that mean that the *natural* rate of interest or the *pure* rate of interest increased? Not necessarily. It would even be possible that the presumed pure rate has actually decreased, through miscalculation or otherwise. If, for example, the financial and labor union developments during the 1958 "recession" convinced many people (and reasonably so) that inflation will continue indefinitely and maybe with an accelerated tempo, then a potential borrower might be happy to pay 1% more for borrowed money (an increase from 5% to 6%), if he believes that stock prices will inch upward say an *extra* 3% per year. The higher interest rate of 1% is then only a partial allowance for the accelerated inflation of 3%. Really, under those assumptions, borrowed money is "cheaper" in the final analysis at 6% than at 5% because it is well compensated by the 3% increased inflationary rise in prices.

* * *

Having considered the varied forms in which "interest" manifests itself — in money rates in the long-term and short-term money markets; in central bank rediscount rates; in yields on stocks and rent on lands — we can come to the question itself: what *determines* the interest rate?

In this question the word *interest* does not mean the generic term, but only the *loan* money rate, especially the short-term commercial loan rate and the long-term bond rate. There are three main factors determining this rate:

1. The current *natural rate* of interest, as explained, is the basic factor. This is supplemented by:

2. An adjustment or correction, up or down, for expected change in the purchasing power of money. And finally there is a further adjustment or correction caused by

3. The deliberate actions of men, motivated by purposes (a) of affecting the money supply, (b) of creating prosperity (or the illusion of prosperity), (c) of counter-balancing policies which will create chronic unemployment, etc.

In regard to the second item, the Brazilian illustration is a case in point. Instead of 15% allowed for inflationism in the cruzeiro loan rates, let us take a more moderate rate of 1% a year. If the natural rate is 5%, then 1% would be added to the rate on loans. Vice versa, if the long-term trend of prices was estimated to be downward by 1% a year, then the rate would be 5% for the natural rate, minus 1% for the expected price decline, and the rate would be 4%.

Finally, although neither central bankers nor commercial bankers can control the natural rate nor the effects of changes in the quantity of money, they can — and do — endeavor to affect the interest rate on commercial and long-term loans *by vary-*

ing the supply of money. (As previously outlined, the *real effect* of that action is to influence prices, not interest rates.) But men believe (erroneously) that by issuing more money, they can influence interest rates. *Temporarily* they can *if, furthermore, the increase in the amount of loan money is NOT expected by the public.* If the increase is generally and confidently expected, borrowers will in their thinking and planning fully allow for the expected changes in the quantity of loan money; demand will vary accordingly, and consequently there will be little or no effect toward reducing the interest rate. Bankers (central or commercial) can *affect* loan money rates up or down temporarily by doing what the public does not expect. Otherwise, they have *no* influence, because the public effectively "defends" itself against *expected* money and interest rate changes.

We come then, finally, to the *unexpected* action of bankers in regard to interest rates. *It is the role which bankers play in affecting interest rates, as hapless agents of public opinion, which causes booms and depressions.*

V. HOW DOES LOWERING THE INTEREST RATE CAUSE BOOMS?

The purpose of all production is ultimately *consumption.* Work is not for work's sake. Work is designed to supply the material and spiritual goods to satisfy our needs. Work itself is wonderful, but it must have a *purpose,* valued by those who do the work.

The production process, with the pleasure of consumption as its goal, always takes *some* time, and not infrequently a very long time, maybe years and years. The complex of production is therefore a mixture of things which takes varying time to produce, and which are in varying stages of their respective production time. Production can be looked at as a mighty stream.

Human beings (from a mundane viewpoint) control that stream. Some are people-of-the-moment, that is, they make little or no provision for the future. Others are more timorous and are saving, maybe even anxiously, for their own and their descendants' distant future. The former promote the production of *consumption goods only.* The latter promote the production of consumption goods *and of production goods,* known as *capital,* that is, the transformed products of nature which greatly increase the production of human labor but which require more time. (See Volume III, September 1957, pp. 266-297.)

This stream of production, influenced by everybody, may appear chaotic, disorganized, unplanned, but that appearance is misleading. Everything in it *is* planned. Some of that may be unwise, short-sighted, idealistic — but it is planned nevertheless. If we view production as a gigantic stream or complex of events, it is equally necessary to have the vision to see that it is an equally gigantic stream or complex of *plans*.

Producers anxiously watch what their customers (and eventually the consumers) will buy. Every shift in demand is responded to as soon as it is noted. The sagacious producers early note what is happening but stupid producers do so belatedly. Business, therefore, is transferred by consumers to the sagacious operators, who are the people who serve the consumers best, and *consequently* should continue in business. That the incompetent, inexperienced or the reckless are eliminated is not an evil, nor chaos, but a blessing, and is evidence of the valuable groping by finite human beings for what is best for most people.

It is illogical to *interfere* with this production stream — in order to *plan* it. Such *plans* are nothing more, finally, than the program of *one* single finite human mind to plan the whole, instead of letting millions of finite human minds plan it. The millions of minds know more than the one mind. A *central* plan can *never* be so good as the aggregate individual plans of the people. Common men, aggregatively, are smarter than *one* prince; or a committee of economists and statisticians; or a few party leaders.

Plans must be based on facts as well as on motivations and principles, and the facts will be in the form of data. If the data are misleading, then the plans inevitably will be wrong. Is anybody or anything making the figures misleading, so that the planning is wrong? Unfortunately yes, and here is where we come to the interest rate as the disturbing factor.

Let us contrast, for the purpose of explanation, two activities in the production stream — the saving by investors and the use of those savings by business men on the one hand, versus the current consumption by all men. Here is the problem — if something (for example, creation of circulation credit) induces business men to try to invest in capital goods more than the savers will save, two maladjustments will develop — (1) the savers will not save enough for business men to *complete* their attempted expansion of the production of capital goods, and (2) the consumers not having intended to reduce their consumption will insist on consuming consumption goods rather than having "too much" capital formation. The stream of production then becomes unsteady. Not that that stream is unplanned. But it is planned wrongly — too much is attempted to be put into capital contrary to the wishes of the public. Doing that — attempting to put too much into capital formation — can be begun, *but the projects cannot be completed;* the savings and supplies are not there; the consumers will not allocate — set aside — enough of the production stream *for the future* — as the business men have planned *for an erroneous reason.* What may that erroneous reason be?

The natural interest rate is the balance wheel determining the allocation of production effort between the present and the future. The higher the rate, the greater the saving and the greater the production effort that is allocated to the production of capital goods, which will yield their return as consumers goods only in the later future. The lower the rate, the smaller the savings and the formation of capital goods and the greater the production of consumers goods for early use.

What the savers look at as savings, the business man looks at as funds to use in capital expansion. As there are no quotations of the *natural rate of interest,* business men look at the prevailing interest rates for short-term commercial loans and long-term bonds. A low interest rate in those fields signals to them that there are ample funds for capital expansion or, in other words, that savers are allocating much to future goods and are proportionately prepared to abstain from consuming consumers goods. Vice versa, a high interest rate signals to them that there is a short supply of funds which the people are willing to allocate to capital formation, or in other words, that savers are allocating less to future goods so that they may have more for current consumers goods.

The interest rates paid on commercial loans and for bonds are *costs* to businesses. If those rates are *lower* than the natural interest rate, business men will get too optimistic a signal concerning funds available for capital formation. This lower-than-natural rate of interest will be a consequence of an increase in the supply of loan funds. This, as has been explained, will be *temporary,* because goods prices will advance so that the new loan funds are eventually as urgently needed as was previously the case. But *in the transition period from less funds to more,* interest rates will *temporarily* be lowered, especially when those endeavoring to affect interest rates operate unexpectedly.

The manner in which funds are increased and rates lowered consists of a whole complex of intricate transactions which have been developed in financial circles, but the essence consists in this: *more circulation credit is put into the monetary structure.* (For the meaning of circulation credit, see Volume V, August 1959, page 243ff.; and October 1959, page 313ff.)

And so, by making available more circulation credit than previously existed, interest rates — which are important costs to business men — are *temporarily* lowered. Business men *therefore* consider expanding their operations, by investing in more capital formation. The money market rates, which they watch, indicate that the funds are available *at a rate which will make new capital formation profitable.* Why should they not engage in more capital formation, since the interest rate indicates that funds are available and that it is low enough so that the calculations now show that projects (which were previously unprofitable) are profitable. The boom begins.

VI. WHY DO BOOMS, INEVITABLY, END IN DEPRESSIONS, OR IN SOMETHING EVEN WORSE?

But the quoted interest rates are too low for reality. The public does not want so much capital formation; instead it wants consumers goods. What then happens is that the over-expanded industries become unprofitable; employment is restricted; business men are disconcerted and become as excessively cautious as they formerly were excessively optimistic. The bankers begin to look at the situation with anxiety; refuse to make more loans; demand the repayment of loans coming due which look precarious; and in order to ration new loans, they raise interest rates. *Instead of a boom, there is now a depression.*

The alternative to this contraction of business, known as a depression, is *continuously* expanding circulation credit. This is inflationism, worse than a depression.

VII. A SUMMARY, ANSWERING THE QUESTION: WHO AND/OR WHAT CAUSES DEPRESSIONS?

The role of the central bank (in the United States, the Federal Reserve Banks) is a fateful one:

1. As Chart IV earlier in this issue shows, the rediscount rate is regularly *under* the prevailing commercial and long-term rates. Certainly, these rediscount rates are below the natural interest rate, and consequently systematically inflationary.

2. As Charts I and IV show, the rediscount rate varies fantastically; in nine months in 1957-8 it dropped 50%; in the succeeding 17 months in 1958-9 it increased 129%.

This rate policy — in general, too low and fluctuating too widely — is not (in all probability) the will of the members of the Federal Reserve Board, but is a policy imposed upon them by law and politics.

The Federal Reserve System has been assigned the fantastic task of "stabilizing the economy." For this purpose it has only two methods, which are really the two sides of the same coin — putting out more circulation credit (or contracting it), and lowering (or raising) the interest rate. But by these policies, instead of stabilizing the economy, the Federal Reserve Board is a disturbing element in the business situation. By following the course dictated by law and politics, the Federal Reserve Board is *causing* booms and depressions rather than ameliorating them.

It is the *variation in interest and lending policies* which is the cause of booms and depressions in the United States. This is not the fault of the bankers but of the public.

The people of the United States should abandon *completely* the idea that the rate of interest can genuinely be influenced by the quantity of money. Low interest rates are only very temporarily obtainable by issuing more circulation credit. Circulation credit is theft. When issued, it causes booms; when withdrawn, depressions; if continued, it causes inflation, chaos and the collapse of society.

Ideas in the foregoing are derived from the writings of Eugen von Böhm-Bawerk; see his *Capital and Interest;* and of Ludwig von Mises; see his *Theory of Money and Credit* and his *Human Action.* Of course, the writer only is accountable for the foregoing presentation. The subject matter will be continued in future issues.

Present-Day Protestantism Has, Without Realizing It, Laid A "Moral" Foundation Under Socialism-Communism

The Nature Of The Problem

A distinguished business man some years ago was invited to join an economic society. He asked the president: "Is the society anti-Christian? If so, I do not wish to join."

To that the president of the society replied about as follows:

> The society is *economic* in character; it does not concern itself with religion; nor does it teach morality or ethics; it does not appraise the objectives or aims of men; that is each man's own imprescriptible right; it concerns itself only with the realities of the world around us which affect the welfare of men; and it analyzes whether the *means* which men select to attain their ends are effective and best suited to accomplish them. Our society concerns itself only with the *consistency and logic* of men's thinking about their aims and the means they use to attain them. We call it bad economics if it can be shown that the means are not suited to the declared or obvious ends sought. But whether the ends (for this life or a future life) are valid — *that* is something outside of the field of economics and of the activities of our society. We teach no religion, and we favor no religion.
>
> "However," and the president smiled, "I maybe should add that we have *one* member who considers Christianity the greatest evil in the world."

That reference was, apparently, to an American economist, whose fame is international and who considers what Protestant theologians generally teach in America, in the field of economics, to be intellectually a sad mess, and destructive to a sound economy — something logically indefensible. We are not acquainted with the economist referred to, but if that is his position we are (in the fields of morality and economics) inclined to agree with him. The reason for this is: *the ethics taught in many Protestant churches have become a "moralized" foundation for socialism-communism.*

There are evils which men have traditionally condemned, but nevertheless in weakness have perpetrated and then suffered a sense of guilt. However, others may take a different tack. Whereas originally men (1) considered doing wrong; (2) nevertheless committed the wrong, and (3) suffered a guilt complex — the situation may be radically altered by a basic change in judgment of what is moral or immoral, so that now (1) what was once considered wrong is proclaimed as a virtuous deed; (2) its perpetration is encouraged; and (3) a guilt complex is blandly eliminated.

That is what a strong stream in Protestant thought has accomplished. And that is what the famous economist must apparently have had in mind if the other man's appraisal of his attitude was accurate, "That Christianity is the greatest evil in the world." Not that this economist has evident moral fervour for unalloyed resistance to socialism-communism. But he apparently despises the logic of much modern Protestantism in his own specialized field of economics.

In what follows it is shown how Protestant ethical thought has developed a moral sanction for socialism-communism. Whether it intended that or not does not negate the fact.

The Character Of Syllogisms

Most people are acquainted with the character of syllogisms. A syllogism is a series of propositions by which men help themselves to reach valid conclusions. A standard, illustrative syllogism is the following:

Major Premise: All men are mortal (that is, will die).
Minor Premise: Socrates is a man.
Conclusion: Therefore, Socrates is mortal (will die).

Whether the *conclusion* is correct depends on whether the two premises are true, (1) whether all men are mortal, and (2) whether Socrates is a man. If those are true, then the conclusion, that Socrates will die, is a reasonable conclusion. In the ordinary course of events, known to human experience, this syllogism describes past events correctly, or predicts correctly.

Another often-used, illustrative syllogism, is the following:

Major Premise: All swans are white.
Minor Premise: John's bird is a swan.
Conclusion: Therefore, John's bird is (must be) white.

Again, the conclusion is valid, if the premises are true. It is reported, however, that some swans are black. In that case, the conclusion in the foregoing syllogism is incorrect, *because* the major premise is erroneous.

There are other reasons why conclusions in a syllogism may be incorrect, but the foregoing suffices to show how syllogistic reasoning is helpful for reaching conclusions, that is, *valid* conclusions, *if* the premises are true and properly related.

The Conclusion In The Socialist-Communist Syllogism

The *Conclusion* in socialist-communist thought is:

> From each according to his ability to each according to his need.

If this is really a conclusion in a syllogism, then it should be interesting to discover what the premises in that syllogism are. The foregoing conclusion would stand as follows in the syllogism:

Major Premise: ....
Minor Premise: ....
Conclusion: From each according to his ability to each according to his need is true morality (or true brotherly love, or is the essential ethical principle for right conduct).

It is often a difficult task to find — discover — the two antecedent premises, but it is fruitful to attempt it. When that is done, a man may doubt a conclusion he previously accepted, because he becomes aware that one or both of the premises is false, or that they are not properly related. It will be interesting for readers to interrupt their perusal of this article in order to take a piece of paper, and themselves work out the premises which *must* underlie this socialist-communist conclusion:

The Socialist-Communist Ethical Syllogism

One way to work out the problem is to endeavor to formulate the minor premise first. Here is an attempt at that:

> The rule, *from each according to his ability to each according to his need,* consists in treating men equally, in the sense of ignoring their merits or demerits, that is, to treat them *without any discrimination based on their worthiness.*

Surely, when men are rewarded according to their *need,* and when their need is supplied by the efforts of others, then they are not rewarded according to what their work deserves. Similarly, whenever another by greater effort produces more, which greater production he allocates to others (according to their need), then that harder worker is not rewarded according to his greater performance. There is in the expression, From each according to his ability, to each according to his need, a denial of the right to rewards according to *merit;* the rewards *are,* contrarily, according to *needs.* That is the same as saying that it is not moral to discriminate according to merit.

It is to be recognized that there *seems* to be a different proposition underlying the socialist-communist rule. Literally, it reads, From each according to his *ability,* to each according to his needs. In the foregoing, that has been interpreted as, From each according to his *effort,* to each according to his needs. But in the socialist-communist *theory* there has been no distinction between *ability* and *effort.* In fact, it is not possible to measure accurately whether a greater output results from ability or effort.

So much for the *minor premise.*

It is not too difficult to formulate the *major premise.* This is what it is:

> To treat men equally in the rewards they get in life, that is, without being willing to discriminate between them according to their productivity, is true morality (or true brotherly love, or is the essential principle of right conduct).

We can now put together the two premises and the conclusion in the socialist-communist syllogism, as follows:

Major Premise: To make the rewards (which men are to get) equal, without adjusting them in proportion to their ability and effort, is brotherly love.
Minor Premise: To follow the rule, From each according to his ability to each according to his need, is to make the rewards of men equal without adjusting them in proportion to their ability and effort.
Conclusion: Therefore, to follow the rule, From each according to his ability to each according to his need, is brotherly love.

In still simpler language the syllogism is this:

Major Premise: To refuse to discriminate (that is, to vary rewards according to merit) is brotherly love.
Minor Premise: Socialism refuses to vary rewards according to merit.
Conclusion: Therefore, socialism is brotherly love.

The proposition can be reversed and be made to read:

Major Premise: To engage in discrimination is evil.

Minor Premise: To reward men according to merit (ability and effort) is to engage in discrimination.
Conclusion: Therefore, to reward men according to merit is evil.

The conclusions in these syllogisms stand or fall, depending on whether the major premise is right, whether: *To engage in discrimination is evil.* If that is true, then the morality of socialism-communism is unimpeachable.

In the illustrative syllogism about swans, the major premise was: All swans are white. That statement is not true, because some swans are black. If John has a swan, it is unjustified to deduce that John's swan *must be* white. Similarly if it is not true that, To engage in discrimination is evil, then the conclusion does not follow that to discriminate in rewards (according to merit) is evil.

The crucial question therefore is, what is the soundness of the major premise of socialist-communist ethics?

Modern Protestantism's Major Premise On Brotherly Love

Present-day Protestantism has devoted major attention to defining and proclaiming what it considers true brotherly love to be. Only if the Protestant definition of brotherly love is understood can the relationship of Protestantism to socialism-communism be understood.

Protestantism has a high and exacting definition of brotherly love. An example will be helpful, before giving the general definition, and it will be well to examine first what is declared *not* to be true brotherly love.

A well-treated and generously remunerated employe may have a feeling of gratitude and affection for his employer. This, in ordinary parlance, would be called "love." The employe "loves" the employer in response to good treatment, and because he considers it to be an appropriate attitude. But, according to the present-day Protestant definition of brotherly love, the "love" just described is not genuinely the "love" which the Christian Scripture requires. This employe "loves" his employer *because his employer is good to him*: This is an "earthy," inferior "love." If this employe really "loved" his employer, then even though he received bad treatment from that employer, his affection for the bad employer would nevertheless be equal to what it would be if the employer were very good to him. Why? Because then the "love" would patently be *independent of the merit of the object.* According to this definition, a man does not "love" his employer unless he is prepared to "love" a bad employer as well as, and as much as, a good employer.

Or suppose a young man "loves" a handsome and desirable young woman. He probably would not court an undesirable girl so fervently. His "love" is "self-centered." It is a reflection of his mood to get something *for himself.* When this is called "love," it should be realized to be, so some Protestant divines teach, just what it is, mere *eros* (one of the Greek words for love), that is, love down-graded from unalloyed "brotherly love," so that it takes into account *the attractiveness or the merit of the object. Eros,* then, is a lower grade of "love." It may be natural and it may make people happy, but it is not the genuine article. If "love" of a man for a woman were really the unalloyed article, then a man would not take the merit of a woman, whom he would "take to wife," into account. He would "love" his wife-to-be regardless of her merit. Then he would have more than selfish *eros;* then he would have magnanimous *agape* (another Greek word for love), that is, a nondiscriminating love.

We ourselves appraise women differently. We think *eros* is wonderful relative to the other sex. Imagine a woman who believes her husband "loves" her, *regardless of her merits;* and who believes that her husband would love her as much — or should — if she had no virtues at all. Then she could be comforted that she has his *agape,* his true love, rather than his down-graded *eros,* which is a response, unfortunately (!), to her merits. However, it is worth pondering whether women want *eros* or *agape.*

Agape calls for the type man who has the unadulterated type of "love" which induces him to wink at a girl in the dark, and concerning whom he does not have the slightest knowledge what she looks like or is. *Eros* calls for the type man who winks at a girl after he has appraised her in broad daylight. But then, it is so sad to admit, he will develop no more than selfish *eros,* because he wants her because she has merit or attractiveness.

The derivation of the two words for "love", *agape* and *eros,* is the Greek language used in the New Testament of the Christian religion. Both words are used for love, but the allegation is that there is the difference in the meaning of the two words which has just been outlined.

That there are two words used in the Greek for love and that they have a different emphasis is not surprising. In the English language the expression might be that a man was *infatuated* with his bride-to-be, but ten years later the statement might be changed to: he has a genuine *affection* for his wife. There are many words for love in the English language.

Eros is the term from which the English *erotic* is derived, which refers to passionate, sexual desire. Although this idea is not wholly removed from the idea of *eros* as allegedly used in the New Testament, the contrast between *eros* and *agape* is not essentually between the sexual and the nonsexual. The difference lies in whether you are affected by the object of your love. To have *agape* you must love regardless of the merit of the object; if the existence or degree of your love for an object is affected by the merit or demerit of the object, then you have only *eros,* because there is discrimination, and a vein of selfishness, in such selective love.

The Origin Of The Agape Idea

This idea of "love", covered nowadays by the word *agape,* has an exalted origin, namely, the alleged love of God. God has *agape,* not ordinary *eros.* This idea is related to the dogma of "salvation by grace." This dogma has always been present in the Christian church. St. Augustine (354-430) brought it to the fore in the fifth century. He was known as the Doctor of Grace. The doctrine fitted his own personal needs and psychological make-up.

Augustine, when young, took a mistress for himself. He had at least one son by her. He never married her. His mother wanted him to be *married,* but considered the mistress below her son's station in life. And so they sent the forlorn mistress back from Italy to Africa. In due time Augustine was to marry respectably, a woman having been selected who was approved by his mother. But the loss of his mistress and the waiting for the wife was too much for Augustine, and so he took another mistress. Augustine, possessing an extraordinary capacity for introspection, naturally had a strong guilt complex. And so he needed a lot of "grace" — merciful forgiveness — from God, of which he would be the undeserving beneficiary. God's grace — or love — would be *undiscriminating* — without regard to his (Augustine's) lack of merit. The grace of God, then, is pure *agape*. It goes *beyond* discriminating according to the merit of the object of that love.

Pelagius, a British monk (maybe from Wales), a contemporary of Augustine, had a different psychological make-up. He is reported to have been a man of austere morals and excellent self-control. When he went to Rome he was shocked by the prevalent looseness of living. He emphasized restraint in living. A man with so much less emotional imbalance than Augustine had would naturally keep his definition of the love of God on a more restrained basis than Augustine's. It would be natural for him to be sympathetic to sober living. The unemotional Saxon would view things radically different from the hot-blooded Roman of North Africa. He would emphasize the *rational* aspect of things rather than the *emotional*. He would not need the *agape* idea so strenuously as Augustine needed it.

Augustine's idea of the love of God was reborn in the theology of the Calvinist protestants. According to this theology, God predestines everything — the salvation of some and the reprobation of others. To the agonizing question why some are reprobated, the Calvinist answer is that they are undeserving. But why, then, the election of others to salvation? To this the answer is that they too are *equally* undeserving, but that God according to his sovereign privilege *without taking into account their merit* — because they intrinsically have no more merit than the reprobates — elects them to eternal salvation. Both reprobates and elect being equally undeserving, the fact that the elect are elected is evidence of an *undiscriminating* selection — a selection not made on the merits of those elected. God's love to the elect is therefore, pure *agape*, love manifested regardless of and independent of and unrelated to the merit of the object. This is *sovereign grace*. And human *agape*, toward other human beings, is supposed to be of the same character — *undiscriminating* love.

This Calvinist doctrine has, however, never been popular. Many may belong to so-called Calvinist churches, but outside of ecclesiastical environment they disclaim acceptance of the doctrine: that is, they usually disclaim it if they know what the Calvinist doctrine is; (many, naturally, do not).

The trouble is that the *agape* of God toward the elect does not solve the absence of *agape* of God to the reprobate. The problem therefore is not "solved" in the minds of most people who profess Calvinism. Even orthodox Calvinists are hard pressed to round off the corners of this doctrine, as is evidenced by the doctrine of Common Grace, still discussed and accepted by people who appear to be confused.

The *agape* idea then comes down in the Christian era (1) from the Apostle Paul, (2) via Augustine and the Reformers, especially Calvin, to (3) the modern age. The unique thing that has been added in the twentieth century is that the *agape* (love) of God to the elect is the pattern which men must universally show to each other. God has *agape* toward the elect; therefore, so the reasoning goes, men must have similar *agape* toward each other.

There is an important difference. God has *agape* to the elect *only*. But men must have *agape* to all men. The modern *agape* doctrine requires that men outclass God in the possession of *agape,* that is, *undiscriminating* love.

Bishop Nygren's "Agape and Eros"

Agape, as *nondiscriminating* love, or *unmotivated* love (as it is also described), is explained in greatest detail in Bishop Anders Nygren's book, *Agape and Eros* (English translation, Westminster Press, Philadelphia, 1951). Bishop Nygren is one of the two leading theologians of the theological faculty of the state University of Sweden, located at Lund, Sweden. His background is Lutheran or Evangelical.

The ideas in Nygren's book dominate alike nonconservative and conservative thought in the field of ethics in the present-day protestant religious world. A foreign delegate to the meeting of the World Council of Churches, in Evanston a few years ago, commented in private conversation enthusiastically about Nygren's book. That man personally is a conservative, and orthodox in religion. But the most unconservative clergy of the Protestant churches are equally enthusiastic about Nygren's *agape* doctrine. Nygren, in fact, is the real ethical "prophet" among modern Protestant theologians.

In his *Translator's Preface* to the English edition of *Agape and Eros,* Philip G. Watson writes (pages viii and ix):

> Eros is an appetite, a yearning desire, which is aroused by the attractive qualities of its object; . . . *Agape* . . . is entirely independent of external stimulus and motivation.

> [God's] . . . loving consists not in getting, but in doing good.
> *Agape* is further distinguished from *Eros* in that it is "indifferent to value." That is to say, it is neither kindled by the attractiveness nor quenched by the unattractiveness of its object. . . . man can show [*agape*] towards his fellow-men. . . . This freedom of Agape-love in relation to its object is the main point when it is said to be "indifferent to value."

The definition of *agape* by Nygren, and by those who accept his ideas, is an ethereal definition. The standard is unearthly: you must love everything *equally,* overwhelmingly, *regardless of relative merit,* wholly *undiscriminatingly.* In short, *all discrimination is sin,* and falls short of the Biblical requirement of brotherly love.

Such is the basic "morality" of much of modern Protestantism. It is declared to be scriptural, or more accurately, New Testamental. The fact, however, is that it is neither moral nor Biblical. It is a form of irrationalism. What is probably its greatest deficiency is that it burdens Christianity with so heavy a requirement of sanctity. Not without reason is religion in contempt among many intellectual people. Not without reason does the economist to whom we have referred earlier accuse Christianity as being the most harmful thing in the world.

Some people take exception to emotional fervor in connection with conversions. Whatever objection there may be to that, it is a trifle compared to the exception which may legitimately be taken to the fundamental ethical proposition of modern Protestantism, namely, that *to discriminate is sin.*

The only thing that can be said for this doctrine is that it is "modern." No equal ethical extravagance has been taught until this twentieth century.

There was a day when the morality of socialism-communism was considered to be irreconcilable with the ethics of Christianity. That idea was undoubtedly correct, but it has been abandoned. Instead, Protestant Christianity has obligingly supplied the socialists-communists with the required major premise in their ethical syllogism, to wit, *to discriminate is sin.* To show the relationship most clearly, it is simplest to cast the syllogism in this form:

Major Premise:	To *not-discriminate* is true brotherly love.
Minor Premise:	To follow the socialist-communist rule, From each according to his ability to each according to his need, is to *not-discriminate.*
Conclusion:	Therefore, From each according to his ability to each according to his need, is true brotherly love.

The major premise, despite its origin, is *false.*

Of all the dispositions and habits which lead to political prosperity, religion and morality are indispensible supports. In vain would that man claim the tribute of patriotism, who should labor to subvert these great pillars of human happiness, these firmest props of the duties of men and citizens.

—George Washington

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