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Website: www.fraserinstitute.org
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Canadian Publications Mail Agreement #40069269

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Date of Issue: Fall 2010.

Printed in Canada. ISSN 1192–490X (print edition) ISSN 1707-116X (online edition)

The Fraser Institute's vision is a free and prosperous world where individuals benefit from greater choice, competitive markets, and personal responsibility. Our mission is to measure, study, and communicate the impact of competitive markets and government interventions on the welfare of individuals. Founded in 1974, we are an independent research and educational organization with locations throughout North America, and international partners in over 80 countries. Our work is financed by tax-deductible contributions from thousands of individuals, organizations, and foundations. In order to protect its independence, the Institute does not accept grants from government or contracts for research.

Canadian student review

Welcome!

We are excited to announce that *Canadian Student Review* is going strictly digital, which will enable us to provide more interactive features, a superior on-screen reading experience, and enhanced social networking tools to you, our readers.

Our fall 2010 issue features the winning essays from our annual student essay contest. The top 3 papers were selected from 149 entries from around the world and the authors won cash prizes for their answers to the question "What should government do in times of economic crisis?" which examined the unintended consequences of government action, the shortcomings of stimulus spending, and the contrast between tax reductions and stimulus packages. In addition, we've included Jeff Bone's look at why young Canadians should become informed about government debt, a commentary from Niels Veldhuis and Mark Milke on subsidizing sports arenas, as well as an "Ask the Professor" article on the economics of fascism by Steven Horwitz.

We always welcome articles on economics and public policy from students. Starting with our winter issue, we will pay a $200 honorarium for published articles. See the last page of this issue for more information.

Best wishes,

Lisa-Diane Fortier
Editor, *Canadian Student Review*

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1st Place Winner

Fraser Institute 2010 Essay Contest

Fiscal Policy: Not an Option

by **Michael Dial**
Truman State University
Missouri, US

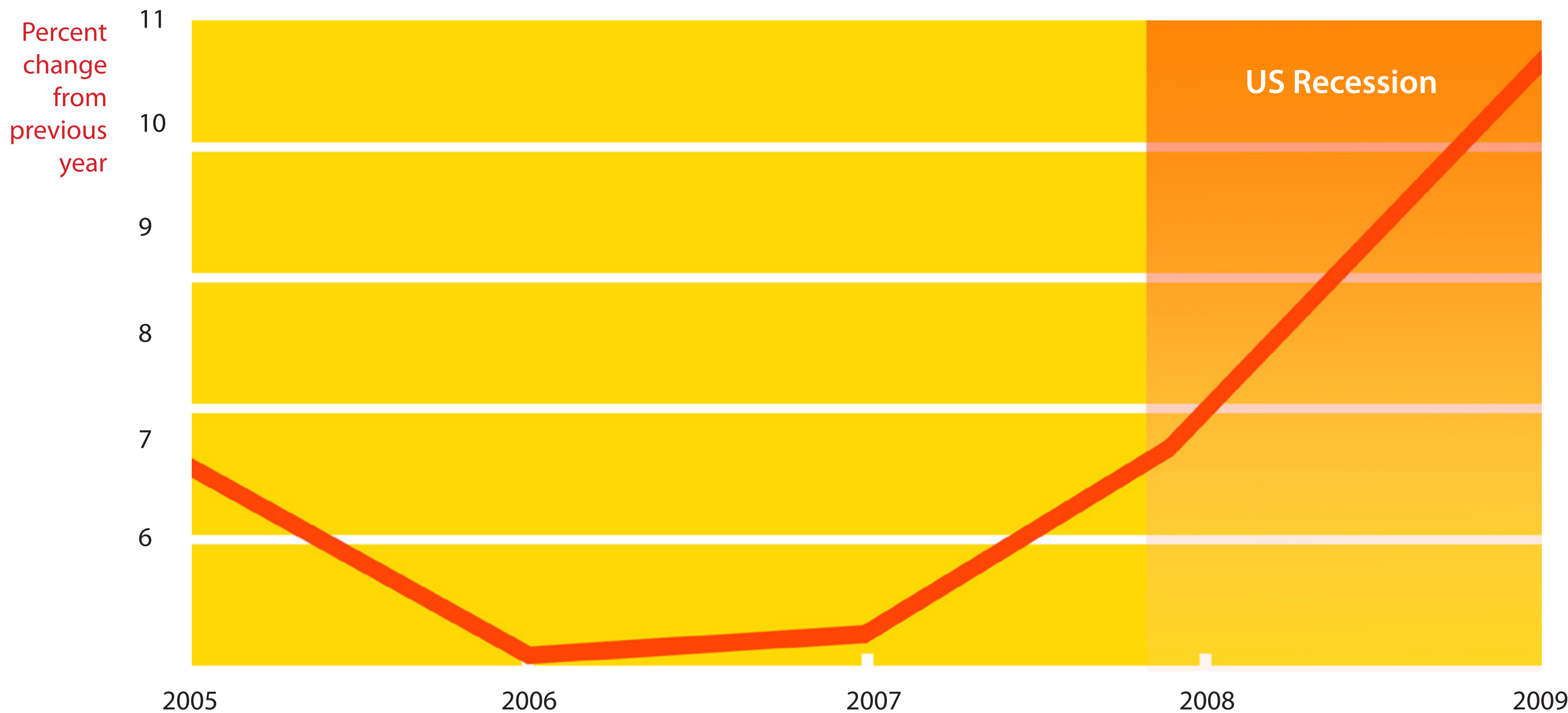
"Persistent high inflation is always and everywhere a fiscal phenomenon," claims economist Thomas Sargent (Jones, 2008). Nowhere has this become more obvious than in Greece as it currently goes through its tumultuous debt crisis. Poor fiscal responsibility and outrageous stimulus plans have shattered the Greek economy and even shaken the economic "superpowers" of Germany and France. The trillion dollar bailout for Greece has caused the value of the Euro to plummet, and still the future of Greece and its debt liabilities is in jeopardy (*New York Times*, 2010)

Long-term growth is built upon investment

For some, the story of Greece is enough to question the effects of deficit spending and the effectiveness of the fiscal policy in steering an economy. However, Greece has a developing economy, an often-corrupt government, and also lacks monetary independence. Couldn't fiscal policy be effective in a large, developed economy with monetary independence? Fortunately, this question can be answered by studying the American economy and its unprecedented stimulus plan, the American Recovery and Reinvestment Act (ARRA).

ARRA is a $787 billion government stimulus, the goal of which is to increase investment and consumption in order to jumpstart the economy by encouraging spending, employment, and GDP growth. Long-term growth is built upon investment, which, according to Keynes and other liberal economists, should come from the government during a recession. Overall, the ARRA is intended to end the recession, increase demand, stimulate economic growth, and improve employment in the short term by deploying government funds to pay for work projects and investment into industries such as green technology, research, and infrastructure (Recovery.org, 2009).

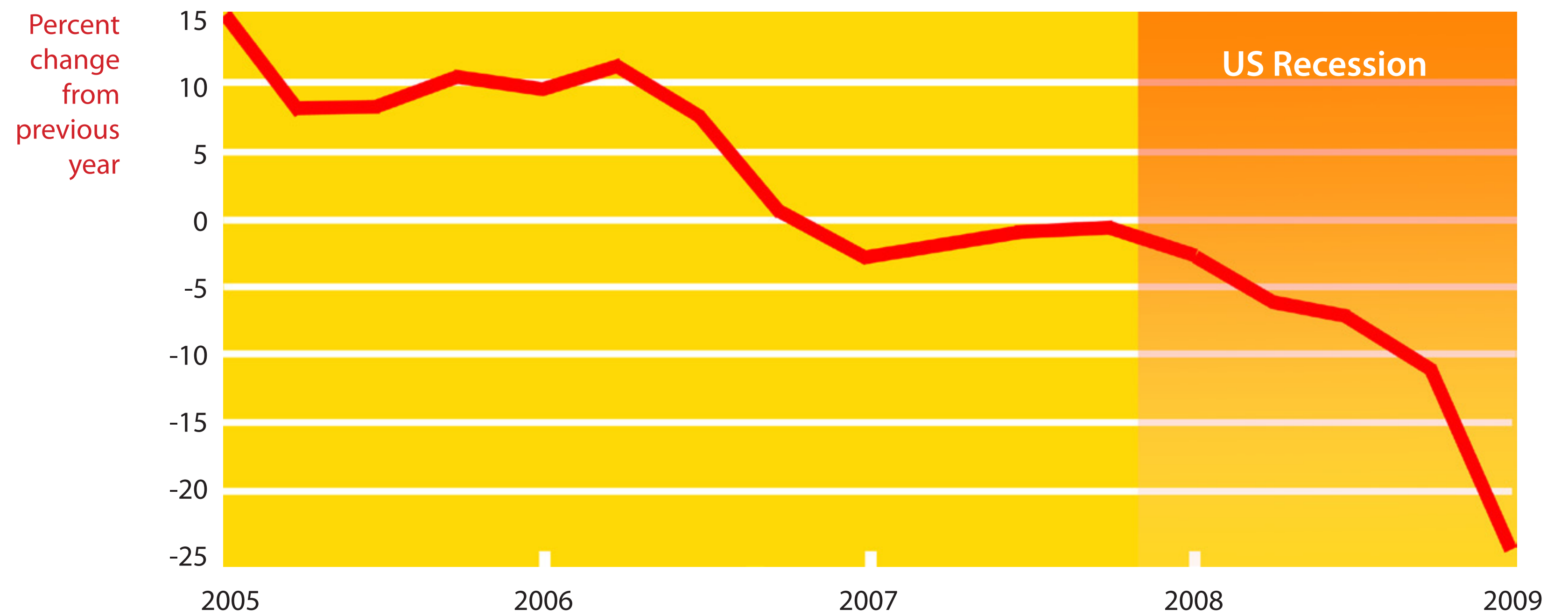
In spite of this full-blown fiscal stimulus plan, recovery and reinvestment have not burst onto the American economy. First, the multiplier effect that many Keynesian economists have hoped for may not exist. A multiplier effect is the amount that an economy's output increases in terms of a multiple of the amount of stimulus, usually in the form of deficit spending. In a Keynesian Economic Model, prices are treated as rigid in the short term, so if government spending is to increase through deficit spending, then this increase in spending in the short run will result in an increase of actual output, partly because prices and inflation are not able to adjust (Blinder, 2008).



Although this effect is widely accepted, the size of the multiplier is still debated. The usefulness of stimulus spending requires a multiplier effect that is greater than one. This means that for every stimulus dollar spent, output increases by more than one dollar. The Obama administration uses a value of 1.5 for the multiplier in predictions for stimulus spending (Becker, 2009). However, research by economist Robert Barro of Harvard University shows empirically that past multiplier effects have never been greater than 0.8; and this at a time of increased defense spending during World War II, the best time to observe a large multiplier effect (Redlick, 2009). Possible reasons for these small multiplier effects are inefficiencies in government decision making, administrative costs of stimulus packages, a lack of relevant information in determining important spending opportunities, politicizing of spending, tax policy, and the rational expectations of consumers to save money in preparation for the end of stimulus spending (Becker,

2009). This means that government stimulus in the past has cost more than the increases in output, making stimulus spending an inefficient way to boost output or employment.

Second, fiscal stimulus and budget deficits have a possibility of crowding out private investment. As government presence in the economy increases, spending is financed by selling government bonds. Since the government is a large percentage of GDP, it can consume a large enough quantity of loanable funds to drive up interest rates, making it harder for private investment to obtain funds, thus crowding out that private investment. If Ricardian Equivalence holds true, then the public will further curtail spending in investment in order save for future tax liabilities (Ley, 1999).



The US central bank has lowered interest rates as low as possible to bolster investment in the short run, regardless of large budget deficits. However, the empirical evidence from the St. Louis Federal Reserve Bank shows that as government expenditures have increased in the last five years, private investment has fallen precipitously (The St. Louis Fed: Economic Data 2010).

The problem with falling private investment is that private investment is one of the key factors to sustainable long run growth, the kind of growth that is needed to bring the economy out of the deep recession currently gripping the world. It is investment that increases the capital stock of an economy, allows for research and development, and fuels the entrepreneur (which fuels innovation and economic growth). The increase in capital allows for greater production and lower costs so consumers buy more from a wider array of products (Skousen, 2010). Fiscal stimulus spending in the pursuit of economic growth creates large deficits, crowds out investment, and translates to less economic growth and recovery in the long run.

Thirdly, large deficits also imply that a government must raise large sums of money in the future due to the government's budget constraint of paying all debt and budget expenses. In order to pay high interest, money is raised quickly through government bonds, which bring into question a government's ability to pay down current debt and the bonds taken out to cover interest. The result is a fall in consumer confidence, causing new recession and a devaluation of government bonds as well as currency. A fourth critique of fiscal stimulus as ineffective crisis intervention by the government is the rational expectations critique put forward by economist Robert Lucas. As

investors and consumers expect a fiscal stimulus, they change their reaction to stimulus spending according to what they expect out of the economy. If people expect the economy to perform less than optimally, then it becomes very difficult for policy makers to successfully manipulate expectations about the economy. Since recessions are usually coupled with poor expectations for the economy, the rational expectations critique implies that fiscal (or other kinds of stimulus) will always be less effective than what might be suggested by economic models (Spector, 1999).

Even if multiplier effects greater than one were observed, crowding out of private investment did not occur, debt was not an issue, and the effects behind the rational expectations critique did not detract from the effectiveness of intervention to stimulate the economy, there is still the obstacle of actually implementing fiscal policy quickly enough to have the desired effect.

First, the business cycle is difficult to forecast. This means that any counter-cyclical fiscal intervention will have to occur after the economy is well into the recession (Spector, 1999). As an example, the American economy had been in a recession for two quarters before the ARRA was passed.

The second time lag when implementing a fiscal stimulus comes after it has been approved by the government. The ARRA was passed 15 months ago, but less than half of that spending has yet been implemented. This dissipates the effects of government fiscal stimulus even more by spreading the spending out over a long period of time, lowering the chance of changing expectations of the economy (Spector, 1999).

Fiscal stimulus translates into less economic growth

Finally, the lag in experiencing the full effect of a stimulus package in the economy can be quite long. Since it is difficult to implement the entire spending of a stimulus package quickly, it sometimes takes years for the entire effect of a stimulus package to be felt throughout an economy. The real threat is that the impact of all of these time lags in fiscal stimulus, from recognizing the recession, deciding on a stimulus package and implementing it, to the effects of stimulus being felt in the economy, can result in a stimulus package that, while intended as a counter-cyclical influence, actually becomes a pro-cyclical measure (Spector, 1999). The existence of other, quicker counter-cyclical interventions such as monetary policy, make deficit spending a dangerous and ineffective tool for intervening in an economic crisis (Skaggs, 1999).

Large deficit spending by the government in an economic crisis is recognized as a way to manipulate the economy in the short run in the Keynesian and neo-classical economic models. However, from past attempts to influence the economy through government fiscal intervention economists have learned that there are a plethora of unexpected and often negative consequences. The multiplier effect is often, if not always, less than one, implying that fiscal policy in general wastes money, crowds out investment, and sets the stage for future inflation and recessions. As far as government intervention in the economy goes, fiscal policy is a tool that should be left by the wayside; the costs far outweigh the benefits. Whatever the government's role is in an economic crisis–be it in Greece, the US, or elsewhere–fiscal policy is not an option. ■

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Michael attends Truman State University as an economics major and statistical methods minor. Michael also represents Truman State University in NCAA Division Two Cross Country as well as Track & Field.

Let the Market Correct Itself:

The Unintended Consequences of Monetary Policy

by **Joshua Schultz,** Ottawa, ON

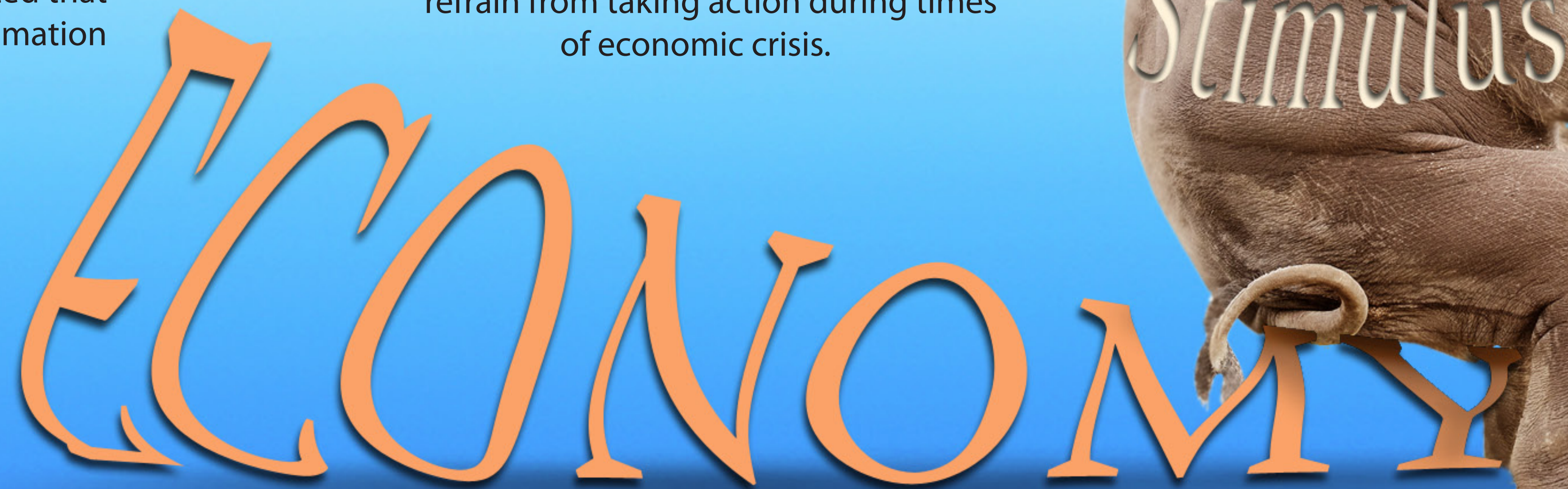
"All history is the history of unintended consequences" quips historian David Blackbourn (2006, 16). This is implicit in Adam Smith's notion of an "invisible hand" guiding economic action (1976). In his opinion, *laissez-faire* is the wisest course of action for economic growth, since it allows

the "invisible hand" to do its work. Smith is warning government about too much interference. His *laissez-faire* approach avoids the unintended consequences of government action. Let the expansion of the economy be the result of individual self-interest.

Over two hundred years later Smith's admonishment to "let it be" provides a simple but poignant lesson for governments responding to the recent global recession. Yet the approach of modern statecraft towards the economy has proven to be a far cry from a mantra of non-interference. If the actions of governments since the economic downturn of December 2007 indicate anything, it is the belief that with the right amount of stimulus and the proper monetary policy, the economy is fixable. At the heart of this conceit is the notion that the state is the prime agent of change and the impetus for the improvement of society. While campaigning in 2008, President Barack Obama betrayed such a sentiment when he stated that "Globalization and technology and automation all weaken the position of workers, and a strong government hand is needed to assure that wealth is distributed more equitably" (WSJ, June 17, 2008). In October of the same year, the American House of Representatives under then-president George W. Bush passed the *Emergency Economic Stabilization Act of 2008*, which authorized Secretary Treasurer Henry Paulson to buy up toxic assets and inject capital into major banks. This cost taxpayers US $700 billion (Lawder, 2008). Under Obama the United States Congress passed the *American Recovery and Reinvestment Act of 2009*. The measures included in this act cost a further US $787 billion (Pub.L.: 111-5). The intended consequences of these acts were to prevent a major financial meltdown and to stimulate growth in the economy. Alas, the unintended consequences of such massive spending will prove to be far worse.

What are the consequences of bailouts and massive stimulus packages?

All this is not to say that government should refrain from taking action during times of economic crisis.



Rather, it is the type of measures enacted that is at issue. Contrary to John Maynard Keynes' suggestion that government spending should make up the shortfall in consumer spending during a recession (1936), the best course of action for government is to cultivate an environment conducive to long-term economic growth through purely negative measures such as tax cuts, cuts in government spending, and the facilitation of free trade through the abolition of subsidies and tariffs. It should refrain from tampering with the interest rate and financing stimulus packages.

Government has an important role to play in creating a stable environment for economic activity through the provision of law and order, the protection of property rights, and national defence. During the 20th and 21st centuries its purview has been extended far beyond this role. A 1998 article by James Gwartney, Randall Holcombe, and Robert Lawson in the *Cato Journal* demonstrates that government spending as a share of the GDP rose on average from 27% in 1960 to 48% in 1996 in the 23 nations that comprise the Organisation for Economic Cooperation and Development (OECD). The United States government fares well here in comparison to other nations with its expenditures at only 35% of GDP. The total increase in spending from 1960 was only 6.2%. The overall trend, though, is a worrying one. The findings of the authors confirm that for every 10% in government spending GDP growth is reduced by 1% (Gwartney, Holcombe & Lawson, 1998: 163-165). This begs the question: what are the consequences of bailouts and massive stimulus packages for developed economies such as the United States?

Future generations in the European Union and the United States will be paying off government debt for years to come. As Richard Salsman outlines in a recent *Financial Post* article, the federal deficit in the US will have risen from 1.2% of GDP in 2007 to 10.6% by the end of 2010 (May 11, 2010). This most certainly means higher taxes. In countries that print their own money, higher prices as a result of inflation will become a problem. In countries that do not, austerity measures will be the only recourse. Undoubtedly, future consumer spending has been sacrificed in the name of a short-term political boost in the present. The process of creative destruction--that is, the failure of uncompetitive businesses and the reallocation of labour--is necessary for future innovation and is the reason for capitalism's success (Schumpeter, 1987). If governments continue to prop up failed enterprises and bail out irresponsible financial in stitutions, it will be impossible to tell what sort of technological and financial innovations will never occur as a result (Acemoglu, Feb., 2009). Economic stagnation becomes a very real possibility. What of the plethora of unintended consequences?

The overall trend is a worrying one

Governments **must** let the market correct itself

Fortunately, history provides some guide for how governments should act in response to economic crisis. Against the grain of conventional economic wisdom, Thomas E. Woods Jr. holds up President Warren G. Harding's response to the depression of 1920-21 as exemplary. In contradistinction to the countercyclical policy of later governments, Harding reduced the government's budget by half and lowered taxes for all income groups. Additionally, the Federal Reserve did not move to increase the money supply in order to fight the economic contraction (Woods, Fall, 2009). The economy rebounded relatively quickly. By the late summer of 1921, recovery was already evident. Unemployment, which had jumped from 4% to 12% at the onset of the depression in 1920, was down to 6.7% in 1922 (Woods, Fall, 2009).

Harding's prudent response to the depression of 1920-21 paved the way for the economic boom of the 1920s. Economic historian Gene Smiley notes that the '20s were marked by innovations in business organization, transportation, and manufacturing technology. While it is generally assumed that the bust years of the Great Depression were an inevitable consequence of the boom years that preceded them, he argues to the contrary that the 1930s and World War II were interruptions to economic growth that only resumed in the 1950s (Smiley, March 26, 2008). The New Deal and World War II spending delayed an economic recovery that would have greatly eased the poverty caused by the Great Depression. Thus, the lesson of Harding's presidency is that sustainable and long-term growth results from a fiscally responsible government that refrains from tampering with the free market.

The teachings of Austrian economist Ludwig von Mises are instructive here. Recessions are inevitable in a free market, but their length and severity can only be enhanced by government interference. Artificially low interest rates and an expansion of the money supply encourage continuing investment in failing enterprises. When the recession does come, government intervention has only succeeded in the higher production of more unwanted goods (Mises, 1953). The 2008 crisis in the housing market is an example. Cheap loans made possible by the federal government led to the construction of houses for which there was no real demand. As soon as the demand for houses was revealed to be artificial, prices dropped and houses could no longer serve as collateral for the loans that purchased them, rendering them unprofitable (Butler, 2010, 78-80). The best solution is no solution at all: governments must let the market correct itself.

Keynsians like Paul Krugman would have us believe that simply stimulating more consumer spending will revamp the economy. In this scenario, rather than saving their money, consumers would spend it on more goods, which would in turn prevent job losses and market failure (Krugman, Oct. 31, 2008). Unfortunately, this also results in less saving. Resources will be put to use creating non-essential items. Loans will not be available for businesses to invest in long-term projects, artificial demand is sustained, and another market correction is inevitable (Murphy, Nov. 11, 2008). Short-term political gain is traded for long term economic pain.

In 1933 Keynes remarked of capitalism, "[it] is not a success. It is not intelligent, it is not beautiful, it is not just, it is not virtuous--and it doesn't deliver the goods (Keynes, June 1933: 762)." Keynes was correct in that there is nothing intelligent or elegant about capitalism. It provides no moral instruction. There is no blueprint for creating a future utopia. It is simply a system whereby individuals are allowed to freely exchange goods, and where the money-grubbing merchant and avaricious banker must ultimately cater to the fancies of the fickle consumer. Thus, the one thing it does do is deliver the goods. In the final analysis, a robust free-market is the solution to economic crisis. The government's role in this is common sense: "peace, easy taxes, and a tolerable administration of justice" (Smith, 1829: 64). ■

Joshua Schultz completed an undergraduate degree in history and philosophy at Brock University. Then pursued his M.A. in history at the University of Waterloo and graduated in 2008. That same year he began his Ph.D in history at Carleton University with a focus on the history of medicine in Germany.

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Crises & Responses:

How Should Free Societies Respond to Economic Calamities?

by **Ryan G. Hauser**
Patrick Henry College
Virginia, US

To some extent, the response of a government in times of economic calamity depends on the type of crisis. A different response—or rather, different facets of the same coherent economic policy—can be used for different types of crises whether they occur in the banking system, fiscal policy, monetary policy, etc. But then the question inevitably arises: from which overarching economic policy do we reason? As freedom-loving nations, we ought to craft policies that favor liberty. Especially with regard to economic policy, liberty is essential because it permits freely informed decisions by individuals, families, and institutions that in effect provide the foundation for a free-market economy and also enable us to experience all of the blessings therein.

So we are faced with a predicament: in an age of increasing regulation, high taxes, and a seemingly omnipotent bureaucracy, is it possible to craft a policy for economic recovery that favors freedom? Furthermore, can it also increase prosperity? The answer to both of these questions is yes. For the purposes of this essay, we shall consider perhaps the best-known example of an economic policy that both increases freedom and aids market recovery: the reduction of taxation.

In America in recent years, we have seen the rise of a sort of neo-Keynesian economic

policy by way of the "stimulus package." This is best exemplified by the American Recovery and Reinvestment Act of 2009. While such stimulus packages do not operate on the explicitly Keynesian doctrine of promoting deficit spending, they end up doing so in consequence. This type of economic recovery plan does, however, hold the Keynesian view that government spending is *the* solution to economic catastrophe (or something milder). It is presumed, whether directly or indirectly, that the government best knows how to spend taxpayer money to get the economy on its feet again. This mindset is not all that different from the old economic philosophy of central planning, which explicitly stated that planners knew how to better allocate capital and resources. But this is a fundamental denial of the basic operations of the market economy with independent individuals, families, and institutions making their own decisions. In the end, a single government administrator or even a well-informed group of congressmen or parliamentarians can never possess enough information to make knowledgeable decisions about *exactly* where the money is most needed in the ailing economy. That is to be left to the processes of the market as guided by what the classical economist Adam Smith referred to as the "invisible hand." If that were not enough, the stimulus packages of today only deal with the peripherals of pork projects, public works, and various other enterprises; they do not supply money to where it is needed the most–in individual homes and businesses to be invested as needed. Therefore, it is necessary to give this money back to the constituents to let *them* reinvest it. Or, better yet, the money should be left to the individuals in the first place with the government only taking enough for its strictly defined duties and responsibilities.

The thing about economics though, along with any other form of historical analysis, is that theories beg examples and vice versa. Therefore, let us examine two examples from the post-war economic landscape of the United States, one in a progressive administration of the early 1960s and one in a conservative administration in the 1980s.

Shortly after taking office in 1961, President John F. Kennedy recruited the Keynesian leader of the Yale School of economics, James Tobin, to serve on the Council of Economic Advisors. During that period, the Yale School advocated the use of loose money and high taxes to overcome the Eisenhower slump of the '50s. And, like all well-bred Keynesians, the Yale School advocated deficit spending. But in the face of a stock market collapse in the summer of 1962, Kennedy (who himself was personally educated by leading American Keynesian Paul Samuelson) opted for tight money and tax cuts. These "unorthodox" tax cuts became law in 1962 and 1964 and ended

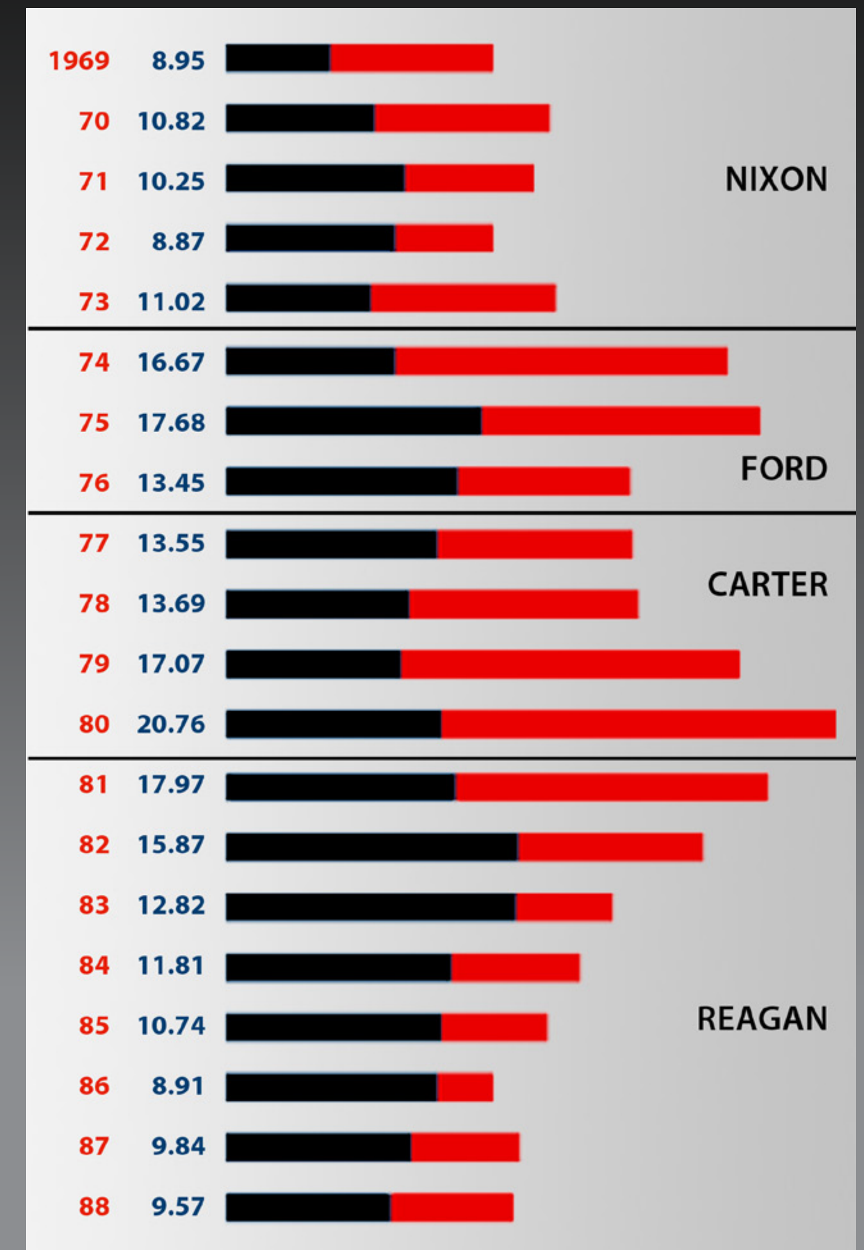
In 1962 Kennedy opted for tight money and tax cuts

Carter was hostile to tax cuts

up boosting economic growth to 5.1% from 1962-1968, which was more than double that of the Eisenhower years (Domitrovic, 2008: 37). Unfortunately, all of this work would be erased by the tax hikes of the Johnson and Nixon administrations–a time that the economic historian Brian Domitrovic would term some of the "truly most unenlightened" years in federal economic policy (Domitrovic, 2008: 37).

Alas, the lessons of the early sixties would not last. Instead, the '70s ushered in a period of tremendous inflation and slothful growth known as stagflation. Indeed, the misery index (a combination of inflation and unemployment rates) had tripled from the post-war average of 7 to an astounding 21 in 1980 (see accompanying graph) (Domitrovic, 2008: 34). As for President Carter, he was hostile to the congressional clamoring to lower marginal tax rates, especially from Congressman Kemp and Senator Roth. Despite passing both the Senate and the House, the Kemp-Roth bill (which would have lowered tax rates by 30%) was terminated on the president's explicit orders (Domitrovic, 2008: 40). Carter chose instead to focus his efforts on another part of the tax code: specifically, whether or not martinis could be deducted at a business lunch. Meanwhile, the misery index soared.

Unemployment and Inflation Rates



Note: The black part of the bar represents the unemployment rate, and the red part represents the inflation rate.

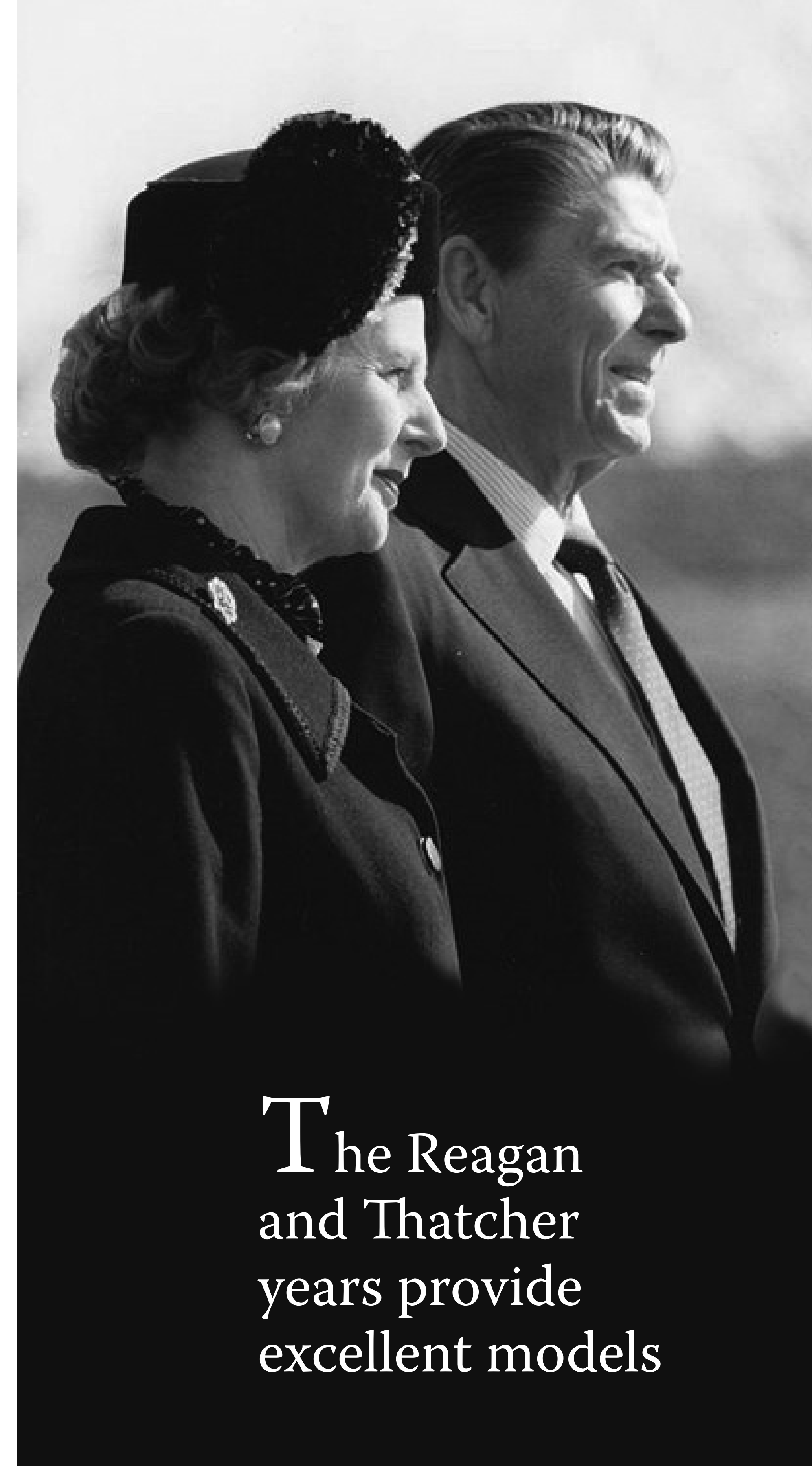
Provided by http://www.miseryindex.us/customindexbyyear.asp - May 30th, 2010.

Enter Ronald Reagan, who in 1980 campaigned for the U.S. presidency with a firm grasp of supply-side principles, and who would later name such supply-side notables as Milton Friedman and Arthur Laffer to his Economic Policy Advisory Board. Upon taking office in 1981, Reagan immediately sought to pass the Economic Recovery Act which called for deep tax cuts to be phased in over three years as well as industrial deregulation and tighter control of the money supply (Henrie, 2006: 714). He achieved further victory in 1986 with the Tax Reform Act which lowered the highest personal tax bracket to 28% (from a high of 70% in 1981) (Henrie, 2006: 714). Over the span of his eight-year administration, the misery index was reduced by 46.7% and stagflation was defeated--a remarkable feat by any criterion.

Soon, the tax reduction method of combating recession would abound throughout many parts of the world; perhaps most notably in Britain where Prime Minister Margaret Thatcher would provide a much needed supply-side shot in the arm for what was termed "the British disease." These were important events in both economic history and the fight for human freedom as the supply-side revolution swept the stage. As Nobel economics laureate Robert E. Lucas wrote in the *Wall Street Journal* in September of 2007, "In the past 50 years, there have been two macroeconomic policy changes in the United States that have really mattered. One of these was the supply-side reduction in marginal tax rates, initiated after Ronald Reagan was elected in 1980..."(Lucas, 2007: A20). Both the heterodox tax cuts of the Kennedy years and the supply-side revolution of the Reagan and Thatcher years provide excellent models of what governments ought to do in times of economic crisis.

However, in the grand scheme of things, it is not enough to simply administer a lowering of the tax rate whenever a recession rolls around, only to be lifted once the market reaches equilibrium again. Indeed, "the full positive effects of lower marginal tax rates are not observed until labor and capital markets have time to adjust fully to the new incentive structure," writes economist James D. Gwartney, former chief economist of the Joint Economic Committee of the US Congress (2008). Simply put, tax cuts work best in the long run. Nevertheless, it should be noted that recessions provide an excellent opportunity for marginal tax deductions to be implemented, thus encouraging a return to prosperity and growth as evidenced by the Kennedy and Reagan administrations in the US, and the Thatcher administration in the UK.

So that is the thrust of the argument, that in times of economic uncertainty, it is better that even more freedom to spend should be granted to the people—not the government.



The Reagan and Thatcher years provide excellent models

Consider the lessons of history...and come down decisively on the side of economic liberty

Furthermore, the implementation of strenuous taxation is fundamentally incompatible with sustainable, ordered liberty. As the Austrian School political economist Wilhelm Röpke writes, "Again and again we see ourselves cheated of the hope of reducing to tolerable limits the crushing weight of taxation, *which in the long run is incompatible with a free or even moderately sound economy and society.*" (Röpke, 1960/1998: 29) [Emphasis added.] Recessions have a great capacity to make or break the struggle for liberty and against statist policies. The onus is on the people of a nation: will they secure even more economic freedom for themselves or will they transfer their spending power to the state to be invested poorly or even capriciously? Before they make their decision, they ought to consider first the lessons of history with regard to that very predicament, and, in the end, come down decisively on the side of further economic liberty. ■

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Financial Armageddon

by **Jeff Bone**

Ronald Reagan had a clever joke: "I am not worried about the deficit" he said, "It is big enough to take care of itself." A deficit occurs when a government spends more money then it brings in through taxation. The former US president said this in 1984. Since then, governments around the world have continued to borrow at ever increasing rates for public funding. Today, most governments have accumulated large and looming public debts. This leaves serious questions about the future. Firstly, who is to pay for the consequences of this debt? Depending on whether you were born after 1980, you may not want to hear the answer because it is you who will pay. Therefore, if you are not currently aware of this situation, you should become intimately involved as this will likely become the paramount political issue for the next 50 years.

For instance, a recent working paper from the Bank of International Settlements (BIS), which is known as a bank for the central banks of the world, is concerned that the European Union is in serious economic decline. Further, the report suggests that the public debt of several western countries will exceed 100% of their Gross Domestic Product (GDP) within a year. GDP is the measure of countries overall economic output by including all goods and services

made within that nation each year. Without "drastic measures" countries such as Austria, France, Germany, Ireland, Italy, Spain, Portugal, Britain, and even the United States will be confronted with paralyzing debt obligations in a serious and restrictive manner (Cecchetti; Mohanty and Zampolli, 2010). As seen with Greece in May 2010, the consequences of even a single country cracking under the weight of its debt obligations will reverberate throughout the entire global economy. The price tag on this most recent bailout sponsored by the European Union and the International Monetary Fund (IMF) was US $1 trillion (Abma, 2010).

A country coming to terms with a debt problem must undergo a painful process of so-called austerity measures where, simply put, taxes increase and services recede. These are necessary conditions that the IMF attaches to most bailouts. In the case at hand, Greece has credit problems, so in order to demonstrate their credit worthiness, they have to display a serious commitment towards emerging out of this debt crisis through a reduction in public spending.

While the IMF is willing and ready to step in as a white knight considering the economic events in Europe, it is less likely they would exert the same measures in the United States, which, despite its size and influence, is potentially close to paralleling similar financial problems if public debt is not managed. However,

if such a time did come, practically speaking, who is the IMF to dictate the terms of economic surrender to the United States? The United States remains the world's lone super power and carries rights and responsibilities associated with that title. Although, if history may provide a lesson, it should be remembered that there was a time in the known world that the ultimate power was Rome, which reigned in a supreme and secure fashion and no one would have predicted its demise. It took several hundred years of precipitous decline, but eventually Rome did fall.

The United States may be an enviable nation, but it is a monster with a weakness, and right now that seems to be its ignorance and willful blindness to the realities of the current economic climate. As according to the BIS working paper, the U.S. debt-GDP ratio will hit 150% in the next decade. Unfortunately, it will have company, as Britain's debt-GDP will hit 200%, and Japan at an astronomical 300% by decade's end (Cecchetti; Mohanty and Zampolli, 2010). Therefore, these austerity measures that have been mandated in Europe are clearly a taste of things to come.

This should serve as an ominous warning even in Canada where we have remained relatively unscathed by the credit crisis of 2008. Arguably, we have emerged as a global leader in financial solvency and fiscal restraint. However, after two years of prodigious bailouts all over the

If nothing is done...it will certainly release financial armageddon

world, Canadians seem apathetic towards our own spending. For instance, recall the domestic $47.2- billion Economic Action Plan, which essentially failed to contribute improvements to the Canadian economy (Veldhuis et al., 2010). Or consider the preceding years of corporate welfare provided to the Ontario auto sector and paid for by Canadian taxpayers (Milke, 2009). Finally, looking into the future, it is important to understand the consequences of Canada's obligation as an IMF shareholding nation to provide liquidity to those countries in need. If one factors in Canada's commitment to the World Bank along with the IMF, that amounts to over $30-billion (Morgan, 2010). This warrants the serious and full attention of young Canadians. If nothing is done differently in the world's economic order, it will certainly release financial Armageddon, but probably only in time to completely saddle the next generation. I think we need to have a serious and open debate about these problems before the gravity of this situation sinks the western economic world into a state more akin to the Dark Ages than that of the Great Depression. ■

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Subsidizing arenas means putting taxpayers in hock for decades, with zero benefit to the economy

By **Mark Milke** and **Niels Veldhuis**

Given the federal government's past, present and projected future red ink, Canadians could be forgiven for thinking Ottawa might prefer to pinch pennies rather than dole out hundreds of millions more in corporate welfare, this time to the most undeserving recipients of all, pro-sport franchises, most owned by billionaires.

But politics may soon trump economic sense once again. While Prime Minister Stephen Harper said last week that his government will never directly fund professional sports teams, he did leave open the door that taxpayers might be forced to ante up for the facilities such teams play in.

Moreover, his comments this week—he downplayed a federal role but then said "if there is a role for the federal government, it must be equitable across the country and also affordable" did nothing to dispel the possibility of taxpayer-funded largesse for professional sports.

In fact, his comments upped the potential bill. The rumoured amount for a Quebec City arena is $175-million from the Quebec government and a similar amount from Ottawa. Add to that "equitable" and similar amounts for other sports venues in Calgary, Edmonton, elsewhere in the Prairies, and perhaps in Hamilton for a dreamed-of NHL team there, and soon taxpayers will be spending real money.

To fund such arenas is no different than to fund factories for automotive or aerospace companies and yet claim taxpayers are not being forced to "directly" fund General Motors, Chrysler, Pratt & Whitney or Bombardier. It's a distinction without a difference.

There are so many reasons not to fund for-profit sports teams that it is difficult to know where to begin.

Start with supposed benefits to local economies that promoters of government subsidies trumpet—increased economic activity, more jobs, increased tax revenues, higher incomes and a more attractive

environment for future business prospects.

The myth here is that sports teams have a magical "multiplier effect" upon the local economy. Build-it-and-they-will-come economics—or in the case of threats to leave a city, the notion that massive amounts of economic activity and tax revenues will be lost—are unsupportable claims.

Money spent on professional sports tickets comes at the expense of spending on other activities—movies, concerts, or dining out. Thus, heaven forbid, if the Calgary Flames or Toronto Maple Leafs left their respective cities, some sports fans who previously spent $1,000 on tickets and beer every season aren`t going to throw such money into the fireplace in their absence; they'll likely spend it somewhere else, on minor hockey, more beer, or on some other event, and economic activity and tax revenues will still result.

The economic logic is the same if an NHL team ended up in Quebec City. People who previously might have spent money on skiing or the Quebec winter carnival will spend some of their disposable income on NHL hockey tickets.

So do taxpayer subsidies for sports teams have a net beneficial economic effect? Not according to University of Maryland professor Dennis Coates and University of Alberta professor Brad Humphreys, who recently reviewed the academic literature on the economic impacts of professional sports franchises and stadiums. They conclude that, "No matter what cities or geographical areas are examined, no matter what estimators are used, no matter what model specifications are used, and no matter what variables are used, articles published in peer-reviewed economics journals contain almost no evidence that professional sports franchises and facilities have a measureable economic impact on the economy."

Ironically, rather than increase local economic activity and income, a diversion of consumer spending to professional sports teams (or their "facilities") can often have the exact opposite effect. Given that salaries make up most of a team's expenditures, and that professional sports teams players most often do not live in the city in which they play, the result is that much of the money consumers pour into tickets ends up getting spent in other cities and often other countries.

Even worse, all a subsidy for an arena will do is put taxpayers in hock for decades.

The *New York Times* just reported that the now-demolished Giants stadium in New Jersey has US$110-million in debt taxpayers must still pay off; in Seattle, the Kingdome demolished one decade ago is still pulling tax dollars away from citizens with US$80-million in outstanding debt.

The economics of subsidies to professional sports teams have always been abysmal and haven't changed; it's why proponents usually resort to emotional arguments. Perhaps that's why in Quebec City last week, jersey-wearing Veterans Affairs Minister Jean-Pierre Blackburn said it was important to remove the "scars" Quebecers suffered when the Nordiques moved to Colorado in 1995.

Such made-up psychological "wounds" are nothing in comparison to the actual fiscal damage done if provincial and federal balance sheets engage in more corporate welfare, but this time to professional sports teams. ■

Mark Milke is director of Alberta policy studies and Niels Veldhuis is vice-president of research at the Fraser Institute.

Mark Milke

Niels Veldhuis

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In the meantime feel free to explore the archives at: ***http://www.fraserinstitute.org/education-programs/students/ask-the-professor-blog.aspx***

The following article is from the January 2010 "Ask the Professor" discussion about the economics of fascism with Dr. Steven Horowitz.

The topic of fascism is so vast that it will be very hard to do it justice in this short space. To make it manageable, I want to focus on the economics of fascism. That is, what were the economic institutions and practices that were put into place by fascist regimes in places such as Mussolini's Italy and Hitler's Germany? In exploring this question, I hope to make two points. First, contrary to the accusations made by many on the Left, fascism is not some extreme form of capitalism. I hope to show that it's more accurate to say that fascism is a form of socialism. Second, there are indeed similarities between the economic practices of 20th century fascism and some of the transformations we are seeing in the US economy and elsewhere in the Western world, particularly in the wake of the Great Recession.

What the fascism of Italy and Germany shared was a rejection of the liberal order of the 19th century. The influential thinkers in both countries disdained capitalism and democracy as both "individualist" and "internationalist." The problem with both systems was that they paid insufficient attention to the collective needs of the nation. Capitalism in particular allowed individuals to profit as they saw fit and that led to them placing profit over the common good of the nation. It also led to the breakdown of international barriers through free trade. The intellectual architects of the various fascist movements thought that the collective goals, especially the military ones, of a nation were to be valued far more than the crass commercialism of capitalism. As a result, they rejected free markets and the other trappings of capitalism (and democracy).

At the same time, however, they also rejected classical socialism. Marxian socialism argued that one's class was the most important element of one's identity. For the fascists, putting one's class over one's nation was a mistake; one's national (or racial) identity should be primary. The Italian worker had more in common with the Italian capitalist

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than the Italian worker did with a German or Russian worker. Nation trumped class.

What emerged as the fascist economic system then was a combination of the socialist rejection of capitalism and the nationalist rejection of internationalist socialism. It's not coincidental that "Nazi" was short for National Socialist German Workers' Party. The very name suggests that the fascists started from a socialist premise (including the emphasis on being a "workers'" party), but added the "nationalist" (and specifically "German") twist. Rather than have full-blown socialism as we saw in the early years of the Soviet Union, the fascists generally preferred hybrid forms that often maintained the appearance of elements of capitalism, but with a much larger role for the state in allocating resources. A look at the Nazi Party platform of 1920 shows the very strong influence of socialism in the economic planks, including objections to the earning of interest, the desire to nationalize industries, the confiscation of profits, and land reform. Not all of these were put into place when Hitler gained power, but the Nazis' antipathy toward capitalism is quite clear, even as they often co-opted big business into their power structure in during their reign. The trappings of private ownership were often preserved, but the Nazis used the power of the state to try to ensure that private ownership was used as a means toward the national ends that they defined.

The Italian model was similar in its broad outlines, though different in its execution. The Italians were more clear than the Germans about the way in which market competition was destructive of national goals. They didn't see Russian socialism as a solution for the reasons noted above. Instead, they argued for industry-level partnerships among labor, capital, and the political class. The idea was that by working collectively, these cartel-like organizations could resolve questions of what to produce, what price to charge, what wage to pay, and the like all without the need for cut-throat competition among firms or workers, or the use of strike threats between workers and capitalists. By putting national interests first, these collectives could plan out production industry by industry and ensure a cooperative peace among Italians. So, once again, the system kept some of the trappings of capitalism, such as nominally private ownership, but set them in a system where collective planning of a limited, and nationalistic, sort was the overarching structure.

Both of these systems are probably most accurately called "corporatism." In such a system, we get these sorts of private-public collaborations in which private ownership is combined with state control and privileges for labor, and where all are expected to serve some larger national goal. It looks like private ownership, which is often the source of the claim that fascism is a form of capitalism, but the degree of distrust of the unplanned order of free markets and the de facto power that falls into the hands of the state to set goals both point to it as being more accurately a form of socialism or planning.

This brief overview should shed light on what most people mean when the refer to the ongoing increase in government involvement in the US economy as "fascist." Most people are not saying that concentration camps and book burning are right around the corner. The thoughtful folks are pointing out, quite seriously, that the bailouts, the government ownership stakes in the car companies and banks, as well as the various public-private partnerships that have characterized the end of the Bush years and the beginning of the Obama administration do represent (more of) a move away from market capitalism, though not toward true socialism but something else, namely something much like the economics of fascism. Many of these changes have been justified by reference to the need to "save" the US economy or other overarching national goals, again akin to the arguments the fascists made for rejecting both capitalism and classical socialism.

As I have argued in previous columns, any movement away from markets is likely to impoverish people. And as Hayek argued in

The Road to Serfdom, giving people power over the economy also means giving them power over the rest of our lives as we cannot separate "economic ends" from non-economic ones.

Unfortunately, ignorance about the economics of fascism has led to much misunderstanding of all of these points. Although a few people do think that the jackboots will be kicking in the doors any day now, they are the exception not the rule. Most of those who are seeing elements of fascist economics in the response to the Great Recession are genuinely concerned about the corporate-state partnerships and the increasing government role in the private sector in the name of national needs. These changes run a serious risk of damaging the economy permanently and do encroach that much more on individual liberty, both in the market and the rest of our lives. Recognizing it now for what it might become is the first step to ensuring that the future is one of more, not less, freedom.

Lisa asks:
If these fascist leaders felt that nation trumped class, isn't this simply a way of encouraging the public toward nationalist pride, and thus entrusting more and more power to their "nationalist" leader who probably cares more about their own power than about the nation? Were these leaders always elected? Can we incorporate public choice theory here somehow?

Professor Horwitz writes:
Great questions, Lisa. I'm not sure the "national pride" stuff was as calculated as all that. I think they really did believe in it, although it certainly also made it more likely that they would have popular support. And yes, in fact fascist leaders were generally elected. Hitler was, although there are issues with how clean the election was.

You can read all of this as a giant rent-seeking machine if you want. It certainly helps to explain why so many capitalists went along with fascism so willingly—they stood to gain from it if those in power liked them. It also explains why we're seeing movement in this direction in the US today. It's Horwitz's First Law of Political Economy: no one hates capitalism more than capitalists. It also helps to have a crisis (as Germany did after the hyperinflation of the 20s) to make the case that a strong leader is needed to restore national pride.

Frankie Paul asks:
It seems contentious to compare FDR and Mussolini. Regardless, was the reason FDR was less overt and militaristic because US citizens were more strongly rooted in the idea of fundamental freedoms?

Professor Horwitz writes:
It's contentious alright, but it's true. You can look it up. :)

I think you're probably right, Frankie. We did/do have a stronger culture of individual freedom, but do keep in mind that many in the 1930s were willing to toss that away in the name of fighting the Depression (sound familiar?). I think probably more important was that we had a written constitution that provided protection for those freedoms, even if it did so imperfectly in time of crisis.

The two most fascist parts of the New Deal - the National Industrial Recover Act and the Agricultural Adjustment Administration—were both ended by Supreme Court decisions that declared them unconstitutional. I think that was the big difference. Had we not had a truly independent judiciary and written constitution, I suspect the history of the last 75 years would have been very different and we'd be a lot less free. ■

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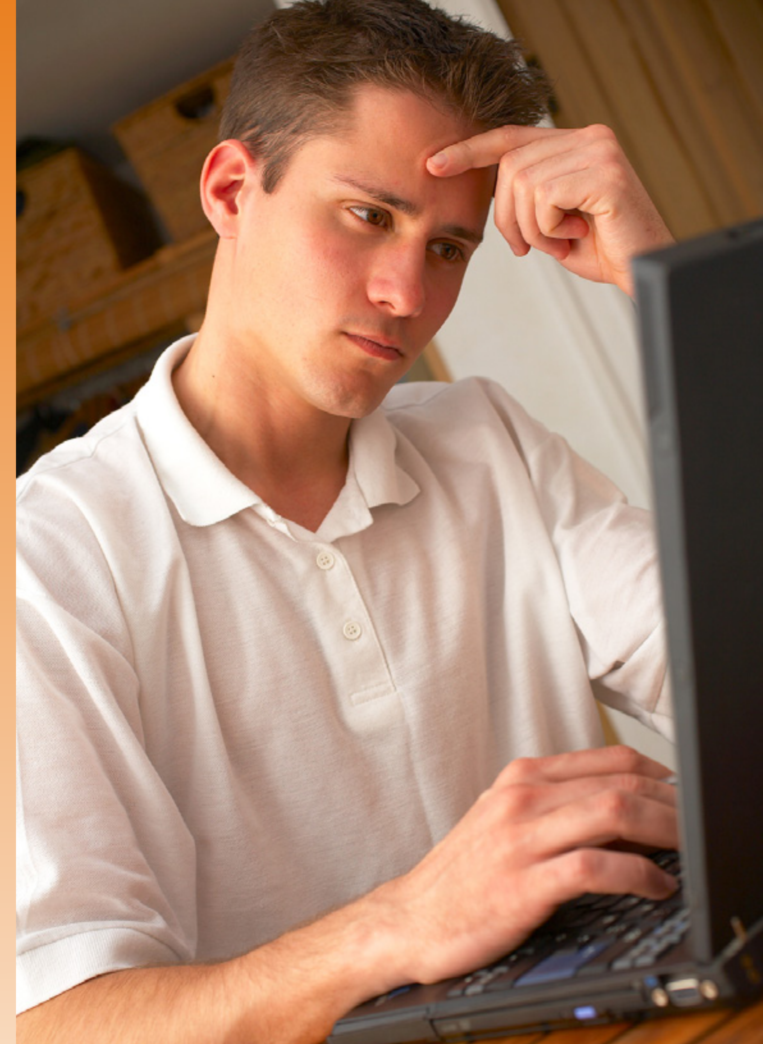

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