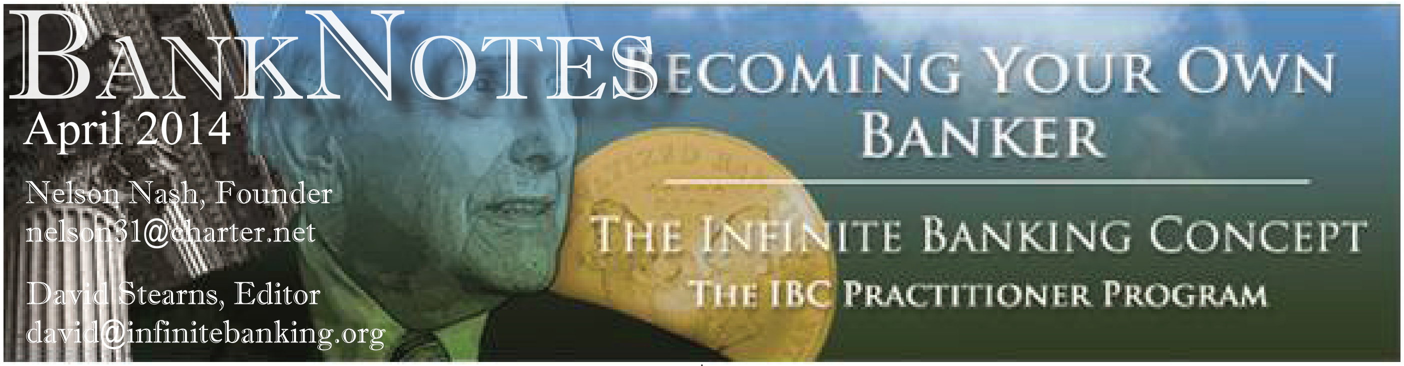

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How Inflation Destroys the Wealth of Nations

By Joseph Salerno Mises.org

March 6, 2014

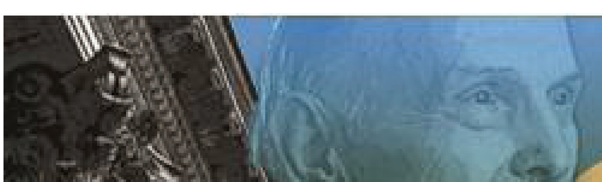
[Editor's Note: This article is adapted from Joseph Salerno's foreword to the new third edition of Brendan Brown's book *Euro Crash: How Asset Price Inflation Destroys the Wealth of Nations*.]

Brendan Brown is a rara avis — a practicing financial economist and shrewd observer of financial markets, players, and policies, whose prolific writings are informed by profound theoretical insight. Dr. Brown writes in plain English yet can also turn a phrase with the best. "Monetary terror" vividly and succinctly characterizes the policy of the Fed and the ECB (European Central Bank) to deliberately create inflationary expectations in markets for goods and services as a cure for economic contraction; the "virus attack" of asset price inflation well describes the unforeseeable suddenness, timing, and point of origin of asset price increases caused by central bank manipulation of long-term interest rates and the unpredictable and erratic path the inflation takes through the various asset markets both domestically and abroad.

Indeed Dr. Brown's prose is reminiscent of some of the best writers in economics and economic journalism such as Lionel (Lord) Robbins and Henry Hazlitt. And like these eminent predecessors, Brown is generous to a fault in carefully evaluating the views of those he criticizes, while rigorously arguing his own position without waffling or compromise. Best of all, Brown is fearless in naming names and ascribing blame to those among the political elites and the upper echelons of financial policymakers whose decisions were responsible for the chaotic state of the contemporary global monetary system.

In this book, Brown deploys his formidable expository skills to argue the thesis that the current crisis and the impending collapse of the EMU (European Monetary Union) are attributable to profound flaws in the original monetary foundations of the euro. These flaws rendered the EMU particularly vulnerable to the asset price inflation virus which was originally unleashed on an unsuspecting world by the Federal Reserve shortly after the euro saw the light of day in 1999.

In the course of presenting his case, Brown courageously stakes out and defends several core theoretical positions that are in radical opposition to the prevailing orthodoxy. For example, Brown



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strongly dissents from the conventional view of what constitutes monetary equilibrium. He explicitly rejects the position associated with Milton Friedman and Anna Schwartz that is now deeply entrenched in mainstream macroeconomics and central bank policymaking. This superficial doctrine arbitrarily and narrowly construes monetary equilibrium as "price stability" in markets for consumer goods and services, while completely ignoring asset markets. In contrast, Brown formulates a much richer and more profound concept of monetary equilibrium that draws on the ideas of Austrian monetary and business cycle theorists, namely Ludwig von Mises, Friedrich Hayek, Lionel Robbins, and Murray Rothbard.

In Brown's view, a tendency toward monetary equilibrium obtains when monetary policy refrains from systematically driving market interest rates out of line with their corresponding "natural" rates. Interest rates determined on unhampered financial markets are "natural" in the sense that they bring about spontaneous coordination between voluntary household decisions about how much to save and what profile of risk to incur and business decisions about how much and in what projects to invest. Such coordination ensures accumulation of capital and increasing labor productivity and a sustainable growth process that maintains dynamic equilibrium across all goods and labor markets in the economy. The main thing that is required to maintain monetary equilibrium in this sense is strict control of the monetary base as was the case, for example, under the classical gold standard regime. In the context of existing institutions, which is Brown's focus, monetary equilibrium requires a rule strictly mandating the Fed to completely abstain from manipulating market interest rates and, instead, to exercise tight control over growth in the monetary base.

Brown's concept of monetary equilibrium therefore countenances — indeed, requires — price deflation over the medium run in response to natural growth in the supplies of goods and services. This was the experience during the heyday of the classical gold standard in the latter part of the nineteenth century when declining prices went hand-in-hand with rapid industrialization and unprecedented increases in living standards. For Brown, it is precisely the attempt to stifle this benign and necessary price trend by a policy of inflation targeting on the part of "deflation phobic" central banks that inevitably distorts market interest rates and creates monetary disequilibrium.

Brown explains that such monetary disequilibrium is not necessarily manifested in consumer price inflation in the short run. In fact, it is generally the case that the symptoms first appear as rising temperatures on assets markets. Indeed some episodes of severe monetary disequilibrium, such as those that occurred in the U.S. during the 1920s, the 1990s, and the years leading up to the financial crisis of 2007-2008, may well transpire without any discernible perturbations in goods and services markets. Yet overheated asset markets are completely ignored in the Friedmanite view of monetary equilibrium that underlies the Bernanke-Draghi policy of inflation targeting. Brown perceptively argues that one reason for the wholesale neglect of asset price inflation is the positivist approach that is still dominant in academic economics. Speculative fever in asset markets is nearly impossible to quantify or measure and thus does not neatly fit into the kinds of hypotheses that are required for empirical testing.

Having laid out his theoretical approach, Brown uses it as a foundation to construct a compelling interpretive narrative dealing with the origins, development, and dire prospects for the euro. In the process, he pinpoints and details the flawed decisions and policies of the ECB and the Federal Reserve that account for the current condition of the euro. But Euro Crash tells more than the story of the currency of its title; it unravels and makes sense of the complex tangle of events and policies that have marked the parlous evolution of the global monetary system since the 1990s.

This book is a radical challenge to the prevalent, but deeply flawed, doctrines that have defined monetary policy since the 1980s. Be forewarned: reading it is a bracing intellectual experience. Like a headlong dive into a cold pool, it will refresh your mind and awaken it to a wealth of new ideas.

Joseph Salerno [send him mail] is academic vice president of the Mises Institute, chairman of the graduate program in economics at Pace University, and editor of the Quarterly Journal of Austrian Economics.

Comment by R. Nelson Nash – *Joe Salerno gives us another book recommendation to read in EURO CRASH. I have not read it yet and so it is not on our website Book Recommendations list. That is because I don't put a book on that list unless I have first read it.*

Do PUAs Grow Less Efficient Over Time? Should Clients Buy New Policies to Better Utilize PUAs?

This article was posted on the Truth Concepts Blog, http://truthconcepts.com/blog/ on 27 March, 2014. It originated from Todd Langford's presentation at the 2013 IBC Think Tank Symposium.

As you know, in the early months and years of a whole life policy, the PUAs are more efficient than the base premium as far as generating cash value for the policy. While the base premium alone can take years to generate a positive internal rate of return where cash value is concerned, the PUAs are converted to cash value right away, which increases the efficiency of the policy overall.

However, after 5-7 years of funding a whole life policy, the impact of the PUAs appears to lessen. Illustrations of a policy funded with maximum PUAs vs. no PUAs at all show that, several years into the policy, the PUAs no longer have a dramatic affect on the internal rate of return of the policy.

For instance, in one example, adding PUAs to a 12k premium whole life policy for the first five years increased the internal rate of return on the net cash value in the 12th year from only .57% (no PUAs) to 3.29% (with 5 years of PUAs) – a difference of 477%!

However, when the PUA is paid for 10 years, the PUAs only bring the IRR up to 3.52%. The difference between 3.29% – the IRR produced when 5 years of PUAs were added to the policy – and 3.52%, the IRR resulting from 10 years of PUAs – is only 6.99%.

Why is this? Do PUAs become less efficient over time? And what should the client do? After the initial years of the policy, should a policy holder start a new policy and put their PUAs into the new policy to increase the efficiency of the PUAs? Is the "old" whole life policy not the best place for the client's PUAs? To test this, Todd compares the effect of transitioning the PUAs to a second new policy after 5 years to see if the average internal rate of return (of the policies combined) is greater when the newer policy receives the PUA payment as opposed to the older policy. This example is given in the first 15 minutes of Todd Langford's *2013 Think Tank* presentation, along with a related discussion (and a hilarious story) about how the numbers alone don't always tell the whole truth about a situation. What Todd discovers is this: the combined IRR of both policies when the PUA stays with the first policy is 2.34%, while the IRR of both policies when the PUA shifts to the new policy is a nearly identical 2.32%.

Todd also discovers virtually no difference in internal rates of return when the policies are extended to age 70. (The results are 4.76% and 4.75% IRR of the combined policies when the PUA is shifted from one to the other.)

The conclusion? Starting a new policy is not necessary to increase the effect of a PUA. Therefore, there is no numerical reason to start a new policy to "increase the efficiency of the PUA." However, the numbers alone don't always tell the whole story. There may be other reasons to start a new policy. As Todd mentions in the video, starting a new policy creates a new "bucket" into which cash can be stored, which may be very beneficial for the client. Each new policy creates an opportunity to store more cash in the way of PUAs. If a client is easily maxing out their PUAs or must prepare for a way to store additional cash, then it may be time to begin a new policy. The PUA may appear to lose efficiency, but in fact, it does not. It keeps performing as well as it ever did, but the impact lessens because the base premium catches up over time in its efficiency. Therefore, the PUA does not continue to create as much contrast when compared with the efficiency of the base premium. A very simple metaphor to understand or explain PUAs vs. base premium efficiency might be that of two joggers. If Jogger A gets a 5-minute head start on a marathon, that will put him or her way ahead of Jogger B in the first few miles. However, by the time they both reach the finish line, that five-minute head start will seem much more insignificant. If they progress at the same speed, at an "average" marathon pace, their times will be less than 2% apart. In the same way, the differences between the efficiency of a PUA and the base premium become negligible as time goes on. Like the first jogger, the PUA gets a "head start" while the base premium is responsible for establishing the foundation of the policy (paying for the death benefit, commission, and other policy costs), which slows it down, initially. Ultimately, the PUA will earn (or "run") at the same pace in an existing or a new policy. The PUA does not grow less efficient with time, the base premium simply becomes more efficient, which narrows the contrast between the two. The only way to start a new policy and have the PUA earn at a greater rate and efficiency than in an existing policy would be to begin a new policy on a child or grandchild. When this is done, typically, the new policy is more efficient because the cost of insurance is less for a younger person. However, as you are limited as to the amount of insurance you can take on a child – often a maximum of half of what the parent is insured for – you will want to make sure that you are adequately insured.

Anti-Logic and the Keynesian "Stimulus"

by William L. Anderson on March 3, 2014

Selected from the Mises Daily on Mises.org

American political culture always seems to be "celebrating" the anniversary of something, be it JFK's assassination (we just passed the 50th anniversary of that sad event) or the signing of some (mostly bad) legislation. The latest political activity to be enshrined with an anniversary is the so-called stimulus, the $800 billion monstrosity passed five years ago ostensibly to "put America back to work."

Not surprisingly, the *New York Times* has editorialized that any criticism of the spending bill — at least any criticism which says "too much" was spent — is a Republican "myth and falsehood." Not only was the "Stimulus" a legitimate piece of legislation, sniffed the NYT, but it also: prevented a second recession that could have turned into a depression. It created or saved an average of 1.6 million jobs a year for four years. (Where are the jobs, Mr. Boehner.) It raised the nation's economic output by 2 to 3 percent from 2009 to 2011. It prevented a significant increase in poverty — without it, 5.3 million additional people would have become poor in 2010.

Like all examples of the Broken Window Fallacy, the spirited defense of this spending bill is based upon "accounting" methods that count the people hired through "stimulus" spending as "new jobs" but fail to note how others might have lost their own means of employment. Now, this was a bill that, among other things, had workers rolling sod into the grass median of I-68 (which is near my home) in an area where runoff collected from tons of salt thrown onto roads by state highway crews (our area receives a lot of snowfall). Not surprisingly, within a year, all of the new grass was dead.

I liken the "stimulus" to throwing a bit of lighter fluid onto a pile of soaking wet wood. The flames pop up for a few seconds, but then disappear as the effects from the fluid go away. (No, repeated douses of "stimulus" fluid do not ultimately gain traction and then lead to a miraculous economic recovery.)

If Beltway political culture permits any criticism of the Holy Stimulus, it is this: "the stimulus wasn't big enough." Intones the NYT: "The stimulus could have done more good had it been bigger and more carefully constructed."

The rest of the editorial is a compilation of near-plagiarism from Paul Krugman's columns and blog posts, and it reflects how Keynesian anti-wogic works. The "logical" narrative goes as follows:

•"Enough" government spending during a recession will bring the economy to "full employment."

•The economy is not at full employment.

•Therefore, there wasn't enough government spending.

Should one question the Keynesian premises of this awful syllogism, the standard answer is: America had "full employment" during World War II. (Robert Higgs has thoroughly debunked this enduring myth.) But, then, so did Germany and the U.S.S.R., according to Keynesian standards, but no one envies what people there experienced!

The problem that occurs when one wishes to interpret the results of the Stimulus is not due to bad politics. To put it another way, Stimulus spending always will confer political benefits, given that the money is transferred from taxpayers to preferred political constituents. Those footing the bill include both present and future taxpayers, since they will have to pay later for the public debt incurred to pay for present stimulus spending.

I make this point because the stimulus always has been presented as a government action that improved general or overall economic conditions, as opposed to being a political wealth-transfer scheme. The NYT editorial drips with what only can be a religious faith in the whole system, as though politicians seeking votes are going to "carefully" construct a process that is aimed at making certain political constituencies better off — but at the expense of other constituencies.

In reality, the government-based stimulus is based upon bad economics or, to be more specific, one of bad economic logic. To a Keynesian, an economy is a homogeneous mass into which the government stirs new batches of currency. The more currency thrown into the mix, the better the economy operates. One only needs to read Krugman's writings to see that belief in full bloom.

Austrian economists, on the other hand, recognize the relationships within the economy, including relationships of factors of production to one another, and how those factors can be directed to their highest-valued uses, according to consumer choices. The U.S. economy remains mired in the mix of low output and high unemployment not because governments are failing to spend enough money but rather because governments are blocking the free flow of both consumers' and producers' goods and preventing the real economic relationships to take place and trying to force artificial relationships, instead. (Green energy and ethanol, anyone?)

Simply put, the stimulus could work only if it were directing factors of production from lower-valued uses to higher-valued uses as determined ultimately by consumer choice. If that actually were the case, then the government would not have to force consumers to use stimulus-funded ethanol and electricity created by wind power.

Austrians arrive at their position through logic, but logic that is based in what we already know about human action. Unlike Keynesian "logic," the premises of Austrian economics are sound, so the conclusions derived from them also are sound. No wonder the Austrian position is banned from the NYT editorial page!

Note: The views expressed in Daily Articles on Mises.org are not necessarily those of the Mises Institute.

William Anderson, an adjunct scholar of the Mises Institute, teaches economics at Frostburg State University.

Comment by R. Nelson Nash – *William Anderson has been a consistent, clear thinking economist friend for a number of years. It has always been amazing to me that folks like Krugman and Ben Bernanke actually get paid for the nonsense that they advocate. Even more amazing is the fact that many Americans really believe their nonsense.*

Herbert Spencer, Freedom, and Empire

by Bryan Cheang on March 12, 2014

Selected from Mises Daily on Mises.org

Herbert Spencer was born into a nineteenth-century world where the traditional logic of imperialism interacted with new developments like the Industrial

Revolution, and new ideas like free trade and liberalism that emerged out of the Enlightenment of the previous century. The key to understanding Spencer's importance is to realize that he was a radical proponent of laissez faire, individualism, natural rights, and capitalism. His call for the limitation of state power was so extensive that it included an individual's right to "ignore the state," that is, to "drop connection with the state — to relinquish protection and refuse paying toward its support." These views were strongly articulated in his book Social Statics, considered by Murray Rothbard to be "the greatest single work of libertarian political philosophy ever written."[1]

This meant that while many developments, such as the burgeoning trade relations of the time, would fall in line with Spencer's outlook, his radical and purist laissez-faire ideology put him at odds with the philosophy of imperialism that accompanied the perpetuation of overseas territorial expansion and militaristic activities of the British Empire.

At a time of great economic transformation brought about by the Industrial Revolution, nineteenth-century Britain saw an expansion of trade and commerce. This was in part due to the embracing of relatively free markets that arose in the decades following Adam Smith's Wealth of Nations, and which were radically propounded by Herbert Spencer. Spencer believed that human progress is best achieved through the spontaneous activities of individuals, since such free competition, absent excessive government regulation, provides powerful incentives for individuals to seek constant development.[2]

Spencer anticipated Friedrich Hayek's concept of "spontaneous order,"[3] and explained that socio-political order depends not on deliberate design or a rational blueprint, but rather emerges spontaneously over years of evolution. Thus, industrial civilization, which was clearly taking form in Britain, emerged not due to the "devising of any one," but rather through "the individual efforts of citizens to satisfy their own wants ... in spite of legislative hindrances."[4] Even the famous steel entrepreneur Andrew Carnegie, who desired to know what propelled human development, was so inspired by Spencer particularly, that he was convinced his work served a grander purpose.

Thus, Spencer welcomed the repeal of the Corn Laws, and the unprecedented increase in the standard of living in Victorian Britain that accompanied rapid population growth and urbanization. He saw these developments as part of a long-run tendency of social evolution toward industrial society, and thus peace. This is related to his belief that there are two chief modes of social organization: the "militant" and the "voluntary."[5] The former is one of compulsory cooperation directed by the State, and oriented toward violent conflict, while the latter is one that is governed by his Law of Equal Freedom, that "every man has freedom to do all that he wills, provided he infringes not the equal freedom of any other man."[6] The selective pressures of social evolution would help mankind progress from the former mode to the latter mode, since "a society in which life, liberty, and property, are secure and all interests justly regarded, must prosper more than one in which they do not."[7]

At this point a tension arises. While Britain was traveling on the long-run path toward industrialism and peace, the traditional structure of empire and Britain's short-run activities vitiated this potential for progress.

Accordingly, Spencer attacked the foreign military adventurism that Britain continued to engage in, since it ran counter to the spirit of liberal progress. Britain had engaged in overseas wars in India, Afghanistan, and South Africa (the Boer War), and elsewhere. He denounced the hypocrisy in imperial policy which often used euphemisms like "defensive war" to mask, what to him was the true nature of imperial aggrandizement.[8] The following becomes clear: Spencer's radical stance struck at the heart of the essence of empire, for it denounced the foreign occupation of colonial territories. At a time when the race for colonial lands was seen to be a prerequisite for the glory and prestige of empire, especially during the late 1800s, Spencer argued that such foreign expansionism fostered tyranny over the domestic people. Britain's need to maintain overseas colonies would inescapably necessitate establishing increasing controls on the British citizens themselves, until the "army is simply the mobilized society and the society is the quiescent army."[9] Colonial empires subjugating other parts of the earth were unlikely to "have so tender a regard" for the rights of their own citizens.[10]

Spencer would ask: how could the pursuit of trade, which is in essence voluntary, and the concomitant drive toward industrialism, which brings peace, sit well with the practice of militarism that makes imperialism and colonialism possible? The uneasy relationship between the spirit of free commerce and the very essence of the imperial structure of Britain is thus brought to light. Free trade was desired for the twin purposes of imperial power and profit; yet, "free trade imperialism," as Spencer contended, is a contradiction in terms, since free trade in essence need not require military action for its promotion. Thus, British naval and military expeditions to secure foreign trading opportunities obscured the hidden motive to "benefit powerful special interests" at the expense of "the poor, starved, overburdened people."[11] Spencer's criticism of state-directed commerce provokes a question: might the new forces of trade undermine the traditional logic of imperialism itself?

In light of these considerations, it is then possible to understand Spencer's pessimism and even despair during his later years. Though Spencer believed that modern civilization, which was taking shape in Britain, was headed toward peaceful industrial society after a long period of liberalization, there would be "temporary reverses and detours" along this upward path. Besides the continued persistence of overseas colonialism, Spencer was also disheartened by what seemed to be the rising tide of Fabian socialism.[12] This movement was accompanied by state interventions into charity and education, which only provoked Spencer's ire: at a time when liberal individualism should be consistently championed, these increasing regulations of society could result only in a "lapse of self-ownership into ownership by the community."[13]

Examining Spencer's intellectual radicalism highlights the ambivalence of empire at a time when vestiges of the old and forces of the new intersected in an uneasy relationship. It was a time when the new spirit of liberal trade and commerce sat tenuously with the use of state power to gain foreign markets; it was a time when the language of modern civilization was used to subjugate other nations for motivations that ran against civility itself, and it was a time when the individual was asserting his dominance against an imperial state that clung on for relevance.

Note: The views expressed in Daily Articles on Mises.org are not necessarily those of the Mises Institute.

Bryan Cheang is a college student from the National University of Singapore, in Singapore. He is currently pursuing his double major in political science and history, with a focus on political theory. His main academic interests are libertarian political theory and Austrian economics, and also European/American history.

Comment by R. Nelson Nash – *I honestly believe that the insights Herbert Spencer blessed us with are due to the fact that he didn't have a college degree. The same can be said for the writings of Henry Hazlitt and my mentor, Leornard E. Read.*

Notes:

[1] Murray Rothbard (1971). Recommended Reading. (M. Rothbard, Ed.) *The Libertarian Forum*, vol. II, p. 5.

[2] R.F Cooney (1973). "Herbert Spencer: Apostle of Liberty." *Freeman* 23.

[3] The idea of a "spontaneous order," i.e., an order that emerges as result of the voluntary activities of individuals and not one which is created by a government, is a key idea in the classical-liberal and free-market tradition, of which Spencer is a part. The key contemporary figure is Austrian School economist and Nobel Prize winner F.A. Hayek, who described it as an extended order consisting of those institutions and practices that are the result of human action but not the result of some specific human intention. http://www.econlib.org/library/Essays/LtrLbrty/bryTSO1.html

[4] Herbert Spencer (2000). *Illustrations of Universal Progress: A Series of Discussions*. Chestnut Hill, MA: Elibron Classics, p. 320.

[5] Herbert Spencer (1992). *The Principles of Ethics*, Vol. II (T. R. Machan, Ed.) Indianapolis: Liberty Fund, p. 6.

[6] Herbert Spencer (1970). *Social Statics: The Conditions Essential to Human Happiness Specified, and the First of Them Developed*. New York: Robert Schalkenbach Foundation. p. 95.

[7] Herbert Spencer (1884). *The Principles of Sociology*,Vol. II. New York: D. Appleton, p. 608.

[8] Herbert Spencer, (1992). *The Principles of Ethics* (Vol. II). (T. R. Machan, Ed.) Indianapolis: Liberty Fund, p. 67, and R. Long (2004, July). "Herbert Spencer: Libertarian Prophet," *The Freeman: Ideas on Liberty*, pp. 25-28.

[9] Herbert Spencer (1992). *The Principles of Ethics* (Vol. II). (T. R. Machan, Ed.) Indianapolis: Liberty Fund, p. 74

[10] Ibid., pp. 239-240.

[11] Ibid., p. 220.

[12] The late 19th century saw the rise of the "Social Gospel," which called for government not to keep order in society but to transform society. The Fabian society operated on the principle that the people of England would not accept socialism under its own colors but would accept it under the guise of social programs claiming to help the poor and laborers. The Fabians thus committed themselves to achieving socialism in small steps. (McBriar, 1966) In many ways, it was Germany and Britain, in the waning years of the 19th century, that led the way in turning away from reliance on free markets and individual initiative toward governmental planning. (Veryser, 2012).

[13] Spencer, *Social Statics*, p. 605.

Embracing Economic Liberty: A Commitment to Justice and Mercy (con't)

By Paul A. Cleveland

II. The Meaning of Economic Justice

> *The root from which theft proceeds is discontent with the portion God has allotted, and therefrom a coveting of what He has withheld from us and bestowed upon others.*[8]

If free enterprise, along with its institutions of private property and mutually agreeable exchange, is economic and a part of the natural order of things, why do we face so many economic problems? The answer is simple: Sin. By disrespecting God and His natural order of things, Adam and Eve brought sin into the world. From that point forward all people were and are born into the world with a sin nature. That is, we naturally tend to disrespect not only God, but each other as well. We even disrespect ourselves. In passing judgment on the Adam and Eve, God cursed the ground. In other words, nature is no longer cooperating with us as we seek to take dominion over it. Rather, nature is often working against us. Indeed, earthquakes, hurricanes, tornados, floods, droughts, and wildfires all disrupt our economic efforts by bringing destruction and ruin. Nevertheless, in passing judgment, God did not leave mankind without hope as He promised to bring redemption. In doing so, He set up a sacrificial system to remind mankind of His promise. Two important themes in the Scriptures should be considered. The two are the issue of justice and righteousness which people fail to uphold and the issue of God's mercy, grace, and redemption which He is bringing about through the course of human history.

The failure of mankind is told through countless examples both in the Scriptures as well as in recorded human history. For example, the story of Cain and Abel provides a good illustration of the progression of sin and of man's hope for redemption. One thing to note in the story is the continuation of the created order and economic achievement through specialization as Cain became a farmer growing vegetables and Abel became a rancher raising sheep. However, only one of the two brothers trusted God's promise. The promise rested on a sacrifice. To remind men of the promise God set up a sacrificial system that remained in place until His sacrifice was made. To offer the appropriate sacrifice, Cain would either have to find an animal in the commons or engage in a trade with Abel. Relying on the commons would take time, so there was an opportunity for a mutually beneficial trade. Cain apparently did not value the promise enough to engage in either a search or a trade and chose to offer God something less than was instructed. When God rejected his offering, Cain, acting on his sin nature, blamed Abel and murdered him. Evidently, he thought Abel's price for one of his sheep was just too high and he was unwilling to seek his own sheep in the commons. The truth is that voluntary exchange can only take place when both parties agree that they would be better off to trade rather than not to trade. The value someone places on property, whether it is already his or someone else's, is always subjective and the choices we make are always based on what we value. Thus Cain did not value God's promise, but Abel did. Cain thus dealt unjustly with Abel.

Our sin, and the perversion of our desires, creates all sorts of problems for us. The sinful passions of jealousy, envy, and greed often motivate us to acquire our economic means in a non-economic way. That is, we steal what we want from others. We simply try to obtain the means for achieving our ends by taking it from others by force or fraud. As was just pointed out, free enterprise refers to the situation in which people trade freely with each other for the things that they desire. Coercive force and deceptive fraud undermine such trade and, thus, tend to destroy the free market and liberty. It also tends to undermine our ability to take dominion because theft is based on the redistribution of existing output and cannot be generalized. In other words, you cannot found an effective economy on theft because if everyone is trying to live as a thief, there is nothing to steal because there is nothing produced. As a result, it is clear that economic justice requires there to be a healthy respect for, and adequate protection of, private property. This recognition leads to a question. How can we best promote respect for and protection of private property?[9]

This question is immediately related to the development of a sound understanding of the role of government in society. The reason why this is true is because all people live their lives in conjunction with all other people. By nature human beings are capable of thinking, planning, willing, and acting. In fact, these attributes are simply part of bearing the image of God and as we have already seen, people must be free to act. Therefore, purposeful human action is appropriate behavior for human beings as long as it is carried out in ways that respect the coequal rights of others. Thus, the best form of government is self-government. That is, we recognize that as long as each individual acts in a way that fully respects the rights of others, harmony and cooperation results. As John Locke put the matter in his second treatise on government, "The state of nature has a law of nature to govern it, which obliges everyone: and reason, which is that law, teaches all mankind, who will but consult it, that being all equal and independent, no one ought to harm another in his life, health, liberty, or possessions."[10]

Again, this has not been the general experience of people in this world. History provides ample evidence that some people have abused the rights of others in order to gain their own ends. In truth, anyone wishing to engage in a close examination of his own life will discover that he has abused other people at least to some degree. "As an infant, man is observably self-centered, concerned only with his own desires and gratifications. Only slowly, and often painfully, does the child learn more sociable and thoughtful behavior, and if enlightened self-interest replaces self-centeredness as an adult, considerable progress has been made. In truth, man is subject to strong emotions, to fits of temper, may become violent, aggressive, and destructive ...It is these potentialities in the nature of man ...that make [state] government necessary."[11]

This tendency in human nature, to disregard others, gives rise to a fundamental problem of taking dominion and building civilization. Moreover, how can mutually beneficial human action exist when people do not respect the property rights of others? To adequately address this question, we must first explore the nature of human action a little deeper. While it is true that people do not fully respect the rights others, it is also true that they do not violate such rights absolutely and continually. That is, people do not behave as badly as they possibly could. If that were true, no trade or social interaction would ever be possible since the continuous desires of all people would prompt them to violate others. Such a world would be one of continual conflict and warfare as each person fought against all others to achieve his ends. It would be hell itself. Like the experience of a perfect world of self-government, absolute depravity of this sort has not been the general human experience either. The real world falls somewhere in between the two extremes. Human experience is sometimes better and sometimes worse. For instance, in the last hundred years or so the American experience has been far better than that of Russia, but it has by no means been perfect.

Given that life in the real world falls somewhere between paradise and hell, we can rightly wonder which factors move us closer to paradise. It ought to be clear that the only way that a community would move nearer to paradise is when the people in the community freely choose to recognize and respect the coequal rights of others. Without this volitional and individual choice, no such movement would occur. One of the first institutions of importance in this regard is the family. One of the reasons America has fared better than Russia has been its historical regard for the family. While the commitment to family life in America today appears to be fading, traditions die hard and the benefits of even a memory are long lasting.

Consider the following example. Human beings are moral creatures whose choices matter. We are all born with a conscience of right and wrong and that conscience can either be cultivated or squashed. Jennifer Roback Morse wrestled with the implications of this truth in her lecture, "Putting the Self Into Self-Interest: An Economist Looks at Values."[12] In that lecture she recounted some of the difficulties that her family encountered rearing her son who was adopted from a Romanian orphanage. Many of the difficulties they experienced in raising this child stem from the way that he was treated as a baby. As Morse recalled her early efforts to help her son:

> A short time ago, I attended a conference for parents and professionals who have a responsibility for Eastern European adoptees. At the conference, one of the mothers remarked, "My son was fed like a hamster." Perhaps that seems like a strange thing to say, but all of us in the audience that day knew exactly what she meant. For many of us have children who were fed by a bottle wired into place in their cribs. Our children were fed, and indeed raised, with minimal human contact.[13]

Morse went on to explain the difficulties that such children have adjusting to social situations. They seem to lack the ability to trust others in any significant way. They tend to withdraw into themselves and act in antisocial ways that harm their actual and potential relationships. They tend to be manipulative and calculating in order to gain whatever advantage might be had even at the expense of others. In short, they tend to disregard the interests of other people. As she learned of these tendencies in such children, she asked, "Who is this child?" She answered her own question:

> Why, it is *homos economicus*: the person who considers only his own good, who is willing to do anything he deems it in his interest to do, who cares for no one. All of his actions are governed by self-interested calculation of costs and benefits. Punishments matter, loss of esteem does not. He does not self-monitor, so he can always find some opportunity to evade the rules. As to his promises, he behaves opportunistically on every possible occasion, breaking promises if he deems it in his interest to do so.[14]

For this reason, Morse came to recognize that she and her husband had their work cut out for them if they were going to overcome these tendencies in the life of their son. In fact, she realized that those tendencies could only be overcome by love and that would mean applying discipline when discipline is needed, compassion when compassion is needed, and affection when affection is needed. In effect, she recognized that all the traditional aspects of good parenting would be needed to overcome her son's lack of trust and lack of affection for others. Having been abandoned from the start, such trust was alien in her son's life.

Children will not naturally respect the rights of others because of original sin. Any parent who knows their children well can give numerous examples of how they were willing to violate others to gain their own ends. Parents have the task of patiently and steadily using their position of authority in their children's lives to help them develop the self-discipline necessary to get along with others. Some parents accept this task more readily than others, some are more gifted than others, some have better insights than others, and for these reasons will be more or less successful in promoting self-government. Unfortunately, some parents abdicate their responsibility or look to others to do those things that they should have done. In this regard, other people and institutions such as teachers and schools, pastors and churches, and even market place interactions can remediate and reinforce or undermine and destroy the efforts of the parents, but these institutions cannot replace the family. When the family structure of a society breaks down, that society is heading for trouble.

To the extent that parents are successful, greatly determines the extent to which the free market flourishes. An adult reared in a loving home, who has been taught the virtue of working to achieve his ends and the evil of stealing what he wants from others, will not even consider stealing someone else's property even if the opportunity to do so arises. Human beings make their choices on the basis of their highest affections at the moment of choice. A person who comes to understand the general demands of justice will not generally be a threat to others. He will be a person who can be trusted. Such people are typically reared in good family circumstances where the parents take an active role in their lives. While some people might develop self-discipline apart from their upbringing, that will generally not be true. Dysfunctional families tend to beget dysfunctional and antisocial human beings. The economy cannot thrive in such an environment, but despotism and tyranny can.

This brings us to the issue of state government. There will always be at least some people in any society who are more antisocial than the general population and whose activities can undermine civilization. When their excessive transgressions against others go unpunished, society itself breaks down. Therefore, the purpose of government is to punish this behavior. As the Apostle Paul observed in Romans chapter 13, government exists to "punish wrongdoers." Notice that this function in society is limited and negative. In the case of economic justice, government should protect individual property rights by punishing thieves, adjudicating against fraud, enforcing voluntary contracts, and providing for national defense. For the most part, government action can be confined to state and local areas, but some issues will rise to the national level. At this point we need to be careful that we do not expect more from government than it can realistically do. It cannot right all wrongs or supposed wrongs, it cannot change the inward hearts of the people, and it most definitely cannot provide economic provisions for the people under its rule. Government action is always coercive. That is, it uses force to accomplish its ends. The question that must always be asked when we appeal to government action is, "when is it appropriate for government to use force?" The answer is rather simple, it is lawful to use force for adequate self-defense.[15]

One of the real problems of government is that its force can be used to defeat its purpose. Since one method of stealing from others is by force as opposed to deception, and since all government action is accomplished by force, what prevents someone from using the force of government to steal what he wants from others? As the Psalmist's laments, "Can wicked rulers be allied with you, those who frame injustice by statute? They band together against the life of the righteous and condemn the innocent to death."

History is littered with examples of how government authorities used their power to oppress and rob the people they were supposed to protect. Moreover, they accomplish this in a wide variety of ways all of which provided special privilege for some at the expense of many. Thus, partiality in the law, bribery in adjudication of disputes, business subsidies, bailouts, protectionist tariffs, licensing agreements, and the monopolization of industries and commerce are all examples of the abuse of power. In order to promote theft of this sort, rulers must promote the illusion that they are benefactors of society. They must make people think that they are providing the economic means to the achievement of our ends. Nothing could be further from the truth since government as an institution is dependent upon the produce of others to fund its existence. When people begin to look to government to provide them with the means to their ends they are actually asking the authorities to steal their economic wherewithal from their fellow citizens and are engaged in the most immoral sort of behavior imaginable. Under the guise of legalities, those with the most political clout use governmental coercion to steal from those without such influence. This is to call good evil and evil good. Mankind is never more like Satan than in practicing this kind of foolishness.

[Part III: The Practice of Economic Mercy will follow in next month's BankNotes.]

Notes:

[8]Pink, A. W.,

[9]I've made the following argument in another article. See Paul A. Cleveland, "Government: The Good, the Bad, and the Ugly," The Journal of Private Enterprise, Fall 1987, pp. 81-99.

[10]Locke, John, Two Treatises of Government, (Everyman: London, 1996 printing), p. 117.

[11]Carson, Clarence B. and Paul A. Cleveland, op. cit., p. 42.

[12]Jennifer Roback Morse, "Putting the Self Into Self-Interest: An Economist Looks at Values," The Russell Kirk Memorial Lecture, (Washington D.C.: The Heritage Foundation, 1997, no. 575).

[13]Ibid., p. 2.

[14]Ibid., p. 4.

[15]A highly recommended treatise on this is by Frederic Bastiat. Bastiat was a nineteenth century French economist and statesman. His essay, The Law, provides a well-reasoned defense of the natural law right to property. It can be found online at www.econlib.org.

Nelson's Newly Added Book Recommendations
https://infinitebanking.org/reading-list/

That Which is Seen, and That Which is Not Seen: An Economic Essay -- by Frederic Bastiat

You Are Greater Than You Know -- by Lou Austin

The Tariff Idea -- by W. M. Curtiss

Nelson's Favorite Quotes

The act of taking the first step is what separates the winners from the losers. — Brian Tracy

Imagination is everything. It is the preview of life's coming attractions. — Albert Einstein

Good communication is as stimulating as black coffee, and just as hard to sleep after.
— Anne Morrow Lindberg

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