

# TWENTIETH-CENTURY COMMON SENSE

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UNDER THE DIRECTION OF E. C. HARWOOD

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## I.

### WHAT MUST WE DO TO SURVIVE?

What must we do to survive? For Western Civilization and especially for that portion of it within the United States, this has become the crucial question of our times. In attempting to answer this question we propose:

- A. To review pertinent economic facts of the past and present.
- B. To summarize the Nation's long-term objectives.
- C. To point out the route toward those objectives.

#### *A. Pertinent Facts*

For many decades the economic growth of the United States so far surpassed that of other countries that our Nation became the industrial colossus of the world. The great European industrial empires, England, Germany, and France, although far in the lead as industrial nations only a century ago, also have grown, but so slowly in relation to the expansion of industry in the United States that they are not even close seconds in the race today. Measured by the production of steel, a basic commodity in a modern industrial society, the United States in recent years has produced nearly 5 times that of the leader among the three others mentioned and almost double their combined total.

From its earliest days our Nation has repeatedly suffered from the adverse effects of an unsound money-credit system. The days of "wildcat" banking in the first few decades of the 1800's were notorious; and, even after the national banks were well established in the decades following the Civil War, the elementary lessons of sound commercial banking had not been learned. In the 1890's a great depression with many hundreds of bank failures was the usual aftermath of unsound credit expansion, of the inflationary creation of excess purchasing media by the Nation's banks. Again in the first decade of the present century a financial panic and depression followed serious abuse of the banking system with the resulting failure of hundreds of banks.

These harsh lessons were not ignored, however. At long last, advantage was taken of the example provided by nearly a century of relatively sound commercial banking in England. After prolonged study by a National Monetary Commission and equally prolonged consideration by Congress, the Federal Reserve System of regional central banks and member banks was begun in 1914. For the first time in its history, the Nation had a banking system based on recognition and application of the basic principles of sound commercial banking.

Whether or not the new banking system might have functioned soundly, thereby limiting overexpansion during prosperity booms and as a consequence lessening the severity of subsequent recessions, we do not know. Before the new system was well established, the United States had entered World War I. Once again the politically expedient course, inflation, was chosen; and into the discard went the principles of sound commercial banking on which the new system had been based.

The wartime inflation was continued into the early postwar years until drastic deflation seemingly became the only alternative to a further skyrocketing of prices generally. The deflationary collapse of 1920-21, again with hundreds of bank failures of course, testified to the preceding inflationary misuse of the banking system.

So extensive was the collapse in prices that the political pressure for supporting commodity prices became great. The managers of the Federal Reserve System, including especially the then influential Governor of the New York Federal Reserve Bank, determined to try an easy-money policy in order to support prices at higher-than-prewar levels. Other factors, such as an attempt to aid England in restoring the gold standard, also were involved. The net effect of the prolonged easy-money policy through most years of the 1920's was another great inflation with its inevitable aftermath, the great "boom and bust" at the end of the decade. Nearly one-third of the Nation's banks failed in the next 3 years, thereby confirming once again that the basic principles of sound commercial banking had been generally ignored.

In order to understand what followed we must turn our attention to another aspect of economic developments. During most of the Nation's prior history vast areas of free land available for the taking had provided a "safety-valve" in times of depression. Many of the unemployed could "go west, young man, go west," and many others could rely on the folks "back home" on nearby farms. Most of the population still had roots in the land, parents, brothers, uncles, or cousins on whose farms food, at least, was available in the worst of depression periods. During the most extensive depression in the Nation's history, that of 1873-1879, few people lacked the necessities of life. Even during the severe depression of the 1890's only a small portion of the unemployed became desperate for food.

But by the 1930's the situation had altered greatly. The absence of free land accentuated the privileged position of those who enjoyed the natural resource monopoly privilege, and the city proletariat one or two generations removed from the Nation's farms had nowhere to turn. A situation long prevalent in Europe finally had become commonplace in the United States.

Under such circumstances the pressure for desperate measures

became overwhelming, or at least so the politicians of the times concluded. Instead of probing once again for underlying causes of the difficulties, as was patiently done after the depression at the turn of the century, the politicians hastily treated symptoms with one obvious result, prolonged depression.<sup>1</sup>

So unsuccessful were the efforts to cope with the Great Depression of the 1930's that nearly 8,000,000 were unemployed even in the abortive-recovery year, 1936; and nearly 10,000,000 were still unemployed in the last year of the decade. Throughout the 1930's approximately one-fifth of the labor force was unemployed despite the notion, widely prevalent today, that the New Deal somehow remedied the Great Depression.

Then in the 1940's another great war ended the problems of depression and substituted others equally familiar. Once again, monetization of public debt was adopted as the expedient means of financing the war effort. By 1946, nearly \$70,000,000,000 of Government debt had been monetized by stuffing Government bonds in the commercial banks, which created new Treasury accounts in payment for the bonds.

As the Treasury wrote checks to pay for munitions, etc., this huge amount of inflationary purchasing media was transferred to businesses and individuals. Fortunately, much of the total purchasing media, about half, was held unused either as hoarded currency or as idle checking accounts, apparently because new automobiles and many other consumer goods were not available and because new equipment and materials for new plants were not available for purchase by businesses. Consequently, the effects of the great inflation were largely postponed until after World War II.

If the huge total of inflationary purchasing media hoarded (or held inactive in checking accounts) during World War II had been spent almost immediately after the war, the resulting rise in prices generally would have been far more rapid than the rise that did occur. (As usual when resort is had to price controls, many of the price rises prior to the abandonment of futile price controls were concealed from the statisticians by quality deterioration, etc.) At least two factors were responsible for the relatively slow use of the hoarded purchasing media.

First, countless individuals including many managers of corporate businesses expected a postwar depression within a few years. In fact

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<sup>1</sup>Lest the reader assume that the facts cited are the products of selectively imaginative hindsight, it seems desirable to add at this point that the author is prepared to offer proof of all such statements. Citation of references would unduly clutter an article intended for the general reader. Other readers who desire such references in detail may have them on request. Such references will include many economic analyses that correctly *predicted* the outcome of measures adopted by Congress and other pertinent developments.

so widespread were the fears of a depression in 1946 that the Federal Government was urged to adopt strong measures in order to cope with anticipated mass unemployment. For several years thereafter, many who remembered the 1920-21 experience held funds idle in the expectation that a depression would provide better opportunities for those who wanted to buy.

The second factor responsible for the slow rate of dishoarding was the time required for factories to convert to peacetime output and to produce enough for the postwar demand. For a few years demand for such items as automobiles, housing, some types of machinery, etc. was greater than the existing productive capacity could satisfy. Moreover, the Korean War, although relatively minor in its economic effects, again restricted to some extent the availability of numerous items desired for civilian consumption and for business.

As the hoarded or idle inflationary purchasing media were gradually used in the postwar years, the amount available was supplemented by the monetization of increasing private debt (largely real-estate loans and installment loans) by the commercial banks. Thus the amount of inflationary purchasing media in circulation was almost continually increased until 1957, except for minor interruptions in 1948-49 and 1953-54.<sup>2</sup>

The great inflationary development, begun during World War II and continued through 12 subsequent years, had the usual chain of effects. Although on a larger scale in several respects, these effects duplicated those experienced several times during the Nation's history. They may be summarized as follows:

1. Effective demand (that is, desire implemented by purchasing media) during most of the period and for most types of products exceeded the supply of goods at prevailing prices.
2. Therefore, prices generally rose with a resulting succession of "windfall" profits to most businesses. (In some instances, certain prices that otherwise would have fallen were supported at relatively high levels by the great inflation.)
3. With the encouragement of increasing demand and partly by using the funds that "windfall" profits provided, productive capacity was greatly expanded, so much so in the later years of the period that, as in the 1920's, the expansion of plant and equipment itself became a major factor in the growing intensity of the business "boom."

<sup>2</sup>Some of the increasing real-estate and consumer loans were *not* inflationary; that is, part of the loans did *not* result in the creation of new and inflationary purchasing media, because the funds loaned were derived from current savings rather than from new credits to demand deposits or checking accounts. For a more detailed discussion, see E. C. Harwood, *Useful Economics*, American Institute for Economic Research, third edition, 1957, Chapters VII and VIII.

4. Organized labor, stronger than ever before, demanded a share of the "windfall" profits. Business management acquiesced, in some instances perforce, in others believing or hoping that the conditions creating ever-increasing profits would continue indefinitely. Thus, for example, assembly-line workers in Detroit (as well as workers in the basic steel and construction industries) saw their prewar wages more than quadrupled (including fringe benefits) while teachers in the public schools fought a losing battle to have salaries increased as rapidly as the cost of living rose. In fact, so great have been the wage increases in *some* industries profiting most from inflation that the armed services have been unable to retain vitally needed technicians who leave after one or two enlistments for the far better pay available elsewhere.

5. Of course, most owners of common stocks and real estate profited from the prolonged inflation. The great increase in the value of such holdings and in the incomes from them reflected in substantial part the shift of real wealth from retired individuals dependent on pensions, from holders of life insurance, savings bonds, and savings deposits, and from that large portion of the population whose incomes were relatively fixed or who could not obtain sufficient increases to offset the continuing depreciation of the dollar (rise in prices).<sup>3</sup>

6. The easily won profits for businesses of many types and for many individuals encouraged speculative expansion in various segments of the economy. For example, new office buildings in New York and other cities were constructed in the later years of the recent boom period on a scale rivaling that of the ill-fated 1920's; otherwise competent business executives with their eyes on "pie in the sky" in the 1960's embarked on over-ambitious expansion programs.<sup>4</sup>

7. Perhaps most unfortunately situated are the millions of wage earners enabled by the subtle robbery of their own and others' pension funds, life insurance, etc. to claim a higher standard of living in the form of the new cars, new homes, etc. thus made available to them on the installment plan. Encouraged to incur debt beyond their ability to pay under less favorable circumstances, many such individuals are finding that the growing population supposed to perpetuate increasing prosperity includes in large part their own children (more numerous because of prosperity's optimism) whose needs only make more burdensome the debt so hopefully assumed.

<sup>3</sup>Government-sponsored "theft" via inflation has taken nearly \$200,000,000,000 worth of real wealth (goods and services) from holders of life insurance and savings bonds, savings depositors, etc., since 1940.

<sup>4</sup>In the *Wall Street Journal* as this is being written is the report of one major company that even at this early stage of the recession has been forced to postpone indefinitely putting machinery in factories newly completed.

8. By no means the least of inflation's effects has been the subsidizing of that proficient spendthrift, the Federal Government, with increasing taxes seemingly almost painlessly extracted from continually increasing personal incomes and business profits. The huge sums so easily obtained have fostered national delusions of economic grandeur. Grandiose plans for aiding other nations and silly schemes for remedying our own internal problems such as those of agriculture have been fostered by politicians seeking votes and by exuberantly confident bureaucrats who have, it must be conceded, at least the ability to spend money rapidly if not wisely.<sup>5</sup>

At this writing (late winter 1958), a recession is under way. Already apparent is the fact that it exceeds in severity the minor setbacks of 1948-49 and 1953-54. But as yet an adequate scientific basis for predicting the probably severity and duration of this recession is not available.

We do know that the inflation (creation of excess purchasing media) in recent years has been the greatest in the Nation's history. Fortunately, speculation on margin, in the stock market at least, has been much less than that of 1928-29; although the expansion of inflationary private debt in recent years has exceeded that of any earlier period. That there are many serious distortions within the economy seems obvious; such always has been the situation after prolonged inflation.

Much of the recent inflation was attributable to the monetization of Government debt. Such inflation is not subject to the automatic deflation that results from widespread bankruptcies and the collapse of innumerable private debts. Consequently, only part of the present inflation is as vulnerable as that of 1929, and precisely how vulnerable that part is cannot be ascertained until the recession testing process has carried further.<sup>6</sup>

In any event, questions about this aspect of the problem will be answered in the months ahead. If the deflation of private debt becomes extensive, a depression as severe as that of 1937-38 is well within the range of possibilities, but we do not expect a depression such as that of 1929-32, primarily because the inflation reflecting monetization of Government debt is not vulnerable to forced deflation via private bankruptcies.

<sup>5</sup>In fact, so lavish was the giving and "lending" to other nations that, *in addition* to providing Cadillacs for oil princes in Saudi Arabia and an infinite variety of other goods from armament to zippers, we managed in a single decade to give foreigners demand claims on two-thirds of the Nation's basic gold reserves.

<sup>6</sup>We believe that the huge total of private debt incurred in recent years (\$300,000,000,000 since 1945) includes a small percentage of vulnerable loans reflecting unwise borrowing. Only 3 percent of it would equal the loans for stock speculation on margin in 1929, and we suspect that even more may have been unwisely incurred.



### B. *The Nation's Long-Term Objectives*

We now turn to consideration of the Nation's long-term objectives. Unless our objectives are clearly stated and kept constantly in mind, we cannot reasonably hope to make wise day-to-day decisions regarding the route to be followed. The principal pertinent objectives stated and implied in the Nation's basic plan, the Constitution of the United States, may be summarized as follows:

1. A society so organized by Constitution, statute, and custom that each adult member will be continually influenced to cooperate with others by serving their needs as they in turn are under a like compulsion to serve his in order indirectly to serve their own. The end desired is perfect cooperation, and the means clearly implied in the Constitution is free "competition." ("Free" implies not the chaos of anarchy but operations under "rules of the game" intended to preserve the maximum freedom for all, large and small, among the providers of economic goods and services.)

2. Within the society freedom for individuals to plan and choose their occupations and goals.

3. For all men equality of opportunity to find their places in the economy and seek their goals.

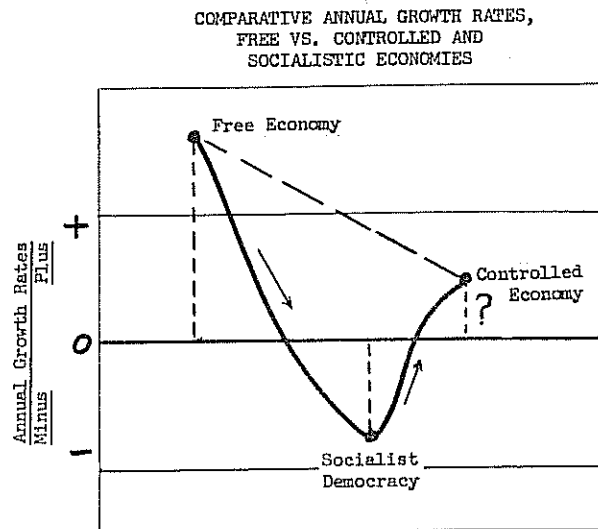
4. To each individual the fruits of his own labors not only as an incentive and reward but also *and even more important for the Nation as a whole* so that the individual (or business) who demonstrates capacity to serve his fellow citizens most effectively will have increased means at his disposal enabling him to become more and more effective on a larger and larger scale.<sup>7</sup>

5. A rate of economic growth and development that not only will foster achievement of the objectives listed above but also will insure a widening rather than a narrowing of the present gap between the industrial power of the United States and that of Russia.

<sup>7</sup>For a detailed discussion pointing out that "free competition" is simply a different name for voluntary cooperation and that such free competition is essentially different from war, see Appendix C "Free Competition is Voluntary Cooperation" of the book, *Useful Economics*, by E. C. Harwood, American Institute for Economic Research, third edition, 1957, Great Barrington, Massachusetts.

<sup>8</sup>The historical developments that gave rise to the Great Revolution in human affairs and culminated in the Constitution of the United States are outlined in the editor's book, *The Counterrevolution*, American Institute for Economic Research, 1956. As the title suggests, it also discusses the counterrevolution as embodied in socialism including its militant form, communism. Even more dramatic than the great industrial growth of the United States, because compressed within a relatively short period, has been the economic recovery of Western Germany following application of certain basic principles of the Great Revolution, including a large measure of economic freedom and sound money policies, applied shortly after World War II.

The last objective indicated warrants more detailed discussion in order that it may be fully understood. For this purpose the diagram below illustrates the discussion that follows.\*



Referring now to the diagram above, the annual growth rate of a free economy is indicated as a plus value signifying a compound rate of growth year after year such as that experienced by the United States for much of nearly two centuries. The only prolonged departures in the United States from well-sustained economic growth have occurred following major interferences with its relatively free competitive economic system. For the latter part of the 19th century in particular, the record of industrial production is sufficiently accurate and the conditions of relative freedom were adequate to establish clearly that such an economy enjoys a high rate of growth.

Some readers may wonder whether the lessons of the American historical experiment are applicable elsewhere, for example in Europe. The experience of Western Germany since World War II provides a convincing demonstration that a relatively free economy assures rapid growth even when hampered by the prior existence of extensive controls and by the wartime destruction of its means of production.

\*It seems desirable to emphasize that the diagram does not attempt to represent accurately in detail the relative differences in growth rates between free, socialistic, and communistic economies. However, the historical record clearly establishes that a free economy grows more rapidly than a controlled economy and that a socialistic economy (without strong-man controls) has a negative rate of growth, in fact cannot even survive in the long run (for example, the fate of the early Plymouth Colony and more recently the effects of even partial socialism on Great Britain, France, and other nations).

The annual growth rate of an economy operating under a socialistic dictatorship such as communist Russia, i.e. of a ruthlessly controlled economy, is shown as a smaller plus value. Whether or not its annual rate of growth will be a plus value in the long run is indicated by a question mark. Evidently a positive rate of growth is possible for a prolonged period, but there is as yet no proof that it will last for centuries and will pervade the entire economy. That the annual growth rate of such an economy, *in its entirety*, is less than that of a relatively free economy is well established.<sup>10</sup>

Below the zero rate of growth and indicating negative growth or economic decay and retardation we show socialist democracy. This is the situation where the state seizes all factories and other wealth and distributes the goods currently produced according to some plan specified from time to time by the legislative branch of government. No economy operated in this manner *without* dictatorship and ruthless controls thus far has been able to survive. Numerous economies have experimented with varying degrees of socialism, and convincing evidence of growth retardation is provided by the experience of such countries as Great Britain under the labor government and France in recent decades.

Nations that have continued state ownership and control of all wealth, natural resources and capital equipment as well as current production, have survived only by the imposition of rigid controls in the hands of a ruthless dictatorship. By such means socialism (of a kind) has been made to work and, at least for a few decades, to provide a growing economy. Such growth never has been great enough to compare favorably with that of nations having relatively free economies, although in some aspects of industry rapid growth may have been forced.<sup>11</sup>

Many people may believe that the gap between a relatively free economy and a controlled economy can be bridged as by the dashed straight line connecting the two points on the chart above the zero line. However, such never seems to have been the case. As an economy has become more socialistic while attempting to preserve political free-

<sup>10</sup>See, for example, G. Warren Nutter, *Some Observations on Soviet Industrial Growth*, Occasional Paper 55, National Bureau of Economic Research, New York 1957.

<sup>11</sup>Some observers seem to believe that Sweden has proved that a democracy can adopt socialism successfully. However, in the first place Sweden is only partially socialistic, and emphasis has been placed on government control or ownership of natural resources rather than on the nationalizing of industry generally. (Even the basic steel industry was *not* nationalized as it was in Great Britain.) Second, the following figures on industrial production since 1950 (the year when West Germany regained its prewar rate of output) are of interest.

Percentage Increase in Industrial Production  
1950 to 1955

Sweden	15
West Germany	79
Western Europe	41

doms, the rate of growth has lessened and has become negative when complete socialism was approached. Then the inevitable inefficiency of a bureaucracy lacking ruthless power becomes evident. In order to restore a positive rate of growth (that is, in order to survive) such an economy has two choices: 1, to struggle back toward its lost freedom, as England has attempted to do under its present government, unscrambling the scrambled eggs of socialism (returning factories to private ownership etc.); or 2, to adopt more and more stringent controls until finally the reins of power are concentrated in the hands of a dictator (individual or small group). Whether or not a nation can struggle back from the economic morass of nearly complete socialism to the status of a relatively free economy remains to be seen. England may or may not provide the answer in due course.

Of vital importance in connection with our Nation's objectives are the following:

a. Continuing on the road to socialism will *not* maintain American economic growth at an annual rate in excess of Russia's; that path is *not* the dashed line on the chart, but the solid line that goes down to a negative rate of growth, to economic deterioration in fact.

b. If we continue into the morass of socialism and attempt to "control" inflation by price controls and a broadening multitude of other controls that soon would seem "necessary," we shall experience economic retrogression for years and at best succeed eventually in recovering to Russia's rate of growth (after prolonged delays) only by adopting a ruthless dictatorship thereby possibly achieving survival at the cost of much that, to many Americans at least, makes survival worth striving for.<sup>12</sup>

### *C. The Route Toward the Nation's Objectives*

That maintenance of an adequate national defense is essential for survival is obvious. However, defense in the long run involves more than preparedness for military operations; it also involves the continuing development of scientists, of science and technology, and of a growing industrial power capable of producing the unknown weapons of an unpredictable future.

<sup>12</sup>In this connection we should also realize that once the absolute power implied in multitudinous centralized controls is permitted to exist, seizing of that power by a ruthless dictatorship will follow as night follows day. Such has been the invariable experience of mankind from ancient Greece to modern Russia or for that matter to modern America where concentration of nearly absolute power in some labor unions has brought to the top of those unions ruthless individuals from the gangster stratum of our society. That "power corrupts and absolute power corrupts absolutely" is but a half truth; the further truth is that where power is absolute, only the most alert, clever opportunist who is also utterly ruthless in grasping for power can hope to survive. By a process as inevitable in its outcome as evolution itself, only the "fittest" can survive and the "fittest" in such circumstances usually is the most brutal enemy of his fellow citizens.

The Nation's defense expenditures alone already are so great that the taxes providing the funds constitute a burden tending to retard industrial growth and hamper education of the Nation's youth. The financial problems of fathers attempting to educate their children require no emphasis for the hundreds of thousands in the moderate-income group who must pay income taxes in many instances exceeding the cost of the children's education. As for the young man earning his own way through college, if he succeeds in earning \$1,500, hardly enough for a year in most colleges, the Government will take from him 10 percent of his income under present tax rates.

That existing taxes retard industrial growth is readily seen by anyone who understands that complex process called economic growth. Many people apparently believe that economic growth of an economy is achieved by a simultaneous general expansion of nearly all business elements within the area concerned, such as a region or nation. Actually, however, that is *not* the situation. Economic growth is achieved, if and where it is achieved, as some elements of the economy expand more rapidly than those that are static or are contracting and perhaps are in the process of dissolution.

A striking example of a rapidly expanding segment of the economy was provided by the automobile industry through the 1920's. During the same period the carriage industry and to a lesser extent the motorcycle and bicycle industries were contracting. A small city not far from where this is being written was then known as the "whip city of the world." Today few youngsters in that city have ever seen a "buggy" whip, although many of the older citizens still remember the Sears two-cylinder "buggy" complete with dashboard and whipsocket, a memorial to the day when few believed the automobile could ever replace the horse.

Many factors other than obsolescence of the product account for the decline of business enterprises. These other factors include what may be called entrepreneurial arteriosclerosis (too much deadwood at the top) and numerous other forms of inadequate managerial ability as well as all the many reasons for personal and corporate failure including fires, floods, and earthquakes.

The vital point is that an economy can grow only when the increased production of goods and services by the growing businesses exceeds the decreases in production by the declining and failing businesses. Moreover, the most important function of profits in a competitive economy is to provide *both* the incentive *and the funds* for business growth, whether it be, at one extreme, the small business started by one man in its early stages or, at the other extreme, the huge corporate enterprise that has served the public for many decades. In short, profits are the food for

growth, and whatever the corporate income tax takes necessarily lessens the means available to businesses for expansion. Without doubt, today's corporate tax at 52 percent is a *most serious* inhibitor of business growth. Therefore, it retards development of the industrial power essential to maintain United States supremacy in a hostile world.

Obviously, the Nation's economic growth can be most rapid when *all* of the profits obtained in free competitive markets by businesses generally (excluding, of course, monopoly gains and other profits attributable to special privilege) are left in the hands of the businesses concerned. Whether the profits are directly invested in new plant and equipment for expansion or in part are paid out as dividends (thereby attracting more capital to the industry) is a relatively unimportant operating detail.

Moreover, taxes on profits can kill over-all economic growth if the discouragement to growing enterprises slows their growth enough so that it is equalled or exceeded by the decreases in production of obsolescent and failing enterprises. Perhaps the tax on corporate profits already is so high that aggregate growth will be prevented in the absence of such a great and dangerous inflationary stimulus as that of the past decade. If such is the situation, the Nation already is seriously jeopardized.

These considerations point to the following route toward the Nation's objectives.

1. Defense expenditures must be kept at the minimum consistent with adequate defense by strict economy, elimination of duplication, etc. (For example, are separate postgraduate "colleges" for senior officers of the three armed services plus a fourth National War College, all with various duplicating courses, really essential? Are missile submarines more effective and less costly than super-aircraft carriers that, in the near future, can be "seen" anywhere in the world from televising satellites and therefore readily destroyed by atomic missiles? Also, what should we learn from Great Britain's reappraisal of its most effective defense needs?)

2. All unnecessary Government expenditures should be eliminated, especially those interfering directly with achievement of the Nation's objectives. As a specific instance for application of this basic principle, the farm price supports and soil bank programs may be selected. Combined budget expenditures for these purposes in fiscal 1958 are scheduled at \$3,683,000,000, nearly 10 percent of the military budget. These programs are an interference with free markets, a disruption of free competition. They encourage an uneconomic use of land, labor, and capital. They delay readjustments that would strengthen American industrial power because they create inducements for marginal farmers to remain on the farm and tend to retard a shift of manpower to industry. They penalize the general public both by raising the price of food and

because the money spent for supporting prices is taken from individuals and businesses who are further damaged thereby. (Perhaps one last year of payments to farmers for not growing crops, using as payment *not* money but percentage shares of the surplus crops in storage would solve the surplus problem.)<sup>13</sup>

3. Expenditures for aid abroad should be reduced to those *clearly and directly* in support of our national objectives. This would preclude most aid to England when under a socializing labor government; to France except under the most stringent controls and restrictions both to prevent misuse of American armament, as apparently occurred in Tunisia, and to inhibit the further socialistic deterioration of the French economy; and would deny aid to India's socialist government for further extension of already failing grandiose schemes of the Indian socialists, etc., etc.

4. The following principles should be applied in reducing and readjusting the Federal tax burden:

a. Taxes on business profits, except profits attributable to monopoly and other special privileges, should be *reduced rapidly and eliminated as soon as possible* in order to encourage economic growth to the maximum extent.

b. Because of the great and obvious need for more and better education for the Nation's youth, college tuition and other necessary expenses should be allowed as deductions from family incomes before taxes.<sup>14</sup>

c. As rapidly and extensively as possible personal taxes should be shifted from *earned* incomes to incomes derived from special privilege of every form and variety. In this connection three important distinctions, wherever feasible, should be made.

(1) There is no important economic reason why tax rates on special privileges (including site monopolies, etc.) should not rapidly approach 100 percent of income after certain basic personal exemptions.

(2) Taxes on interest and dividends from capital invested in competitive enterprises (as distinguished from funds used to buy mo-

<sup>13</sup> Anyone who has studied the stimulating effects of free markets and relative freedom of competition in West Germany during the last several years would conclude, we believe, that the farmers themselves who chose to remain in agriculture would be far better off in a short time if somehow they could be saved from their political "friends." The rapidly growing population of the United States is certain to provide adequate markets for well-managed farms run on a competitive basis. The farm benefits may buy some votes, but they don't contribute to the achievement of national objectives, rather the reverse.

<sup>14</sup> Consideration might also be given to putting *all* estate and gift tax receipts into a special fund distributed to all accredited colleges for scholarships. Such an arrangement (using already existing and least costly administrative facilities) would help in achieving that national objective, *equality of opportunity* for all. In effect, some of the States now follow this procedure with their share of such taxes through their support of State universities open to all qualified applicants at minimum tuition.

nopoly privileges, etc.) should be kept as low as possible in order to avoid inhibiting investments in such enterprises; but, for defense and other vital needs, some progression in such rates on personal income more or less similar to the tax rates now prevailing probably would be necessary under present circumstances.

(3) Taxes on *earned* incomes should be eliminated or reduced to the lowest possible levels, especially where the earnings are from potentially growing but small individual enterprises.

To some readers these recommendations may seem unrealistic counsels of perfection without hope of practical application. Three objections probably will be offered, viz:

1. That the great mass of the voters are "too damn dumb to understand."
2. That the pressure groups, for example the farmers, are too strong.
3. And, with reference to the current recession, that we must do something to restore prosperity promptly at all costs because, as the witty Lord Keynes put it, "In the long run we are all dead."

There are two effective answers to the first objection. Too many people, including historians who should know better, seem to have forgotten that in the depths of one of the Nation's worst depressions, in 1932, the American people chose as President *not* a "pied piper" who promised to restore prosperity by spendthrift magic but a man who promised over and over *to reduce Government expenditures by 25 percent*, who deplored in the strongest terms Washington meddling with and direction of the economy, and who, during the first months in office, actually pressed Congress for and obtained reductions in spending. The New Deal spend-for-prosperity notions came later; and, if the public apparently did approve them in 1936, that presumably was because of the delusive business improvement at that time and the claims "we planned it that way" broadcast before the elections. Subsequently, the 1937-38 depression, one of the most rapid and extensive declines in the Nation's history, dispelled the earlier illusions of success in restoring prosperity.<sup>16</sup>

The second answer to the first objection is that a relatively small group of the better-informed independent voters, even those who are

<sup>16</sup>Those who would cope with depression today by increased Government spending might well reflect on the fact that there were still nearly 10,000,000 unemployed in 1939, a full 5 years after the New Deal spending program began, and that even during the abortive recovery of 1936-37 nearly 8,000,000 were unemployed. Yet by late 1932 earlier distortions in the economy had largely been removed by the influence of prolonged deflation, and the stage had been set for the usual cyclical recovery; in fact, the record reveals that recovery actually had begun. In addition to repeating in substantial part the inflationary follies of post-World War I, should we now repeat the blunders that prolonged the Great Depression?



registered Democrats or Republicans, hold the balance of power in most elections. Once the politicians sense that this group has decided views on any question, those views will be reflected in political action. If sound economic analyses are made available to and are accepted by the Nation's more thoughtful and independent voters, the conclusions of such analyses may become the guide to action.

With reference to the second objection, that the pressure groups are too powerful, the fact is that a decisive majority of the farmers responding to a recent poll *disapproved* of the Government's efforts to support prices of agricultural products. Half of those replying wanted no Government aid in any form. There simply is no evidence convincing to us that the Nation's farmers as a whole put their personal welfare ahead of the Nation's.

As for the third objection, that "in the long run we are all dead," one cannot deny the truth of this assertion, but one can deny its apparent significance as an argument for more inflation to restore prosperity. The fact is that our children and grandchildren will be alive in the long run unless we continue to mismanage the Nation's economic affairs as we have during our lifetimes and leave for our descendants a nation vulnerable to Russia's attack. In short, if the Nation is to survive, we must focus our attention on what is wise in the long run and struggle as best we can to cope with the difficulties of the short run.

This does not imply that the unemployed should be permitted to starve nor that all in debt beyond their immediate ability to pay should be forced into bankruptcy and should lose their homes or other possessions; but it does imply that the gross distortions within the economy basically responsible for the recession should be corrected by the sometimes painful processes of freely competitive markets rather than be augmented by still more inflation with even more unfortunate future results.

To summarize: in order that our Nation may survive;

1. Taxes retarding industrial growth should be minimized as rapidly as is possible lest economic growth be markedly less than the maximum practicable.

2. The deterioration of the Nation's educational system should cease, and the relative economic status of educators should be improved, even at the cost of ending the monopoly powers of unions as well as those of industry; moreover, means should be provided to move toward equality of opportunity for youths capable of benefiting from higher education. We should never forget the lesson of long experience: that deterioration of the Nation's schools tends to parallel depreciation of the dollar simply because inflation results in adverse selection of educators by tending to shift the more competent to other jobs and by attracting the least competent to fill the vacancies.

3. Sound comparative analyses should be substituted for the grandiose dreams of recent years; we should face the fact that resources are limited and put first things first by weeding out programs that hinder progress toward the Nation's objectives and by reducing expenditures on programs having a relatively low priority in comparison with the Nation's need for economic growth and maximum educational opportunities.<sup>10</sup>

Of course, the basic requirements of American citizens at this time are willingness to face the facts, to learn the lessons of costly experience, and determination to follow the route to national survival regardless of whatever personal inconvenience may be involved. One function of the Institute is to analyze the facts and transmit to the public the economic lessons thus provided. Determining that a sound course will be followed and urging that course on the Nation's legislators are *not* Institute functions but are the tasks of every American citizen who chooses to do his duty in the Nation's hour of need. Unless these things are done, we shall not only pass along to our sons and grandsons the mess that we of Western Civilization have made in recent decades but also we shall betray them finally by destroying that one great hope for the future of mankind, the basic principles of a free and just society embodied in the Constitution of the United States.

<sup>10</sup>For example, which is the better "calculated risk," as the proponents of foreign grants and loans like to describe their speculations with the public money, more millions for communist Poland or putting the same funds into more nearly equalizing educational opportunities for American youth by means of scholarships? (Not via still another Government handout agency but via grants to accredited colleges for their scholarship funds.)

## SUPPLEMENTARY NOTES

*Note 1.* The following quotations taken from our analyses of the latest business cycle, from 1954 to 1957, illustrate the results of research in progress for many years. (Beginning in 1928, analyses by the editor of this special bulletin discussed the inflationary aspects of the then "New Era" in leading financial and economic journals. For the past quarter century the results of continuing studies under his direction have appeared in the *Research Reports* and other Institute publications.)

From *Research Reports*, January 3, 1955:

Because we believe that others may have overlooked an important factor, we should choose resumption of the boom as the most probable development during 1955. The overlooked factor, we believe, is the huge volume of idle purchasing media (hoarded currency and demand deposits), a substantial part of which may come back into circulation during 1955.

Present indications are that inflation will be increased during 1955 by means of expanding real-estate and installment loans. If such proves to be the case, that stimulant alone could account for a resumption of the boom.

We conclude that resumption of the boom with industrial production reaching new records is the most probable of the several possible developments during 1955.

From *Research Reports*, January 7, 1957:

This is the beginning of the 16th year since the greatest inflation in the Nation's history began. (See our index of inflation in the preceding bulletin.) For 14 years, from 1942 to 1955 inclusive, with only minor interruptions for two 2-year intervals (1947-49 and 1951-53) the relative amount of inflationary purchasing media circulating in the economy was increased. Peak levels were reached in December 1955 and January 1956. Since then, some deflation has occurred, apparently not yet comparable in magnitude to the minor deflations already mentioned.

\* \* \* \* \*

Present indications are that the Nation is nearing the end of a great inflationary "spree." The relative moderation of day-to-day developments, compared with those of 1928 or 1929, has reflected a gradual rather than a sudden ascent to speculative heights. However, a dangerously vulnerable situation has been created. Regardless of the fact that an adequate scientific basis for predicting the beginning of the end is not available, we recommend avoidance of commitments that might prove disastrous to any individual or business in the event of a severe recession.

From *Research Reports*, September 16, 1957:

The avoidance of recessions is so widely appealing that ideas or plans advanced as a means to that end are sympathetically received until they are seen to be impractical or dangerous. "Creeping inflation" has been tried again and again in the history of the world; but inflation long-continued always has outgrown the "creeping" stage and in the end has proved to be an intractable and destructive offspring of the "phony money" advocates. One recent striking example is found in France, a nation reduced from the status of a leading industrial nation to that of a fourth-rate and backward, almost impotent, economy within 4 decades. Similar long-run consequences of "creeping inflation" in the United States could destroy the advantage our industrial power has over that of Russia and invite destruction from without even if it did not insure economic destruction from within.

From *Investment Bulletin*, October 7, 1957:

As for the Government's preventing a severe depression, that may not be so easy as many seem to believe it will be. Even if business activity turns downward rapidly in the early months of 1958, corporate tax pay-

ments based on 1957 profits will be large next March and June. Not until a year from now would corporate tax payments reflect markedly decreased profits. In the meantime, there would be no large scale new inflation attributable to that so-called "automatic stabilizer," a Government deficit to be monetized.

After a year or so Government expenditures probably would exceed tax receipts substantially. But even then, the securities sold to finance the deficits might be purchased largely with the savings of individuals and corporations who feared to invest otherwise. Unless the deficits were extremely large, little or none of them might be monetized for many months. (Such deficits are monetized with a resulting creation of inflationary purchasing media when the securities issued to finance the deficits are sold to the commercial banks in amounts that exceed the new savings placed with the banks for investment.)

Finally, liquidation of private debt may well result in greater deflation for a year or two than the added inflation resulting from Government deficits. In that event, net deflation could result with accompanying depression.

*Note 2.* The science of economics is relatively immature. Much that is published on the subject, including supposed remedies for recessions etc., has no more scientific standing than the notions of the itinerant medicine men who sold health elixirs to a gullible public a few decades ago. More specifically:

a. Confidence is *not* a satisfactory substitute for the correction of serious maladjustments in the economy; in fact, confidence insofar as it invites complacency and a "stand pat" attitude can delay recovery by postponing needed readjustments in prices, wages, etc.

b. "Pump priming" by means of large government expenditures never has resulted in a sound, stable, and lasting recovery from depression.

c. Contrary to the implications of those who recommend perpetual inflation and rising prices as the road to prosperity, rising prices are *not* essential to prosperity. The record shows that the most rapid and best sustained economic growth in the Nation's history occurred from 1879 to 1892, when prices were declining almost steadily and by the end of the 14 years had decreased 40 percent.

*Note 3.* For readers who wish to check the facts discussed in this analysis we suggest reference to *Current Economic Trends*, an Institute publication available at one dollar. (See inside back cover.)

## II.

### THE UNITED STATES STANDS ALONE

Nearly two centuries ago an embryo nation of a little more than 3,000,000 population occupied part of the eastern coastal area extending from southern Maine to northeastern Georgia. All but 10 percent of the people lived in small villages and remote clearings connected (one might better say separated) by trails that for the most part were passable only to men on foot or horseback. Only 6 cities had populations exceeding 8,000; and the largest, Philadelphia, numbered only 42,000.

The industrial revolution had hardly reached this side of the Atlantic. The first cotton mill in North America had not then been established, and other industries were in the primitive handicraft stage. For most manufactured goods the people were dependent in large part on imports from England or the other developing industrial nations of Europe.

To the north of this nation-in-embryo was Canada, colony of the great European power from which independence had just been won. In the South and Southwest a vast area, including what is now Florida and much of the great Mississippi Valley, was held by Spain, a second great European power. Within a few years Napoleon, Emperor of still another European power, was to claim the great Mississippi area for France. Compared with those giants of the times, the embryo nation was but a pygmy about equal in population to the smaller nations of Europe.

In the remote villages and wilderness clearings men went to their work in the fields equipped with muskets, prepared to repel Indian attacks. The inhabitants of the cities, which were all on the coast or on navigable rivers near the sea, well knew that at any time their homes might be burned to the ground by hostile sea-born forces; and threats of such assault were not infrequent. As disputes flared up with first one then another of the European powers that had a foothold in North America, one could never know when a monarch's dreams of conquest would incline him to order his fleet to burn and pillage on the coast of the New World. Almost as though to emphasize that fears of such action were justified, the capital city of the infant nation was burned by British marines before three decades had elapsed.

Nevertheless, the people of this embryo nation somehow found the courage to stand alone. Instead of seeking an arrangement whereby the ruler of one of the three great European powers might have become their Emperor and protector, the inhabitants resolved to create a new

society in the family of nations. A Constitution was formulated, finally adopted, and the United States was born.

The objectives of the new nation as outlined specifically and implicitly in its Constitution were revolutionary in the sense that they visualized and provided for overturning the old and establishing the new in the affairs of mankind. The citizens of the new society were to be equally subject to the law and were to cooperate voluntarily by means of free competition with special privilege for none and equality of opportunity for all. With those objectives so clearly sculptured in the very foundation stone of the new society the United States stood alone in a largely hostile world, a world organized far differently and with greatly different objectives.

### *The Situation Today*

How stands the former infant nation among the great industrial powers of today? To the new small nation of two centuries ago the industrial revolution came in due course, and progress at a rate not elsewhere equaled was the fruit of relatively free enterprise. Countless individuals were stimulated by relatively free competition, were financially strengthened by being permitted to reap where they had sown, and were encouraged by unlimited opportunity to do on a larger and larger scale that which they could do best for society. From their talents, in some instances bordering on genius, innumerable businesses, even whole industries grew. John Fitch, Robert Fulton, Eli Whitney, Peter Cooper, Phineas Davis, Francis Lowell, John Goulding, Cyrus McCormick, Charles Pillsbury, Gustavus Swift, Andrew Carnegie, Thomas Edison, Henry Ford; these were but a few of those whose talents were reflected in the vast growth of industry in the United States.

The result has been that the United States today is the industrial colossus of the world. Steel is the basic material of modern industry. The total capacity of the United States steel industry is 141,000,000 tons annually, more than 40 percent of the 1957 steel production for the entire world; our capacity is more than double that of England, France, and Germany combined and is 2½ times that of Russia. The *increase alone* in American steel capacity since World War II began roughly equals Russia's *total* output in 1957.

With reference to numerous other products of a modern industrial nation the story is much the same. Although including only a little more than 6 percent of the world's population, the United States produces and consumes nearly two-thirds of the world's aluminum, more than two-thirds of the motor vehicles produced in the world, about 40 percent of the electric energy (nearly 4 times that of Russia); and it has two-thirds of all the world's telephones in use.

Yet there are those who assert that we dare not stand alone in a possibly hostile world; that we must have friends to help protect us from potential enemies; that we must outbid Russia in the search for allies; that we must support governments abroad determined to impose on their citizens procedures and objectives alien to our own and that in the long run must conflict with our form of society. Although we know, if we have learned anything from our own experience, that the road to socialism is the road to ruin, we are told that foreign governments "hell-bent" for socialism must be supported by taxes levied on our citizens, all because some assert that we dare not stand alone.

Isn't it long past the time to face the fact that the United States still stands alone as it has for nearly two centuries? Except for a few small nations, relatively inconsequential measured by industrial might, no other nations are with the United States in pursuit of the same basic objectives.

Consider England, for example, with whom we probably have more in common than any other large nation. True, England is a "freedom-loving democracy" in the popular meaning of that rather vague phrase, but England's objectives are *not* the same as ours. England is still a nation divided, in large part, between a landed aristocracy and other custodians of great wealth on the one hand and on the other hand a multitudinous and largely disinherited proletariat.<sup>1</sup> When the financial and other vested interests of Great Britain and the remnants of the empire are threatened by such an event as Egypt's seizure of the Suez Canal, the governing group not only has no hesitation in sending the common citizen to war but also the government does not even bother to consult the people about the matter. (That the government also neglected to keep its supposed ally informed, the ally who was paying some of the bills, was only what we should have expected had we stopped to reflect on the differences between England's objectives and our own.)

Then consider France. Once there was hope that the objectives of the United States would become the objectives of France, but that was nearly two centuries ago when the French Revolution first began. Lacking a foundation as stable as our Constitution, that unfortunate nation soon reverted to a monarchical form of government, crowned Napoleon emperor, and since has regained only the semblance of a free-enterprise

<sup>1</sup>England has a more numerous middle class than have most European nations, but this element of the population in recent decades has become politically impotent. When in power, the Labor Party has turned to socialism as a means of taking capital and income from the aristocracy of wealth in the hope of effecting a different distribution of income. Ground between the millstones of socialist taxation and inflation, the middle class has experienced drastic deterioration of its economic status. Of course, the aristocracy of great wealth, although subject to high income and estate taxes as long as they remained vulnerable within Great Britain, have transferred holdings to relatively tax-free Bermuda, the West Indies, and elsewhere. Also, and especially in the absence of a capital-gains tax, the wealthy readily have found ways to profit from the continued inflation.

republic. Special privilege exerts an influence in government such that apparently interminable war has been chosen in order to protect French vested interests in North Africa.<sup>2</sup> The French Government joined Britain in the ill-fated attack on Egypt, also without consulting either its own citizens or the United States, and only recently has used American planes for an attack on an undefended Tunisian village.

Does any sensible man really expect France to prove a stouthearted ally if Russia attacks, regardless of how much money and equipment we give to France? Inasmuch as France capitulated at the threat of German bombing of Paris in 1940 (with ordinary bombs) when her own existence as a nation was involved, why should we expect France to brave the threat of nuclear bombs from Russia in order to assist the United States?

The fact is that Europe, with minor exceptions, is an aggregation of countries where special privilege long has held the reins of power. The disinherited proletariat has found but two principal ways of coping with the situation: 1, to emigrate to the New World; or 2, to impose socialism at home in a misguided effort to obtain "fair shares." If the more numerous underprivileged of those nations ever have entertained the notion that our objectives should be theirs, they have not yet displayed competence to effect the change.

As for the landed aristocracy and in the present age the equally or more numerous beneficiaries and guardians of great corporate wealth, their privileges have been held so long as to seem like natural rights. They have no more intention of giving up their strangle hold maintained by means of land monopoly and international cartel arrangements than a tiger would have of giving up her cubs. To those powerful interests, the American Dream of a better society seems like a foolish dream indeed, and they would not hesitate to use their counterparts and financial allies in our own Nation to defeat progress toward our objectives if that progress seemed to endanger their power and privilege. Many United States citizens and many more of the parents of present citizens came to this country from Europe in order to escape from the situation that there prevailed and for the most part still prevails. Taxing them now to support the conditions from which they fled hardly seems a worthwhile project. Would not the funds be better used here in furtherance of their and our objectives or, if used abroad, used in support of those same objectives elsewhere?

<sup>2</sup>"The result has been that during the entire period of the Third Republic capitalist interests, whether industrial, commercial, or agricultural have practically dominated the political arena. Evidence of this domination is ample, but one significant indication of it is that no successful attempt has been made to alter the character of the conservative Senate. Control of politics by moneyed persons has been so complete that Frederick Schuman in his excellent book, *War and Diplomacy In the French Republic*, . . . " etc., from Shepard Bancroft Clough, *France, A History of National Economics*, Charles Scribner's Sons, New York (1939).



Parenthetically, we should make clear at this point that we do not imply that the United States should turn a cold shoulder to England, France, and other possible allies. Wisdom dictates that even such allies as Spain be sought if the end result is to the best advantage of the United States. However, in cooperating with other nations wherein and to the extent that our mutual interests coincide we should avoid the sloppy sentimentalism that is blind to many significant facts in the situation. At least, we should avoid strengthening the hands of socialist governments whose ultimate "success" must ruin our erstwhile friends. Moreover, not a dollar should be given or loaned abroad unless sound comparative analyses indicate that such use will accomplish more toward achieving United States' objectives than could be expected by either using that dollar at home or leaving it in the pockets of the citizens from whom it must otherwise come.

As for many other nations of the world that have been the recipients of our lavish gifts and "loans" in recent years, most are either absolute monarchies, military dictatorships, or oligarchies under the control of powerful landholders or other privileged groups. Some of our aid has served only to make the rich richer, to put more Cadillacs in families where there was only one before. In other instances we are attempting to aid impoverished and backward peoples without sufficient analysis of the reasons for their ages long condition and therefore without an adequate basis for believing that our aid will be effective in the long run.

Of course, this liberal distribution of largess and advice reflects two aspects of our own misconceptions: 1, the delusions of economic grandeur that always have accompanied our periods of prolonged inflation; and, 2, a singular overconfidence in our ability to prescribe how prosperity may be attained by others in view of our obvious inability to preserve it for ourselves.

In the meantime, what have we done at home in recent years? We have engineered the greatest inflation in the Nation's history; we have induced millions of our own citizens to incur debts for homes, cars, etc., in the belief that ever-increasing prosperity would be or could be made permanent; we have robbed holders of life insurance, savings, etc., of nearly \$200,000,000,000 in the short space of 15 years; we have encouraged a widespread and fatuously complacent overconfidence in the Nation's future while failing even to see the basic problems that must be solved if United States' objectives are to be attained.

Now the time has come when continuing to avoid facing the facts may be disastrous. If we ask the right questions, we may in time find the right answers and thus progress toward our objectives. When and if we do that we shall be in a position to invite the rest of the world

to follow, if they choose to leave the swamps of socialism and the deserts of despotism. In the meantime, we should remember that we still stand alone and must continue to stand alone unless we choose to abandon pursuit of those national objectives that make the United States the only hope for a despairing world.

### III.

#### WHAT QUESTIONS?

Solutions to the problems of men are found, when they are found, by first asking the right questions. Today we in the United States are confronted with three problems of critical importance: 1, the current recession; 2, apparent departure from rather than the desired approach to the Nation's basic objectives; and 3, survival in a hostile world. How shall we ascertain what questions to ask, and how may we find useful answers?

Once upon a time men sought solutions to their problems by asking questions such as: What one or more of the Gods have I offended? How may I appease them? Who among our medicine men possesses the most potent magic and can best intercede for me? Here in the United States, at least, we have long since learned that these are not the right questions.

Not quite so outmoded are questions of a somewhat different type such as: Where in our folklore shall I find the answer?, or Who among the wise men can tell me the proverb that suggests a solution to my problem? But we of Western Civilization no longer expect to find in proverbs handed down from antiquity the solutions to all current problems in this age so influenced by the development of modern science. In the days when most proverbs summarized the common sense of the times, many of today's complex problems simply did not exist.

And at other times and places men have sought the advice of philosophers, have asked them, What is the Truth, the absolutely certain, guaranteed, and everlastingly correct answer to my problem? Philosophers of two general varieties, the Platonic idealists and the Aristotelian logicians, both offered answers for the questions of men, unfortunately not with unqualified success.

Then finally a few men happened upon a different method of conducting inquiries. They put aside the spooks and fairies, demoted the mythical gods and goddesses, discounted the folklore and superstition embodied in proverbs and old wives' tales, abandoned the quest for certainty, and instead asked questions such as these: What measurable changes occur and what uniformities of relationships are found among those changes? What actual sequences do we find in the natural world of things or events? What hypothesis or theoretical explanation is suggested by the facts and can be adequately tested by a check of the necessary implications of the theory against facts of the future and can

even be used for successful prediction and control over the future facts or our adaptation to them? Such questions proved to be "right" in the sense that the answers when found have been useful in coping with the problems of men.

The successful method of inquiry now generally called scientific was first applied to certain physical problems of men. To the question, Does the earth revolve or does the sun move around the earth?, a useful answer was found by the methods of science. True, some of the pioneers who thus sought answers were tortured by rack and screw; and the answers that they found were not generally accepted for many decades; but, in the long run, these answers prevailed.

Similarly with the physiological problems of men, the pioneers of modern medicine were scorned by most professional teachers and students in the field. The conclusions of Vesalius and of Harvey were accepted only after prolonged debate; in fact, some of the pioneers even were cast out of their professional groups and died in poverty because they espoused new ideas.

Less personal sacrifice has been involved for those who are leading the scientific advance, the revolution in methods of inquiry, in the behavioral fields, especially in economics. However, there is every present indication that the battle to enthrone the results of scientific methods of inquiry will last for decades even if it is not so bitter as were the earlier battles in the physical and physiological sciences.

Although scientific methods of inquiry have been well under way on an organized basis for nearly four decades in the social sciences, following the earlier efforts of a few pioneers, many economists still cling to the older methods of inquiry. The Keynesian spend-for-prosperity notions taught in many colleges provide an excellent example of the cultural lag with their foundation resting on secular revelation and their web of theories spun from introspection, casual observation, and vivid imagination in the best scholastic tradition of the dialectical quest for certainty. As a result we find even in one of the Nation's leading technical institutions an economics professor teaching sophomores that perpetual inflation with an increase of 5 percent annually in prices (that is, depreciating the dollar at this rate) is desirable;<sup>1</sup> and in a nearby university we find a bad case of schizophrenia or split personality with one eminent economics professor advocating perpetual inflation (his suggested annual rate of depreciating the dollar being 3 percent), but across the river that splits the campus, in the university's business school, politely expressed professorial disagreement.

<sup>1</sup>For a more extensive analysis of Professor Samuelson's teachings at the Massachusetts Institute of Technology see the review of his book *Economics, An Introductory Analysis*, in E. C. Harwood, *Reconstruction of Economics*, American Institute for Economic Research, 1955, pp. 23 to 31.

Another school of economists, typified by Hayek and von Mises, although their methods are similar to those used by the Keynesians, arrive at diametrically opposed conclusions. Yet neither the Keynesians nor the others have as yet grasped the obvious fact that the answers they provide are suspect because of unsound, in the sense of proven-to-be-inadequate, methods of inquiry. In fact, only because the method they use is unsound is it possible for men of otherwise good intellects to derive such conflicting answers.<sup>2</sup>

Parenthetically, of interest is the fact that application of modern scientific method in the general field of sociology (or what might be called a combination of sociology and anthropology) appears to be on the verge of a major "breakthrough" comparable to Galileo's successes in astronomy more than three centuries ago. Leaders in this field now believe that they have scientific proof of the survival value of individual freedom and equality of opportunity in a human society.

### *The Appropriate Questions*

We turn to some of the questions that should be asked in relation to each of the three major problems indicated at the beginning of this discussion.

Concerning the current recession, we should ask:

1. Has modern scientific method provided a tested explanation of the more extreme cyclical changes in business activity?
2. What are the implications of that explanation as far as alleviating or remedying the present situation are concerned?
3. What should be done to minimize the extent of such developments in the future?

Fortunately, in large part through the work of the National Bureau of Economic Research and our own organization during the past four decades, the answer to the first question above is "yes." Some useful answers to the second question also have been developed. The general character of useful answers to the third question is apparent, but details remain to be worked out.

With reference to the second major problem, apparent departure from rather than the desired approach to the Nation's basic goals, answers to the following questions are needed:

1. To what extent and in what ways are departures from the basic goals measurable, even in a general way?
2. What are the explanations for the divergence of results from expectations?

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<sup>2</sup>For a more adequate discussion of this situation see the reference cited in footnote 5, pages 7-22, 73-82, and 99-103.

3. What changes in statutes, customs, etc. can serve as a means of achieving the desired ends?

Although some work in the attempt to answer these questions has been done, much more remains. We hope to do some work in our own organization.

Concerning the problem of survival in a hostile world, such questions as these should be asked:

1. What are the conditions precedent to optimum growth of a modern industrial nation?

2. How can the Nation develop to the maximum extent its resources of human intelligence in order that our lead in the scientific and technological advance may be maintained?

3. What is the relative importance (for survival) of more expenditures for defense, various kinds of foreign aid, internal subsidies such as those to agriculture, aid to education, etc., etc.?

No one having any conception of the complexities involved would assume that the answers to all these questions can be found in less than several decades of comparative analyses requiring painstaking and continuous application of modern scientific method, although we need not wait long for many useful answers. Our organization has developed portions of some of the answers, but the scope of the problems is greater than our present sphere of activity.

#### *How Find More Answers?*

As for how more of the answers to these questions may be found, we propose that an independent and nongovernmental National Advisory Commission for Inquiry Into the Problems of Men in Society is needed. Such a National Advisory Commission should have the task of developing, by the application of modern scientific method, useful answers that will be available to the public.

Experiences with temporary commissions of inquiry here and abroad have demonstrated that such devices are a logical and essential element of social organization in a republic or "democracy," as most republics are called today.<sup>2</sup> Therefore, for inquiries into problems that cannot be solved in any short period, we believe that a permanent advisory commission of inquiry is needed. With the aid of others we plan to initiate such a National Advisory Commission that will be completely free of all ties to vested interests, political, business, or other.

Surely obvious to all intelligent observers is the fact that pressure groups such as the farmers or organized labor and vested interests such

<sup>2</sup>For a more comprehensive discussion see "Democracy's Device for Analyzing Major Problems," the concluding essay of *The Counterrevolution*, American Institute for Economic Research, Great Barrington, Massachusetts, 1956 edition.

as some major corporate or other groups exert a dominating influence at times on various aspects of legislation without regard to the general welfare. That politicians will respond to the desires of such pressure groups offering votes or contributions to campaign expenses or both is inevitable in any form of popular government. Who can deny that the first objective of even a would-be statesman, not to mention a mere politician, is to get elected and then re-elected? The most high-minded and able statesman in the Nation, lacking a seat in Congress, will hardly be effective in the deliberations of that body.

However, in nearly all parts of the United States the balance of power, either at the primaries or at the elections, is held by a relatively small number of independent voters (even if some of them are registered under a party label). If the work of the proposed National Advisory Commission is sound and if enough of the Nation's more independent voters choose to accept the Commission's findings and recommendations, there is reason to believe that such findings may become influential in legislative halls. We know of no other means by which useful solutions for the Nation's major problems may be developed and applied.

In a republic or a "democracy" the common sense of the citizens presumably provides the guide for legislation and custom. In matters physical, for example in bridge construction, the citizens of the United States have adopted as their common sense the findings of qualified scientists, not of course in full technical detail but as a guide to action; in matters physiological, for example, vaccination against smallpox, the views of qualified scientists similarly have been adopted as the common sense of the citizens. We believe that the warranted conclusions of qualified behavioral scientists must be made available for acceptance by citizens as a guide to action if our Nation is to survive. In short, we believe that twentieth-century common sense should include the findings of qualified economic and other social scientists as rapidly as such scientists and their warranted assertions can be developed.

#### IV.

#### WHAT ABOUT THE UNEMPLOYED?

Few members of a modern industrial society can avoid losses and, in some degree, hardship during a severe recession or depression. Thousands who have invested in businesses forced into bankruptcy lose their accumulated capital; millions who have invested in the securities of businesses that survive nevertheless lose if forced to sell during a depression, and their incomes are curtailed when dividends are reduced. Hundreds of thousands of business managers find their usual worries multiplied as they strive to find the funds to meet next week's payroll. All of these individuals deserve sympathy not only because of their present plight but also because many of the panaceas now under consideration by Congress would hamper rather than encourage the efficient functioning of free markets whose decisions are needed in order to correct maladjustments and restore prosperity at the earliest possible date.

With reference to the unemployed, however, much more than sympathy is required. All citizens bear part of the responsibility for the situation of the unemployed. They are entitled at least to a livelihood for themselves and their families while the necessary readjustments are being made.

The responsibility of all citizens for the plight of the unemployed rests on two bases. In the first place, if more progress had been made toward the Nation's basic objectives, the unemployed as well as others presumably would be in a better position to cope with present difficulties. Second, who but the citizens as a whole should be held responsible for the great inflation since the beginning of World War II and the present aftermath of that prolonged inflation?

The fact is that the public, acting through both Democratic and Republican administrations of the Federal Government, put in motion and kept in motion the great inflation that stimulated the prolonged business boom, that cut short the minor interruptions of 1948-49 and 1953-54, and that accounts for the extent of the distortions now requiring correction. Even the more prudent of those unemployed, who waited as long as they reasonably could before purchasing homes for growing families, found their attempts to be prudent penalized by the continually rising costs of new residences as organized labor in the building trades and elsewhere took advantage of the great inflation.

The unemployed as well as others may have incurred debt unwisely, may have undertaken too large a burden of monthly payments. Some



would have been improvident in any event; but was not the continuing rise in prices more than an inducement, was it not an actual threat that if they did not incur debt they would continue to lose some of the buying power of any dollars they saved?

Moreover, who is responsible that the unemployed now receiving half or a third of their regular wages must still pay high prices for food that, in freely competitive markets, would be available for much less? The economic folly of subsidizing agricultural surpluses by maintaining artificially high prices becomes worse than mere folly in depression times; how should we characterize the actions of a government that deliberately raises the price of food when millions of its citizens are on a bare subsistence dole? Surely this is a strange procedure for a nation to adopt under the guise of promoting the general welfare.

Even continuation of the dole, of public relief, to say nothing of the more liberal unemployment compensation available to a portion of the unemployed, will be partly at their expense unless more inflation by the monetization of deficits is avoided. More inflation will push prices up further, will depreciate or lessen the buying power of the unemployed's last reserves, the currency in the pantry sugar bowl, the last life insurance policy, perhaps a few U. S. savings bonds, or a savings deposit. Thus to the obvious robbing of Peter to bribe Paul via taxes to support prices of food at unnecessarily high levels will be added the subtle embezzlement effected by a depreciating dollar.

In fact, the very process of paying people who are not producing tends to result in more inflation. Dollars thus go chasing goods without a corresponding addition to the supply of goods in the markets. Unless care is taken to raise taxes or to borrow from the current savings of those whose incomes do represent production, (that is, unless further monetization of Federal deficits is avoided), the more the doles or the relief and unemployment payments, the less each dollar of them will buy in the markets.

Reabsorption of the unemployed into the production processes as rapidly as possible is the objective. What can be done to expedite progress in that direction?

The situation in the automobile industry offers a case in point. During the years of prolonged inflationary prosperity the principal companies concerned found increasing profits readily obtainable. Organized labor was alert to the possibilities and demanded a share of the windfall profits. Corporate managers acquiesced, perhaps because they saw no other way or perhaps because they simply concluded that continuing inflation would enable them to keep one jump ahead of labor's demands. Be that as it may have been, the net result has been a

quadrupling of automobile labor's average weekly wage (including fringe benefits) since 1939.

The automobile industry is not the only segment of the economy where wages have more than quadrupled, but in several important segments the increases have been much less, and in some segments the increases in wages have not even compensated for the rise in the cost of living. For example, wages of employees in the entire educational system of the Nation, from kindergartens through the university graduate schools, have lagged far behind. Even full professors in most of the Nation's colleges today receive little more than many steel workers or automobile workers were earning including their overtime pay during the latter part of the boom period. Below the grade of full professor and down through the public schools, most teachers of the Nation's youth are less well off today than they were in 1939.

Another large segment of the population, those who have retired on pensions and other more or less fixed incomes, also have lost buying power during the years of prolonged inflation. Bitter indeed has been the experience of thousands, perhaps millions, of such persons who have seen what seemed like enough income for retirement needs reduced in buying power as inflation proceeded. A citizenry that thus condemns its aged and infirm to a declining standard of living seems singularly careless of the future, because those of the rest of us who live to retire will find ourselves in the same situation unless recent trends are changed.

In any event, the principal point to be made here is that some segments of the population that have derived most advantage from the great inflation now have priced themselves out of much of their former markets. In the absence of more and more inflation, how can some segments of the economy hope to maintain their seriously unbalanced position in relation to the rest of the population?

With these facts in mind, we offer a suggestion. In order to outline it definitely we use specific figures, but the principles involved rather than the illustrative figures are important.

The managers of, for example, General Motors might say to their employees something like this:

1. Obviously, our employees, the stockholders, and we, the management, have profited greatly from and during the prolonged inflation of the postwar years. Equally obvious is the fact that our product cannot be sold in the volume we should prefer at today's prices. Many of our former employees have no wages, and most of our present employees are earning less than they were, management's bonuses will decrease, and dividends will be reduced or cease unless we can alter the situation.

2. Profits have been reduced 100 (or whatever) percent from the peak levels of recent years.

3. We propose a *temporary* reduction in *all* wage rates and salaries of *half* the percentage reduction in profits, plus a bonus with the following understanding:

a. The company will resume production at what is believed to be the most efficient rate of operations, rehiring as many as practicable of the capable, former employees.

b. Simultaneously, prices of cars and other products will be reduced to what the management believes will be a break-even level with normal production for a 40-hour week. Prices may be adjusted upward if the resulting demand proves to be even more elastic (responsive to lower prices) than the demand for cars always has been.

c. Shortly after the end of each quarter, any profits obtained will be shared with employees as an incentive bonus or supplementary wage so that when net profits, after deducting taxes and the supplementary wages, have recovered to half those of the last peak year the supplementary wage payments will restore half the cut in wages (bringing wages to 75 percent when profits are at 50 percent of former peak levels); when profits have recovered to 80 percent, supplementary wage payments will restore 80 percent of the cut in wages (bringing wages to 90 percent of peak levels), and so on. (Dividends to stockholders presumably would be in proportion to the net profits remaining for the company.) It is further understood that a final adjustment will be made annually and that when and if net profits again reach the last peak levels, the wage and salary scales shall be fully restored and employees shall be free to bargain and strike for higher wages or whatever arrangements they prefer. The accounting aspects involved may be checked by independent auditors.

Perhaps we should add that we at the Institute are not so naive as to expect such a plan to be welcomed at first consideration either by General Motors or by organized labor. However, there is nothing like a depression for stimulating the exercise of ingenuity. Inasmuch as the management of General Motors had the brains to foresee the effects of prolonged inflation and profit by it, and inasmuch as the leaders of organized labor were smart enough to get labor a share of the windfall profits while the getting was good, perhaps there is enough combined intelligence in the two groups to recognize the merits of such an arrangement.

In effect both labor and management, if such a plan were adopted, would simply be taking advantage of the lesson to be learned from free, competitive markets. One can, of course, learn the hard way, by prolonging unemployment, forcing great losses on the company, possibly bankrupting the union, and in general being as shortsighted as organized

labor and management were in England after World War I for several years or as lacking in wisdom as such groups have been at other times and places. However, we see no inherent necessity for such stupidity, especially when there is so much to be gained for all by a more intelligent approach to the problem.

That other distorted segments of the economy probably would be wise to adopt similar arrangements seems obvious. The more rapidly prices and wages could be restored to levels that encourage the maximum of exchanges, the better for all concerned.

How long a period would be required for wages and profits in such presently maladjusted industries to recover to former peak levels, no one can foresee. Given renewed opportunity for balanced growth, recovery to and extension beyond former peak levels might occur in a surprisingly short period of a few years. One has only to observe the results in Germany of the resort to the decisions of free markets to realize that a seemingly miraculous recovery of an exceedingly "sick" economy is possible; in fact we consider such recovery under free-market conditions a reasonable expectation.

When conditions seemed darkest in the spring of 1933, President Roosevelt inspired some people by his confident assertion that we had "nothing to fear but fear itself." Heartening as this message may have been to many listeners, subsequent events proved that the Nation had much more to fear than fear itself. What should have been feared far more was that men of unquestioned good intent would be governed by their hearts rather than by wiser heads, that good intentions would pave a six-year-long road through the "hell" of unemployment for those who already had endured such hardship too long. Good intentions are not enough. Good intentions play a vital part in providing the urge to act, but impulsive action aimed at alleviation of symptoms rarely remedies serious economic or other maladjustments. This time we can avoid burdening the unemployed with a decade of frustration and heartaches if we apply the lessons of past experience, lessons that now should be part of our common sense.

## V.

### THE COUNTERREVOLUTION<sup>1</sup>

The struggle against communism is not an attempt either to destroy Russia or to preserve the United States; it is not merely another of the numerous rivalries between nations that have crowded the pages of history. The struggle against communism is a crucial one for the survival of Western Civilization. Whether this struggle will mark the decline and fall of Western Civilization or will set the stage for a new, great advance comparable to that of recent centuries remains to be seen.

Because this is not merely a struggle between jealous or greedy monarchs nor solely a war for empire and trade nor a religious war between ignorant and intolerant tribesmen, we must seek below the surface and behind events of the day for the fundamental causes of the conflict within Western Civilization. At least briefly we must sketch the outline of developments on a broad front and in the perspective of recent centuries.

Several hundred years ago Western Civilization consisted of many vast feudal estates, innumerable peasant holdings of small farms, uncounted villages and towns, and a few cities, small by today's standards. For the most part, men lived as their fathers and grandfathers before them had lived; folklore and superstition were generally considered the intellectual keys to understanding, and scientific knowledge as we think of it today was almost unheard of; class distinctions were rigid in many parts of the civilized world; village industry was controlled by the guilds and other authorities; progress was not generally expected and often was not tolerated; most men were slaves, seemingly held in perpetual bondage by custom, fear, ignorance, and superstition. Only the more fortunate who had been granted domination over the earth and the fruits thereof, seemingly by an inscrutable Providence, could live much differently than did beasts of burden in that almost-forgotten age.

Nevertheless, within that civilization an idea began to find increasing acceptance. In a word, this was the idea that individuals might be *free*; but its scope developed gradually, and even today we are not sure that we grasp its full implications.<sup>2</sup>

<sup>1</sup>First published as a Special Bulletin in August 1950 and later supplemented by additional explanatory articles in book form. See inside back cover.

<sup>2</sup>One suggestion is that men are free to the extent that the culture or society in which they live permits them to plan and choose their goals, provides equality of opportunity to act effectively in pursuit of those goals, and permits

Aided by many circumstances that need not be described in detail, this idea of freedom found more and more disciples. It attributed worth and dignity to the individual man; and, as men gradually and almost reluctantly accepted this new idea, they likewise accepted many increased responsibilities that fostered individual growth in countless ways.

Intellectual freedom opened the doors of the new frontiers of science. As a result, technological progress rose like a giant from sleep to aid the wealth-producing activities of men. Here in America circumstances were most propitious for a civilization based on the idea of freedom. The results we are familiar with; but the magnitude of them is sometimes overlooked, because to us they have become commonplace.

Freedom found acceptance in parts of Europe also. Major social changes marked its advent, and great material progress was one result. However, in much of that area the great revolution never was so successful as it was in the United States. Apparently in only two countries of Europe, Denmark and Switzerland, has the great revolution maintained its gains or progressed in recent decades.

Even here in the United States, however, complete freedom was not reached. Conditions here differed greatly in many respects from those in the Old World; but we now realize that various laws and customs carried over from the Old World had the effect of denying freedom, at least in some degree, to many of the people of our own Nation.

The results of imperfect or partial freedom were not all good. Great material progress came, but the greatly increased production of wealth was not equitably distributed to those who produced it. As a result, 12- and 14-hour days for women and children were common in the factories of England, more extensive and more degrading poverty pervaded the slums of Europe, and urban and rural slums developed in the United States.

So striking did the increasing maldistribution of wealth become that many men abandoned the battle for freedom and turned back; thus the counterrevolution within Western Civilization was born. For the past hundred years the counterrevolution has been gaining strength. Its basic ideas were developed earlier by the Utopian Socialists and were organized as counterrevolutionary doctrine by Karl Marx and his followers. These ideas are the roots from which modern communism, socialism, fascism, the New Deal, and the Welfare State all have grown.

In Russia the counterrevolution has reached the apparently inevitable

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them to retain the fruits of their labors. Throughout this report we shall use "freedom" as a blanket label for these circumstances and such others as may be necessary to constitute optimum circumstances for the economic welfare of men in society. We realize that such use of a term is loose characterization rather than scientifically accurate specification or naming, but it will serve the purpose here.

goal; a new despotism has replaced the old. In this fact there is a lesson for all who desire to learn it. Marx and Engels predicted success for communism (the militant branch of socialism) first in the great industrialized nations where they expected the proletariat to unite and cast off its chains. But communism succeeded first, not in the more advanced industrial nations, but in Russia, where the progress of the great revolution had been retarded. The reason is not difficult to understand. The counterrevolution is fundamentally a retreat from individual freedom, from responsibility and authority for each individual, to the sheltering arms of an all-powerful state. Naturally, communism succeeded first where the progress of the great revolution had been least; and it still achieves success most readily in the backward nations of the world, where the substitution of a new despotism for the old is relatively easy.

#### *The Source of Communism's Strength*

However, the fact that communism succeeded first in Russia and that it gains ground most rapidly in the more backward nations of the world should not be permitted to encourage a false sense of security. The basic principles of communism have been widely accepted; and the counterrevolution has gained strength during the past century in nearly all nations of Western Civilization, including our own. In order to grasp the significance of these gains, we must first understand the source of the strength of communism.

Although the hopes it offers are known by many to be illusory and although its promises are vain, communism derives its strength from those who, because of the inequitable distribution of incomes, have become the underprivileged of all lands. What other hope have those who are denied a substantial part of the fruits of their labor (in order that the perquisites of the privileged may be preserved) than that someone will somehow redistribute currently produced wealth in accordance with men's needs? The Marxian slogan, "From each according to his abilities; to each according to his needs," offers to the poor a hope comparable to the hope of a better world offered by many religions. Communism has the added advantage of promising to provide in this world now or in the immediate future what some religions offer only in the next world at some future time.

The strength of communism's appeal results from its promise to eliminate special privilege for the few and the inevitably corresponding inequality of opportunity and obvious inequity of reward for the many. Communism has grown in strength as special privilege has grown; the farther the nations of Western Civilization have departed from equality of opportunity, one ingredient of freedom, the more they have drifted toward communism.

Fascism often is discussed as though it were the opposite of communism, but such is not precisely the case. Hitler, Mussolini, and Stalin were different in many respects; but the principles of their economic ideologies were the principles of socialism; their initial appeal was to the underprivileged; and the final result, a new despotism, was the same in all three instances.

In view of the foregoing, we may summarize the present situation somewhat as follows: Western Civilization as we know it today is the outcome of a great revolution that followed the acceptance of new ideas and that accompanied the progress toward individual freedom including equality of opportunity and economic justice<sup>a</sup> for all men. However, virtually complete freedom as herein described has not yet been reached except in relatively small areas of the world and even there only for brief periods.

Perhaps primarily because we of this civilization have stopped short of the goal, the results have in part been an inequitable distribution of currently produced wealth. In the minds of many, not even the material progress made possible by the great revolution can offset results that seem so evil. Either not realizing that the goal had never been reached or not understanding that the evils they deplored were attributable to imperfect freedom, many leaders in thought and action sought to turn back; thus the counterrevolution was born.

The counterrevolution is in progress throughout the world. It is recognized as communism; but fascism, various Socialist governments, the New Deal, and the Welfare State all have grown from the same roots.

Such is the situation in this midpoint of the twentieth century. American foreign policy, if it is to be successful in the long run, must cope with the counterrevolution in Western Civilization.

#### *Lesson of the Immediate Past*

Before proceeding to a discussion of American foreign policy, a brief review of recent developments will be helpful. A valuable lesson can be learned from mistakes of the recent past.

Germany and Russia were enemies in World War II, not because their ideologies differed, but because there was not room on the same continent for their ambitious rulers. We were allied with Russia, not because Russia was one of the democracies fighting for freedom, but because Russia happened to be fighting Germany and could be induced to fight Japan.

However, Americans are sometimes thought by their political leaders

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<sup>a</sup>Economic justice refers to the third part of the definition of freedom previously given. Men who are free to plan and choose their goals and who enjoy equality of opportunities to seek their goals may be said to receive economic justice if they are permitted to retain the fruits of their labors.



to be squeamish and unwilling to face the facts of life. Consequently, the wartime administration sought to "sell" the American people the notion that Stalin was a respectable companion in arms. They were not content to use him to the extent that he was useful, while keeping in mind that he was the leader of the counterrevolution threatening Western Civilization; they insisted on adopting Russia into the family of peace-loving nations. In our preoccupation with winning World War II, the Nation's leaders apparently closed their eyes to the important long-term developments that have been described here.

Our foreign policy during and immediately after World War II was a series of blunders precisely because we dealt with successive short-term situations as though there were no long-run fundamental conflicts of aims or as though we were blind to other than immediate pressing developments. Such was our major error, and the lesson should not be forgotten.

Prior to World War II, American foreign policy had to cope with two classes of potential enemies. The first included Germany and Japan as potential enemies for the same reason, ambition for power, that nations have so often been enemies since the dawn of recorded history. The other class of potential enemies may be roughly designated communists or, to be more specific, the counterrevolutionary elements within Western Civilization.

Fortunately, the problem of formulating an adequate foreign policy is simplified in some respects by the fact that, in coping with Russia as our only potential enemy of substantial strength in the first class (having a ruler whose ambitions for more territory and power make him a potential enemy), we shall be coping to some extent with the world-wide counterrevolutionary movement.

On the other hand, the situation is complicated by the fact that, in choosing a foreign policy intended to cope with Russia's ambitions for more territory and power, we may erroneously assume that the long-run problem of the counterrevolution is automatically solved merely because we associate the long-run problem also with Russia. Actually, the ruler of Russia is not the long-run problem: he is merely its temporary figurehead or symbol. Regardless of what happens to him or to Russia in the next several years, the long-run problem of the counterrevolution will remain.

#### *What Can Be Done about Counterrevolution?*

We now come to the question, "How can the foreign policy of one nation deal with counterrevolution within a civilization?" A nation faced with such a counterrevolution has any one of three courses available. Each of these will be discussed in turn.

The first possible course is to join the counterrevolution. To a far greater extent than many people realize, the United States already has chosen this course. Many internal policies, especially (but not by any means solely) some of those adopted in the past two decades, conform to the principles advocated by the counterrevolutionists. In our foreign policies also we have not hesitated to give extensive financial aid to the political parties in control of various governments that are aiding and abetting the counterrevolution. We refer to the Socialist governments of England and France.

It should be apparent that the first possible course, which we have already chosen in part, will be self-defeating in the long run. If we encourage the counterrevolution in other nations and yield to its wiles at home, we shall end by joining wholeheartedly, while Western Civilization declines and falls as others have done before.

The second possible course is to attempt to preserve the status quo, that is, neither to press on with the original revolution nor to join the counterrevolution. This apparently was an objective of the Truman policy. Although the Truman policy appeared to be somewhat inconsistent for several months, including as it did the extension of military aid to Greece and Turkey and the denial of military aid to Nationalist China and Korea, subsequent actions and announcements indicated that the policy had become firm. In essence it appeared to contemplate preservation of the status quo as of June 1950 indefinitely.

The second course, preserving the status quo, would seem to us impossible if we may legitimately deduce from history something other than that men never learn anything from history. And, aside from the lessons of history, we know that the conditions in which communism is rooted and from which it derives its strength have become increasingly favorable to communism; this trend seems destined to continue until progress toward the goals of the great revolution is resumed. Preserving the status quo would become increasingly costly and increasingly difficult as the years pass. Such a policy is only a slower, not a less certain, road to destruction in the long run than the first possible course.

The third possible course is to oppose communism, but what effective means are there for opposing communism? An answer is not difficult to find if one remembers that communism is the ideology of the counterrevolution. Only if Western Civilization presses on toward the goals of the great revolution will the circumstances that have fostered the counterrevolution be changed. Only as the source of its strength is reduced and finally eliminated will the counterrevolution be weakened and finally defeated in the long run.

Only the third course, to oppose communism by pressing on toward the goals of the great revolution within Western Civilization, appears

to be a practicable means of coping with the counterrevolution.

Fortunately, no other great nation is as well prepared as our own to undertake this task. In order to reorient our aim, we should study again the Declaration of Independence, the Constitution of the United States, the writings of Jefferson, and other documents, such as Lincoln's emancipation address, that have described the goals we once sought so eagerly. Then, we must ascertain why the goals have not been reached, why inequality of opportunity and an inequitable distribution of currently produced wealth became so marked even in the United States as well as in the rest of Western Civilization. Only then shall we be in a position to correct the fundamental errors in our procedure that have delayed progress toward the goals of the great revolution.

The United States has become a great nation, a tower of industrial strength in the vanguard of Western Civilization, primarily because the goals of the great revolution were more nearly approached here than they were in Europe. In the greater material progress here in the United States, we have all around us tangible evidence that should more than justify the faith needed to press on. Surely we of all peoples of the world should know that freedom for the individual (not merely freedom from outside domination for a nation), equality of opportunity, and economic justice are among the important goals to be sought.

We have concluded that the only sound foreign policy for the United States in the long run is to resume our former place in the vanguard of the great revolution, to press on toward the goals of more nearly complete individual freedom, and to encourage other nations to follow. However, we shall be ill-prepared for such a position of leadership until we have reoriented the policies that we apply at home.

Too long have we yielded to the urgings of those who have joined the counterrevolution. Alger Hiss and others like him may not be traitors in the ordinary sense of that word, implying betrayal of their country in order to give advantage to a foreign enemy; perhaps they are merely miseducated men whose good intentions have led them to join the counterrevolution within Western Civilization. We shall underestimate the potential danger if we do not realize that such men are not misanthropic freaks but the legitimate products of some of the Nation's leading educational institutions.

#### *Domestic Policy*

Coping with the counterrevolution at home will not be easy. In order to regain the road toward the goals of the great revolution, we shall have to retrace some steps taken in recent years and turn aside from other goals toward which considerable progress has been made.

Specifically, corrective action will be needed along at least three

general lines. First, the distortion of and interference with free-market relationships must be reduced as rapidly as possible and ultimately ended; second, all special privileges must be eliminated; and, third, the activities of the Federal Government must be reduced to the role of national defense and prevention of license or abuse of freedom.

Restoration of free markets is essential if progress is to be made toward the goals of the great revolution. If men are to choose wisely among possible economic alternatives, they must be free to buy and sell at prices agreed among themselves without government intervention, subsidies, or controls; they must be free to select, hold, and exchange the money or standard of value that they deem most suitable for the purpose (with men's customs and views as they are, the gold standard must be restored); and such abuses of the monetary system as inflation must be eliminated. For 35 years Government intervention and "management" of the Nation's money-credit mechanism have resulted in progressively greater distortions and more extreme interference with free markets. The counterrevolutionists throughout the world have long regarded inflation as their most potent weapon; and events in Russia, Germany, France, and elsewhere have confirmed their judgment.

Holders of special privileges, especially those related to monopolies of natural resources (including land), under existing customs and laws acquire, at the expense of the producers, an expanding portion of the wealth currently produced. This situation results in increasing the number of underprivileged members at the base of society from whom communism derives its voting strength (but not, of course, its intellectual "front"), and it diverts from producers some of the means that could be used to increase production. Because the situation in this respect is more acute in various other countries, for example Italy, many observers see the problem there more clearly. Nevertheless, this problem is evident here in the United States and seems destined to become far more acute as the temporarily stimulating effects of prolonged inflation diminish.

Reduction of the role of the Federal Government to the national defense and to the function of umpire for the purpose of preventing license or abuse of the principles of freedom is essential to the efficiency of the Government in performing its primary functions. United States Senators, who should have time for analysis and study of important policy matters such as those described here, spend their valuable time bickering over the price-support levels for Valencia peanuts and innumerable other trivialities that have become the day-to-day business of an elephantine bureaucracy. A republic need not be as inefficient as a totalitarian form of government that attempts to control all economic activities; but, if we continue adding to the functions of our Federal Government as we have during recent decades, the fundamental efficiency

of free men functioning in free markets will be replaced by the lumbering and creaking performance of a vast bureaucracy. We shall then be as inefficient as our totalitarian enemies.

#### *Foreign Policy*

For the purpose of coping with the immediate threat resulting from Russia's ambitions for more territory and power, our short-term foreign policy may well be based on the expedient, for the time being, rather than on principle. If war with Russia is imminent, we should not scorn any allies, even one such as Spain. However, there is no need to repeat the silly process we went through when we used Russia as an ally in World War II; we need not fool ourselves that we are coping with the counterrevolution when we "make a deal" with men like Franco of Spain.

On the other hand, our intervention in Korea had no other excuse but as part of our long-run plan to cope with the counterrevolution. All of our military experts seem to be agreed that Korea would be a liability rather than an asset in the event of war with Russia in the near future. Obviously then, in Korea we should have insisted on pressing the great revolution, on progress toward the goals of individual freedom, equality of opportunity, and economic justice for all men. Was there any other goal in Korea worth the life of a single American soldier? (Surely our battle cry in Korea should not have been, "Restore to the landlords their vast feudal estates!")

If in doubt as to how progress toward those goals can be made in Korea, we might well study the situation in Denmark and New Zealand. The lessons we should learn would have the added advantage that they could also be applied here in the United States when we finally realize how badly we need to apply them.

#### *A National Policy Commission?*

We realize that the policies we have suggested may not be generally accepted at first. The Nation's legislators who have been preoccupied with Valencia peanuts can hardly be expected to see world affairs in the perspective here described at first glance, and shallow or confused thinking about the problems of Western Civilization in the twentieth century is by no means confined solely to the halls of Congress. Therefore, we raise the following question: Has not the time come for selection of a National Commission on Foreign and Domestic Policy? Such a commission, composed of the most competent men who can be drawn to its service, could be expected to survey the entire problem of American foreign and domestic policy from a nonpolitical viewpoint. By means of extensive public hearings and discussion of various possibilities involved,

public attention could be focused on these critical problems of our times, and the public could become informed regarding these matters. Finally, before its work ended, such a commission could be expected to report findings and recommendations concerning foreign and domestic policy much as the Constitutional Convention did in 1787 or as the National Monetary Commission did on a less extensive scale four decades ago.

Unless something like this is done, we greatly fear that the statue in New York Harbor of the goddess of liberty enlightening the world will no longer be an appropriate symbol of United States policy at home and abroad. And, in that event, what shall it profit us if we gain widespread dominion and for the time being stabilize the world if in so doing we lose our own principles? We shall gain nothing but a little temporary security and shall lose all that we treasure highly as the United States declines and falls with the rest of Western Civilization, a victim of the counterrevolution.

### SUPPLEMENTARY NOTE

The foregoing essay, first published August 28, 1950, suggests the advisability of a National Commission on Foreign and Domestic Policy for the purpose of reviewing the present situation and making appropriate recommendations. In the interests of avoiding confusion, we clarify below the differences in nature and purpose of this proposed commission from the permanent National Advisory Commission for Inquiry into the Problems of Men in Society proposed in the third essay of this series.

We assume that the temporary National Commission on Foreign and Domestic Policy would be appointed by the President under a formula for membership prescribed by Congress. (This is the procedure used in the past for other temporary commissions of inquiry.) Thus it would be a temporary agency of the Federal Government with the costs paid from Government funds.

If earlier precedents were followed such a Commission presumably would include some members of Congress as well as distinguished experts and leaders in various fields including among others the military, economic, governmental, academic, scientific, and business segments of the Nation. The Commission would be empowered to employ technical experts for various aspects of the Commission's inquiries.

Some of the questions that such a Commission might consider would include the following:

1. Is the Truman Doctrine of preserving the status quo as of 1950 an appropriate foreign policy?
2. To what extent should the American people be willing to sacrifice their sons on foreign battlefields;

- a. For more stalemates in other Koreas?
- b. To safeguard the privileges of vested interests such as those of the French in North Africa?
- c. To maintain military dictatorship or government by privileged cliques in various nations of the world?
3. To what extent should the American people be taxed to support foreign governments whose objectives differ markedly from those of the United States?
4. To what extent should the Nation's defense rest on countries such as France, for example?
5. Is it sound national policy for the United States to support and strengthen socialist governments abroad? In this connection we should keep in mind that:
  - a. Socialism and Communism have the same basic ideology, the same intellectual parentage;
  - b. Socialist governments such as the Labor Party provided in England or as we now find in India are notoriously "soft" toward Russia for reasons that seem obvious;
  - c. The basic objectives of such governments are diametrically opposed to our own.
6. Does the United States desire to prepare for numerous small wars anywhere in the world; or, if the blood of American youth is not to be offered on the altar of preserving the status quo throughout the world, what should we prepare for?
7. Should atomic missiles etc. be substituted for American troops in Western Europe?
8. Precisely what areas of the world are essential to the national defense?
9. Do we propose to fight to preserve the independence of every nation in the world, in effect to act as the world policeman?
10. Under present conditions, and possibly with changed emphasis on defense plans, should a professional career defense establishment be substituted in large part for the drafted forces and reserves now in being and in prospect?

These questions are intended to be representative rather than all-inclusive. Moreover, they are *not* rhetorical questions implying that we already know all the answers to them. The report and recommendations of such a Commission could greatly aid in clarifying issues now too much obscured by political controversy and could aid the citizens in deciding policy issues of immediate pressing importance.

The proposed National Advisory Commission for Inquiry into the Problems of Men in Society would be a quite different agency in the following respects.

1. It would be nongovernmental, nonpolitical, and nonrepresentative of any particular segments of the United States. All of its members would be scientists fully qualified in the application of modern scientific method in the behavioral sciences.

2. The costs of this Commission would be met by the Institute and through the donations of large numbers of individuals possibly supplemented by large donations through certain colleges who would cooperate in administering such funds. The aim would be to make the Commission as nearly as possible independent of all ties to vested interests or particular segments of the Nation.

3. The members of this Commission would themselves be qualified to make and direct inquiries into specific problems. Of course, they also would be qualified to choose technical assistants as needed from time to time.

4. Because application of modern scientific method in the behavioral fields is in its early stages, this Commission necessarily would be small in number at first but would be expanded as highly qualified individuals became available.

5. This Commission would *not* be responsible for recommending legislation nor would it function in any other way than as its name implies, that is, as a source of advice for the citizens on the problems of men in society. To the extent that the time of Commission members and available funds permitted, the Commission would critically analyze proposed solutions to problems, would indicate which proposed solutions, if any, were scientifically sound, and would conduct continuing inquiries in order to develop scientifically warranted assertions or answers to the problems of men.

Until recent decades making such a Commission permanent might well have insured its ultimate uselessness. However, one of the most significant of recent developments in modern scientific method has been the realization by qualified scientists that useful answers rather than absolutely certain, incontrovertible, and everlastingly true answers are the fruits to be expected. In short, modern scientists now leave open the door for improvement, correction, even eventual overthrow of findings that may, for the time being, be useful.

Man's quest for certainty was carried on for many centuries, and even as recent and as distinguished a scientist as Einstein found abandonment of that quest difficult. But by abandoning the notion that theirs is and will be the last word, more modern scientists have provided for the self-correction in the longer run that seems to be essential in view of man's still limited and still improving ability in conducting inquiries. In the absence of this self-correctional feature of modern scientific method, we should be reluctant to suggest that any commission of inquiry be permanent.