

FIRST PRINCIPLES IN MORALITY AND ECONOMICS

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

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Russian Interest In American Unemployment

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

. . . the traveler is left with raw particulars in his notebook of things said and asked, overheard or noticed about some Russian people.

Here are some excerpts from that notebook: . . .

After citing various matters Frankel goes on:

The unemployed. Always the unemployed. [Frankel is referring to the Russian ideas about American unemployment.] It is a horror ever present in the minds and literature of the Soviet Union.

Why can't you plan to have jobs for all? Why don't you do something? What do the unemployed do? Who helps them? Do they lose goods bought on credit?

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

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

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

An Explanation Of Preference For Security Over Freedom

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

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

Circumstances

Making Labor Immobile

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

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

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

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

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

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

The Cause of the Business Cycle Is Practically Unknown

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

No man is presently immune to the business cycle. Rich and poor, wise and foolish, the strong and the weak, employer and employe, the big business man and the little business man, manufacturers and retailers, doctors and lawyers — everybody, in fact, is afflicted by this economic instability.

What *causes* this economic instability? All kinds of answers are given. Some say underconsumption; others, overproduction; others, too low wages; others, too little money; the explanations are endless. Some are amusing as that of the newspaper man who declared that the business cycle is caused by "too many people having automobiles." (To what absurdities is the human mind subject!)

The number of those who know the *real* explanation of the business cycle is apparently small. And there appear to be still fewer who are prepared to go to the heart of the problem and correct it; they seem to be so few in number that it is reasonable to be pessimistic.

Let us consider a graduate engineer, excellently educated, in physics, electricity, and electronics; (or take any phase of engineering that you wish). After getting, say, a Ph. D. degree in engineering and going to work for some engineering company, and working there on some specialty — what, indeed, will he probably know about the *cause* of booms and depressions? He has probably never systematically endeavored to analyze the problem. He will probably know as much as he reads in the daily papers or in the magazines which predigest news and manufacture interpretations and subtly induce attitudes. Here is an intelligent man, of good character and a responsible citizen, but quite helpless in regard to his own security in the business cycle. Nor is his position unique; his employer is probably equally helpless, unless he is a business man very much out of the ordinary.

And so the terror which men have of economic instability — booms and *depressions* — is easily understandable, and even ex-

cusable because it is a terror of what is not understood. Of course, men then turn toward something which they think will give them security, and any demagogue who promises security finds the average man an eager listener.

The socialists build their appeal essentially on two emotions — covetousness and *fear*. They say (falsely in theory, but truly in fact) that capitalism has a systematic insecurity — regular booms and depressions — which will eventually destroy capitalism. They are right; as presently mal-organized, capitalism has a built-in feature which causes booms and depressions. What capitalism needs to do is to turn from its present evil practice, and purge itself of the cause of booms and depressions.

Unsound Credit Laws and Policies Cause the Business Cycle

The *cause* of booms and depressions is associated with questions of money and credit. The laws of money and credit, in the United States and in other capitalist countries in varying degrees, are inadequate, or evil, whichever word you prefer. Those laws conflict with the moral law. They authorize theft and fraud. Unless and until the law is changed preventing that, booms and depressions will continue in one form or another.

The problem of the business cycle is in a sense simple, but also complex. It is simple in that it is related to theft and fraud; everybody can understand that and ought to be against those evils. But the actual *form* in which such theft and fraud takes place is genuinely complex — practically hidden from ordinary observation.

In these issues of FIRST PRINCIPLES we are endeavoring to make clear the explanation of the business cycle, but not in a formal, textbook manner, because we are writing for nontechnical people. Nor have we organized the material in a systematic manner. To present the explanation in that manner would discourage many readers.

But our efforts will need to be judged charitably and patiently, because the subject is so complex that it is not explainable in a paragraph or two. What is here endeavored is to work through the most difficult subject in economics — money and credit — so that readers will be disposed to use their influence to end booms and depressions — by removing the cause, now imbedded in our Constitution and laws. Further, knowing that all people have

a propensity to appeal to morality, we do the same and condemn that cause, in old-fashioned language, as a grievous sin.

In the meanwhile, instead of berating others for wanting security instead of freedom, we are disposed to endeavor to remove the greatest cause of the insecurity, especially because that cause is too great and overwhelming for the average man to cope with.

Attempts to escape this insecurity by *evasion* rather than *correction* will not be a suitable solution, because the mass attempt at evasion would nullify the effort. Some of us may escape the penalties of booms and depressions, because we are in a singularly fortunate position. We may be gaining at the expense of others; their poison may be our meat, but what is needed is a *fundamental removal of the cause for mass economic insecurity*. Current issues of FIRST PRINCIPLES will continue to struggle with the problem of making that clear.

* * *

If a boy plays a game and the rules are fair to him he will be willing to take a chance on the insecurity of winning. But if the rules are not fair for him, but maybe only for a few initiates, he will seek special security. He will not want freedom but protection. It does not sound unreasonable to us that under such circumstances he demands it. The average employer, employe, professional man, farmer, retailer — the average citizen — is like a boy in a game where the rules are against him.

Freedom is wanted only when there is a sporting chance of profiting from it.

John Law, the Scottish Laird of Lauriston

One of the most fascinating figures in monetary, fiscal and economic history is John Law. All that most people know about him, if they know anything, is that he created a great boom in France in 1716-1719 — for three short years — accompanied however by extreme inflation; and that the boom ended in a terrific collapse, notorious under the name of Mississippi Scheme or Mississippi Bubble. Law was figuratively a financial skyrocket, soaring and exciting on the rise, but coming down quickly as a scorched stick. The whole operation took less than four years.

John Law (1671-1729), Laird of Lauriston in Scotland, is variously described — as a great financier and economist, but also

as a gambler, seducer, duelist, speculator and adventurer. His father was a goldsmith in Edinburgh of Jewish extraction. His mother was of the noble Scottish house of Argyle.

When seventeen years old he went to London and lived a life of pleasure and extravagance for nine years. He had a love affair with Elizabeth Villiers, alleged mistress of royalty, and wife of Edward (Beau) Wilson. Law killed Wilson in a duel by shooting him; was sentenced to death; but the sentence was commuted to imprisonment; he fled prison and escaped to Amsterdam, where he studied questions of money and banking.

When 34 years old he returned to Scotland and promoted a scheme for a national bank, which would put out *paper* money (notes) secured by the value of state lands. The Scottish parliament rejected the scheme — *wisely*.

Law then set off on his wanderings; his wife said she was married to the "wandering Jew." He made his living as a gambler. He possessed rare mathematical ability and by computing odds at cards and other games of chance made a good living for himself. He made small progress however at selling his idea of *paper money*, until after the death of Louis XIV of France, the regent, the Duke of Orleans, listened to Law and in 1716, when Law was 45 years old, permitted him to establish the *Banque generale* in France, with a capital of 6,000,000 livres (consisting of 1,200 shares of 5,000 livres each), one-fourth cash and the rest payable over three years in *billets d'etat*. This bank was authorized to issue notes, payable at sight in the weight and value of the money mentioned on the day of issue. On April 10, 1717 the regent decreed that notes of the *Banque generale* would be received in payment of taxes. The operation of the bank had become so "successful" that the rate of interest fell to $4\frac{1}{2}\%$! But — and this is illuminating, important and premonitory — *the note issue was increased to 60,000,000 livres*, that is, ten times the original capital of the bank! (The *livre* was worth about twenty cents.)

Let us follow the further steps in Law's career, before describing his policies in economic terms. In 1717 he founded the *Compagnie de la Louisiane ou d'Occident*, in the process absorbing two older companies. Law's company had extensive authority to develop the whole valley drained by the Mississippi, Ohio and Missouri rivers. In 1718 his company acquired a valuable monop-

oly. Success however stimulated competition, and there was some drop in the shares of Law's company. Nevertheless Law's star continued in the ascendant.

Toward the end of 1718 the name of the bank was changed from *Banque generale* to *Banque royale*; the notes of the latter were guaranteed by the king (through his regent, Law's patron).

In 1719 the *Compagnie d'Orient* absorbed the *Compagnie des Indes Orientales et de la Chine* and the merged company was designated the *Compagnie des Indes*. Despite Law's high-powered promotion and despite his overly optimistic expectations, the colonial companies did not expand quickly nor become profitable; (there was not enough time for that, before Law's financial policies were sure to catch up with him).

Law's *Banque royale* obtained the management of the mint and coin issue for nine years; the farming of the national revenues; and it undertook the liquidation of the elephantine national debt of France largely created in the extravagant and warring days of the late Louis XIV.

In the meanwhile this bank, which had begun in 1716 with only one-fourth of its capital of 6 million livres paid in cash, by this time was rapidly approaching a peak in its note issue of 3 billion livres! (The amount of coined metallic money amounted to only 700 million livres.)

In October 1719, the shares of the bank went to 40 times the original value. But the actual climax to the financial orgy came in 1720 when the *Compagnie des Indes* and the *Bank royale* merged.

The smart people, however, for some time already had been observing the hand-writing on the wall. In the preceding fall (1719) shrewd speculators began to sell out their investments in paper securities of any kind, and to replace them with gold, silver, diamonds, lands and *real* property. Eventually, everybody tried feverishly to get rid of *paper* and to own instead *goods*. Tallow, soap and other necessities rose to fantastic prices. A piece of soap, after all, was a real good, and was worth more than a printed piece of paper. It should have been obvious from the beginning that the public would *eventually* lose confidence in the whole scheme; the only question was *when*.

Law was a man of courage and resource as well as being brilliant (although basically completely unsound). Of course, Gresham's Law, that bad money would drive out good money, was certain to operate. According to that economic law, Law's bad notes would drive out as money good gold and silver; and that is what happened. Drastic measures were taken to endeavor to check the drain of coin out of the country.

On May 21, 1720 a decree was issued by which the value of Law's bank notes was to be reduced gradually to one-half their face value. This action naturally precipitated a panic, which took the form of frantic efforts to get rid of paper bank notes. Law tried to restore confidence by paying out metal as long as he could, but of course the bank could not pay out metal for all the notes for billions of livres which had been issued, and so the bank suspended payments, went broke — in a week.

Law was removed from his position. His system was destroyed by those who had opposed him and seen it operate destructively. In December 1720 Law secretly left France, returned a while to England, resumed his wandering and eight years later in 1729, at the age of 58, died in Venice in *straightened circumstances*. The burnt stick of the skyrocket had come down!

Law himself seems to have believed sincerely in his scheme to the day of his death. He attributed its failure in France (1) not to the basic unsoundness of his economics, (2) nor to the immorality of his monetary ethics, but (3) entirely to the enmity of others and the panic and lack of confidence of the public. Surely, he was a dazzling man of action — a profligate, seducer, duelist, monetary student, banker, politician, the man who created the greatest one-man inflation-boom and crash in history, and a talented economic theoretician and author. Despite all his brilliance, courage and force nevertheless a bedraggled failure in the end.

Those who wish to learn more of John Law might first read, especially if they want entertainment, Raphael Sabatini's *The Gamester* (Houghton Mifflin Company, Boston, 1949). Anything written by Sabatini is enthralling and brilliant, and not too bad history (but, of course, not *history*). The important English biography of Law is by A. W. Wiston-Glynn, *John Law of Lauriston* (1907). Law himself wrote more than one book; the best known

carries the title, *Money and Trade Considered, with a Proposal for Supplying the Nation with Money* (1st edition, 1705; republished in Somers' *Tracts*, 1809).

The reputation of Law has fared amazingly well in the appraisal by historians and economists. The reason is not easy to find; maybe the explanation is the fact that *inflation* is so extremely seductive and adorable as a proposed solution to economic problems, similar to a beautiful woman with excessive muliebrity.

Schumpeter in his *History of Economic Analysis* (Oxford University Press, 1954) page 295f. writes of Law as being in "a class by himself." Schumpeter wrote:

He worked out the economics of his projects with a brilliance and, yes, profundity, which places him in the front rank of monetary theorists of all times. And this is all that matters for us. Since it is plain, however, that his analysis has been condemned, for about two centuries, primarily on the strength of the failure of his *Banque Royale*, it is pertinent to point out, first, that its predecessor, the *Banque Générale*, founded 1716, was a perfectly orthodox bank that was to issue notes and to receive deposits payable on demand and to discount commercial paper — no antimetallism about that — and that the *Banque Royale* and the *Compagnie des Indes*, which it absorbed, failed because the colonial ventures combined in the latter did not, for the time being, prove to be the source of anything but losses. If these ventures had been successful, Law's grandiose attempt to control and to reform the economic life of a great nation from the financial angle — for this is what his plan eventually amounted to — would have looked very different to his contemporaries and to historians. Even as it was, that gigantic enterprise was not simply a swindle and it may well be doubted whether France was the worse for it, on balance. However, economists not only fell in with the popular opinion that the scheme was nothing but swindle but also pointed to certain technical defects in it that were in fact important subsidiary causes of its failure. Thus that event acquired considerable influence on the evolution of what eventually became the classic theory of banking. . . .

One of his plans was concerned with a land bank that was to issue legal tender paper money up to a certain proportion of the value of land and to receive as deposits for *placement* money that would otherwise lie idle, so that money would never be either too cheap or too dear. In this he followed the English land-bank projectors . . .

Later in his book, Schumpeter (page 321f.) designates John Law as the "ancestor of the idea of a *managed currency*" (our italics). Schumpeter is probably correct about that, and it is probably equally correct to add that a *managed currency* is the very essence of present-day (1959) monetary theory; and so Law's

ideas are the prevailing ideas in the banking world today! Schumpeter wrote:

(b) *John Law: Ancestor of the Idea of a Managed Currency.* Manufacture of money! Credit as a creator of money! Manifestly, this opens up other than theoretical vistas. The bank projectors of the seventeenth century, especially the English land-bank projectors and Law, . . . fully realized the business potentialities of the discovery that money—and hence capital in the monetary sense of the term—can be manufactured or created. Their reputation, at the time and later, suffered greatly from the failure of their schemes—Law's schemes in particular—just as, in the nineteenth century, the reputation of fundamentally similar ideas suffered from association with wild-cat banking and with the failures of schemes that turned out badly without being fraudulent or nonsensical, such as the *Crédit Mobilier* of the brothers Pereire. But since there is a far cry from an economic principle to a banking project, these failures are not evidence in the court of theory.

The idea of Schumpeter that it was a great "discovery" (rather than a great hallucination) "that money—and hence capital in the monetary sense of the term—can be manufactured or created" is a shocking economic fallacy.

Schumpeter goes on to explain that there is *some* evidence that Law was a "metallist," a hard-money man. However, the evidence is really wholly inconclusive; the *fact* is that Law was just the opposite.

What has especially intrigued later economists is Law's excellent analysis of how certain metals (gold and silver), used for money, acquire their *value*. Obviously these metals have value for industrial uses. The question is: what is the effect on the value of gold that it is also in demand *as money*. All subsequent economists are indebted to Law for that analysis. Law wrote: "Money is not the value for which goods are exchanged, but the value by which they are exchanged. This makes clear that Law did not consider *gold* to be a good monetary unit and a good hedge against inflation, *just because it had value as a commodity in the industrial arts*; contrarily, Law realized that the value of gold depended on its monetary use as well. On this he was entirely and lucidly correct.

But then Law jumps to his fallacious and fatal conclusion, namely, that in order to insure an *adequate money supply* the quantity of money *should be managed*.

Schumpeter describes Law as the "genuine ancestor" of the

managed currency idea, which came into vogue (as if it were new!) in 1919. Schumpeter considers Law's original *Banque generale* "almost orthodox"; Law's *Compagnie des Indes* "more visionary"; and Law's last measures in 1720 during the crash as the "ultimate resort of a strong swimmer in his agony," but Schumpeter appraises it all as a "great plan" for "controlling, reforming and leading on to new levels the whole of the national economy of France." Schumpeter considers that idea of comprehensive management of an economy as the feature that "glorifies" Law's main treatise on money. It is this very principle of a *managed currency* which is the worst cancer in present-day capitalism.

Others beside Schumpeter are sympathetic to Law's *managed currency* ideas, but despite all the sympathetic acceptance of it a managed currency means uncontrollable inflationism — that is, uncontrollable whether or not the would-be actual managers think they have control of it. The adjective, *managed*, in the term, managed currency, implies or assumes that some demi-god bureaucrat can *manage* or *control* a monetary system, but all history proves that such men have never existed. The monetary system must be "unmanaged" by *individual* men; if it is to be safe and sound it must instead be *managed* by economic law in order to be reliable and conducive to prosperity.

The *Encyclopedia Britannica* article on Law ends with the somewhat contradictory statement: "Though subject to the errors of his time, *he was undoubtedly a financial genius*" (our italics). Collier's *Encyclopedia* ends with the still more erroneous statement: "The credit basis of Law's schemes was sound, but they could not justify the public belief that they would produce untold wealth." This statement should read: "The credit basis of Law's scheme was *wholly unsound* . . ." It was not the belief of the public that Law's scheme would "produce untold wealth" that caused the eventual catastrophe.

The *Encyclopedia of the Social Sciences* does no better. Its article on John Law contains the following:

. . . "commerce depends on specie" which consists of precious metals. As these are rare, Law conceived the scheme of substituting for metallic currency paper money, which can be created at will and more easily transported, the cost of which is insignificant and the circulation much freer."

* * *

As the value of money does not result from its intrinsic

nature but from the uses to which it is put, the public would become use to it and accept no other. Then the bank could extend its activities and e.g., redeem the public debt by profitable commercial operation . . .

* * *

The combined bank and company failed owing to paper issues far beyond the necessary security, for which the regent [the Duke of Orleans] appears to have been mainly responsible.

There is also mention in this encyclopedia of lack of confidence engendered by "overexpansion" of the combined activities (of banking and colonial development) and of too much haste.

* * *

In the two preceding issues we gave information on a Canadian lady whose solution of the problem of prosperity in Canada consisted in the simple formula — *more money* — obtained through more credit extension. Basically her idea was identical with John Law's. To this question on how to increase prosperity either of two answers might be given: (1) more production; (2) more money. The Canadian lady and John Law are among those who have held or hold that more money creates more prosperity!

* * *

We have now mentioned three men as representing three different schools of thought on the question of money and about the influence of changes of the quantity of money on prosperity. These men are John Law, a brilliant financial adventurer and monetary theorist; Henry Thornton, devout evangelical and conservative banker; and Ludwig von Mises, the greatest living economist. Law essentially was a man who would *increase* the amount of money; Thornton was a man who would tolerate *variation* in the amount of money by voluntary action of men; Mises is a man who would neither increase nor vary the quantity of money by any action of an individual who considered himself called upon and competent to "manage" the currency supply. Law would *manage* money; Thornton would have the quantity of money *respond* to trade variation; Mises believes neither in *managing* money nor *responding* to changing business conditions, but instead making the quantity of money subject to *economic law* only. All this should become clearer later in this issue and in future issues.

On this money question, as generally in regard to his economics, we adopt the views of Mises. All logic is on his side; and also the moral teachings of the Hebrew-Christian Scriptures.

To Adjust To Economic Reality There Are Two Alternatives, The First Immoral And The Second Moral, Namely, (1) Varying The Quantity Of Money, Or (2) Varying The Prices Of Goods

There is a choice between good and evil in economics as definite as the choice of Adam in the Garden of Eden when he decided whether or not to eat the fruit of the forbidden tree.

That choice concerns the question whether economic objectives of all kinds — matching supply and demand, expanding one industry and contracting another, full employment, hope of prosperity — are to be made by varying the quantity of money, or by adjusting prices. The former, when thoroughly understood, is as definitely unsound as anything can be. The choice then becomes a choice between good and evil.

In the explanations which follow we shall compare and contrast three answers: (1) the answers of men who wish to create or *increase* the quantity of money; (2) the answers of men who wish to *vary* the quantity of money; and (3) the answers of men who do not wish to create money. To make the analyses more interesting we shall use individual men as prototypes of these three programs: *John Law* as a prototype of the money creators; *Henry Thornton* as a type of the money variators; and *Ludwig von Mises* as a type of the men who *seek neither to create nor vary the quantity of money, by fiat action of men (the state)*.

In *private* morality all men of honor are with Mises; they are all against counterfeiting. But in *public* morality nearly all men of honor (so-called) are with Henry Thornton, at a minimum; and basically they are often with John Law; the Thornton men are the men who favor the present *variable* credit policy of the United States Federal Reserve Board. The John Law men are all those who talk about reducing gold reserve requirements of Banks, or changing the gold content of the dollar, etc. In FIRST PRINCIPLES we follow Mises — on questions of both private and public morality. We are against the creation of money — always. It is the path to ruin.

Let us tie in what will be presented in this issue with what was published last month. In that issue attention was called to a peculiar and paradoxical cause for there being a shortage of money,

namely, fear that the quantity of money will be increased. The mechanism by which this fear of an increase in the quantity of money creates a shortage is as follows: sellers have anxiety that the prospective increase in the quantity of money will result in a rise in prices of goods before they themselves will be prepared to buy again. Their imagination then goes to work and they try to advance prices even faster than the feared increase in the quantity of money actually occurs. And so there is a "shortage of money." Taking into account such increases in prices there is not enough money to result in all goods and services finding buyers, and so some of these go a-begging, i.e., because of a "money shortage." Obviously, a "money shortage" in this case is caused not by the insufficiency of the actual money supply but by the *expected* increase in the supply, which reflects itself in the too-aggressive pricing policies of sellers.

From the foregoing, an important conclusion can be reached. It is this: *a money shortage is unthinkable, except in relation to pricing goods and services.* If there is a shortage of money, that can be corrected in two ways: (1) increasing the quantity; or (2) lowering prices.

Let us say that there is available \$100,000 in money, and that there is a quantity of various kinds of goods and services all properly priced to total \$100,000. (Let us assume a turnover of goods of one.) The goods should then all be "turned over," that is, sold, and money and goods are "in balance" because prices are right. There is no shortage of money.

Let us next say that there is a change in the situation with sellers increasing prices to a total amount to \$120,000, but that the quantity of money remains the same at \$100,000. There is now a "money shortage." Some goods — \$20,000 worth — will not be sold. The money quantity has not decreased, and so it is really incorrect to say that there is a money shortage. The real cause of the imbalance is that prices were increased unduly. Still, in popular usage, this situation may be described as a money shortage.

Next, let us say that there is no change in either prices or the quantity of money. Both are constant. But let us vary the physical quantity of goods. Let us say that the physical quantity is increased 20%. The 20% larger quantity at the old price means

that \$120,000 is needed to move the whole quantity. But the money amounts to only \$100,000. Again there appears to be a money shortage. But what ought the correction to be? The price of the individual units should be reduced enough so that the \$100,000 would suffice to move the whole quantity.

Let us continue our variations in circumstances. Let us next assume there was an inescapable and unfortunate reduction in physical production. There is now only \$80,000 worth of goods. But the money supply is \$100,000. At the old prices, \$20,000 of the money supply will not be used. Do we then have too much money? Or should prices be increased so that they aggregate \$100,000. Anyone taking that view — which is the correct one — espouses the proposition that prices should be increased whenever there is a disturbance between the relation of the supply of goods and the supply of money, with the disturbance being caused by the supply of goods. The alternative is to reduce the supply of money in some manner — maybe arbitrarily — to \$80,000. There might be an assessment by which 20% of the money supply was called into a central depot and destroyed. But this is never proposed, nor is it sound.

There is, it will be clear, a choice open to all who are concerned about the *money supply*. They can “solve” the problem in either of two ways: (1) change the money supply; or (2) let prices be flexible, that is, not permit anyone to use coercion of *any kind* to decrease or increase prices.

If prices for everything — goods and services without exception — were genuinely flexible, then for all practical purposes *there would never be a money shortage*. All “money shortages” are really caused by prices not being flexible and/or right.

A fantastic fear — a phobia — has developed among men. That fear consists of anxiety and alarm about price *reductions*, particularly reductions in the price of labor, but also of commodities as, for example, of farm products. It is a fear besetting nearly everyone.

And so men come to the alternative solution: instead of flexible prices — instead of relying on the “market” and being prepared to abide by it — men turn to *varying the quantity of money*. This varying of the quantity of money was at one time considered

to be a problem of increasing *and decreasing* the quantity of money, that is, it was a question of *varying* the quantity of money rather than *increasing* it. But the inveterate tendency is to change that to *increasing only*. The former opened the door to the latter. Once it was agreed that the solution was not *variable prices* but *variable quantities of money*, a fatal principle was adopted. What psychology, economics and morality all taught consistently was thereby abandoned.

Now, it is not socialism that perpetrated this abandonment of wisdom and morality in regard to the question of keeping money and goods in balance, but men who were "capitalists" in every popular meaning of the term.

In the early years of the nineteenth century there were two "schools of thought" regarding varying the quantity of money — one the *Banking School* and the other the *Currency School*. Of these two the *Currency School* was by far the more right, but in principle it was not wholly right either. Both schools of thought were thinking in terms of varying the quantity of money rather than relying fully on varying prices.

Great errors and great sins are not perpetrated heinously by "good" men. When they finally end up in an immoral morass and in practical ruin, they got there by small steps, all designed for "good purposes." From step to step they went the downward path, not realizing to where it would lead.

External dangers may or may not destroy capitalism, but an internal danger gravely threatens it. Unless capitalism reforms — relies solely on flexible prices and abandons the idea of a flexible quantity of money — it will be destroyed.

Matters Of Money Need Not Be Identified With Mammonism

The dictionary defines *Mammonism* as "devotion to the acquisition of wealth; worldliness." The term comes from the name of the Syrian god of riches.

This would be a sorry world if everything pertaining to money would be described as mammonism.

Money (as a tool for facilitating exchange) is one of the greatest blessings men have ever obtained. Where is there a society, and where are there men, who wish to have a moneyless society?

A moneyless society would mean that men could exchange — that is, *cooperate* — only by barter. When business cannot be transacted except as barter, society will be grievously impoverished.

Mammonism really refers to avarice for riches; (we are not here defining avarice.) Money may be a symbol for avarice. But such a metaphorical use of the word *money* in connection with avarice should blind no one to the great utility of money as a *means of exchange*. In this last sense money is an unmixed good.

Some of the interpretations of statements in the Hebrew-Christian scriptures about serving God or Mammon are unrealistic. Such interpretations are usually studies in *motivations*, that is, potential forms of avarice, which are not being discussed here; instead attention is being directed to money as a *means* to an end: to wit, as a tool for facilitating exchange. The question here is whether money *as a tool* can be grossly misused, as well as avarice can be a perversion of the proper, admirable desire for good and fine things. Unfortunately, in the arrangements for using money as a tool for the good end of exchanging goods, as great evils have crept in as avarice is an evil in itself.

Although money as a tool can be wonderful, its fine function can be abused. It is that phase of money that we are considering. Obviously, this has nothing to do with Mammonism, in the sense of avarice.

The Demand For Money, In Economic Science

The *demand for money* is a term that can have many meanings.

It may mean, for example, that we all have desires greater than our means in terms of money; we want more money in order to get more goods than we have; in other words we have some need, wish or covetousness which exceeds our means. We are not using the term *demand for money* in that popular and dubious (maybe covetous) sense. Instead we refer to *demand for money* in the framework of the science of economics.

In economics, the term *demand for money* means quite the opposite of the popular sense just described. In the popular sense, the demand for money is demand for money *to spend*. In economics, the demand for money is money *to hold*. Everybody who has foresight and judgment has a demand for money (*as money*, or

qua money), to have as a reserve against emergencies and future needs.

If Percy is a clerk for a company and receives his pay every two weeks he has a demand for money, at a minimum, which consists of enough to pay his expenses for surviving for 14 days. If it costs him \$8.00 a day to live, then his demand for money on payday is 14 days x \$8, or \$112; on the next day, 13 days x \$8, or \$104; and so on down to 1 day x \$8, or \$8. Percy's demand for money, then, varies depending on his circumstances; or his estimation of his circumstances; his minimum demand appears to be for the various days in a two-week period, \$112, \$104, \$96, \$88, \$80, \$72, \$64, \$56, \$48, \$40, \$32, \$24, \$16 and \$8, an average of \$60. But the average is meaningless. The demand varies acutely from day to day, and Percy is operating financially in a hazardous manner. He has no reserve whatever on the last day if his employer fails to pay him on payday, or if Percy is sick on that day and cannot get his paycheck. Most people will want more money on hand than merely to squeak by, with just enough to pay the last meal before the next check is received. Percy may, if he is of a more prudent type, have a demand for \$200 as a general reserve plus the daily variations between paydays. Just after receiving his pay his demand for money will then be \$112 plus \$200, or \$312; it will go down by \$8 a day so that just before the next payday he will have a demand for money of \$8 plus \$200, or \$208.

Everybody's demand for money *varies*. If someone has so much that he hardly ever calculates whether he needs more or less, then the situation is not correctly described by saying his demand for money is invariable, but by saying that (for some reason or other) he has such a large demand for money *relative to his actual needs*, that it *seems* his demand does not vary.

In an economic sense, the *demand for money* is the amount a man estimates he needs as money against his requirements, before more money becomes available to him. It is the *store* of money, in one form or another, that people need or at least want, to take care of their known needs and emergencies.

The demand for money will vary not merely according to needs, but also according to temperament. A thrifty, provident man seeing potential dangers of all kinds, will have a bigger demand for money than a careless, optimistic man.

Finally, the same person will not have the same demand for money according to a predictable pattern. If something suddenly scares him, his demand for money will immediately increase — as a protection to himself. If he becomes buoyant in enthusiasm and expects money soon to come rolling in, he will reduce his current demand for money proportionately; why have “idle” money, when it will soon be coming in faster than needed.

The variation in the demand by men for money will have an effect on the business cycle. Suppose everybody becomes optimistic because money seems plentiful, because the banks are liberal in creating new credits — creating fiat credit (see April issue, page 119ff. for the significance of fiat credit). The demand for money *in the economic sense* (i.e., demand for money as a reserve to hold) will then decrease. What does that mean? People will prefer goods and services to money; they will bid for goods and services; prices will go up. But now assume that bankers become apprehensive about the soundness of an economic situation. Instead of putting out more fiat credit they demand payment on the old credit. The psychology of businessmen will then change. Men will try to accumulate money — that is, their demand for money will increase — but the only way that they can accomplish that is by selling more and buying less. For everybody, or at least most people, to try to do that, means that prices of goods will go down. How could it be otherwise when nearly everybody wishes to sell and few wish to buy. Then confidence is disturbed further. More and more people increase their demand for money (in an economic sense). Prices tumble. People become unemployed. We have a depression.

In regard to this demand for money we shall quote Henry Thornton, the great banker, the Christian leader, and monetary theorist, whom we described in the preceding issue. Thornton says the same thing that we have just said. But before quoting Thornton it is desirable to make a few explanatory remarks so that what is quoted will be more readily understandable. Thornton wrote a book which is famous in economic history, entitled, *An Enquiry into the Nature and Effects of the Paper Credit of Great Britain*, originally published in 1802, and republished in 1939 by Rinehart and Company, Inc., New York, with an introduction by Prof. Friedrich A. von Hayek. Thornton begins his book by describing

Commercial Credit, Bills of Exchange, Real Bills and Fictitious Bills, Notes of private banks, and Notes of the Bank of England. He explains which of these kinds of money people will be willing to retain, according to their *demand for money* under various circumstances. Readers of the quotation should keep the general thought in mind which we are discussing, namely, that the demand for money (money to hold as a reserve) increases in times of anxiety, and decreases in times of optimism. The additional point that Thornton makes, to wit, that people will prefer safer money for their fund of money than less-safe money will be obvious to all. And, of course, it will be readily imagined by readers who have not read all that Thornton explains prior to what we are quoting, that the promissory notes of an ordinary merchant may be less acceptable as money, in bad times, than the promissory notes of a big private bank; and that the notes of a big private bank may not be so acceptable as a promissory note from the Bank of England. All this will be considered later, because of its fundamental importance, but at this time we are quoting Thornton only in order to emphasize how public psychology will affect the size of the *demand for money*. We quote from Thornton's book, pages 96 to 98. (The italics have been added.)

Now a high state of confidence contributes to make men provide less amply against contingencies. *At such a time, they trust, that if the demand upon them for a payment, which is now doubtful and contingent, should actually be made, they shall be able to provide for it at the moment; and they are loth to be at the expence of selling an article, or of getting a bill discounted, in order to make the provision much before the period at which it shall be wanted. When, on the contrary, a season of distrust arises, prudence suggests, that the loss of interest arising from a detention of notes for a few additional days should not be regarded.*

It is well known that guineas are hoarded, in times of alarm, on this principle. Notes, it is true, are not hoarded to the same extent; partly because notes are not supposed equally likely, in the event of any general confusion, to find [that is, retain] their value, and partly because the class of persons who are the holders of notes is less subject to weak and extravagant alarms. In difficult times, however, the disposition to hoard, or rather to be largely provided with Bank of England notes, will, perhaps, prevail in no inconsiderable degree.

This remark has been applied to Bank of England notes, because these are always in high credit; and it ought, perhaps, to be chiefly confined to these. They constitute the coin in which the great mercantile payments in London, which are payments on account of the whole country, are

effected. If, therefore, a difficulty in converting bills of exchange into notes is apprehended, the effect both on bankers, merchants, tradesmen, is somewhat the same as the effect of an apprehension entertained by the lower class of a difficulty in converting Bank of England notes or bankers' notes into guineas. The apprehension of the approaching difficulty makes men eager to do that to-day, which otherwise they would do to-morrow.

The truth of this observation, as applied to Bank of England notes, as well as the importance of attending to it, may be made manifest by adverting to the events of the year 1793, when, through the failure of many country banks, much general distrust took place. *The alarm, the first material one of the kind which had for a long time happened, was extremely great. It does not appear that the Bank of England notes, at that time in circulation, were fewer than usual. It is certain, however, that the existing number became, at the period of apprehension, insufficient for giving punctuality to the payments of the metropolis; and it is not to be doubted, that the insufficiency must have arisen, in some measure, from that slowness in the circulation of notes, naturally attending an alarm, which has been just described. Every one fearing lest he should not have his notes ready when the day of payment should come, would endeavour to provide himself with them somewhat beforehand. A few merchants, from a natural though hurtful timidity, would keep in their own hands some of those notes, which, in other times, they would have lodged with their bankers; and the effect would be, to cause the same quantity of bank paper to transact fewer payments, or in other words, to lessen the rapidity of the circulation of notes on the whole, and thus to increase the number of notes wanted. Probably, also, some Bank of England paper would be used as a substitute for country bank notes suppressed.*

In times of economic alarm the rate of circulation of money decreases. People wish to get hold of money earlier than otherwise; they want more for apprehended emergencies; they let go of money slower. The *demand for money* is then greater than normal. Then prices *must* fall. If they do not, unemployment *must* ensue. Depression will be here just as sure as the earth rotates, and the sun seems to rise and set.

The Worst — Most Dangerous — Clause In Any Of The Articles In The Constitution Of The United States

Paragraphs 5 and 6 of Section 8 of Article I of the Constitution give the following General Powers to the Congress of the United States:

5. *Money, weights and measures.* To coin Money, regulate the Value thereof, and of foreign Coin, and fix the Standard of Weights and Measures.

6. *Counterfeiting.* To provide for the Punishment of counterfeiting the Securities and current Coin of the United States.

The innocent-sounding clause in paragraph 5, which may be the underlying cause of the eventual disintegration of the United States, is the clause "to regulate the Value of Money."

In contrast, Section 10 of the same Article I of the Constitution restrains the individual states on an entirely different basis; Paragraph 1 of Section 10 reads (our italics):

No state shall enter into any Treaty, Alliance or Confederation; grant Letters of Marque and Reprisal; coin money; emit Bills of Credit; make any Thing but gold and silver Coin a Tender in Payment of Debts; pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts, or grant any Title of Nobility.

Undoubtedly the restriction is wise which prohibits the individual states from "coining money" or "emitting Bills of Credit;" or of making "any Thing but gold and silver Coin a Tender in Payment of Debts." To have "complexified" the money situation in The United States by permitting the *individual* states to coin money, emit bills of credit, or make anything except gold and silver legal tender in payment of debts has nothing to commend it.

The question is: were the states prohibited from doing those things for the narrow technical reason that they should not "complexify" monetary and credit matters; or were they prohibited from doing those things because one or all of them *are wrong in principle*; that is, should they not have those powers because no government of any kind, high or low, big or small, should have all those powers?

It is noteworthy that the individual states may specify that gold and silver coins are legal tender and may be used for paying debts. *Gold* and *silver coin* are here put in a different class from any other "legal tender" money. The implication is that there cannot be a legitimate objection to gold and silver coins as being legal tender, but that other "legal tender" may be or always is of a more-questionable character, and that therefore the states may not make anything but gold and silver coins legal tender. There is however no restriction of a similar kind on the Federal government: it can "coin money and regulate the value thereof" without *any* restraint whatever. The Federal government may print paper money as Congress wishes, according to its capricious pleasure.

Interestingly, too, the Federal government has decided that

gold coins are not to be legal tender in the United States; it has been decreed in fact that no individual may own gold for monetary purposes. Consequently, the right reserved to the states to make gold and silver coins legal tender is now utterly meaningless.

The clause authorizing Congress to regulate the value of money is almost unique in the Constitution, because there are no restrictions or limitations of any kind in this clause. The power is absolute.

The Constitution here adopts a dubious course—it states something positively rather than negatively—a procedure which has little to commend it.

There are other positive powers granted in the Constitution, such as, (in Article I, Section 8, paragraph 12) to “raise and support armies,” but immediately there is a limiting clause which reads, “but no Appropriation of Money to that Use shall be for a longer Term than two Years.” The power is therefore limited.

Or there is the power (Article I, Section 10, paragraph 2) which reads, “To borrow Money on the credit of the United States.” The power here appears absolute, but it is not; it is in fact limited by the “credit of the United States.” *Credit* in this case, cannot properly mean any credit other than *voluntary* credit, something which remains with the sovereign people.

Or there is the power (Article I, Section 10, paragraph 6) to “provide for the Punishment of counterfeiting the Securities and current Coin of the United States.” The power appears absolute and the authority to do so is in positive language, but the limiting factor is the existence of counterfeiting. If there is no counterfeiting the right to exercise the power to punish counterfeiting is academic and theoretical. In contrast, in a very peculiar fashion, the clause about “coining money and regulating the value thereof” is wide open. There is no limit.

The Constitution of the United States is the ultimate law of the land. No higher authority is acknowledged *in the courts*. But the authority granted by the Constitution of the United States is not the ultimate authority before the bar of human reason, or what is known as morality. There is an ultimate moral law, or a perfectly rational law—whatever it may be—which finally outranks any document such as the Constitution of the United States. Such an ultimate law may not be enforceable in courts, but it is

enforceable in reality. Men will eventually always find a way, motivated by legitimate self interest, to circumvent any law or any constitution which is contrary to "ultimate morality," which properly understood is "ultimate reason."

The Constitution of the United States is a marvelous document, maybe the greatest constitutional and legal document ever written by men. But it is not the ultimate law in the United States nor is any other Constitution the ultimate law in its territory. The ultimate "constitution" is the *constitution of constitutions*, to wit, the moral law, as expressed in the Decalogue of Moses. This short, simple document completely outclasses any other legislative document written at any time.

An outstanding characteristic of the Decalogue of Moses is that it is cast in a negative formulation: *Thou shalt not* is the customary style. All of the Ten Commandments are negative, from first to last: "Thou shalt have no other Gods before me" to "Thou shalt not covet."

The greatness of the Mosaic *Decalogue*, if correctly appreciated, lies exactly in its negative aspect as in the First Commandment just mentioned, Thou shalt not have any other gods before me. That could never have been effectively phrased affirmatively. Even if rephrased to read, Thou shalt have me only for thy God, the *only* would have been as negative as the formulation actually used by Moses. Similarly, all the negatives in the ethical part of the *Decalogue* — thou shalt not kill, commit adultery, steal, lie, or covet — have singular merit for two reasons: (1) they leave all else free, except what is specifically prohibited; and (2) there is the prohibition of specific evil-doing. The *Decalogue* therefore is a document legislating more freedom than any other code in the world, but it leaves no one with sovereign freedom to do evil (see Volume I of this publication, Nos. 2, 3, 4, and 5).

Now that which is wrong with Article I, Section 10, paragraph 5, clauses 2 and 3 is that they are positive and therefore in this case unlimited, rather than negative and consequently limited, because these clauses set no limit on controlling money, such money need not be gold or silver or any item of value, and any value that Congress wishes to be put on that money can be put on it.

The basic function of a constitution is to restrict the powers of government. The Constitution of the United States does *nothing* to restrict the absolute and arbitrary power of Congress in regard to money. *Our Constitution on this vital subject is defective.*

The consequence of that is that the sorriest aspect of the whole history of the United States is its monetary history, consisting of authorizing fraud and theft in abstruse money matters.

It might be expected that the *sovereign power* of this mighty nation could eliminate the consequences of these sins (despite the Biblical declaration, "Your sins will find you out") but that is a hallucination. The consequences have been there despite the Constitution and all that men can do, towit, depression on depression, and latterly (because of a new phase and a worse one) progressive inflation.

Until the right negative is added to Article I, Section 8, paragraph 5, clause 2 of the Constitution of the United States, the economic stability of this country is in jeopardy; further when there is no confidence in the economic stability of this country, citizens will constantly turn toward tyrannical arbitrary power as a protection against instability; men will seek security rather than freedom, because their basic laws are deficient and do not make freedom a reliable opportunity for all men. When freedom creates insecurity which ordinary men cannot master, they no longer want freedom. It is because there is a pervasive sense of economic insecurity *related to money regulated by Congress* that men in the United States no longer love freedom with enthusiasm.

Applying What Calhoun Wrote About Constitutions To The Specific Case Of Coining Money

In the January 1959 issue of *FIRST PRINCIPLES*, on pages 22ff., we quoted Calhoun's great treatise on government, entitled *A Disquisition on Government*. We shall repeat a fragment of that quotation.

Readers may remember that Calhoun's treatise has profoundly realistic premises, and that he with perspicuity appraised the true nature of man. From consideration of man as man, Calhoun turns to the nature of government, and from government he advances to the character of constitutions. Constitutions, he de-

clares, are primarily designed to protect citizens against their own government; it is that which is the purpose of constitutions. Calhoun wrote:

But government, although intended to protect and preserve society, has itself a strong tendency to disorder and abuse of its powers, as all experience and almost every page of history testify. The cause is to be found in the same constitution of our nature which makes government indispensable. The powers which it is necessary for government to possess in order to repress violence and preserve order cannot execute themselves. They must be administered by men in whom, like others, the individual are stronger than the social feelings. And hence the powers vested in them to prevent injustice and oppression on the part of others will, if left unguarded, be by them converted into instruments to oppress the rest of the community. That by which this is prevented, by whatever name called, is what is meant by *constitution*, in its most comprehensive sense, when applied to *government*. [Pp. 22f.]

These ideas of Calhoun can be applied to clauses one and two, of paragraph 5, Section 8, Article I of the Constitution of the United States. These clauses read: The Congress shall have power to "coin money [and] regulate the value thereof." But the glaring weakness of the United States Constitution consists exactly therein that *it does not even try* to restrain the government in any way in money matters!

We therefore, at this stage of the analysis, propose the following change in the Constitution:

The Congress shall have powers to coin metals into money of specified weight and fineness; or print paper money as a substitute for metal money, but such paper money shall only be for convenience and shall have full coverage in metal. Metal money only shall be legal tender. Congress shall not have the power to change the weights or fineness of coins in a manner which has the effect of altering the terms of settlements between creditors and debtors. If, because of changed circumstances in regard to metals suitable for use as money, it is desirable to change from one metal to another, then the change shall be made on the basis of the prevailing market relationship of the metals. Congress shall not endeavor to stabilize the value of any metal used as money, nor shall it undertake to make money plentiful. The supply of metal for money which is legal tender is to be left to the world supply and demand situation, for industrial and monetary uses, in that metal market.

Such an article in the Constitution on money will restrain Congress; and consequently protect the people, significantly, to wit, (1) only metal money would be legal tender; (2) the weight and fineness of legal tender coins would not be changed in a man-

ner which breach contracts; (3) paper money, for *convenience*, might be circulated, but would have metal behind it one hundred percent, so that, if there is a demand for metal coins for use as legal tender, they indubitably would be available; (4) the quantity of metal available for monetary uses would be determined by the demand for it at *prevailing market prices*, which in turn would have been set by the demand for *both* industrial and monetary uses; no arbitrary values would be set at the caprice of Congress; (5) no metal market price would be manipulated in order to affect the value of metal for monetary uses; and (6) there would be no power of Congress, at all, to *regulate* the value of money; the value of our money would rest on world supply and demand conditions.

Obviously, the foregoing proposal is metallist in character; and, considering the present money situation in the United States, it is idealistic; it proposes what cannot be accomplished at once, nor except by the use of temporary compromises. In a sense, it is a proposal to return to a gold standard. Doing that entails solving several and difficult problems. However, the proposal outlines a true gold standard, and one which will contribute to stable economic conditions, rather than one which has supplementary features which cause economic instability — the business cycle. This, therefore, is more than a mere return to the gold standard. It will not permit a continuation of planned variation, by monetary authorities, of the quantity of fiat money, something which the old gold standard permitted with disastrous consequences. There will be further discussion of the problem in future issues.

Tale Of A Coat

The following page shows a reprint from *The Freeman*. But we have added a panel of our own, at the bottom. We have labeled it COOPERATION, with the explanatory phrase, "according to Ricardo's Law of Association." Then, not being artists, and lacking design imagination, we have merely inserted the question: "What is this system?"

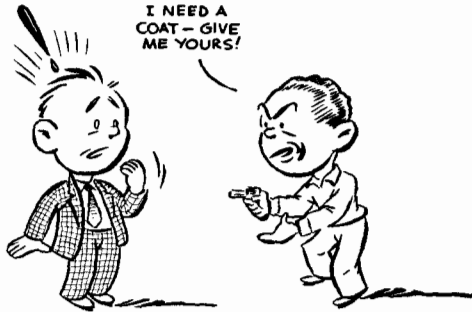
Our purpose in supplementing the admirable cartoon of *The Freeman* is to enlarge the message. The original message is negative; it needs something positive. The original shows three systems — *charity*, *robbery*, and the *welfare state*. The chart shows

Tale of a Coat

CHARITY



ROBBERY



The WELFARE STATE



Reprinted from *THE Freeman* May 1955

COOPERATION, according to Ricardo's Law of Association.

(What is this system?)

that charity is voluntary, and as such is distinguished from compulsory systems. The two compulsory systems are private coercion, labeled *robbery*; and public coercion, labeled *welfare state*. Clearly, coercion is an evil and is not to be preferred in collective form just because it has a deceiving name (*welfare*). Robbery is robbery whether individual or collective in origin, and whether a good name hides it or not.

Society cannot be organized properly on any of these bases — whether charity, or robbery by individuals, or robbery by a group.

Some additional organizing principle, this time a sound economic principle, is necessary. What is it?

It is *cooperation*. That is the principle on which human association is founded, although the fact may be obscured. That is the principle that needs a panel in the cartoon. Then the cartoon will be complete.

The mere word, *cooperation*, will mean nothing significant economically unless Ricardo's Law of Association (or you could call it as well, Ricardo's Law of Cooperation), is understood. What is this Law? The idea can be put this way:

Let us say *A* can produce products worth \$3 and *B* products worth \$4, a total of \$7. But by division of labor *A* can concentrate on what he can do best, and *B* on what he can do best. Men are *never* equal by endowments; each can develop special skills; natural resources make some things less costly to produce in specific locations; investment in special equipment makes one man more productive in one job than in another. What happens then under *division of labor*? We no longer have *A* and *B* aggregatively producing \$7 worth of products, but something involving a *seeming* multiplication, like $3 \times 4 = \$12$. That illustrates the "miraculous" character of *cooperation* in the Ricardian sense.

In an earlier issue we presented an example of how Ricardo's Law of Association works. We quote from the July 1958 issue, page 207ff., Volume IV, No. 7:

... we shall take a simple case; we shall imagine a primitive society consisting of two men and their families. Secondly, each man needs a shelter for his family. Thirdly, one of the men is bigger, stronger, wiser, *superior in everything* to the other one. The first man we shall call Mr. Strongman and the second Mr. Feebler.

... [We shall assume that both] men have the same size families and need the same space. They are both going to build simple shelters of the same size. All the material that they need is 2,000 logs (or boards) apiece and 9,000 nails.

We shall assume that both men have a hammer and the nails, but that the logs or boards must be cut and the nails pounded.

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

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

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

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

Table 1
Two Unequally Unequal Men Working Separately

2,000 logs at 100 an hour	= 20 hours
9,000 nails at 300 an hour	= 30 hours
Total for STRONGMAN	50 hours
2,000 logs at 25 an hour	= 80 hours
9,000 nails at 200 an hour	= 45 hours
Total for FEEBLER	125 hours

The two together (50 + 125) = 175 hours

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

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

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

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

Table 2
Two Unequally Unequal Men Working Together

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

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

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

The foregoing is the *positive* principle underlying society. It is not a positive principle which is *materialistic* only, because men will be seeking to achieve various values and goals, some of which may be wholly immaterial. But this principle of *cooperation*, first worked out most clearly by Ricardo, and carrying his name, is the real cement in society — the factor that makes association of one man with another *mutually* profitable.

The reprint shows two *coercive* systems — robbery and the welfare state. We have balanced these two by two noncoercive systems, charity and *cooperation*. Cooperation is properly about nine-tenths of the combination of charity and cooperation.

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