Moving Money Around Won’t Make Us Richer

January 28, 2015  Peter St. Onge

One of the great debates today between left and right is whether government stimulus is worth it. The left says “yes, early and often.” And the right says “only in the right circumstances.” Unsurprisingly, both left and right are completely off — stimulus is the quickest way to impoverish an economy.

To see why, we’ll start with America’s most famous burglar, Richard Nixon.

Nixon is said to have remarked that “We are all Keynesians.” This is probably true; everybody Richard Nixon listened to was “all Keynesians.” And even today nearly every talking head on TV or in major newspapers is “all Keynesians.” Right-wing, left-wing, it’s just a big pile of Keynesians.

This is important when we see “balanced” debates among prestigious economists — “prestige” in mainstream economics is short-hand for “Keynesian.” Future generations may well find this funny, but today this is where we are.

Why does this matter? Because if the Keynesian orthodoxy is ridiculous, say, then all we get is “balanced” flavors of ridiculous.

Why ridiculous? Keynesians’ original sin is that it proposes that spending makes us richer. The other fallacies flow out of that core error. This rich-by-spending doctrine obviously doesn’t work in real life — if you’re poor, the solution is not to borrow money and have a party about it. The solution is to work hard and save up. It’s not rocket science.

Why the appeal? Why are nearly all economists, left and right, Keynesians? The idea that spending makes us richer is a very old one. It’s not original to Keynes, who wasn't much of an economic or original thinker anyway. Keynes was just regurgitating the age-old fallacy known as “underconsumption.”

“Underconsumption”

Underconsumptionism holds that economies do well when the cash flows. It seems intuitive from the top-down: if people are spending money then times must be good. If they’re not spending money there must be a problem.

Unsurprisingly, this gets it exactly backward. Spending is what happens once you're rich. It doesn’t actually make you rich. So if an economy is doing well then people do indeed buy more swimming pools. But it’s obviously not the swimming pools that made them rich.

So what did make them rich? Investment. More specifically, market-led investment. Why the “market-led” part? Because zany bureaucrats define their bridges to nowhere and squirrel-menstruation research as “investment.”

Now, it’s not that all government spending is useless — they do build gutters and sewage plants, after all. But we’ve really got no way to know whether some bureaucrat’s “investment” is growing the economy. Hence it’s tempting to say “private investment” is all that matters, but I’ll be open-minded and just say “market-led.” Meaning that a government that actually did find out market demand (for a bridge from Manhattan to New Jersey, say) would qualify as “market-led” investment and make us wealthier.

We can see the role of private investment in the
classic Robinson Crusoe picture. Poor Robinson wakes up hungry, wet, and cold. It rained all night, and he’s picked up a nasty cough. Robinson looks up at the sky, shaking his fist at the Gods of Poverty.

How does Robinson improve his lot? Why, he invests. He builds fishing hooks, fish-nets, berry-shaking sticks. He collects wood, first to build a shelter then to keep a fire going. Investments all.

And over there, in the corner, you can see the Keynesian tsk-tsking, “Why do all that hard work investing when you can just spend more, Robinson?” Remember, these are “prestigious” economists.

So how does this fatal error translate into policy today? The key thing to remember is that when the government increases “spending” it is simply making pieces of paper — known as “dollars.” Not fish hooks. Not firewood. Bidding tickets is what government makes. Why do they do this? Partly to buy votes, of course: if I could print up dollars, I guarantee I’d have a lot of Facebook friends. And partly to “boost” the economy with all that spending.

Fiat Money ≠ Wealth

The problem is, printing tickets isn’t a real resource. You don’t eat paper, as they say. Printing dollars merely bids away resources from other uses.

Let’s say Fed Chair Yellen made an error and printed me up a trillion dollars. Why, I’d use those dollars to buy all — and I do mean all — the beach-front property. I would have the most galactic beach-front party in history. Thing is, Yellen just gave me bidding tickets. She didn't give me the booze, the DJ’s, the concrete, or the wood.


So is my resource-sucking mega-party making the economy grow? Nope. When it’s all over, when the hangovers along with the ear-ringing subsides are gone, we’ve used real resources. We’ve got no factories. No decks. We’re all poorer. But the politicians did get re-elected, right?

This, in a nutshell, is Keynesian “stimulus.” Whether it comes from government spending (“fiscal stimulus”) or from Federal Reserve money-printing (monetary stimulus). In either case, real resources were bid away from the rest of us and handed out to others.

Stimulus isn’t some magical leprechaun dropping ice cream and puppies from heaven — it’s merely redistribution of resources. Stimulus is taking from those who have and giving to the government’s pals.

So the question “does stimulus work?” is completely missing the point. Putting aside the injustice of redistributive theft, the productivity question is whether the guys who got the bidding tickets did more market-led investment than the guys whose tickets were devalued.

There is no economic reason to think mere redistribution would make us richer. In fact, there are excellent reasons that show redistribution hurts the economy. “Stimulus” itself is nothing more than widespread impoverishment so a clutch of politicians can buy friends.

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

Comment by R. Nelson Nash – I love the way Peter St. Onge writes! He does a fabulous job of explaining away the nonsense of the teachings of Keynes and the folly of those who have fallen to him. The tragedy is that the entire world has fallen prey to this fool!

How Economic Aggregation Hides the Problems of Interventionism

FEBRUARY 7, 2015 — Gary Galles

I was going through the textbook for my economics principles course recently, thinking about how I could better reconcile the fact that since only individuals choose, the logic of economics is about individual choices facing the fact of scarcity. Yet macroeconomics is generally presented directly in terms of aggregates
and how to control them, as if aggregates were the relevant measures.

The Limits of Macroeconomics

Perhaps in over-reaction to the paltry discussion such issues received in my undergraduate and graduate training, I spend a substantial amount of class time on the limitations of macroeconomic aggregates. For instance, I emphasize that not a single macroeconomic variable measures what we would like to know accurately. This is why we often evaluate more than one imperfect measure to see if the “story” they tell is consistent. We do this to estimate how much confidence can be placed in a particular “fact” (like what the official unemployment rate or a measure of inflation-adjusted output did over a given period). This is why I feel the need to drive home problems aggregation can cause more clearly to my students.

With that in my head, I read the textbook’s introduction to “net taxes.” It struck me how “looking behind the curtain” at that category illustrate how aggregation can hide information and distort important conclusions.

“Net taxes” equals taxes paid to the government minus transfer payments from the government to recipients, for the household sector as a whole. It is a useful category for looking at the net effect of government programs on the disposable income of the sector as a whole. But it can paper over massive amounts of income redistribution and substantial supply-side effects on productive incentives.

Say that the government taxes one subset of the population $3 trillion, and provides $2 trillion in transfer payments (food stamps, unemployment insurance, Social Security, etc.) to another subset. The net effect on households’ aggregate disposable income is a reduction of $1 trillion. But to consider only that net number in an analysis is to ignore very important considerations.

What’s Behind The Big Numbers?

Most obviously, the net number ignores what can be vastly different treatment of different households. And that is crucial to any moral or ethical evaluation of the effects. That is particularly true when we want to know the extent to which government offers “liberty and justice for all,” as we say in the Pledge of Allegiance — that is, how much it honors individuals’ self-ownership and their derivative rights to their own production. A state that steals from Peter to pay Paul on a massive scale violates our inalienable rights in ourselves, but aggregating the effects into “net taxes” hides those effects from view.

The adverse supply-side effects that such policies have also disappear from view when we overlook the redistribution. The reason is that when we “tax the rich and give to the poor,” we reduce both parties’ productive incentives. The higher tax rates faced by higher income earners reduces the fraction of the value they produce for others that they take home, so they shelter more and earn less income. That is, they do less for others with the resources at their disposal than they otherwise would have.

Less noticed is that the aid given to the poor is also conditional on them staying poor. For instance, people lose 30 cents in food stamps for each dollar of earnings counted by the program. They, too, therefore keep a smaller fraction of what their efforts produce for others, and will also produce less for others than they would otherwise.

Hiding redistribution — and the extent to which it reduces jointly-beneficial production by focusing on “net taxes” — is not the only way in which aggregation distorts. For example, it is notable that those who back policies such as higher minimum or “living” wages because they will “help the poor,” primarily argue for it because they assert lower income earners, as a group, will have greater incomes.

Now, there are a host of issues involved in deciding whether that is true, but a focus on that question ignores that there will be a substantial number of lower skill workers who will lose their jobs and/or hours worked, fringe benefits, on-the-job training that builds future income potential, etc. They will be worse off. And arguing that the group in the aggregate might have higher incomes, which only means one subset’s increased earnings will be at least somewhat greater than another subset’s decreased earnings, in
no way justifies harming large numbers of that group who are also poor, in the name of helping the poor.

Aggregation Provides Little Useful Knowledge

As Friedrich Hayek notes in “The Use of Knowledge in Society” (and elsewhere), the aggregation that is part and parcel of central planning by its nature throws away a great deal of valuable information. The “particular circumstances of time and place” which enable value creation and that only some individuals know (i.e., not the central planner), can be utilized only by decentralizing decisions to those who are most expert in those details, in combination with the information others provide via their market choices. But such knowledge by its nature cannot enter into statistics and therefore cannot be conveyed to any central authority in statistical form. The statistics which such a central authority would have to use would have to be arrived at precisely by abstracting from minor differences between the things, by lumping together, as resources of one kind, items which differ as regards location, quality, and other particulars, in a way which may be very significant for the specific decision. It follows from this that central planning based on statistical information by its nature cannot take direct account of these circumstances of time and place and that the central planner will have to find some way or other in which the decisions depending on them can be left to the “man on the spot.”

Aggregates used in constructing gross domestic product (GDP) have severe limitations as well. They rely on prices paid to assign values to goods or services exchanged. This demonstrated preference approach makes sense for purely market driven behavior, as the value for each unit would have to be greater than the price paid for self-interested individuals who make the purchases. Even here, however, the excess value over what was paid that motivated the purchases (termed consumer surplus) is ignored. But where government intervenes, accuracy is severely degraded.

For example, if government gives a person a 40 percent subsidy for purchasing a good, all we know is that the value of each unit to the buyer exceeded 60 percent of its price. There is no implication that such purchases are worth what was paid, including the subsidy. And in areas in which government produces or utilizes goods directly, as with defense spending, we know almost nothing about what it is worth. Citizens cannot refuse to finance whatever the government chooses to buy, on pain of prison, so no willing transaction reveals what such spending is worth to citizens. And centuries of evidence suggest government provided goods and services are often worth far less than they cost. But such spending is simply counted as worth what it cost in GDP accounts.

Other Aggregation Sins

These aggregation issues do not do more than scratch the surface of the problems that arise with aggregation. There are plenty more once we dig into the details. For instance, the way employment and unemployment data are aggregated and reported, it is possible to have a job but not be officially employed or unemployed (e.g., workers under age 16), to have a job but be officially unemployed (e.g., workers in the underground economy), and to be officially employed but not currently working (union members on strike). Further, one person can be counted as multiple employees and employment and unemployment rates can move in the same direction at the same time.

The main point, however, is that to rely on aggregates as the focus moves attention away from individuals, who are the only ones who choose, act, and bear consequences. Even without further complexities and problems, that approach can hide everything from income redistribution between different groups (net taxes) to income redistribution within groups (minimum and living wage laws) to supply-side effects on production (taxes and means tested government benefit programs) to the impossibility of central planners directing an economy efficiently (with statistics that throw away details that are crucial to the creation of wealth) to the ambiguity of measures of the value of output (government production assumed to be what it cost). That is a lot to disguise or misrepresent, and such issues provide more than ample reason for suspicion whenever someone puts forth an argument from a major premise that “government aggregate X did Y, therefore we know that Z follows.”
Comment by R. Nelson Nash – *Macroeconomics is nothing more than “groupthink” and does nothing more than give credibility to things like Central Banking. It is a means of manipulating the minds of people.*

**You Can’t Create More Savings by Printing More Money**

FEBRUARY 12, 2015 — Frank Shostak

Savings has nothing to do with money. For instance, if a baker produces ten loaves of bread and consumes one loaf, his savings is nine loaves of bread. In other words, the “savings” in this case is the baker’s real income (his production of bread) minus the amount of bread that the baker consumed. The baker’s savings now permits him to secure other goods and services.

For instance, the baker can now exchange his saved bread for a pair of shoes with a shoemaker. Observe that the baker’s savings is his real means of payments — he pays for the shoes with the saved bread. Likewise, the shoemaker pays for the nine loaves of bread with the shoes that are his real savings.

**What Is Savings?**

The introduction of money doesn’t alter what we have so far said. When a baker sells his bread for money to a shoemaker, he has supplied the shoemaker with his saved, unconsumed bread. The supplied bread sustains the shoemaker and allows him to continue making shoes. Note that the money received by the baker is fully backed by his unconsumed production of bread.

Yet without the medium of exchange, i.e., money, no market economy, and hence, the division of labor, could take place. Money enables the goods of one specialist to be exchanged for the goods of another specialist. In short, by means of money, people can channel real savings, which in turn permits the widening of the process of real wealth generation.

Also, in a world without money it would be impossible to save various final goods like perishable goods for a long period of time. So the introduction of money solves this problem. Instead of storing his bread, the baker can now exchange his bread for money.

In other words, his unconsumed production of bread is now “stored,” so to speak, in money. There is, however, one proviso in all of this: that the flow of the production of goods and services continues unabated. This means that whenever a holder of money decides to exchange some money for goods, these goods are there for him.

**Having Money Is Not the Same as Having Savings**

Money can be seen as a receipt, as it were, given to producers of final goods and services that are ready for human consumption. Thus when a baker exchanges his money for apples, the baker has already paid for them with the bread produced and saved prior to this exchange. Money therefore is the baker’s claim on real savings. It is not, however, savings.

Now what about the case where money is used to buy unprocessed material — is the unprocessed material real savings? The answer is no. The raw material must be processed and then converted into a piece of equipment, which in turn can be employed in the production of final goods and services that are ready for human consumption. In this sense, the buyer of unprocessed material transfers his claims on real savings to the seller of material in return for the prospect that the transformed material, some time in the future, will generate benefits far in excess of the cost incurred.

Furthermore, the buyer of the material also buys time (i.e., by having the material readily available, he can proceed immediately with the stages of making the final tool). If the material weren’t available he would have to extract it himself, which of course would delay the making of the final tool.

Once real savings are exchanged for money, the recipient of the money can exercise his demand for money in a variety of ways. This, however, will not have any effect on the existent pool of real savings.

An individual can exercise his demand for money either by holding it in his pocket, or in his house, or by placing it in the custody of a bank in a demand deposit, or even in a safe deposit box.
Also, whether he uses it immediately in exchange for other goods, or lends it out, or puts it under the mattress, it does not alter the given pool of real savings. Thus by putting the money under the mattress, an individual doesn’t engage in the act of saving. He is just exercising a demand for money. What individuals do with money cannot alter the fact that real savings are already funding a particular activity. Whether individuals decide to hold onto the money, or lend it out alters their demand for money, but this has nothing to do with savings.

Whenever an individual lends some of his money he in fact transfers his claims on real goods to a borrower. By lending money, the individual has in fact lowered the demand for it. Note that the act of lending money (i.e., the transferring of the claim) doesn’t alter the existent pool of real savings. Likewise, if the owner of money decides to buy a financial asset like a bond or a stock he simply transfers his claims on real savings to the seller of financial assets. No present real savings are affected as a result of these transactions.

How Does Money-Supply Expansion Affect Savings?

Now let us examine the effect of monetary expansion on the pool of real savings. Since the expanded money supply was never earned, goods and services therefore do not back it up, so to speak. When such money is exchanged for goods it, in fact, amounts to consumption that is not supported by production. Consequently a holder of honest money (i.e., an individual who has produced real wealth), that wants to exercise his claim over goods discovers that he cannot get back all the goods he previously produced and exchanged for money.

In short, he discovers that the purchasing power of his money has fallen — he has in fact been robbed by means of loose monetary policy. The printing of money therefore cannot result in more savings as suggested by mainstream economists, but rather to its redistribution. This, in the process, undermines wealth generators, thereby weakening over time the pool of real savings. So any so-called economic growth, in the framework of a loose monetary policy, can only be on account of a private sector that manages to grow the pool of real savings despite the negative effects of the loose money policy.

We can thus conclude that savings is not about money as such, but about final goods and services that support various individuals that are engaged in various stages of production. It is not money that funds economic activity but the flow of final consumer goods and services. The existence of money only facilitates the flow of the real stuff.

Comment by R. Nelson Nash – I have enjoyed the writings of Frank Shostak for many years. I urge you to read everything that this great economist writes.

A Liberal Education at a Zero Price

FEBRUARY 23, 2015 — Christopher Westley

Frank Bruni saw a woman swoon and sway back in the 1980s, and the recent memory of it caused him to call for increased federal support for liberal arts education.

The woman, Anne Hall, taught Shakespeare at UNC-Chapel Hill back in the days when North Carolina students were more focused on beating Duke in basketball than on Hall's captivating performance of King Lear. Nonetheless, she made quite an impact on Bruni. “It was by far my favorite class at the University of North Carolina,” he wrote, “though I couldn’t and can’t think of any bluntly practical application for it, not unless you’re bound for a career on the stage or in academia.”

The Purpose of a Liberal Education

Today, some thirty years later and as a New York Times columnist, Bruni recalls this memory to bemoan the loss of liberal education at the large state universities in favor of piddling concerns such as skill acquisition and job placement. Will future generations learn Lear like he did when they are instead focused on learning things that might actually land them a job?

Bruni is right to revere the liberal arts, but wrong to assume that its benefits are purely emotional. The
goal of liberal education — at least before state funding diluted it — has always been about teaching students to think clearly about the world around them, develop a sense of right reason when confronting the great questions of life, and grasp natural laws so as to better follow them and live happier lives. There is no question that the widespread effect of liberal ideas throughout Europe in the Middle Ages gave common man the framework within which to question the outlandish claims of kings over the people, such as those of divine rights and tribute.

From parish to pub and from family and factory, they were a major contributor to a decentralized Europe, leading to unprecedented levels of human flourishing and social freedom. Indeed, the liberal ideas had to be denigrated and then overcome in order for the modern nation-state to emerge in the nineteenth century, and we know the suffering and death this brought about in the century that followed.

The Shakespeare whom Bruni so admires was himself a product of liberal ideas still reverberating in England despite the efforts of Henry VIII, Cromwell, and others to squelch them. Furthermore, a modern-day Shakespeare would rightly ask the question Bruni avoids, which is whether one can receive the benefits of Lear and the liberal arts without also assuming $40K in debt in order to continue to feed the education-industrial complex (for which Bruni is actually lobbying).

To Bruni, such spending can never be enough, because liberal education is priceless. Whether it is or not, the irony is that the internet can now spread the benefits of liberal education at practically a zero-price, and one no longer must sit in a dank classroom of an elite university to receive its benefits. I speak with experience as a home-schooling father whose children have learned logic, Latin, the Classics, and the sciences, and whose freshman son is now nodding off in the logic class at his university that I (a public-school product) once struggled through as an undergraduate.

**Do We Need Government To Fund the Liberal Arts?**

Bruni should take heart: Many firms desiring a talented and smart labor force recruit liberal arts graduates. But do tuition revenue-focused public universities now oversupply them, and does this contribute to the problems associated today with the Millennials who are often over-trained, unemployable, and living with their parents? And do those graduates really learn to be critical of, well, anything, as opposed to having developed a sense of (in Bruni’s words) a “rawness and majesty of emotion”?

If so, the liberal education in its modern form has become part of the problem and should no longer be left to postmodern thinkers tied to the government dole. In the 1980s, Peter Drucker predicted that firms would start hiring workers out of high school because (1) they required a lower reservation wage, and (2) they could be trained to suit the needs of the firm in ways that were no longer happening at the universities. Many firms are doing just this in 2015. Thanks in part to the state of federally-funded liberal education, such practices will become more common.

None of this is meant to deny the tremendous need for classical liberal education, as our body-politic is directly affected by the loss of critical thinking skills by the median voter underexposed to it. One might argue this was the actual intent of Progressive Era education reformers who wanted to implement a national education system — modeled after the one in Bismarck’s Germany — in which the masses would be forced into public schools to be prepared for lives in the factory or army. People like Obama or Boehner want the man-on-the-street to be compliant and unquestioning of the world around him, thinking more about Fifty Shades of Grey than perpetual war, the national debt, and the NSA. So from that perspective, it’s exciting to think about how technology is wresting liberal education from those avenues favored by the State, largely by rebels who value it more and who opt out of the system.

Liberal education and the liberal society it fosters, noted Mises in *Human Action*, brought about “an age of immortal musicians, writers, poets, painters, and sculptors; it revolutionized philosophy, economics, mathematics, physics, chemistry, and biology. And,
for the first time in history, it made the great works and the great thoughts accessible to the common man.”

It still does. Although much of this is happening sub rosa, the liberal arts are actually flourishing relative to where they were twenty years ago, thanks to the internet and without regard to higher-education funding levels. I wouldn’t hold my breath waiting for the New York Times to acknowledge it.

Comment by R. Nelson Nash – Our friend, Christopher Westley has left the hills of Alabama for the balmy shores of West Florida to serve as Professor of Economics at Florida Gulf Coast University. That university is to be congratulated on their recruitment of such a fine Austrian Economist!

Christopher presents us with the tremendous changes that are occurring in the world of education

Along with this thought, please note that all four of the articles that I have selected for this month’s issue of BANKNOTES come from www.Mises.org. Their website has been recently reworked and the articles are all spectacular! If you are not a member of the Mises Institute then you are missing out on a great opportunity for a superior source of education.

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

The Great War and Modern Memory by Paul Fussell
Wartime: Understanding and Behavior in the Second World War by Paul Fussell