



11350 Random Hills Road, Suite 800, Fairfax, Virginia 22030 Phone (703) 934-6101 Fax (703) 352-3678

fff@fff.org www.fff.org

Hope Is No Substitute for Theory **by Sheldon Richman**

Should libertarians hope that Barack Obama succeeds or fails in his presidency? The question comes to mind because conservatives got embroiled in the issue when their leading radio star, Rush Limbaugh, said he hoped Obama would fail. Some commentators thought that was a horrible thing to say. Radio stars need regular public controversy to keep their listeners tuned in, so there's no point in analyzing what the Republican partisan Limbaugh might have meant. But the question may lead us to other insights.

Everything hinges on the underlying question: succeed or fail at what? The goal determines the answer. If we assume Obama wants to use the power of government — the power of the gun, really — to redesign society, then any advocate of liberty hopes he fails. The core liberal idea (in the original sense of “liberal”) is that society runs itself without a central plan. Government is already too involved in configuring the political economy. A more intensive effort in that direction would only make things worse.

But if we define his goal sufficiently abstractly, there's more we can say. Assume that Obama in good faith wants a free, prosperous, and peaceful America. (We'll get to means in a moment.) In that case any libertarian would certainly hope for success. Failure would mean oppression, poverty, and war.

So now things shift to the “how.”

Libertarians understand that the best chance for freedom, prosperity, and peace is through a radical retrenchment of government at all levels and a full flowering of the free market. We'll focus on the central government and the domestic economy.

We can say with certainty that Obama is not planning to free the economy and dramatically cut back government power. On the contrary, he is embarking on a major Keynesian program of government spending financed by borrowing and central-bank expansion of money and credit. On the basis of sound economic theory and experience we know this approach to economic policymaking cannot create sustainable economic growth. We also know that the

program will violate individual liberty because inflation is an implicit tax that transfers wealth from those who have earned it to those who have not.

Given this knowledge, it is moot to hope it succeeds in creating anything good. Success is impossible.

Keynesianism versus the Austrians

On the other hand, we can hope Obama succeeds in this sense: we can hope he eventually ignores his Keynesian advisors, discovers Mises, Hayek, Rothbard, Israel M. Kirzner, and Robert W. Garrison, and follows the Austrian prescription for economic progress: *laissez faire*.

I'm not holding my breath, of course. The political breed of human being (with only a few exceptions) finds it irresistible to not to *do something* during a crisis. Unfortunately, *undoing* something doesn't count. So I suspect that even a president who realized that Keynesian prescriptions are self-defeating would find it hard not to increase deficit spending, monetary expansion, and regulation. The incentives, perverse as they are, would be too strong to ignore. This is the problem with representative democracy, well-documented by the Public Choice economists and Bryan Caplan in *The Myth of the Rational Voter*. Most people don't understand economics, so they are easy prey for interventionist appeals and will vote accordingly. I recall many years ago a touted "libertarian" U.S. senator (no longer in office) who explained that he had to cast bad votes because if he didn't, he wouldn't be reelected — and, presumably, be in a position to cast more bad votes.

Ludwig von Mises was aware of this problem. In *Human Action* he wrote,

We may admit that for the British and American governments in the 'thirties no way was left other than that of currency devaluation, inflation and credit expansion, unbalanced budgets, and deficit spending. Governments cannot free themselves from the pressure of public opinion. They cannot rebel against the preponderance of generally accepted ideologies, however fallacious. But this does not excuse the officeholders who could *resign* rather than carry out policies disastrous for the country. Still less does it excuse authors who tried to provide a would-be scientific justification for the crudest of all popular fallacies, viz., inflationism [4th rev. ed., p. 793, emphasis added].

Inflation and wealth

In our modern society we pride ourselves on being free of superstition, yet many people fall for the hoary and groundless belief that general economic improvement can come from creating money. That belief once marked the people known as "monetary cranks." But as we

know from the commentary over today's economic turmoil, respectable people hold this belief. The Federal Reserve System last year embarked on a perhaps unprecedented campaign to create money in order to inject liquidity into the financial system rocked by the failure of the mortgage-based securities market. Monetary crankism is back, despite the theoretical beating inflation has taken at the hands of the Austrians and Monetarists.

The inflationist theory is so absurd that one wonders how it ever caught on. Demagogues seeking power would have an obvious interest in promoting the theory, but why did anyone else fall for it? How much thought does it take to see that paper money is not wealth?

Money is a medium of exchange that emerged when man began to realize that the inconveniences of barter can be overcome by use of a highly tradable commodity, such as gold. A unit of money is recognized as an economic claim on some quantity of goods or services. In the normal course of events, people produce useful things and trade them for money. Thus a unit of money signifies that the holder had previously produced something of value. Indirectly, goods trade for goods, which is the root of Say's Law, the insight that a general glut of products is impossible in an economy with free pricing.

Now see what happens when government creates money. There is an increase in *claims* to goods and services *without any increase in the goods and services*. No general improvement can arise from this situation — quite the opposite. But prices will rise.

What is unappreciated about inflation is its deep distributionist consequences. Money, Mises taught, is non-neutral. It doesn't simply overlay a barter system without introducing its own peculiar effects. Doubling everyone's money holdings, even if it could be done at one fell swoop, would not raise the price of all things proportionally because people wouldn't merely double the quantities of everything they buy. (Would you double the quantity of soap and salt you buy?)

But the increase in the money supply does not increase everyone's cash balance at once. The government spends the new money on particular goods and services. Banks lend it to particular borrowers. Mises gives an example:

If the additional money is spent for military purposes, the prices of some commodities only and the wages of only some kinds of labor rise, others remain unchanged or may even temporarily fall. They may fall because there are now on the market some groups of men whose incomes have not risen but who nevertheless are obliged to pay more for some commodities, namely for those asked by the men first benefited by the inflation. Thus, price changes which are the result of the inflation start with some commodities and services only, and are diffused more or less slowly from one group to the others. It takes time till the additional quantity of money has exhausted all its price changing possibilities.... ["The Non-Neutrality of Money," in *Money, Method, and the Market Process*.]

The key idea here is relative prices. The common focus on an overall price level distracts us from the fact that inflation changes the configuration of prices, benefiting some people and harming others.

Inflation, then, is a subtle way for the government to transfer wealth. Many victims are the very people the “progressives” claim to champion. Most of the beneficiaries are well off.

The other important effect of inflation is that by depressing interest rates, Fed policy disrupts the market’s natural tendency to allocate scarce resources in harmony with people’s consumption-saving preferences. Inflation emits misleading signals to entrepreneurs, encouraging them to think that people are inclined to defer consumption now in order to consume more in the future. But since consumers have not really changed their preferences, monetary expansion creates a contest for resources between early and late stages of production that would not exist but for the expansion. Since resources are no less scarce than previously, a bust inevitably follows an inflationary boom.

The upshot is that inflation — and the deficit spending that “requires” it — cannot succeed in making society better off.

One hopes Obama succeeds in ushering in an era of freedom, peace, and prosperity. But hope is idle. He will have to discover sound economic theory and a reservoir of courage to make it happen.

*Sheldon Richman is senior fellow at The Future of Freedom Foundation, author of **Tethered Citizens: Time to Repeal the Welfare State**, and editor of [The Freeman](#) magazine.*

This article was originally published in the April 2009 edition of *Freedom Daily*.