

WHY FREE MARKETS ARE BENEFICIAL AND POLITICIANS DON'T LIKE THEM

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The Constitutionalist Society: Member Papers of R.L. Peterson Referenced

- Profits Are Good: Non-Profits Are Questionable
- The Seen and Unseen: Economics in One Lesson
- Monopoly and Government: Enemies of the Free Market
- Political Capitalism vs. Free Market Capitalism
- Political Capitalism: Socialism and Fascism

Other Economists and Works Referenced

- Adam Smith, *The Wealth of Nations*
- Frederic Bastiat, *What Is Seen and What Is Not Seen*
- Henry Hazlitt, *Economics In One Lesson*
- Gordon Tulloch, *The Charity of the Uncharitable*, *Western Economic Journal*, Nov.1970
- Frederick A. Hayek, *The Road to Serfdom*
- Daniel Kahneman, *Thinking Fast and Slow*
- Economics Noble Prize Winners Referenced: F.A. Hayek, Milton Friedman, James Buchanan, Daniel Kahneman

Arguments for the Value of Free Markets

- Adam Smith said the “Invisible Hand” that guides work effort and resources toward their most valuable use and economizes on costs
- My “Profits Are Good” paper explains how people who wish to profit will sell goods to the people at the minimum price that will make buyers value those goods more than any alternatives. Those producers will also pay their workers and suppliers at least as much as they could make elsewhere. If producers earn more from sales than they must pay workers and suppliers, they will profit.
- If profits in an industry or trade are large, existing suppliers will tend to hire more workers, buy more supplies, and expand. In addition, others will be attracted who hope to profit by providing goods that people want at a price they are willing to pay. Thus more resources will be devoted to producing what people desire if the resources and labor needed to make the goods can be used efficiently.
- If profits are low or negative, producers will tend to cut back production or even negative, others will not be attracted to that area and existing producers will shrink their operations—thereby freeing up labor and other productive resources to be used elsewhere—in ways that consumers prefer more.
- Non-profits and governments typically do not shrink and free up resources if the public demand for their products fall. They can continue to produce at a loss while asking donors or taxpayers for more money. Their incentive is often to continue employing themselves rather than to use resources efficiently.

The Seen and Unseen: Arguments
Against Unthinking Government
Policies by Bastiat

The Seen and Unseen

- The Broken Window Fallacy: If government spends money to repair a window (or Hurricane Sandy damage, money cannot be used elsewhere.
- Taxes, If the government collects taxes so it can spend more, the taxpayers will have less to spend or lend to others who want to spend
- Government spending, If the government spends more and either borrows or taxes, others will have less to spend
- Trade Restrictions, If government prohibits imports that compete with a favored industry so it can earn more, prices in that industry will rise and users of that good must pay more so prices will rise in general
- Demobilization, if the government lays off excess soldiers, they will not stay unemployed and many will find more valuable ways to spend their time.
- Labor saving equipment, if better equipment is produced some people may lose their jobs but more jobs will be generated in making that equipment, in doing other things, and in providing additional goods for people who can buy goods more cheaply.

Free Market vs. Political “Capitalism”

- Free Market Capitalists Must produce what they will be rewarded for by market forces at a price that customers are willing to pay. They have incentives to produce efficiently and to provide desired goods or they will deploy their capital elsewhere—through bankruptcy reorganization if not voluntarily.
- Political capitalists are rewarded for producing what the government wants, and possibly for employing people whom the government wants to have employed. They obtain favors from the government that may keep them in business or enhance their “profitability.” They have less incentive to be productive and efficient since they can count on government bailouts if they get in trouble.

Types of Political CAPITALISM

- Communism: All productive resources are owned in common. Initially their use is directed by a “dictatorship of the proletariat.” Ultimately, the theory is that all resources will be subject to common control. In practice, the dictatorship never goes away peacefully.
- Socialism: Productive resources, like capital can be totally or partially owned by the “state.” Some “states” ban all private ownership; others just nationalize a few or many “key” industries.
- Fascism: Was sold as state control of the economy to serve the interests of the working classes (the proletariat). Private ownership was allowed as long as all private resources were subject to employment as directed by the “elite” managers of the state (nation). Hitler’s party was the “National Socialist Workers Party.”
- New Socialism (my term): productive resources (capital) can be owned by private parties but state regulation will dictate how those resources can be used. Similar to Fascism in effect, but the proponents often call themselves socialists or social democrats.

Performance of Economies Post WWII

- North Korea—Communist—Hereditary leaders did well as did their associates. Ordinary people often suffered and a number starved.
- South Korea—Free Markets—Most people thrived and many grew wealthy.
- East Germany—Communist—Leaders did O.K. Ordinary people did not, Many were repressed and tried to flee.
- West Germany—Free markets—The economy thrived and people, in general, became wealthy.

HOW CAN Politicians Profit From Government Power and Money?

- Earn Monopoly Rents by restricting entry of competitors into professions or markets.
- Restrict foreign competition and market entry.
- Earn Monopoly rents by allowing favored firms to merge and establish monopolistic positions.
- Earn monopoly rents by writing specifications in government purchase contracts that favor only one bidder or supplier.
- Obtain direct payments in salary or perquisite.
- By receiving future payment promises for employment or consulting from those whom they have granted favorable regulations or contracts prior to retiring from government.
- By receiving favorable information about future stock market opportunities.

Asia Economies—Post WWII

- Hong Kong—Free Markets—Went from poverty to prosperity
- Singapore—Free Markets—Went from poverty to prosperity
- Taiwan China—Free markets—Became economically prosperous.
- China under Mao—Communist—People suffered, Many died, Most remained poor. Mao lived lavishly.
- China after Deng—Communist with Free markets allowed in specific areas. Many prospered, the economy grew rapidly, but many individual freedoms were still repressed.

Political Capitalism: Socialism and Fascism

- Socialists believe that the government should own “the means of production;” i.e. capital. Communism is the extreme case where ideally all production is conducted in the public interest. In other case, socialists are content with nationalizing private industry, or maybe only limited numbers of “key” industries.
- Fascism allows for private ownership of the means of production as long as it is used in the interest of the corporate state—with those interests defined by the elite. Like the other forms of political capitalism, Fascists claim they need power so they can provide benefits for the common man (the working class or the proletariat. Hitler’s Nazi party was the “National Socialist Workers Party.”
- The “New Socialists” (my term) allow for private ownership of capital but tax it and use myriad regulations to tell the owners of private capital what they can and cannot do with it. Like other socialists they claim that they are acting in the public interest.

Incentive Problems with Socialism

- Socialists claim they want to help the common man and the have-nots of society by taking from those who have too much and giving to those who have too little of what they want.
- Those who expect to receive benefits without working have less incentive to work, so many will work less.
- Those who expect to pay high taxes may elect to take more leisure rather than work more and harder. In addition, they may take less risk since the government will tax the proceeds of successful ventures and they will bear the loss if the venture is unsuccessful.
- Those who have secure government sponsored jobs will take less risk lest they make a mistake and will have less incentive to work hard.
- Consequently, economic growth is likely to lag in socialistic countries.

Outcomes Under Strong Socialism

- Yugoslavia—Communist-- The New Class of Leaders lived well. Ordinary people did not. Country broke up.
- USSR—Communist—Leaders lived well with Dachas. Ordinary people suffered queues, purges, gulags, poor consumer goods, low life expectancies. Country ultimately broke up.
- Cuba—Communist—Castors' and their associates lived well. Ordinary people did not. Many are still extremely poor.
- Venezuela—Bolivarian Socialism—Leaders are doing O.K. The economy is a shambles. Ordinary people are destitute and desperate.
- Britain under Labor party in 1970s—Socialized many industries—suffered strikes, low productivity, inflation and a “Brain Drain,” Ultimately elected Margaret Thatcher to get economic freedom.
- European Union Countries—Many have socialized many key industries (owned and controlled by the state)—Studies have shown that the countries with the highest ratios of government spending have grown slower than those with more restricted government.

Given Problems with Socialism; Why Do So Many Voters Favor Socialist Politicians?

- Many voters are short-sighted. In *Thinking Fast and Slow*, Kahneman points out people often make quick emotionally based decisions rather than more thoughtful, and harder, logically thought out decisions. They may favor the “seen” over the “unseen”
- Mischel's Stanford Marshmallow experiments showed that over 2/3 of preschoolers could not resist temptation. Those people did not do as well when they grew up.
- Credit card data showed that over 2/3 of people did not pay in full even when credit cards rates were high.
- Many people now still carry large amounts of debt incurred when satisfying impulsive purchase decisions.
- Demagogic politicians appeal to voters baser instincts such as greed, envy and malice, etc.
- Peoples’ brains don’t develop their judgment center, the prefrontal cortex, until their early 20s and possibly never, especially if certain drugs are used.
- People are exposed to media barrages that may be biased by the fact that the media members tend to be emotionally oriented, and some may have been educated to favor government control ideals.

Educational Deficiencies of Voters

- Many people do not understand economics—especially free market economics and the concept of “opportunity costs.” Most do not understand that “there is no such thing as a free lunch.”
- Schools and “elite” universities often emphasize “statist” economic policies. Those policies assume the “elite” who run the state can run the economy so everyone can get what they want. They emphasize the “seen” and tend to neglect the “unseen” opportunity costs.
- Since it is easier to talk about and think about the emotionally based “seen” effects of policy rather than do the “slow” thinking necessary to analyze the “unseen” effects, most educators find it easier to teach people only about the obvious “seen” effects. Since most journalists prefer to talk about emotionally charged “seen” effects also, few people are trained to look for the “unseen” effects of economic policies.
- Statist politicians who seek power and perquisites emphasize the “seen” effects of policy and appeal to voters’ greed, envy, and malice, among other things, to get elected. The short-sighted media tends to amplify their emotionally based arguments.