GEORGE REISMAN'S PROGRAM OF SELF-EDUCATION IN THE ECONOMIC THEORY AND POLITICAL PHILOSOPHY OF CAPITALISM

Second Edition

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of Philosophy, Economics, and Psychology

GEORGE REISMAN'S PROGRAM OF SELF-EDUCATION IN THE ECONOMIC THEORY AND POLITICAL PHILOSOPHY OF CAPITALISM

Second Edition

**The Jefferson School of Philosophy, Economics, and Psychology,
PO Box 2934, Laguna Hills, California**

on line at www.capitalism.net

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Note: For short-answer questions on Chapters 1-19, see the separate TJS publication *Short-Answer Q&A Supplement to Capitalism: A Treatise on Economics by George Reisman.* This publication is now included in Reisman's *Program of Self-Eductaion in the Economic Theory and Political Philosophy of Capitalism* and can be found on the same CD as the present publication.

INTRODUCTION

The purpose of this program is to provide a comprehensive knowledge of the nature, foundations, and operations of a capitalist society in all of its major aspects, and to do so at an advanced level. As an essential part of this objective, the program aims to develop in the student the capacity for performing his own, independent politico-economic analyses of issues and events related to the subject matter of the program.

As the means of accomplishing its purpose, the program seeks to familiarize the student with the works of Ludwig von Mises and Ayn Rand, and of the earlier "Austrian" and classical economists, as well as with my own book *Capitalism: A Treatise on Economics.* An in-depth knowledge of this material is vitally necessary for anyone who seriously wants to understand capitalism.

The essential and principal themes of the program are (1) the individual pursuit of material self-interest under freedom is the foundation of the development of capitalist institutions and of economic progress and prosperity; (2) the economic institutions of a capitalist society—among them private ownership of the means of production, division of labor, saving and capital accumulation, economic competition and economic inequality, and the profit motive and the price system—make possible *continuous* economic progress and *continually* rising living standards for all; (3) the material self-interests of all men are harmonious under capitalism, and that the extension of economic freedom, and thus the progressive movement toward logically consistent, laissez-faire capitalism, is the solution for all the leading political-economic problems of our time, such as mass unemployment and depressions, inflation, shortages, economic stagnation and decline, monopoly, and international and domestic economic conflict. Consistent with its themes and with the axiomatic nature of the value of human life and well-being, the program is unreservedly *procapitalist* in every respect.

I have used the table of contents of my book as the basis for organizing the program's content. My book is a comprehensive treatment of capitalism, and its organization has been and continues to be the most satisfactory one I know of for the purpose of conveying the scope and level of knowledge of capitalism that this program seeks to convey. In addition, I have incorporated into the program numerous recorded lectures I have given over the years, which I believe make an important contribution to the goals of the program. The great majority of these lectures were originally prepared in close connection with the writing of my book, and all of them serve to reinforce and amplify it. I have placed references to all of the numerous other works that are included in the program, at the appropriate places in this scheme of organization. In effect, organizationally, my book and lectures serve as the program's spinal column, so to speak, to which the rest of the program is attached at various points.

The method of organization I have laid out would be suitable for someone willing and able to read several large books and a greater number of small ones, all fairly closely related in subject matter at any given point but of different degrees of difficulty, all at the same time. It is entirely possible, of course, that this method of organization may not be the best one. It almost certainly is not the one that any given participant should follow in attempting to complete the program. My purpose, which I have not found easy to accomplish, has been to arrive at *some principle of organization* of all of the very vital and extensive material one needs to know in order to defend capitalism competently and effectively. What this program offers—what makes it a program—is that it does possess such a principle. As far as I know, it is the first and only program of its type. And this being so, it should be considered as version 1.0, to borrow an apt expression from the computer software industry. As and when improvements are made in the program, they will appear on the TJS web site on the internet. The URL of the TJS web site is:

http://www.capitalism.net

In accordance with what I have said, each participant, after surveying the various suggestions for reading, and the topics they relate to, should feel absolutely free to follow any particular, special line of interest that he may have. If, for example, someone wants to read all of Henry Hazlitt's *Economics in One Lesson,* or all of my *Capitalism,* or all of von Mises's *Human Action,* or all of *all* of von Mises's works before turning elsewhere, or everything on the subject, say, of inflation, or monopoly, or socialism, or whatever, he should feel completely free to pursue his interest. It is just that sooner or later he should come back and ultimately complete the program.

I estimate that it would take a full-time, dedicated student at least a year to read and study everything that is listed in the program. For those who can devote only their spare time, the length of time over which pursuit of the program might extend is correspondingly greater. Given the collapse of much of higher education, I cannot help but believe that enterprising students who are presently enrolled in colleges or universities could manage to squeeze the necessary time out of their regular courses, which are so often devoid of all real substance. Better still, some of them might arrange to follow all or part of this program for academic credit, under the supervision of a faculty member.

In addition to the above organization of topics and readings, I have included not only a large number (over 1500) of study/review questions pertaining to the contents of my book, but also my syllabi and syllabi supplements that I use in my courses in the MBA program at Pepperdine University's Graziadio School of Business and Management, where I have taught for many years. (Both courses are 4 units and are required. They can be described very loosely as "microeconomics" and "macroeconomics." I describe them below simply as "First Course" and "Second Course.") My syllabi, especially the supplements, provide both a convenient and fully comprehensive overview of what I actually teach in my classes. Hopefully, they will provide yet some further intellectual reinforcement of the program and will serve as a starting point for the preparation of the student's own lectures and syllabi. (The substance of some of the supplements also appears in the form of the supplements that accompany my recorded lecture series.)

It should be noted that the bibliography to *Capitalism* provides publication information for all of the books that appear in the program. The page references to von Mises's *Socialism* apply to the Jonathan Cape edition; however, they can easily be applied to the Liberty Press edition as well.

A Word on Accessing the Lectures. For this new edition, all of my tape-recorded lectures have been converted to mp3 format and transferred to CDs. The best way to access any given individual lecture on a CD residing in one's computer's CD drive, is to go to "My Computer" and then click on the icon of the CD drive. That will then bring up the icons for the various individual lectures. Clicking on such an icon will then launch that lecture.

THE SYLLABUS FOR THE PROGRAM

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UNIT 1. INTRODUCTION

Procapitalist Economic Thought, Past and Present

Pseudoeconomic Thought

- Marshallian Neoclassical Economics: The Monopoly Doctrine and Keynesianism
- Mathematical Economics

Overview of *Capitalism: A Treatise on Economics*

READINGS/LECTURES

- Reisman, *Capitalism,* pp. 1–12
- Ludwig von Mises, *The Historical Setting of the Austrian School of Economics*
- Ludwig von Mises, *Planning for Freedom,* 4th ed., pp. 224–280
- Adam Smith, *The Wealth of Nations,* Book 4, Chapters 1–8, on the mercantilists, and Chapter 9, on the physiocrats.
- Eugen von Böhm-Bawerk, *Capital and Interest,* Huncke and Sennholz translation, Vol. 1, *History and Critique of Interest Theories*
- A history of economic thought text, simply to learn which authors came when and, very roughly, what they said. Two possible choices, neither of which can be recommended strongly, are: Frank A. Neff, *Economic Doctrines,* 2d ed., and Eduard Heimann, *History of Economic Doctrines* (New York: Oxford University Press, 1964).

UNIT 2. ECONOMICS AND CAPITALISM

THE NATURE AND IMPORTANCE OF ECONOMICS

Economics, the Division of Labor, and the Survival of Material Civilization

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- Implications for Ethics and Personal Understanding
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CAPITALISM

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- The Indivisibility of Economic and Political Freedom
- The Rational Versus the Anarchic Concept of Freedom
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- The Growth of Corruption as the Result of the Decline of Freedom

Capitalism and the Origin of Economic Institutions

Capitalism and the Economic History of the United States

Why Economics and Capitalism Are Controversial

- The Assault on Economic Activity and Capitalism
- The Prevailing Prescientific Worldview in the Realm of Economics
- Economics Versus Unscientific Personal Observations

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Economics Versus Irrational Self-Interest
Economics Versus Irrationalism
Economics and Capitalism: Science and Value

READINGS/LECTURES

Reisman, *Capitalism,* pp. 15–38
Lecture: Reisman, "The Nature and Value of Economics" on disk 1 of "Lectures and Speeches on Economics and Politics"
Ludwig von Mises, *Human Action*, pp. 1-10, 279–287, 734–736, 862-885
Ludwig von Mises, *Socialism*, pp. 395-403, 452-453
Ludwig von Mises, "Economic Teaching at the Universities," in *Planning for Freedom,* pp. 161–172
Ludwig von Mises, *The Anticapitalistic Mentality*
Ludwig von Mises, *Epistemological Problems of Economics,* pp. 27–30, 99–102 in the Van Nostrand edition, 28-32 and 107-111 in the 3rd edition, published by the Mises Institute.
For a firsthand glimpse of what the United States started out to be and for most of its history substantially was: "The Declaration of Independence" and "The Constitution and Bill of Rights of the United States"
For learning the essential meaning and application of America's founding documents: Ayn Rand, "Man's Rights," "Collectivized Rights," "The Nature of Government," and "Government Financing in a Free Society" in Ayn Rand, ed., *The Virtue of Selfishness*
For an indication of the previous judicial protection of economic freedom and its subsequent loss: Bernard Siegan, *Economic Liberties and the Constitution,* Chapters 1 and 2
For the essential moral/political meaning of government economic intervention: Frederic Bastiat, *The Law*
For the essential character of modern intellectual history: Ayn Rand, *For the New Intellectual,* title essay
For a knowledge of what can and cannot be changed: Ayn Rand, "The Metaphysical Versus the Man-Made" in Ayn Rand, *Philosophy: Who Needs It*
Ayn Rand, "Faith and Force: The Destroyers of the Modern World" and "Censorship: Local and Express" in Ayn Rand, *Philosophy: Who Needs It*
Ayn Rand, "The Age of Envy" in Ayn Rand, ed., *The New Left: The Anti-Industrial Revolution*
For the whole of the underlying philosophy of capitalism, in the form of the world's most exciting plot novel: Ayn Rand, *Atlas Shrugged*

UNIT 3. WEALTH AND ITS ROLE IN HUMAN LIFE

Wealth and Goods
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Applications of the Law of Diminishing Marginal Utility
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Determination of Consumer Spending Patterns
Say's Law
"Scarcity" and the Transformation of Its Nature Under Capitalism
Time Preference and the Scarcity of Capital
The Foundations of Time Preference

The Scarcity of Capital
A Word on Capital Accumulation and the Rate of Return
Time Preference, Rationality, and Freedom

Wealth and Labor

The Scarcity of Labor and Its Ineradicability

READINGS/LECTURES

Reisman, *Capitalism*, pp. 39–62

Lecture: Reisman, "Wealth, Natural Resources, and the Environment and the Political Concept of Monopoly," Lecture 1

Lecture: Reisman, "Education and the Racist Road to Barbarism," on disk 1 of "Lectures and Speeches on Economics and Politics"

Ludwig von Mises, *Human Action*, pp. 11–142

Ayn Rand, "What Is Capitalism?" in Ayn Rand, ed., *Capitalism: The Unknown Ideal*

On the subject of marginal utility, including its relationship to cost of production: Eugen von Böhm-Bawerk, *Capital and Interest*, Vol. 2, Book 3, pp. 121-183; "The Ultimate Standard of Value" in *Shorter Classics of Böhm-Bawerk;* Carl Menger, *Principles of Economics*.

More on the subject of time preference: Böhm-Bawerk, *Capital and Interest*, Vol. 2, pp. 259–273

UNIT 4. NATURAL RESOURCES AND THE ENVIRONMENT

NATURAL RESOURCES

The Limitless Potential of Natural Resources

The Energy Crisis

The Law of Diminishing Returns

The Law of Diminishing Returns and the Limitless Potential of Natural Resources
Diminishing Returns and the Need for Economic Progress

Conservationism: A Critique

THE ECOLOGICAL ASSAULT ON ECONOMIC PROGRESS

The Hostility to Economic Progress

The Claims of the Environmental Movement and Its Pathology of Fear and Hatred

The Actual Nature of Industrial Civilization
The Environmental Movement's Dread of Industrial Civilization
The Toxicity of Environmentalism and the Alleged Intrinsic Value of Nature
The Alleged Pollution of Water and Air and Destruction of Species
The Alleged Threat from Toxic Chemicals, Including Acid Rain and Ozone Depletion
The Dishonesty of the Environmentalists' Claims
The Alleged Threat of "Global Warming"
Why Economic Activity Necessarily Tends to Improve the Environment

The Collectivist Bias of Environmentalism

Environmentalism and Irrational Product Liability
Environmentalism and the Externalities Doctrine

The Economic and Philosophic Significance of Environmentalism

Environmentalism, the Intellectuals, and Socialism

Environmentalism and Irrationalism

The Loss of the Concept of Economic Progress
Irrational Skepticism
The Destructive Role of Contemporary Education
The Cultural Devaluation of Man

READINGS/LECTURES

Reisman, *Capitalism,* pp. 63–120
Lecture: Reisman, "Wealth, Natural Resources, and the Environment and the Political Concept of Monopoly," Lecture 2
Lecture: Reisman, "Resource Economics," on disk 1 of "Lectures and Speeches on Economics and Politics"
Lecture: Reisman, "The Toxicity of Environmentalism," on disk 1 of "Lectures and Speeches on Economics and Politics"
Lectures: Reisman, "Wealth, Natural Resources, and the Environment and the Political Concept of Monopoly," Lectures 3 and 4
Ludwig von Mises, *Human Action,* pp. 654-663
Ludwig von Mises, *Socialism,* pp. 404–429
Ayn Rand, *The New Left: The Anti-Industrial Revolution*
Ayn Rand, "The Intellectual Bankruptcy of Our Age" and "Apollo 11" "Who Is the Final Authority in Ethics?" in Ayn Rand, *The Voice of Reason*
Ayn Rand, "The Establishing of an Establishment" in Ayn Rand, *Philosophy: Who Needs It*
Jay Lehr, ed., *Rational Readings on Environmental Concerns*

UNIT 5. THE DIVISION OF LABOR AND PRODUCTION

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Rebuttal of the Critique of the Division of Labor
Universal Aspects of Production

READINGS/LECTURES

Reisman, Capitalism, pp. 123–134
Reisman, Lecture: "Essentials of Capitalism," Lecture 1
Ludwig von Mises, Human Action, pp. 143–193
Ludwig von Mises, Socialism, pp. 289–313
Adam Smith, The Wealth of Nations, Book 1, Chapters 1–4

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The Dependence of the Division of Labor on Saving and Capital Accumulation
The Dependence of the Division of Labor on Exchange and Money
The Dependence of the Division of Labor on Economic Competition
The Dependence of the Division of Labor on the Freedom of Economic Inequality
Egalitarianism and the Abolition of Cost: The Example of Socialized Medicine
Government Intervention, Democracy, and the Destruction of the Individual's Causal Role

READINGS/LECTURES

Reisman, *Capitalism,* pp. 135–151
Reisman, Lecture: "Essentials of Capitalism," Lecture 2

Ludwig von Mises, *Human Action,* pp. 194–231, 821–832

Ludwig von Mises, *Planning for Freedom,* pp. 36–49

Ayn Rand, "The Meaning of Money," "'From Each According to His Ability to Each According to His Need,'" and "The Forgotten Man of Socialized Medicine" in Ayn Rand, *Atlas Shrugged,* reprinted in Ayn Rand, *For The New Intellectual*

Carl Menger, "The Nature and Origin of Money," in Carl Menger, *Principles of Economics*

ELEMENTS OF PRICE THEORY: DEMAND, SUPPLY, AND COST OF PRODUCTION

The Meaning of Demand and Supply

The Law of Demand

- The Concept of Elasticity of Demand
- Seeming Exceptions to the Law of Demand
- The Derivation of Supply Curves
- Limitations of Geometrical Analysis
- Confusions Between Supply and Cost
- The Circularity of Contemporary Economics' Concept of Demand

READINGS/LECTURES

Reisman, *Capitalism,* pp. 151–171

Böhm-Bawerk, *Capital and Interest,* Vol. 2, pp. 207–256; Vol. 3, pp. 78–123

UNIT 7. THE DEPENDENCE OF THE DIVISION OF LABOR ON CAPITALISM II: THE PRICE SYSTEM AND ECONOMIC COORDINATION

UNIFORMITY PRINCIPLES

The Uniformity-of-Profit Principle and Its Applications

- Keeping the Various Branches of Industry in Proper Balance
- The Power of the Consumers to Determine the Relative Size of the Various Industries
- The Impetus to Continuous Economic Progress
- Profits and the Repeal of Price Controls
- The Effect of Business Tax Exemptions and Their Elimination
- Additional Bases for the Uniformity-of-Profit Principle
- Permanent Inequalities in the Rate of Profit

The Tendency Toward a Uniform Price for the Same Good Throughout the World

- Why the Arab Oil Embargo Would Not Have Been a Threat to a Free Economy
- Tariffs, Transportation Costs, and the Case for Unilateral Free Trade

The Tendency Toward Uniform Prices Over Time: The Function of Commodity Speculation

- Rebuttal of the Charge That the Oil Shortages of the 1970s Were "Manufactured" by the Oil Companies

The Tendency Toward Uniform Wage Rates for Workers of the Same Degree of Ability

- Equal Pay for Equal Work: Capitalism Versus Racism

Prices and Costs of Production

READINGS/LECTURES

Reisman, *Capitalism,* pp. 172–201

Lectures: Reisman, "Inflation and Price Controls," Lectures 3 (second half) and 4

Lecture: Reisman, "Capitalism: The Cure for Racism," on disk 1 of "Lectures and Speeches on Economics and Politics"

Ludwig von Mises, *Human Action,* pp. 232–256, 646–654

Ludwig von Mises, *Socialism,* pp. 525–543

Ludwig von Mises, *Planning for Freedom,* pp. 1–17, 108–150

Henry Hazlitt, *Economics in One Lesson,* Chapters 13–18 and 22
Eugen von Böhm-Bawerk, *Capital and Interest,* Vol. 2, pp. 168–176, 248–256; Vol. 3, pp. 97–115
John Stuart Mill, *Principles of Political Economy,* Book 2, Chapter 11, Section 1; Book 3, Chapters 2–4
David Ricardo, *Principles of Political Economy and Taxation,* Chapters 4 and 30
Adam Smith, *The Wealth of Nations,* Book 1, Chapters 5 and 10

ALLOCATION PRINCIPLES

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The Pricing and Distribution of Factors of Production in Limited Supply
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Appendix to Chapter 6: The Myth of "Planned Obsolescence"

READINGS/LECTURES

Reisman, *Capitalism,* pp. 201–218
Lecture: Reisman, "Inflation and Price Controls," Lecture 5
Ludwig von Mises, *Human Action,* pp. 257–279, 287–357, 391–397

UNIT 8. THE DEPENDENCE OF THE DIVISION OF LABOR ON CAPITALISM III: PRICE CONTROLS AND ECONOMIC CHAOS

PRICE CONTROLS AND SHORTAGES

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Price Controls No Remedy for Inflation
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The Supply of Goods in a Local Market
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The Agricultural Export Crisis of 1972–73
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Price Controls and the Prohibition of Supply
The Destruction of the Utilities and the Other Regulated Industries
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The Destructionist Mentality
A Defense of Inventory Repricing
The Campaign Against the Profits of the Oil Companies
How the U.S. Government, Not the Oil Companies, Caused the Oil Shortage
The Conspiracy Theory of Shortages

Rebuttal of the Charge That Private Firms “Control” Prices

READINGS/LECTURES

Reisman, *Capitalism*, pp. 219–238
Lecture: Reisman, “Inflation and Price Controls,” Lecture 6
Ludwig von Mises, *Human Action*, pp. 758–769

FURTHER EFFECTS OF PRICE CONTROLS AND SHORTAGES

Consumer Impotence and Hatred Between Buyers and Sellers
How Repeal of Rent Controls Would Restore Harmony Between Landlords and Tenants
The Impetus to Higher Costs
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Chaos in the Geographical Distribution of Goods Among Local Markets
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Applications to Rent Controls
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READINGS/LECTURES

Reisman, *Capitalism*, pp. 238–256
Lecture: Reisman, “Inflation and Price Controls,” Lecture 7

UNIVERSAL PRICE CONTROLS AND THEIR CONSEQUENCES

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Universal Price Controls and Universal Shortages
Excess Demand and Controlled Incomes
The Destruction of Production Through Shortages
The Prosperity Delusion of Price Controls: The World War II “Boom”
Socialism on the Nazi Pattern

READINGS/LECTURES

Reisman, *Capitalism*, pp. 256–266
Lecture: Reisman, “Inflation and Price Controls,” Lecture 8
Ludwig von Mises, *Planning for Freedom*, pp. 18–35, 72–82
Ayn Rand, “The Roots of War” in Ayn Rand, ed., *Capitalism: The Unknown Ideal*

UNIT 9. THE DEPENDENCE OF THE DIVISION OF LABOR ON CAPITALISM IV: SOCIALISM, ECONOMIC CHAOS, AND TOTALITARIAN DICTATORSHIP

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The Myth of Socialist Planning—The Anarchy of Socialist Production
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Shortages of Labor and Consumers’ Goods Under Socialism
Further Economic Flaws of Socialism: Monopoly, Stagnation, Exploitation, Progressive Impoverishment
Socialism’s Last Gasp: The Attempt to Establish a Socialist Price System and Why It Is Impossible

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The Tyranny of Socialism
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    The Imposition of Forced Labor in the United States
Socialism as a System of Aristocratic Privilege and a Court Society
From Forced Labor to Mass Murder Under Socialism
From Socialism to Capitalism: How to Privatize Communist Countries

READINGS/LECTURES

Reisman, *Capitalism,* pp. 267–295
Lecture: Reisman, "Inflation and Price Controls," Lecture 9
Ludwig von Mises, *Human Action,* pp. 689–715, 812–820
Ludwig von Mises, *Socialism,* pp. 1–277, 511–521, 543–592 (Note: pp. 114–142, 196–220, and 516–521 deal specifically with the vital issue of the impossibility of economic calculation under socialism)
Ludwig von Mises, *Planning for Freedom,* pp. 195–223
Ayn Rand, "The Property Status of Airwaves," in Ayn Rand, ed., *Capitalism: The Unknown Ideal*
Henry Hazlitt, *The Great Idea*; reprinted as *Time Will Run Back*
F. A. Hayek, *The Road to Serfdom*

UNIT 10. THE INFLUENCE OF THE DIVISION OF LABOR ON THE INSTITUTIONS OF CAPITALISM

PRIVATE OWNERSHIP OF THE MEANS OF PRODUCTION

The General Benefit from Private Ownership of the Means of Production
    The Benefit of Capital to the Buyers of Products
    The Benefit of Capital to the Sellers of Labor
    The Direct Relationship Between the General Benefit from Capital and Respect for the Property Rights of Capitalists
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    Implications for Redistributionism
    Destructive Consequences of Government Ownership
    Profit Management Versus Bureaucratic Management
    The "Successful" Nationalizations of Oil Deposits: A Rebuttal
The General Benefit from the Institution of Inheritance
    The Destructive Consequences of Inheritance Taxes
The General Benefit from Reducing Taxes on the "Rich"
Private Ownership of Land and Land Rent
    How Private Ownership of Land Reduces Land Rent
    Land Rent and Environmentalism
    The Violent Appropriation Doctrine
    The Demand for Land Reform
Private Property and Territorial Sovereignty
    A Defense of Foreign "Exploitation" of Natural Resources

READINGS/LECTURES

Reisman, *Capitalism,* pp. 296–326
Lectures: Reisman, "Essentials of Capitalism," Lectures 3-5
Lecture: Reisman, "Everyone's Stake in Capitalism," on disk 1 of "Lectures and Speeches on Economics and

Politics”
Lecture: Reisman, “Everyone’s Stake in Capitalism II,” on disk 1 of “Lectures and Speeches on Economics and Politics”
Ludwig von Mises, *Human Action,* pp. 635–645, 804–811
Ludwig von Mises, *Socialism,* pp. 37–42
Ludwig von Mises, *Bureaucracy*
Ludwig von Mises, *Omnipotent Government*
David Ricardo, *Principles of Political Economy and Taxation,* Chapter 2

ECONOMIC INEQUALITY

Economic Inequality Under Capitalism
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Economic Inequality and the Law of Diminishing Marginal Utility
Economic Inequality and the Normal Curve
The “Equality of Opportunity” Doctrine: A Critique
Education and the Freedom of Opportunity
Everyone’s Interest in the Freedom of Opportunity

READINGS/LECTURES

Reisman, *Capitalism,* pp. 326–343
Lectures: Reisman, “Essentials of Capitalism,” Lectures 5(last part)-6

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The Enemies of Competition as the True Advocates of the Law of the Jungle
Economic Competition and Economic Security
The Law of Comparative Advantage
International Competition and Free Labor Markets
Comparative Advantage Versus the Infant-Industries Argument
How the Less Able Can Outcompete the More Able in a Free Labor Market
The Pyramid-of-Ability Principle
Freedom of Competition and the General Gain from the Existence of Others
The Population Question
Worldwide Free Trade
Free Trade and the Economic Superiority of the United States Over Western Europe
International Free Trade and Domestic Laissez Faire
The Birth Rate
Free Immigration
Refutation of the Arguments Against Free Immigration
Free Immigration and International Wage Rates
Capital Export
The Harmony of Interests in the Face of Competition for Limited Money Revenues

READINGS/LECTURES

Reisman, *Capitalism,* pp. 343–374
Lectures: Reisman, “Essentials of Capitalism,” Lectures 7-8
Lecture: Reisman, “Why I’m for Free Enterprise,” on disk 1 of “Lectures and Speeches on Economics and Politics”
Lecture: Reisman, “Some Fundamental Insights into the Benovelent Nature of Capitalism,” on disk 2 of “Lec-

tures and Speeches on Economics and Politics"
Ludwig von Mises, *Human Action*, pp. 664–688, 737–757, 833–866
Ludwig von Mises, *Socialism*, pp. 281–358, 395–453
Ludwig von Mises, *Liberalism*
Ayn Rand, "The Moral Meaning of Capitalism" in Ayn Rand, *Atlas Shrugged,* reprinted in Ayn Rand, *For The New Intellectual*

UNIT 11. MONOPOLY VERSUS FREEDOM OF COMPETITION

THE POLITICAL CONCEPT OF MONOPOLY

The Meaning of Freedom and of Freedom of Competition
High Capital Requirements as an Indicator of Low Prices and the Intensity of Competition
The Political Concept of Monopoly and Its Application
Monopoly Based on Exclusive Government Franchises
Licensing Law Monopoly
Tariff Monopoly
The Monopolistic Protection of the Inefficient Many Against the Competition of the More Efficient Few
Monopoly Based on Minimum-Wage and Prounion Legislation: The Exclusion of the Less Able and the Disadvantaged
Government-Owned and Government-Subsidized Enterprises as Monopoly
The Antitrust Laws as Promonopoly Legislation
Socialism as the Ultimate Form of Monopoly
Further Implications of the Political Concept of Monopoly: High Costs Rather Than High Profits
Patents and Copyrights, Trademarks and Brandnames, Not Monopolies
All Monopoly Based on Government Intervention; Significance of Monopoly

The Economic Concept of Monopoly

The Alleged Tendency Toward the Formation of a Single Giant Firm Controlling the Entire Economic System: A Rebuttal
Incompatibility With the Division of Labor—Socialism as the Only Instance of Unlimited Concentration of Capital
Inherent Limits to the Concentration of Capital Under Capitalism
Government Intervention as Limiting the Formation of New Firms
The Incentives for Uneconomic Mergers Provided by the Tax System
In Defense of "Insider Trading"
Economically Sound Mergers
The Trust Movement
The Predatory-Pricing Doctrine
More Than One Firm in an Industry as the Normal Case
"Predatory Pricing" in Reverse: The Myth of Japanese "Dumping"
The Chain-Store Variant of the Predatory-Pricing Doctrine
Contract Pricing
The Predatory-Pricing Doctrine and the Inversion of Economic History
The Myth of Predation With Respect to Suppliers
The Myth of Standard Oil and the South Improvement Company
Marginal Revenue and the Alleged "Monopolistic Restriction" of Supply
Competitors' and Potential Competitors' Costs—Ultimately, Legal Freedom of Entry—as Setting the Upper Limit to Prices in a Free Market

- Ricardo and Böhm-Bawerk on Cost of Production Versus the Elasticity of Demand
- Pricing Under Patents and Copyrights
- Contract Pricing and Radical Privatization
- Private Streets
- Eminent Domain

Cartels

- Cartels and Government Intervention

“Monopoly” and the Platonic Competition of Contemporary Economics

- The Doctrine of Pure and Perfect Competition
- Implications of Marginal-Cost Pricing
- The Alleged Lack of “Price Competition”

A Further Word on Cost of Production and Prices

READINGS/LECTURES

- Reisman, *Capitalism,* pp. 375–440
- Lectures: Reisman, “Wealth, Natural Resources, and the Environment and the Political Concept of Monopoly,” Lectures 5 and 6
- Lecture: Reisman, “Capitalism vs. Anticapitalism: Reason vs. Muscle Mysticism,” on disk 2 of “Lectures and Speeches on Economics and Politics” (the second half of this lecture contains extensive material dealing with the “economic concept” of monopoly)
- Ludwig von Mises, *Human Action,* pp. 357–391
- Ludwig von Mises, *Socialism,* pp. 361–392
- Ayn Rand, “America’s Persecuted Minority: Big Business,” “Notes on the History of American Free Enterprise,” and “Patents and Copyrights” in Ayn Rand, ed., *Capitalism: The Unknown Ideal*
- Ayn Rand, “Antitrust: The Rule of Unreason” in Ayn Rand, *The Voice of Reason*

UNIT 12. THE DIVISION OF LABOR AND THE CONCEPT OF PRODUCTIVE ACTIVITY

THE ROLE OF MONEYMAKING IN PRODUCTIVE ACTIVITY

The Division of Labor and Productive Activity

- The Doctrine That Only Manual Labor Is Productive

Productive Activity and Moneymaking

- Consumptive Production

Productive Expenditure and Consumption Expenditure

Capital Goods and Consumers’ Goods

- Classification of Capital Goods and Consumers’ Goods Not Based on Physical Characteristics
- Government a Consumer
- Producers’ Labor and Consumers’ Labor
- Producers’ Loans and Consumers’ Loans
- Government Borrowing
- Capital Goods and Consumers’ Goods Internally Produced; Other Revenues
- Capital and Wealth
- Capital Value and Investment
- Productive Expenditure and Capital Value
- Common Confusions About Capital Goods
- Answers to Misconceptions of the Concepts Presented
- Adam Smith on “Productive and Unproductive Labor”

Critique of the Concept of Imputed Income

Critique of the Opportunity-Cost Doctrine

READINGS/LECTURES

Reisman, *Capitalism,* pp. 441–462

Lectures: Reisman, "A Theory of Productive Activity, Profit, and Saving," Lecture 1

THE PRODUCTIVE ROLE OF BUSINESSMEN AND CAPITALISTS

The Productive Functions of Businessmen and Capitalists

Creation of Division of Labor

Coordination of the Division of Labor

Improvements in the Efficiency of the Division of Labor

The Productive Role of Financial Markets and Financial Institutions

The Specific Productive Role of the Stock Market

The Productive Role of Retailing and Wholesaling

The Productive Role of Advertising

READINGS/LECTURES

Reisman, *Capitalism,* pp. 462–473

Lecture: Reisman, "A Theory of Productive Activity, Profit, and Saving," Lecture 5

BUSINESSMEN AND CAPITALISTS: CLASSICAL ECONOMICS VERSUS THE MARXIAN EXPLOITATION THEORY

The Association Between Classical Economics and the Marxian Exploitation Theory

Correcting the Errors of Adam Smith: A Classical-Based Critique of the Conceptual Framework of the Exploitation Theory

Smith's Confusion Between Labor and Wage Earning

The Conceptual Framework of the Exploitation Theory

Smith's Failure to See the Productive Role of Businessmen and Capitalists and of the Private Ownership of Land

The Primacy-of-Wages Doctrine

A Rebuttal to Smith and Marx Based on Classical Economics: Profits, Not Wages, as the Original and Primary Form of Income

Further Rebuttal: Profits Attributable to the Labor of Businessmen and Capitalists Despite Their Variation With the Size of the Capital Invested

A Radical Reinterpretation of "Labor's Right to the Whole Produce"

Implications for the Incomes of "Passive" Capitalists

Acceptance of the Conceptual Framework of the Exploitation Theory by Its Critics

Necessary Revisions in Classical Economics

The Labor Theory of Value of Classical Economics

Harmonization of the Labor Theory of Value With Supply and Demand and the Productive Role of Businessmen and Capitalists

Other Classical Doctrines and the Rise in Real Wages

Classical Economics' Limitations on the Labor Theory of Value

The Actual Significance of Quantity of Labor in Classical Economics

The "Iron Law of Wages" of Classical Economics

Diminishing Returns and the Malthusian Influence

Ricardo's Reservations

Adam Smith's Mistaken Belief in the Arbitrary Power of Employers Over Wage Rates

Ricardo's Confusions Concerning the "Iron Law of Wages"

The Actual Meaning Ricardo Attached to "A Fall in Wages"
Classical Economics' Mistaken Denial of the Ability to Tax Wage Earners
Marxian Distortions of Classical Economics; The Final Demolition of the Exploitation Theory

READINGS/LECTURES

Reisman, *Capitalism,* pp. 441–500, 603–613
Lecture: Reisman, "A Theory of Productive Activity, Profit, and Saving," Lectures 2 and 4
Eugen von Böhm-Bawerk, "Unresolved Contradiction in the Marxian Economic System" in *Shorter Classics of Böhm-Bawerk.* This essay is better known under the title "Karl Marx and the Close of His System."
Eugen von Böhm-Bawerk, "The Exploitation Theory" in *Capital and Interest*, Vol. 1, *History and Critique of Interest Theories,* 241–321
Adam Smith, *The Wealth of Nations,* Book 1, Chapters 6–9
David Ricardo, *Principles of Political Economy and Taxation,* Chapters 1, 5, and 6
"The Martyrdom of the Industrialists" in Ayn Rand, *Atlas Shrugged,* reprinted in Ayn Rand, *For The New Intellectual*

UNIT 13. MONEY AND SPENDING

The Quantity Theory of Money
The Quantity Theory of Money as the Explanation of Rising Prices
The Origin and Evolution of Money and the Contemporary Monetary System
The Potential Spontaneous Remonetization of the Precious Metals
The Government and the Banking System
The Quantity of Money and the Demand for Money
Changes in the Quantity of Money as the Cause of Changes in the Demand for Money
The Demand for Money: A Critique of the "Balance of Payments" Doctrine
The Balance of Payments Doctrine and Fiat Money
The Balance of Payments Doctrine Under an International Precious Metal Standard
Inflation as the Cause of a Gold Outflow
Unilateral Free Trade and the Balance of Trade
Invariable Money
Invariable Money and the Velocity of Circulation
The Contribution of the Concept of Invariable Money to Economic Theory

READINGS/LECTURES

Reisman, *Capitalism,* pp. 503–541
Lecture: Reisman, "Introduction to Money," on disk 2 of "Lectures and Speeches on Economics and Politics"
Ludwig von Mises, *Human Action,* pp. 398–478, 780–803
Ludwig von Mises, *The Theory of Money and Credit,* pp. 9–410
Adam Smith "Of the Principle of the Commercial or Mercantile System" in *The Wealth of Nations,* Book 4, Chapter 1

UNIT 14. PRODUCTIONISM, SAY'S LAW, AND UNEMPLOYMENT

PRODUCTIONISM

Productionism Versus the Anti-Economics of Consumptionism

Depressions and Alleged "Overproduction"
Machinery and Unemployment
Alleged Inherent Group Conflicts Over Employment
Make-Work Schemes and Spread-the-Work Schemes
War and Government Spending
Population Growth and Demand
Imperialism and Foreign Trade
Parasitism as an Alleged Source of Gain to Its Victims
Advertising as Allegedly Fraudulent but Economically Beneficial
Misconception of the Value of Technological Progress
Increases in Production and Alleged Deflation
Consumptionism and Socialism

READINGS/LECTURES

Reisman, *Capitalism,* pp. 542–559
Lecture: Reisman, "An Introduction to Procapitalist Macroeconomics," Lecture 1
Henry Hazlitt, *Economics in One Lesson,* Chapters 1–12
Frederic Bastiat, *Economic Sophisms*
John R. McCulloch, *The Principles of Political Economy,* Part 1, Chapter 7

SAY'S (JAMES MILL'S) LAW

Monetary Demand and Real Demand
The Referents of Say's Law and Its Confirmation by Cases Apparently Contradicting It
Partial, Relative Overproduction
  Say's Law and Competition
Say's Law and the Average Rate of Profit
  Production and the Fallacy of Composition
Falling Prices Caused by Increased Production Are Not Deflation
  The Anticipation of Falling Prices
  Economic Progress and the Prospective Advantage of Future Investments Over Present Investments
  Falling Prices and Accumulated Stocks
  Falling Prices Resulting from a Larger Supply of Labor

READINGS/LECTURES

Reisman, *Capitalism,* pp. 559–580
Lecture: Reisman, "An Introduction to Procapitalist Macroeconomics," Lecture 2
Ludwig von Mises, *Planning for Freedom,* pp. 64–71
James Mill, "Consumption" and "Of the National Debt" in *Commerce Defended,* reprinted in *James Mill Selected Economic Writings*

UNEMPLOYMENT

The Free Market Versus the Causes of Mass Unemployment
  Full Employment, Profitability, and Real Wages
  Government Interference
Unemployment and the 1929 Depression
Unemployment, the New Deal, and World War II
  Why Inflation Cannot Achieve Full Employment
  Inflation Plus Price and Wage Controls
  World War II as the Cause of Impoverishment in the United States

Prosperity Based on the Return of Peace
A Rational Full-Employment Policy
Appendix to Chapter 13: Inventories and Depressions
Inventories and Capital
"Excess" Inventories, Malinvestment, and the Deficiency of Inventories
Inflation and Credit Expansion as the Cause of Malinvestment in Inventories
Why "Excess" Inventories and Monetary Contraction Are Associated

READINGS/LECTURES

Reisman, *Capitalism*, pp. 580–602
Lecture: Reisman, "An Introduction to Procapitalist Macroeconomics," Lecture 3

UNIT 15. THE PRODUCTIVITY THEORY OF WAGES

THE MARXIAN EXPLOITATION THEORY

The Influence of the Exploitation Theory
Marx's Distortions of the Labor Theory of Value
Implications for Value Added and Income Formation
Marx's Version of the Iron Law of Wages
The Rate of Exploitation Formula
Implications of the Exploitation Theory

READINGS/LECTURES

Reisman, *Capitalism*, pp. 603–613

THE PRODUCTIVITY THEORY OF WAGES

The Irrelevance of Worker Need and Employer Greed in the Determination of Wages
Determination of Real Wages by the Productivity of Labor
The Foundations of the Productivity of Labor and Real Wages: Capital Accumulation and Its Causes
Saving as a Source of Capital Accumulation
Technological Progress as a Source of Capital Accumulation
The Reciprocal Relationship Between Capital Accumulation and Technological Progress
The Economic Degree of Capitalism, the Wage "Share," and Real Wages
Other Factors, Above All Economic Freedom and Respect for Property Rights, as Sources of Capital Accumulation
The Undermining of Capital Accumulation and Real Wages by Government Intervention
The Nonsacrificial Character of Capital Accumulation Under Capitalism
Appendix to Section 3: An Analytical Refinement Concerning the Rate of Economic Progress
The Productivity Theory of Wages and the Interpretation of Modern Economic History
The Cause of Low Wages and Poor Working Conditions in the Past
How Real Wages Rose and the Standard of Living Improved
A Rise in the Productivity of Labor as the Only Possible Cause of a Sustained, Significant Rise in Real Wages
The Futility of Raising Money Wage Rates by Means of an Increase in the Quantity of Money or Decrease in the Supply of Labor
The Futility of a Rise in the Demand for Labor Coming at the Expense of the Demand for Capital Goods
The Futility of Raising the Demand for Labor by Means of Taxation
The Limited Scope for Raising Real Wages Through a Rise in the Demand for Labor

Critique of Labor and Social Legislation

Redistributionism

Labor Unions

Minimum-Wage Laws

Maximum-Hours Legislation

Child-Labor Legislation

Forced Improvements in Working Conditions

The Employment of Women and Minorities

The Productivity Theory of Wages and the Wages-Fund Doctrine

The Productivity Theory of Wages Versus the Marginal-Productivity Theory of Wages

The Productivity Theory of Wages and the Effect of Diminishing Returns

READINGS/LECTURES

Reisman, *Capitalism,* pp. 613–672

Lectures: Reisman, "An Introduction to Procapitalist Macroeconomics," Lectures 4–6

Lecture: Reisman, "A Theory of Productive Activity, Profit, and Saving," Lecture 6

Lecture: Reisman, "Capital, the Productive Process, and the Rate of Profit," Lecture 2

Ludwig von Mises, *Human Action,* pp. 479–523, 587–634, 716–734, 769–779

Ludwig von Mises, *Socialism,* pp. 457–515

Ludwig von Mises, *Planning for Freedom,* pp. 94–107, 195–214

Henry Hazlitt, *Economics in One Lesson,* Chapters 19–21, 24–26

James Mill, "Consumption" and "Of the National Debt" in *Commerce Defended,* reprinted in *James Mill Selected Economic Writings*

Nassau W. Senior, *Political Economy,* portion titled "Development of the Third Elementary Proposition"

Eugen von Böhm-Bawerk, "Control or Economic Law," in *Shorter Classics of Böhm-Bawerk*

F. A. Hayek, ed., *Capitalism and the Historians*

Robert Hessen, "The Effects of the Industrial Revolution on Women and Children" in Ayn Rand, ed., *Capitalism: The Unknown Ideal*

UNIT 16. AGGREGATE PRODUCTION, AGGREGATE SPENDING, AND THE ROLE OF SAVING IN SPENDING

Spending Not a Measure of Output

Shortcomings of Price Indexes

Gross National Product and the Issue of "Double Counting": *A* Is *A* Versus *A* Is *A+*

The Role of Saving and Productive Expenditure in Aggregate Demand

The Demand for *A* Is the Demand for *A*

The Demand for Consumers' Goods and the Demand for Factors of Production as
Competing Alternatives

Compatibility With the Austrian Theory of Value

Application to the Critique of the Keynesian Multiplier Doctrine

Saving Versus Hoarding

Saving as the Source of Most Spending

The "Macroeconomic" Dependence of the Consumers on Business

Saving as the Source of Increasing Aggregate Demand, Both Real and Monetary

Saving as the Source of Rising Consumption

Aggregate Economic Accounting on an Aristotelian Base

The Consumption Illusion of Contemporary National-Income Accounting

Gross National Revenue

More on the Critique of the Multiplier

Importance of Recognizing the Separate Demand for Capital Goods for the Theory of

Capital Accumulation and the Theory of National Income

The Inverse Relationship Between National Income and Economic Progress in an Economy With an Invariable Money

Overthrow of the Keynesian Doctrines of the Balanced-Budget Multiplier and the Conservatives' Dilemma

READINGS/LECTURES

Reisman, *Capitalism,* pp. 441–447 (review), 673–718

Lecture: Reisman, "Capital, the Productive Process, and the Rate of Profit," Lecture 1

Lecture: Reisman, "A Theory of Productive Activity, Profit, and Saving," Lecture 6

Adam Smith, "Of the Accumulation of Capital, or of Productive and Unproductive Labour" in *The Wealth of Nations,* Book 2, Chapter 3

John Stuart Mill, *Principles of Political Economy,* Book 1, Chapters 3–5

UNIT 17. THE NET-CONSUMPTION/NET-INVESTMENT THEORY OF PROFIT AND INTEREST

THE POSITIVE THEORY

The Nature and Problem of Aggregate Profit

The Treatment of Interest

The Rate of Profit Not Based on Demand and Supply of Capital, but on the Difference Between the Demand for Products and the Demand for Factors of Production

Determinants of the Average Rate of Profit in the Economic System Different from Determinants of the Rate of Profit of the Individual Company or Industry

Critique of the Doctrine That the Interest Rate on Government Bonds Expresses the Pure Rate of Return to Which Risk Premiums Are Added

The Path of Explanation: Net Consumption and Net Investment

The Problem of Aggregate Profit: Productive Expenditure and the Generation of Equivalent Sales Revenues and Costs

Net Consumption and the Generation of an Excess of Sales Revenues Over Productive Expenditure

Net Consumption: Its Other Sources, Wider Meaning, and Relationship to the Saving of Wage Earners

Confirming the Critique of the Exploitation Theory

The Net-Consumption Theory Further Considered

Why Businessmen and Capitalists Cannot Arbitrarily Increase the Rate of Net Consumption and the Rate of Profit

The Net-Consumption Rate and the Gravitation of Relative Wealth and Income

Accumulated Capital as a Determinant of Net Consumption

An Explanation of High Saving Rates Out of High Incomes

Net Consumption and Time Preference

Net Investment as a Determinant of Aggregate Profit and the Average Rate of Profit

Net Investment Versus Negative Net Consumption

The Prolongation of Net Investment Under an Invariable Money

Net Investment as the Result of the Marginal Productivity of Capital Exceeding the Rate of Profit

Net Investment as a Self-Limiting Phenomenon

Capital Intensification and the Tendency Toward the Disappearance of Net Investment Under an Invariable Money

The Process of Capital Intensification

The Addition to the Rate of Profit Caused by Increases in the Quantity of Money

The Impact of Increases in the Quantity of Money on the Net-Investment and Net-Consumption Rates

Increases in the Quantity of Money and the Perpetuation of Net Investment

THE NET-CONSUMPTION/NET-INVESTMENT THEORY AND ALTERNATIVE THEORIES

READINGS/LECTURES

Reisman, *Capitalism,* pp. 719–808
Lectures: Reisman, "Capital, the Productive Process, and the Rate of Profit," Lectures 3–6
Ludwig von Mises, *Human Action,* pp. 524–537
Eugen von Böhm-Bawerk, *Capital and Interest,* Vol. 2, Introduction, pp. 3–118, 259–381; Vol. 3, pp. 1–77, 137–212

UNIT 18. APPLICATIONS OF THE INVARIABLE-MONEY/NET-CONSUMPTION ANALYSIS

Short-Term Results

Profits, the Balance of Trade, and the Need for Laissez Faire in the United States

Implications for the Theory of Saving

Net Saving and Increases in the Quantity of Money

Why the Actual Significance of Saving Lies at the Gross Level

Net Saving and the Rate of Profit

More on Saving and "Hoarding": "Hoarding" as a Long-Run Cause of a Rise in the Rate of Profit

Implications for the Critique of Keynesianism

Critique of the Investment-Opportunity and Underconsumption/Oversaving Doctrines

The Basic Error of Underconsumptionism

How the Demand for Capital Goods and Labor Can Radically and Permanently Exceed the Demand for Consumers' Goods

Consumption as the Purpose of Production and the Progressive Production of Consumers' Goods Over Time

The Ratio of Demands Between Stages

More on the Average Period of Production

A Rise in the Demand for Capital Goods and Fall in the Demand for Consumers' Goods: The Cross-Hatching of Production

More on Why Savings Cannot Outrun the Uses for Savings

Capital Intensiveness and Land Values

The Housing Outlet and Consumer Interest

The Automatic Adjustment of the Rate of Saving to the Need for Capital

READINGS/LECTURES

Reisman, *Capitalism,* pp. 809–862

Lectures: Reisman, "Capital, the Productive Process, and the Rate of Profit," Lectures 4–6

David Ricardo, *Principles of Political Economy and Taxation,* Chapters 7, 8, 20, and 21

UNIT 19. KEYNESIANISM: A CRITIQUE

The Essential Claims of Keynesianism

Neo-Keynesianism

The Unemployment Equilibrium Doctrine and Its Basis: The *IS* Curve and Its Elements

The Grounds for the *MEC* Doctrine

The Keynesian Solution: "Fiscal Policy"

Critique of the *IS-LM* Analysis

The Declining-Marginal-Efficiency-of-Capital Doctrine and the Fallacy of Context Dropping

The Marginal-Efficiency-of-Capital Doctrine and the Claim That the Rate of Profit Is Lower in the Recovery from a Depression Than in the Depression

The Unemployment Equilibrium Doctrine and the Claim That Saving and Net Investment Are at Their Maximum Possible Limits at the Very Time They Are Actually Negative

The Marginal-Efficiency-of-Capital Doctrine's Reversal of the Actual Relationship Between Net Investment and the Rate of Profit

The Contradiction Between the Marginal-Efficiency-of-Capital Doctrine and the Multiplier Doctrine

A Fall in Wage Rates as the Requirement for the Restoration of Net Investment and Profitability Along With Full Employment

Wage Rates, Total Wage Payments, and the Rate of Profit

Critique of the "Paradox-of-Thrift" Doctrine

Critique of the Saving Function

Critique of the "Liquidity-Preference" Doctrine

The Economic Consequences of Keynesianism

The Growth in Government

Budget Deficits, Inflation, and Deflation

Keynesianism and Economic Destruction

Why Keynesianism Is Not a Full Employment Policy

Keynesianism Versus the Rate of Profit: "The Euthanasia of the Rentier" and "The Socialization of Investment"

READINGS/LECTURES

Reisman, *Capitalism*, pp. 863–894

Henry Hazlitt, *The Failure of the "New" Economics*

Henry Hazlitt, Editor, *The Critics of Keynesian Economics*

UNIT 20. GOLD VERSUS INFLATION

INFLATION OF THE MONEY SUPPLY VERSUS ALTERNATIVE THEORIES OF RISING PRICES

The Analytical Framework of the Quantity Theory of Money

The Vital Demand/Supply Test for All Theories of Rising Prices

The Elimination of Less Supply as the Cause of an Inflationary Rise in Prices

Refutation of the "Cost-Push" Doctrine in General

Critique of the "Wage-Push" Variant

Critique of the "Profit-Push" Variant

Critique of the "Crisis-Push" Variant

Critique of the Wage-Price Spiral Variant

Critique of the "Velocity" Doctrine

Critique of the "Inflation-Psychology" Doctrine

Critique of the Credit-Card Doctrine

Critique of the Consumer-Installment-Credit Doctrine

Critique of the Consumer-Greed Doctrine

The Meaning of Inflation

READINGS/LECTURES

Reisman, *Capitalism*, pp. 895–922

Lectures: Reisman, "Inflation and Price Controls," Lectures 1–3 (1st half)

Lecture: Reisman, "The Economics of Inflation," on disk 2 of "Lectures and Speeches on Economics and Politics"

Ludwig von Mises, *Planning for Freedom*, pp. 150–161

THE DEEPER ROOTS AND FURTHER EFFECTS OF INFLATION

The Connection Between Inflation and Government Budget Deficits

Budget Deficits and the Monetary Unit

The Motives and Rationale for Deficits and Inflation

The Welfare State

Inflation and War Finance

Inflation and the "Easy Money" Doctrine

Inflation as the Alleged Cure for Unemployment

The Underlying Influence of the Socialist Ideology

Inflation and Deficits Versus Representative Government and Economic Freedom
Inflation as the Cause of a Redistribution of Wealth and Income
Inflation and the Destruction of Capital
- Reversal of Safety
- Tax Effects
- The Prosperity Delusion and Overconsumption
- Malinvestment
- The Withdrawal-of-Wealth Effect

Consequences of the Destruction of Capital
- Reduction of the Real Rate of Return
- The Gains of Debtors Less Than the Losses of Creditors
- The Impoverishment of Wage Earners
- The Stock Market and Inflationary Depression

Inflation as the Cause of Depressions and Deflation
- Gold Clauses and Prospective Inflation of Paper as the Cause of Deflation in Gold

Inflation as the Cause of Mass Unemployment
The Inherent Accelerative Tendencies of Inflation
- The Welfare-State Mentality
- Inflation to Solve Problems Caused by Inflation
- Recessions as Inflationary Fueling Periods
- Indexing and the Wage and Interest Ratchets
- The Current State of Inflation
- Inflation and the Potential Destruction of the Division of Labor

READINGS/LECTURES
- Reisman, *Capitalism*, pp. 922–950
- Ludwig von Mises, *Planning for Freedom*, pp. 83–93
- Adam Smith, "Of Public Debts" in *The Wealth of Nations*, Book 5, Chapter 3

GOLD

Freedom for Gold as the Guarantee Against the Destruction of Money
- A Proper Gold Policy for the Government

The Case For a 100-Percent-Reserve Gold Standard
- Falling Prices Under the 100-Percent-Reserve Gold Standard Would Not Be Deflationary
- The 100-Percent-Reserve Gold Standard as the Guarantee Against Deflation
- Further Virtues of the 100-Percent-Reserve Gold Standard
- The Moral Virtue of the 100-Percent-Reserve Gold Standard
- The Monetary Role of Silver

The 100-Percent-Reserve Gold Standard as the Means of Ending Inflation Without a Depression
- The 100-Percent-Reserve Gold Standard, Liquidity, and the Dismantling of the Welfare State

READINGS/LECTURES
- Reisman, *Capitalism*, pp. 951–966
- Lecture: "Monetary Reform," on disk 2 of "Lectures and Speeches on Economics and Politics"
- Lecture: Reisman, "Gold: the Solution to Our Monetary Dilemma," on disk 2 of "Lectures and Speeches on Economics and Politics"
- Ludwig von Mises, *Human Action*, pp. 538–586
- Ludwig von Mises, *The Theory of Money and Credit*, pp. 413–457, 461–483
- Ludwig von Mises, *Planning for Freedom*, pp. 50–63, 185–194
- Henry Hazlitt, *Economics in One Lesson*, Chapter 23

Henry Hazlitt, Editor, Andrew Dickson White, *Fiat Money Inflation in France*. Irvington-on-Hudson, New York: Foundation for Economic Education, 1960.
Murray Rothbard, *What Has Government Done to Our Money?*
Charles Holt Carroll, *Organization of Debt into Currency*

UNIT 21. TOWARD THE ESTABLISHMENT OF LAISSEZ-FAIRE CAPITALISM

Introduction
The Importance of Capitalism as a Conscious Goal
The Capitalist Society and a Political Program for Achieving It
Privatization of Property: Importance of Fighting on Basis of Principles
The Freedom of Production and Trade
Appropriate Compromises
The Case for the Immediate Sweeping Abolition of All Violations of the Freedom of Production and Trade
Abolition of the Welfare State
Elimination of Social Security/Medicare
Elimination of Public Welfare
Elimination of Public Hospitals
Firing Government Employees and Ending Subsidies to Business
Escaping from Rent Control With the Support of Tenants
Abolition of Income and Inheritance Taxes
Establishment of Gold as Money
Procapitalist Foreign Policy
Freedom of Immigration
Friendly Relations With Japan and Western Europe
Separation of State from Education, Science, and Religion
Abolition of Public Education
Separation of Government and Science
Separation of State and Church
A General Campaign at the Local Level
The Outlook for the Future

READINGS/LECTURES

Reisman, *Capitalism*, pp. 969–990
Lecture: Reisman, "Interventionism," on disk 2 of "Lectures and Speeches on Economics and Politics"
Lecture: Reisman, "Regulating Economic Growth, A Debate: George Reisman vs. Ray Catalano," on disk 2 of "Lectures and Speeches on Economics and Politics"
Lecture: Reisman, "The Future of Liberty," on disk 2 of "Lectures and Speeches on Economics and Politics"
Lecture: Reisman, "Toward the Establishment of a Capitalist Society," on disk 2 of "Lectures and Speeches on Economics and Politics"
Ludwig von Mises, *Planning for Freedom*, pp. 173–184
Ayn Rand, "The Anatomy of Compromise," "The Pull Peddlers," "Extremism: or the Art of Smearing," "The Obliteration of Capitalism," and "Conservatism: An Obituary" in Ayn Rand, ed., *Capitalism: The Unknown Ideal*
Ayn Rand, "Fairness Doctrine for Education" and "What Can One Do?" in Ayn Rand, *Philosophy: Who Needs It*
Ayn Rand, "The Question of Scholarships," "Tax Credits for Education," "Representation Without Authorization," and "How Not to Fight Against Socialized Medicine" in Ayn Rand, *The Voice of Reason*

FIRST COURSE

SYLLABUS AND SYLLABUS SUPPLEMENTS

COURSE OBJECTIVES

1. To provide the student with a comprehensive knowledge of the nature, foundations, and operations of a division-of-labor, capitalist society, with special emphasis on the institutions of private ownership of the means of production, competition, the profit motive, and the price system as the basis for economic coordination and economic progress. The consequences of government intervention with respect to these institutions will be considered in depth.

2. To teach the student to think of economic phenomena in terms of their long-run effects on all groups, not merely their short-run effects on those directly concerned.

OVERVIEW OF THE COURSE

The course will focus on five main current problem areas: 1) The validation of economic activity and fundamental economic institutions in the face of widespread criticisms. 2) Environmentalism and energy supplies. 3) Economic "planning" and the reasons for the worldwide collapse of socialism. 4) The monopoly question and antitrust policy. 5) Prevailing ideas on the nature of productive activity and the effect of government intervention on the standard of living of the average wage earner.

Two leading themes of the course will be 1) The possibility of continuous economic progress based on the combination of economic freedom, private ownership of the means of production, division of labor, saving, and technological progress. 2) The ethical implication of the harmony of the rational self-interests of all men under capitalism.

BOOKS FOR THE COURSE

A. George Reisman, *Capitalism: A Treatise on Economics*

B. Ludwig von Mises, *Human Action*, Third Edition (paperback).

[In some years I used von Mises's *Socialism* instead of *Human Action.* The reading assignments in *Socialism* appear in brackets throughout this syllabus. Please note that the page references are those of the Jonathan Cape edition, which can be found in the Liberty Press Edition.]

C. Paul Samuelson and William Nordhaus, *Micro-Economics* (paperback), 15th Edition, (New York: McGraw Hill, 1995).

[I include Samuelson in my university courses in order to avoid the charge of being "one-sided." Somehow professors who use only Samuelson or the equivalent, who have never even heard of von Mises, much less assign his writings, do not have to worry about being considered "one-sided." They are automatically presumed to be fair-minded scholars, who present all viewpoints that those who know little or nothing about capitalism believe should be presented. Participants in this program who think that they need to learn more about leftwing arguments from their supporters should read the assignments in Samuelson and, to the extent necessary, the titles listed in the bibliography to *Capitalism* under the heading "The Enemies of Capitalism."]

COURSE CONTENT AND READING ASSIGNMENTS

[Note: This course meets just once a week, for four academic hours. This explains why the midterm examination coincides with the seventh class session.]

Week 1

Introduction: The nature and value of economics. An overview of the subject's content and history. Principal applications. The philosophical foundations of economic activity. Economics and capitalism.

READINGS

Reisman: Introduction and Chapter 1

von Mises, *Human Action:* pp. 1-3, 7-10, 862-885. Also see glossary at the end of this syllabus.

Week 2

The role of wealth in human life. "Scarcity" and the limitless need for wealth. The law of diminishing marginal utility and its reconciliation with the limitless need for wealth.

READINGS

Reisman: Chapter 2

von Mises, *Human Action:* pp. 257-326
[von Mises, *Socialism*: 289–313, 395-403, 452-453]
Samuelson: *Optional:* Chapter 1

Week 3

Natural resources, the law of diminishing returns, and conservationism. The ecological critique of economic progress: a rebuttal.

READINGS

Reisman: Chapter 3
von Mises, *Human Action:* pp. 119-131, 654-663
[von Mises, *Socialism:* pp. 404–408]
Samuelson, pp. 96–97 (upper left); *Optional:* Chapter 19

Week 4

The division of labor as the central requirement of a high and rising output per capita; its advantages and alleged shortcomings. Dependence of the division of labor on the economic institutions of capitalism, especially the price system. Prices, economic planning, and economic coordination.

READINGS

Reisman: Chapter 4; Chapter 5, Part A; Chapter 8
von Mises, *Human Action:* pp. 143-176

Week 5

Demand and supply curves. The law of demand. Elasticity of demand.

The uniformity-of-profit principle and its applications to consumer sovereignty, economic progress, farm subsidies, rent and price controls, profit taxes, and racial discrimination.

READINGS

Reisman: Chapter 5, Part B; Chapter 6, Part A
Samuelson: Chapters 3–5 (to p. 86)

Week 6

Tendencies toward uniform prices over space and time; applications to the Arab oil embargo and commodity speculation. Tendency toward a uniformity of wage rates at any given level of ability. Equal pay for equal work. Permanent inequalities in wage rates. Prices and costs of production. Ultimate analysis of cost of production. Cost of production and supply and demand.

READINGS

Reisman: Chapter 6, Part B
Samuelson: Chapter 6, Part A; Chapter 7, Parts A and C

Week 7

MIDTERM EXAMINATION

Following Midterm: Pricing of goods and services in limited supply. Costs and economic coordination.

Week 8

The free market's efficiency in responding to economic change. Factor prices. Price controls, shortages, and economic chaos. Illustrations from the energy crisis and rent controls. From partial price controls to universal price controls.

READINGS

Reisman: Chapter 7
von Mises, *Human Action:* pp. 730-736, 758–769; [von Mises, *Socialism:* pp. 527–543]

Week 9

Universal price controls and *de facto* socialism. The chaos of socialism. Understanding the collapse of Soviet Russia and the communist bloc on the basis of price theory. The tyranny of socialism.

READINGS

Reisman: Chapter 8
von Mises, *Human Action:* pp. 689–710, 716–719, 732–736; *Optional:* pp. 710–715
[von Mises, *Socialism*: pp. 114–142, 196–220, 516–521]
Samuelson: Chapters 8–10; Chapter 18, Part B

Week 10

The influence of the division of labor on private ownership of the means of production. Implications for redistributionism, inheritance, taxation, and land rent. Economic freedom, territorial sovereignty, and peaceful international relations.

READINGS

Reisman: Chapter 9, Parts A and B
von Mises, *Human Action:* pp. 737-742, 804-832, 664-688; [von Mises, *Socialism:* pp. 37–42]

Week 11

Economic inequality and economic competition. Equality of opportunity. The law of comparative advantage and the pyramid-of-ability principle. Free international trade. Population growth and the freedom of immigration.

READINGS

Reisman: Chapter 9, Part C
von Mises, *Human Action:* pp. 743-757, 833-861; [von Mises, *Socialism:* pp. 314–358]
Optional: Samuelson: Chapter 22

Week 12

The monopoly question. The political versus the economic concept of monopoly. Capital requirements and entry “barriers.” The alleged tendency toward universal monopoly. The predatory-pricing doctrine. Marginal revenue and marginal cost. The pure-and-perfect-competition, oligopoly, and monopolistic-competition doctrines.

READINGS

Reisman: Chapter 10; [*Optional:* von Mises, *Socialism:* 361–392]

Weeks 13 & 14

The division of labor and the concept of productive activity. Exposition and critique of the Marxian exploitation theory. The productivity theory of wages. Labor unions and labor legislation. A reinterpretation of modern economic history. The productive functions of businessmen and capitalists, of retailing, wholesaling, and advertising.

READINGS

Reisman: Chapters 11 and 14
von Mises, *Human Action:* pp. 592-623, 628-634, 769-779
Optional: Samuelson, Chapter 13

FINAL EXAMINATION

(Accompanies Weeks 1–3)

I. The Nature and Value of Economics

A. Some Definitions

l. Economics: the science that studies the production of wealth under a system of division of labor

2. The division of labor: the separation of the total labor required to serve human life and well-being into separate, distinct occupations. In a division of labor society, each person lives by producing or helping to produce just one or, at most, a very few things and is supplied by the labor of others for practically all of his wants.

B. The Need for Economics; Leading Applications of the Subject

The division of labor doesn't exist or function automatically—e.g., fall of Rome, rise of U.S. and Western World; it depends on human choices; thus knowledge of its nature and requirements is necessary

1. Survival of material civilization:
2. Understanding history and the present-day world
3. Solving current economic problems—e.g., unemployment, inflation, stagnation, shortages, international economic conflict
4. Business and financial applications—influence of anti-business ideas; defending the freedom of businessmen to make money
5. Personal, philosophical applications—understand own and others' economic role, not feel chronically victimized or regard self as victimizer because successful

II. Theme of Course: The Division of Labor Depends on the Institutions of Capitalism

1. Definitions

    a. capitalism: a politico-economic system based on private ownership of the means of production and characterized by the pursuit of material self-interest under freedom
    b. freedom: the absence of the initiation of physical force
    c. freedom and the necessity of limited government

2. The philosophical foundations of capitalism and economic activity

    a. secularism
    b. acceptance of causality—influence on: science and technology; willingness to work hard; self-responsibility; saving and capital accumulation
    c. acceptance of power of reason: consequent view of Man and the individual as valuable and competent—the base for the acceptance of the idea of individual rights and economic freedom; connection to great entrepreneurship

3. Capitalism: its nature and origin. The "spontaneous" emergence of capitalist institutions based on the rational pursuit of material self-interest under freedom: private property and private ownership of the means of production; saving and capital accumulation; economic inequality; the division of labor; exchange and money; financial self-interest and the profit motive; economic competition; the price system. The economic history of the U.S. as illustration.

4. The controversial character of economics and capitalism

    a. the assault on economic activity and capitalism
    b. economics versus unscientific personal observations
    c. economics versus altruism
    d. economics versus irrational self-interest
    e. economics versus irrationalism

III. Wealth and the Economic Problem

A. The Wealth Centeredness of Economics

1. Wealth: material goods made by man

2. Goods (economic goods): things recognized as having the power to serve a human need or want, requiring the performance of labor or effort to be enjoyed, and over which we possess sufficient command gainfully to direct them to the satisfaction of our needs or wants. Examples of things that are not (economic) goods:

   a. atmospheric air and sunlight
   b. oil or uranium before their uses discovered
   c. iron on Mars
   d. desert land
   e. "imaginary goods"—e.g., rabbit's feet, tarot cards

3. The service industries as almost entirely auxiliary to the production or distribution of wealth.

B. "Scarcity"

1. No matter how abundant, wealth is always "scarce" in the sense that the need and desire for wealth is still greater.

2. Scarcity in this sense operates *against* scarcity in the sense of scantiness, insofar as it leads people to increase production—e.g., increasing food production to provide meat safeguards against famines; to provide steak, safeguards against a scantiness of meat, and so on.

3. The ineradicability of "scarcity"

   a. not eliminated by more workers—correspondingly more needs and desires
   b. not eliminated by rise in the productivity of labor—new desires for products accompany the new methods of production

C. The Objective Basis of the Limitless Desire for Wealth

1. The scope of the need for wealth: not just food, clothing, and shelter, but:

   a. art, science, music, athletics, human relationships—virtually every human activity without exception depends upon or is substantially facilitated by the use of wealth adapted to it. (Try to think of exceptions)
   b. the psychological-aesthetic aspects of the satisfaction of physical needs; variety and novelty

2. The perfectibility of human need satisfactions and the use of human faculties: the wealth applicable to the needs for nutrition and health; to the use of our eyes, ears, limbs, and minds.

3. The fundamental bases of our limitless desire and need for wealth: the capacity of our imaginations exceeds the power of our arms; our possession of reason gives us the potential for a limitless range of knowledge and awareness, hence, of action and experience; wealth is the material means of action and experience—in the form of instrumentalities (e.g., tools and machines) and objects of contemplation (e.g., works of art, landscaped grounds); our desire for wealth exceeds our means of producing it because of the abstract nature of knowledge, which has no fixed limits, while our physical capacities are always strictly limited.

4. The "naturalness" and "necessity" of economic progress.

   a. the result of the use of reason as a constant
   b. our awareness of the future and its impact on our happiness in the present.
   c. the need to offset the operation of the law of diminishing returns

5. The division of labor and capitalism the on-going solution to raising the productivity of labor in the face of a limitless need and desire for wealth.

D. The Law of Diminishing Marginal Utility and Its Reconciliation with the Limitless Need for Wealth

1. Statement of the law: *the utility, importance, or subjective value that is attached to a unit of a good diminishes as the quantity of the good one consumes or possesses increases.* The examples of successive glasses of water and Böhm-Bawerk's pioneer with the five sacks of grain.

2. Basis of the law:

a. the progressive satisfaction of wants, so that each additional unit confronts a want that is already more and more satisfied

b. the rational choice to satisfy our more urgent wants ahead of our less urgent wants, leaving only wants of progressively less urgency to be satisfied by succeeding units

3. Observations:

a. the substitutability of units, with the result that the utility of each unit equals that of the marginal unit

b. the marginal unit serves the least important of the most important wants that the supply can serve

4. The reconciliation of diminishing marginal utility with the principle that our need for wealth is limitless (a reply to Galbraith's criticism):

a. so long as there is any marginal utility at all, the utility of a larger supply is always greater than the utility of a smaller supply

b. the availability of more wealth is caused by a process that at the same time raises the marginal utility of additional units of wealth—i.e., more efficient methods of production are accompanied by new types of consumers' goods, which represent new, more important uses for wealth, e.g., the electric motor and all the electrical appliances

c. with the availability of more wealth, the size of the marginal unit tends to increase: e.g., a house versus a hut, a car versus a horse and wagon, a hundred dollars or a thousand dollars versus one dollar or ten dollars; the marginal utility of the second house or car is less than that of the first house or car, but almost certainly greater than that of the second hut or horse. On the basis of such examples, it is mistaken to conclude that the utility of the marginal units *actually under consideration in real life* diminishes as wealth increases, or that the importance of the pursuit of additional wealth diminishes.

d. the ideal arrangement is for the marginal utility of any given sum of wealth to steadily diminish toward the vanishing point, while we deal with larger and larger sized units

5. Applications of the principle of diminishing marginal utility:

a. resolution of the value paradox of classical economics

b. recognition of the actual role of cost of production in price determination—Böhm-Bawerk's explanation

c. consumer spending patterns

d. Say's Law and relative overproduction and underproduction

E. The Assault on Wealth

1. The moralistic denigration; asceticism—the confusion of pleasure and pain.

2. The doctrines of conspicuous consumption and cultural relativism; why wealth *deserves* prestige; the objective advantages of an economically successful culture; socialism and non-material incentives

3. Wealth as the alleged cause of poverty: the overproduction and underconsumption doctrines (elaborated in Second Course)

4. The ecology doctrine

IV. Natural Resources and the Environment

A. The Limitless Potential of Natural Resources

Matter and energy supplied by nature. Goods and wealth character supplied by man. Expandability of the supply of economically useable, accessible natural resources.

B. The Law of Diminishing Returns

1. Statement of the law: *If increasing quantities of a factor of production (or a group of factors of production) are applied to the production of a product, while the quantity of all the other, complementary factors of production is held fixed, then, beyond a certain point, additional output will be less than proportional to the additional input.*

2. Classic illustration of the law: the application of successive equal doses of labor and capital to a fixed quantity of land. The need for more land.

Ricardo and grades of land of decreasing quality.

3. Basis of the law:

   a. physical: "quantitative definiteness"

   b. rational self-interest: choose most productive uses of a factor of production first, leaving only less productive uses for later (this principle applies to Ricardo's grades of land case)

4. Reconciliation of the law with the limitless potential of natural resources: the law applies at any given time, not over time; improving technology and capital equipment can constantly raise the point from which returns diminish; the operation of quantitative definiteness can be offset by our ability to manipulate larger quantities of matter and by our ability to manipulate properties of pieces land (and other forms of matter) that we were unable to manipulate before (e.g., trace elements, new strains of seed, hydroponics, etc.); economic progress permits *less* labor to be employed in agriculture and mining.

5. Applications of the law of diminishing returns:

   a. Why aren't pieces of land and mines exploited to the maximum possible extent?

   b. Why production is not limited by a lack of natural resources even in the short run.

6. Diminishing returns and the need for economic progress

C. Implications for the Ecology Doctrine

1. Why the inherent tendency of production is to *improve* the environment.

2. How the populations of species and the quality of water and air support this proposition.

3. The ethical perspective of the ecology movement: the intrinsic-value doctrine and its implications.

4. Environmentalism, collectivism, and socialism. The alternative of individualism and capitalism as the means of solving alleged global problems.

V. The Gains from the Division of Labor

1. The multiplication of knowledge; the ability to produce products that would otherwise be impossible
2. The benefit from geniuses and other rare talents
3. Concentration on all individual advantages—the Crusoe-Friday example of deer and salmon
4. Economies of learning and motion

   a. ratio of application time to learning time—more learning

   b. subconscious automatizing of motions

   c. elimination of wasted motions in changing positions and operations

   d. specialization in dissemination of knowledge

5. Geographical specialization

6. The gains from machinery attributable to division of labor

    a. sufficient fund of knowledge and materials
    b. science and invention as specializations
    c. simplification of design
    d makes use of machinery pay

    Why the Industrial Revolution began in England

A. Some Implications of the Division of Labor

1. Appropriateness to Man's mind, body, and nature-given environment—accomplish more with the same
2. The individual and society
3. Self-interest and ethics: objective value of other people—their existence and freedom

B. Criticisms of the Division of Labor and Rebuttal

1. The alleged narrowness and one-sidedness of the worker
2. "Alienation" and boredom—rebuttal:

    a. how the division of labor creates the opportunity for everyone to *be* a "Renaissance Man"
    b. how it operates against alienation via providing wealth and leisure and thus education—the means to understand and control one's environment; anti-intellectuality of the alienation charge
    c. anti-boredom: housewives and money motivation; how practically every job could be made challenging (piece-work and team competition), and what prevents it (i.e., unions: anti-piece-work, anti-worker competition, prevent firing bad workers—create split between work and worker's self-interest)

(Accompanies Week 4)

VI. The Dependence of the Division of Labor on the Institutions of Capitalism

A. The Dependence of the Division of Labor on Private Ownership of the Means of Production

1. The direct dependence: separate, independent minds and knowledge; need separate, independent action—separate, independent production—and thus separate, independent wealth holdings—i.e., private property and private ownership of the means of production.

2. The incompatibility of collectivism and socialism—*viz.,*functioning as an indivisible unit—with a division-of-labor society: all or some must know all.

   a. the absurdity of "central planning"; b. contradictory partial planning under socialism
   c. socialist discoordination and the destruction of the division of labor; Western aid and trade prevented famine and collapse

3. The indirect dependence of the division of labor on private ownership of the means of production: the need for a price system as the foundation of economic planning.

   a. the unseen economic planning of capitalism: its existence all around us; its basis in prices; the coordinating function of prices: the harmoniously integrated planning of the capitalist system by tens of millions of separate, independent planners.
   b. the dependence of the price system on the profit motive and competition; the dependence of these on the institution of private ownership of the means of production

B. The Dependence of the Division of Labor on Exchange and Money

1. The need for exchange in a division-of-labor society.

2. The need for *monetary* exchange.

   a. the radical increase in the extent of the division of labor
   b. the ability to make economic calculations and thus comparisons—between input and output, different methods of production, and different industries

C. The Dependence of the Division of Labor on Saving and Capital Accumulation

1. The initial rise in the productivity of labor in agriculture.

2. The division of payments.

D. The Dependence of the Division of Labor on the Freedom of Competition

1. The organization of the division of labor with respect to persons for jobs, products for markets, and technological methods of production.

2. The protection against the exercise of arbitrary power by the companies or workers of any given vital industry.

E. The Dependence of the Division of Labor on the Freedom of Economic Inequality

1. Forced equality and the destruction of causality in production; the destruction of causality in cost—e.g., socialized medicine.

2. Great achievers and great inequality as the means to great achievement.

3. The connection between economic inequality and differences in the degree of saving.

4. Economic inequality and the ability of the less able to compete against the more able.

(Accompanies Weeks 5 and 6)

VII. Demand and Supply

A. Classical Demand and Supply

1. Expenditure and quantity sold; price as the ratio of the demand to the supply.

2. Makes clear the relationship between the direction of price changes and the direction of demand and supply changes. Valuable in "macroeconomics," where competitive factors cancel out.

B. Contemporary Demand and Supply.

1. Schedules or curves: *the set of quantities buyers are prepared to buy or sellers to sell at varying prices, arranged in descending (ascending) order, all other things equal*.

2. For a hypothetical demand and supply schedule, see Figure 5–1 on p. 153 of *Capitalism*

3. Reproduce the diagram based on the data in columns 1–3 of Table 5–1 on p. 152 of *Capitalism.*

4. The law of demand: *other things equal, the quantity demanded increases as the price decreases, and decreases as the price increases; to sell a larger quantity requires a lower price, while a smaller quantity for sale will bring a higher price.*

5. Reasons for the law of demand:

   a. Marginal utility must be above the price; a drop in price puts the price below the marginal utility of additional units and so makes their purchase advantageous. Marginal utility and price "sandwiching."
   b. Substitution effect.
   c. Income effect.

6. Change in quantity demanded versus change in demand—see the column Quantity Demanded II in Table 5–1. Derive the diagram $D'D'$ in Figure 5–1.

7. Reasons for changes in demand: changes in: quantity of money, income, prices of substitutes or complements, knowledge, tastes and preferences; development of new substitutes or of substitutes for complements.

C. Elasticity of Demand

1. Meaning: *the percentage change in the quantity demanded divided by the percentage change in price.*

2. The total revenue test.

3. Examples of elastic, inelastic, and unit elastic demand.

   a. Elastic: close substitutes, luxury goods.
   b. Inelastic: poor substitutes, necessities.
   c. Unit elastic: aggregate spending.

4. Applications of concept of elasticity: employment effects of machinery, the profitability of charging a different price where there is little or no competition.

5. The elasticity of demand for a particular company under freedom of competition almost always much greater than for the industry as a whole.

6. Income and cross elasticity.

7. Elasticity changes even over the length of the same demand curve.

8. No constancy of elasticities.

D. Supply Curves

1. Basic case is vertical supply curve—reflecting a given quantity that sellers are prepared to sell at best price they can obtain.

2. Reasons for supply curves sloping up and to the right.

   a. The marginal utility of sellers—actually not a significant reason.
   b. Riding up other demand curves (case of broader fixed supply—e.g., wheat, gasoline in different partial markets).

3. Partial equilibrium and the confusion between cost of production and supply and demand as the determinant of price.

   a. Upward sloping supply curve typically thought to reflect law of diminishing returns. Most prominent in agriculture and mining. And here not usually relevant in the short run, in which supplies of agricultural commodities are simply given.
   b. *Horizontal* supply curve (the most common case, prevailing throughout manufacturing and retailing) actually represents determination of price by sellers, *based on consideration of costs of production.* Equilibrium price only apparently determined by the intersection of the supply and demand curves here.
   c. Economies of scale and a downward sloping supply curve—again, price actually based on consideration of cost of production.
   d. Ricardo and Böhm-Bawerk on the comparative influence of the buyers and sellers in determining prices—each correct in a different context.

E. Some Errors to Avoid

1. Why it is incorrect to try to derive S and D curves by observing prices and quantities bought and sold over time: all we observe are intersection points of any number of possible S and D curves; with any price change, at least one of them must be different; the curves highly volatile; no reason to assume even one of them the same one over time.

2. The existence of a rising price accompanied by a rising quantity demanded does not invalidate the downward slope of the demand curve: a change in the curve present.

VIII. The Uniformity-of-Profit Principle

A. Statement and Explanation of the Principle

1. *The rate of profit (return) on capital invested tends toward uniformity in all branches of industry.*

   The rate of profit contrasted with a profit margin.

2. Uniformity-of-profit principle based on the fact that capital is withdrawn from areas of low profitability or losses and invested in areas of higher profitability, the effect of which is to reduce the initially high profit rates and raise up the initially low profit rates.

B. Significance of the Uniformity-of-Profit Principle

1. The harmonious balancing of the different branches of industry; incentives and means for the counteraction, delimitation, and prevention of mistakes in production.

2. The power of the consumers to shift the course of production—"consumer sovereignty."

3. The need of businessmen to introduce continuous improvements in production ahead of others in order to earn an above average rate of profit; how the concern with profits expands production in the economy—the significance of cost cuts; why prices rise, even though the uniformity-of-profit principle operates to make them fall.

C. Applications of the Uniformity-of-Profit Principle

1. The repeal of farm subsidies, rent controls, and price controls on oil and natural gas.

2. Differential tax rates—e.g., the depletion allowance on oil and its abolition.

3. Rents and prices in minority neighborhoods.

IX. The Tendency Toward a Geographical Uniformity of Prices

A. Statement and Explanation of the Principle

1. *The price of a good capable of transportation tends to be the same throughout the world, plus or minus costs of transportation (and tariffs, if any).*

2. Basis in the fact that it pays to buy in the cheaper market and sell in the dearer market, which has the effect of raising the price in the former and lowering it in the latter.

B. Significance and Applications of the Principle

1. Why local crop failures don't cause famines.

2. The Arab oil embargo against the U. S.

3. The export of Alaskan oil to Japan.

X. The Tendency Toward a Uniformity of Prices Over Time

A. Statement and Explanation of the Principle

1. *The price of a good in the present tends to equal its expected price in the future,* or, more precisely, the expected price of a good in the future tends to exceed its price in the present by no more than the costs of storage and an allowance for the going rate of return on capital for the period of storage.

2. Basis in the fact that buying and holding to take advantage of a higher price acts to raise the price in the present and, by making larger supplies available in the future, reduce the price in the future.

B. Significance and Applications of the Principle

1. The mitigation of scarcities.

2. The productive role of commodity speculation.

XI. The Tendency Toward a Uniformity of Wage Rates for Labor of the Same Degree of Ability

1. Basis of the principle in the movement of workers from lower paying to higher paying fields and effect of more (less) workers on wages in a field; accomplished mainly by movement in supply of young workers entering the labor force.

2. Corollary tendency toward unequal wage rates for labor of different degrees of ability.

3. Premiums and discounts in wages accompanying non-monetary disadvantages and advantages of employment.

4. Consumer control over the relative size of the various occupations.

5. Seeking the highest paying job means trying to do what the consumers most want you to do

XII. Prices and Costs of Production

1. The tendency for price of products to be governed by their costs of production

   a. Indirect determination by cost through variations in supply.
   b. Direct determination by cost through the decisions of sellers in setting their prices: the need to hold down the profits of competitors and potential competitors.

2. Analysis of cost of production into prices times quantities of factors of production; prices of factors of production at each stage largely determined by supply and demand—e.g., wage rates. Role of supply and demand becomes

cumulatively greater, the further back in the production process one goes—e.g., autos to steel making to iron mining. *Explanation of price by cost, therefore, ultimately comes down to explanation based on supply and demand operating in markets for labor and other factors of production in given supply.*

3. Full explanation of prices based on cost and of all other prices depends on explanation of prices by supply and demand.

(Accompanies Weeks 7–9)

XIII. The General Pricing of Goods and Services in Limited Supply

1. A "catalog" of goods and services in limited (given) supply.

2. The prices of goods and services in limited supply are determined by the quantity of money and by the value judgments of the consumers with respect to the various goods and services on which they spend the quantity of money. The quantity of money determines the absolute height of all prices, and the value judgments of the consumers determine their relative heights.

> Under this head, the value judgments of the consumers determine the relative incomes of the different kinds of workers, e.g., the incomes of skilled workers in relation to those of unskilled workers.

3. The prices of goods and services in limited supply are set high enough in a free market to level down quantity demanded to or below equality with the supply available. Consequently, shortages even of these goods and services are impossible in a free market. By the same token, the competition of the sellers of such goods prevents unsaleable surpluses in a free market—implication of no mass unemployment in a free economy.

4. The setting of prices high enough to limit demand to the supply is to the self-interest of buyers as well as sellers, and of poor buyers as well as rich ones; similarly, the setting of prices low enough to clear the market is to the self-interest of sellers as well as buyers.

5. In a free market, goods and services in limited supply are distributed to consumers in accordance with a combination of their wealth and income and needs and desires.

6. The prices of factors of production in limited supply have the same characteristics and the same significance as the prices of consumers' goods in limited supply, as described under points 3, 4, and 5, above. (Factors of production are labor, materials, and machinery bought for business purposes, i.e., for the purpose of earning profits through subsequent sales.)

7. In addition, factors of production in limited supply have an added dimension of "distribution": Namely, they are distributed to different concrete uses or employments. E. g., wheat is distributed to the production of bread, crackers, etc. This kind of distribution, of a factor of production among its various products, takes place through a process of the different needs, desires, and purposes of one and the same individual consumers bidding against each other.

8. In a free market, factors of production in limited supply are distributed to their most important uses, in accordance with the pattern of consumer spending.

9. The concept of "most important uses" is a variable range, determined by the supply of the factor.

10. Prices of factors in limited supply are determined with respect to their marginal uses—that is, the least important of their most important uses. Consequently, prices determined by cost of production are determined with respect to the marginal uses of the factors of production.

11. All prices of goods and services in limited supply are determined by the consumers' value judgments with respect to marginal quantities, e.g., rental space.

12. More on the rationality and efficiency of the free market in responding to changes in economic conditions: In a free market, every change in the demand or supply of any factor of production is dealt with in a way that maximizes gains and minimizes losses. Factors of production in reduced demand or additional supply are channeled to the most important of their previously submarginal uses. Factors of production in additional demand or reduced supply are taken from the least important of their previous uses—viz., from their marginal uses.

13. More on the harmonious integration of all production and consumption in a free market: The significance of using lower priced factors in place of higher priced factors. The significance of cost calculations. What the prices of consumers' goods reflect.

XIV. Price Controls and Shortages

A. The Distinction Between Shortages and Scarcities

1. The meaning of a "shortage."

2. Why only price controls can cause shortages.

3. Scarcities do not cause shortages but shortages cause scarcities.

4. How price controls create shortages by expanding the quantity of a good demanded and reducing the amount of it supplied.

Five ways that price controls reduce supply: a. Making the production of a good unprofitable: the examples of oil and rent control. b. Making a local market uncompetitive: application to the surge in the demand for wheat and soybeans in 1972 and 1973 and to the natural gas crisis of 1977. c. Making the consumption of a commodity too rapid and thus reducing future supply. d. Making an occupation or industry unable to compete for labor. e. Making some products of a factor of production unable to compete with its other products.
How price controls are equivalent to a prohibition of production.

XV. The Effects of Price Controls and Shortages

A. The Impotence of Consumers

The consumer made worse off than if he were dealing with a protected legal monopolist. Valuelessness of the consumers' business. Consumers reduced to the status of a nuisance and source of expense. Egoistic relation between buyer and seller replaced by altruistic relation. Reduction in quality and service. Hatred between buyer and seller: the examples of the gas shortage and rent control in New York City. How the repeal of rent control would give tenants economic power over landlords and restore harmony between them.

B. The Impetus to Higher Costs

1. The disappearance of low-priced models, cornercutting. More on the decline of quality: effects of shortages on the methods of production. Declining quality as a cause of higher costs. Shortages themselves as a direct cause of higher costs.

2. Price controls and cost-plus pricing. The administrative problem of multiple price controls for the same good, based on different costs: the case of oil prices in the 1970's.

C. Chaos in the Personal Distribution of Consumers' Goods

Destruction of the free market's principle of distribution in accordance with the combination of wealth and desire; nullification of the value of higher incomes. The rule of the random and the accidental.

D. Chaos in the Geographical Distribution of Goods Among Local Markets

How shortages prevent more supply from reducing prices. Indeterminacy in geographical distribution: the case of the gasoline shortage. Why the burden of shortages is randomly distributed, with some areas suffering relatively mild shortages and other areas suffering far more severe shortages. The significance of the time of year when gasoline controls were imposed. Potentially disruptive effects of small bureaucratic adjustments in the controls.

E. Chaos in the Distribution of Factors of Production Among Their Various Uses

Indeterminacy in the allocation of a factor among its various uses. The case of the oil shortage. Accidental nature of which products bear the burden of the shortage. The significance of the time of year when controls were imposed on oil. The instability of supply under controls. The hoarding demand.

F. Shortages and the Spillover of Demand

Shortages increase the demand for other goods and, if the other goods are not controlled, cause their prices to be higher and the profitability of producing them to be greater. Implications: a. Partial price controls (i.e., controls confined to some goods only) are contrary to purpose. b. partial price controls cannot hold dawn the general price level. c. partial price controls do not “save people money” in the aggregate. The bizarre sense in which they do “save people money.” How partial price controls raise the general price level. Why repeal of partial controls reduces the general price level.

Application to rent controls. Present rent controls apply to only part of housing market. Consequences of a fully controlled housing market: compulsory assignment of boarders to private homes and restriction of the internal freedom of migration; the case of the communist countries. Effects of partial rent controls on the housing subjected to them. How partial rent controls raise rents on the uncontrolled housing supply. How partial controls raise the costs of providing new housing. Why the “luxury” housing of recent decades is inferior to earlier housing. The case for the immediate repeal of rent control: the unrecognized victims of rent control: Why repeal on net balance would alleviate hardship even in the short-run. Why there are no beneficiaries of rent control in the long run.

Application to the price controls on domestically produced oil in the 1970’s. How repeal of these controls enabled American oil companies to sell at higher prices, and simultaneously reduced the price received by OPEC.

G. The Tendency Toward Universal Controls

Why partial price controls must be extended to the prices that constitute costs, to prices of alternative products of the same factors of production, to all employments of the same labor, and, finally, to all remaining prices in the economic system.

XVI. Universal Price Controls and Socialism

A. Excess Demand Under Universal Controls

The compounding of the excess demand for each good by the unsatisfied demand for all other goods; how the shortage of each good reflects the sum of the shortages of all other goods. Shortages in Soviet Russia. How excess demand exists even though incomes are controlled. The buildup of surplus, unspendable income resulting from the government’s injection of new money.

Why controls do not produce their full effects immediately.

B. Universal Price Controls and the Destruction of Production Through Shortages

1. Review of the ways that shortages destroy production: (It should he recalled in this review, by the way, that anything that acts to raise costs implies a decline in production.)

a. Shortages make buyers impotent and thereby remove the incentives of sellers to provide good quality and service. As a result, quality and service decline and the costs of maintenance and replacement increase.
b. Shortages of means of production, such as a material, often force sellers to reduce quality and service and make it necessary to resort to more expensive substitute methods of production.
c. Shortages encourage sellers to concentrate on the production of unnecessarily expensive models as a disguised way of raising prices.
d. Shortages create a positive incentive to using more expensive methods of production if the government allows the pass-through of higher costs and makes the incurrence of higher costs a source of higher profits.
e. Shortages result in delays in production.
f. Shortages cause hoarding and the construction of additional storage facilities.
g. Shortages cause the waste of time in searching for supplies.
h. Shortages create chaos in the geographical distribution of a good among local markets—for example, gasoline during the oil shortage.
i. Shortages create chaos in the distribution of a factor of production among its various uses in production—for

example, crude oil in the production of the various oil products.

2. Now, under universal price controls, every industry affected and the problems of each intensified, because of the compounding of the shortage of its product and because of shortages of means of producing its product. Also, a new dimension of chaos: the shortage of capital and labor.

3. Total chaos in production: the expansion of any product at the expense of any other product, irrespective of the will of the consumers. How production declines in such conditions:

a. The reduced benefit from production caused by disproportions among the different kinds of consumers' goods; this equivalent to less production.
b. The reduced ability to produce resulting from disproportions in the individual kinds of capital goods; cumulative self-reinforcing process of less production, less capital goods, less production.
c. The labor shortage: the excess demand for labor and the falling supply of labor; cumulative, self-reinforcing process of shortages of consumers' goods, reduced supply of labor in response, and then worse shortages of consumers' goods.

4. The prosperity delusion of price controls. Mistaken belief that World War II was a period of prosperity.

C. The Government's Response to the Chaos It Causes Through Price Controls: *De Facto* Socialism.

The government's seizure of production and distribution: It decides what and how much of each product to be produced, where, and by what methods, and to whom to be distributed. In conjunction with price controls, this represents total usurpation of powers of ownership. Hence, the government now the real owner.

Why Nazi Germany was a socialist country and why the Nazis were right to call themselves "national *socialists*." Why Israel and Sweden, however, are not in fact socialist countries, but simply "mixed economies." (Why the same was true of Britain under the Labour Party.)

D. The Essential Characteristic of Socialism

Government ownership of the means of production the essential feature of socialism. Socialism the same whether government ownership arrived at through price controls or open nationalization, through peaceful means or forcible means.

E. The Essential Economic Identity Between Price Controls and Socialism

Price controls and socialism essentially the same economically because both destroy the same thing: viz., private property rights and its offshoots the profit motive and the price system. Private property rights and the profit motive are the foundation and driving force of the price system and all of its laws. Their destruction, whether by price controls or by socialism, destroys the one and only source of economic order and harmony in the world and therefore results in chaos. Socialism does not go beyond destroying the system based on private ownership. It is simply an act of destruction, not a positive economic system.

XVII. The Chaos and Tyranny of Socialism

A. The Myth of Socialist Planning

1. See Syllabus Supplement 2, VI. A. above.

2. Socialism's destruction of the price system destroys the possibility of economic calculation, economic coordination, and, therefore, rational economic planning. Rational planning under socialism would require the planning of the economic system as an indivisible whole—i.e., with no division of the intellectual labor involved in planning. Each planner, or *the* planner, would have to be able to see the production of each good in all of its relations to the production of all other goods. This is impossible because it would require a mind able to hold and use all the knowledge that only millions can hold and use—i.e., an omniscient deity.

3. In reality, socialism can never have a rationally integrated plan for the entire economic system. In reality, it is characterized by separate ministries and even factories all planning independently of each other, and at cross purposes. The discoordinated plans of socialism make their mutual execution impossible. Planning under socialism is also made

impossible because each industry is dependent on disinterested monopoly suppliers. Socialism is not a planned economy, but an "anarchy of production"—a true one.

4. Socialism's anarchy of production illustrated by the Russian quota system. This system encouraged the maximum possible production of each good—every farm and factory encouraged to exceed its quota by as much as possible. This creates same situation as universal shortages, in that ready and waiting employment exists in every field for a larger supply of factors of production. Lack of precision of quotas also illustrates lack of rational planning—e.g., quotas for screws in terms of mere number or weight. Chaotic consequences of such lack of precision.

5. Quota system an inevitable result of socialism's lack of ability to determine costs and to trace connections among industries.

6. Socialism's anarchy of production and its shortages of labor and consumers' goods.

B. Further Economic Flaws of Socialism

1. The most fundamental flaw is that government's monopolization of means of production is attempt to monopolize intelligence and initiative in production. This underlies socialism's inability to plan and also its technological backwardness and the utter powerlessness of the plain citizen under socialism.

2. Contrast between capitalism and socialism in the introduction of improvements: capitalism has initiative, incentives, and competition. Socialism lacks all three.

3. Why socialism has no reason to maintain the standard of living inherited from capitalism, even if it had the ability. How socialism's paralysis of initiative and incentives causes death: the case of Russia under the Communists.

4. Why the government of a socialist country is only interested in the values of its rulers. Application of this principle to technology and all production under socialism: socialism's concentration on the technology and production of weapons, spectacles, and "monuments"; its dependence on capitalist technology even for these. Socialism as the true system of the exploitation of labor and the progressive impoverishment of the workers.

C. The Tyranny of Socialism

1. The need for force or fraud to establish socialism: why the methods of the communists are necessary.

2. The need for terror to maintain socialism: a. Stopping the growth of the black market. b. The logic under socialism of accusing black marketeers of sabotage. c. The impossibility of freedom of press or speech when the government owns all the presses and meeting halls and is the sole employer. d. Socialism as a court society. e. The necessity of forced labor under socialism. f. The rulers' dilemma of how to stay in power while promising a life of bliss and yet by the nature of socialism being unable to deliver anything but poverty and misery. Consequent need for diversions of hysterical propaganda, periodic purges, and the ruthless suppression of all criticism. g. From forced labor to mass murder.

(Accompanies Week 10)

XVIII. The Influence of the Division of Labor on the Institutions of Capitalism I

A. Private Ownership of the Means of Production

1. The prevailing view of private property, including private ownership of the means of production, as serving only the interests of the owners.

   a. The alleged need for redistribution or socialism.
   b. The assumption that the advocacy of capitalism implies that one is a capitalist.
   c. The media's treatment of voting patterns.
   d. The belief that fighting communism requires creating capitalists.

2. Prevailing view ignores the division of labor and the fact that under capitalism privately owned means of production *serve the market,* and thus provide a *general* benefit.

   a. The benefit of the buyers of products served by the means of production—if you can buy the products, you don't have to own the means of production to benefit from them.
   The buyers' control over production in contrast with the powerlessness of the consumers under socialism—the dictator and the people's shoes; the lack of stores in Moscow's suburbs.
   b. The benefit of the wage earners from the demand for labor.

3. The *increasing* general benefit from private capital.

   a. Profit and loss incentives and the freedom of competition and individual initiative; the chances for new ideas being tried.
   b. Gains to non-owners greater, the more the property rights of capitalists respected: stronger incentives; higher demand for labor and capital goods relative to consumption; more efficient production of capital goods—all result in capital accumulation and rising productivity of labor and real wages.

4. The special benefits of private ownership of the means of production to the owners: not profits or interest, but limited personal consumption—probably less than ten percent of the national income—and the psychological benefit of the *potential* of personal consumption.

5. The absurdity of "redistributionism."

   a. Already have the benefit of almost all the capitalists' wealth without redistribution—the wealth is in means of production; and the benefit steadily growing
   b. An open demand for capital decumulation and impoverishment.
   c. If not such a demand, then a demand for at most a one-time, non-repeatable transfer of about ten percent of the national income; capitalism gives the equivalent over and over again every few years, through economic progress.

6. Consequences of redistributionism:

   a. Can't achieve even the one-time transfer—the destruction of incentives to maintain and manage capital; collapse into the chaos of socialism.
   b. The lesser case of isolated nationalized industries: the destruction of profit and loss incentives and the freedom of competition and individual initiative—the Post Office case; nationalization and the destruction of the *special* benefits of ownership: the inability to sell one's "shares"; instead of dividends to consume, taxes to cover losses brought on by the nature of government ownership—no profit and loss incentive, uncontrolled costs, run up costs in vote-buying employment and contracts.

7. Conclusion: the institution of private ownership of the means of production in a division of labor, capitalist society serves everyone—*non*-owners as well as owners; the real self-interests of everyone lie with capitalism, not just the interests of the capitalists; better to be a non-owner under capitalism than an equal owner under socialism.

B. Private Property Continued: the Special Case of Inheritance

1. The prevailing view: only the heirs gain; the non-heirs gain by a policy of confiscation and redistribution.

2. Fact: the institution of inheritance promotes capital accumulation, from which *all* gain, non-heirs as well as heirs.

3. Confiscatory inheritance taxes destroy the incentive to accumulate capital insofar as the motive of accumulation is to leave wealth to heirs; the collection of inheritance taxes diverts capital into consumption: if estates did not have to be sold to pay taxes, the buyers would have used their funds to purchase capital goods that would have existed in addition to the estates; with the inheritance taxes, their funds are diverted to the purchase of existing capital goods, and from there to the Treasury.

C. Private Property Continued: the Taxation of Profits, Interest, and Capital

1. As far as the taxes come out of capital or additions to capital, they reduce or hold down the demand for labor and capital goods—cause lower wages relative to the demand for consumers' goods and lower productivity of labor.

2. Also retard innovation—reduce incentive and means for implementing new ideas; especially destructive for new firms, which are prevented from growing large.

3. These the effects in whole or part not just of inheritance taxes, but of corporate income tax, progressive personal income tax, capital gains tax, social security taxes, and government deficits. Need to reduce or abolish these taxes and the deficits to restore economic progress; need to cut government spending.

4. Self-interest of everyone lies with ability of business to save and invest and innovate: interests of non-owners hurt by whatever keeps down the demand for labor and supply of products.

D. Private Ownership of Land

1. Ricardo's doctrine on land rent, and Georgism: land rent, population growth, diminishing returns, and subsistence; the "unearned gains of the landowners."

2. Seeming application of the doctrine in the period l250-l750.

3. The real problem: too slow progress caused by *the lack of private property and property rights in land*—the common lands, feudal restrictions on selling and alienating land, the impossibility of firing unnecessary agricultural workers under serfdom.

4. Private property in land provides the incentive basis for rapid enough progress to more than offset the operation of the law of diminishing returns and the need for inferior lands; it thus works to hold down and actually reduce land rent as a share of national income.

   a. Historical confirmation: the decline in the economic significance of land rent coincides with the enclosure movement in England, the privatization of North America, and the establishment of property rights on the European continent.
   b. Further confirmation: the case of oil today.

5. Conservationist criticisms of private property in land: deforestation, the near extermination of the buffalo. Rebuttal:

   a. Deforestation because of *lack* of private property rights—the land didn't belong to the logging companies, thus they had no incentive to replant; if it did, they would have.
   b. The buffalo not raised on ranches because of the competition of cattle—the price of buffalo meat limited by the price of beef; the price of beef too low to enable buffalo ranching to be profitable. A waste to use labor and capital to raise buffalo when it's better employed raising cattle.

E. Private Property and Political Sovereignty

1. Mistaken view on the need for extensions of sovereignty; what is really needed is free trade and respect for the property rights of foreigners; then the whole world gains all that can be gained from the territory of each country; extensions of sovereignty made unnecessary; implications for world peace.

2. The general interest in free government everywhere—the historic role of the British Empire.

3. The exportation of natural resources not an exploitation but a source of benefit to the countries in which found: higher demand for local labor, the import of goods otherwise impossible to obtain.

4. How the backward countries could be rapidly developed and how their policies prevent it: property rights vs. confiscations and restrictions on dividend remissions.

(Accompanies Week 11)

XIX. The Influence of the Division of Labor on the Institutions of Capitalism II: Economic Inequality

A. The Nature of Economic Inequality Under Capitalism

1. The prevailing view: "the rich get richer, the poor get poorer"—one man's gain is another man's loss.

2. Fact: the division of labor allows for constant increase in the total of what is produced. One man's gain resulting from an increase in the total of what is produced is *not* another man's loss—the example of Crusoe and Friday.

3. How the gain of the one easily leads to the *gain* of the other: productive emulation.

4. The fallacy of unjust "distribution," when what is actually involved is an inequality of production.

5. How in a division-of-labor society, one man's gain *typically implies the gain of others:* productive emulation—present in competition; the nature of free exchange and the sharing of the growing gains from the division of labor.

6. The especially important case of *the origin and disposition of fortunes:* the earning of a high rate of profit over a long period of time, with most of the profit constantly being plowed back. The high rate of profit reflecting the introduction of repeated improvements in production of benefit to the buyers; the plowing back of the profit resulting in growing means of production employed to the benefit of the buyers.

7. Illustration of point 6 in American economic history: the cases of Carnegie, Rockefeller, and Ford.

B. The Marxian Doctrine on Economic Inequality: A Critique

1. The claim that inequality under capitalism is an extension of inequality under feudalism and slavery and that socialism is the culmination of political democracy and will represent the establishment of a classless society.

2. The injustice of comparing capitalist with feudal inequality: productive contribution and general benefit versus force and loss.

> Position of the feudal aristocrats not based on any economic role, such as land ownership, but on governmental power: they lacked essential rights of ownership (such as ability to sell their land, compete for the workers of others, and fire their own workers) and possessed powers far beyond those of any property owner: i.e., tax collection, "low and high justice."

3. Marxist and Galbraithian equivocation on freedom: the doctrine of "wage slavery" and "nominal" freedom (see J. K. Galbraith, *The New Industrial State,* Second Edition, New American Library, New York, 1971, p. 141—quoted in *Capitalism*, p. 331.)

> a. "Having" to work for a capitalist, even a hundred and fifty years ago, at very low wages, not a violation of freedom; the vital importance of being able to choose for *which specific employer one works.*
> b. Capitalists (businessmen) not responsible for workers feeling the pain of hunger, as Galbraith implies, but for paying wages to *alleviate* the hunger.
> c. Opposite character of freedom and slavery shown in the simple fact that a slave is held at his work by force, while it takes force to keep the poor but free worker of the capitalist *from* his work.

4. Inequality under socialism (see *Capitalism*, Chapter 8, Part B).

> a. The observed existence of "the new class"—special stores, clinics, schools, housing, and transportation for the party and government elite.
> b. The existence and servile character of inequality under socialism deducible from the leading moral-political premise of socialism that *the individual is not an end in himself* (as he is acknowledged to be under capitalism), but is *the means to the ends of "society"—which ends the rulers interpret.* It is also implied by the powerlessness of the plain citizen in his capacity as a consumer—only the values of the rulers count.

5. Socialism *versus* democracy (free government)—see *Capitalism*, Chapter 8, Part B.

C. The Equality of Opportunity Doctrine: A Critique

1. A fallback position for egalitarianism.

2. Some unpleasant implications of the equality of opportunity doctrine: Platonic orphanages, eugenics, tearing down advantages.

3. Observations on the nature of opportunities.

   a. The meaning of an opportunity.
   b. Their fundamental superabundance.
   c. Their creation by the individual.
   d. The room for all to rise in the context of a division of labor society.
   e. The need for the *freedom* of opportunity, not the "equality" of opportunity.

f. How individuals beginning under extreme disadvantages overtake others who begin with the greatest advantages—*the self-made man.*

XX. The Influence of the Division of Labor on the Institutions of Capitalism III: Economic Competition

A. The Nature of Economic Competition under Capitalism

1. The prevailing view: law of the jungle, survival of the fittest, dog eat dog, etc.

2. Actual nature: not the grabbing off of limited, nature-given necessities, but competition in the positive creation of new and additional wealth for the market—the inherent general gain; no genuine losers.

3. Competition and the survival of all: e.g., the effects of competition among farmers, eyeglass manufacturers, pharmaceutical makers, etc., on the hungry, the weak, and the disabled.

4. How even the apparent losers gain: e.g., the effects of the competition of the automobile on the horse and buggy makers.

5. The short-run loss periods; differing effects on unskilled and skilled workers; the effects on the losers of fortunes.

6. How *opposition* to free competition implies the advocacy of the law of the jungle.

7. Economic competition and economic security.

   a. Competition and the physical security of having goods—the paradox of the guild system.
   b. Competition and job security—the need for *fully* free competition; the seniority system and the artificial lengthening of the short-run loss periods.

8. More on competition and the "weak": the law of comparative advantage and the room for all in the division of labor. Statement of the law: *Even if one party is productively superior to the other in every respect, it still pays them to engage in division of labor, with the productively superior party concentrating on his area(s) of greatest superiority and the productively inferior party concentrating on his area(s) of least inferiority.*

   a. The boss and the secretary, the lady lawyer and the maid.
   b. International applications: England and Portugal, the US and Brazil.
   c. How both cases work out in terms of money.
   d. The implied dependence of international free trade on a free labor market domestically.
   e. The competitive damage to the less able of attempting to force the market to pay them the wages of the more able.

9. The pyramid of ability principle: *To the degree that the more able obtain the higher positions in the economic system, the productivity and standard of living of the less able are increased*—e.g., the case of the engineer and the mechanic, the foreman and the worker, the great industrialist and the average person.

10. The integration of the law of comparative advantage and the pyramid of ability principle: the gain from the

existence of other people; the greater gains from the existence of the more able—even janitors can have automobiles and television sets.

B. Competition and the Population Question

1. The Malthusian specter of overpopulation: the implied competitive conflict over land and natural resources.

2. Applies only to *non*-division of labor societies; in a division-of-labor society more population means a more intensive division of labor (Adam Smith's principle that the division of labor is limited by the extent of the market) and the realization of more economies of scale—manufacturing, the advantages of cities, the case of the medical school and all other sources of new knowledge; more people and more productive geniuses.

   a. The implicit case for worldwide free trade.

   b. Partial explanation of the higher standard of living in the US compared to Western Europe.

   c. Explanation of the effects of the Common Market.

3. Unlikely problems of too high a ratio of children to adults and of labor to capital.

4. The case for free immigration into a *capitalist s*ociety: the general benefit from others' possession of freedom—the bringing of talent to freedom, where it can flourish.

(Accompanies Week 12)

XXI. The Political Concept of Monopoly

1. The rational versus the anarchic concept of freedom: what violates freedom? Initiation of physical force or "obstacles" in the way of desires?

2. The distinction applied to "censorship," the "freedom of competition," and "barriers to entry."

   The actual significance of high capital requirements.

3. The political versus the economic concept of monopoly. Monopoly as politically versus economically imposed.

4. Meaning of the political concept: *A market or part of a market reserved to the exclusive possession of one or more sellers by means of initiation of physical force by the government.*

   The political concept is the original concept: *an exclusive grant of government privilege*—Charles I—East India Co., guilds.

5. Leading examples of monopoly according to the political concept:

   a. Exclusive government franchises.
   b. Licensing laws.
   c. Tariffs.
   d. Minimum wage and pro-union legislation.
   e. Government owned or subsidized enterprises.
   f. The antitrust laws.

6. Four points to remember about monopoly on the political concept:

   a. Monopoly can be many protected against one or a few (e.g., New York City taxicabs: many driver owners protected against a few large fleets).
   b. Is not necessarily profitable—high cost producers protected, as in tariff monopolies and subsidies.
   c. Patents and copyrights are *not* monopolies—merely give legal recognition to property rights and in the long-run reduce costs and prices by virtue of promoting economic progress.
   d. All monopoly is based on government intervention, which restricts the freedom of entry and competition.

7. Significance of monopoly on this concept—less choice, higher cost and price, lower quality, because of restricted freedom of the sellers and potential sellers.

XXII. The Economic Concept of Monopoly

1. A single seller of a given good in a given territory—embraces hardly anything (1920's) or almost everything (now).

2. "Monopolistic competition" and "oligopoly." Only wheat farming left as "pure competition."

3. The myth of past pure and perfect competition.

XXIII. Significance of Monopoly on the Economic Concept

1. Alleged tendency toward a single firm controlling the entire economic system—General Bullmoose rules the world, via mergers and predatory pricing.

2. Influence: Marx and the alleged inevitability of socialism; the antitrust laws; fears about the marriages of the wealthy.

3. In fact such a state of affairs exists only under socialism—established and maintained by force.

4. Why no tendency toward such situation under capitalism—critique of the merger route.

a. Anti-division of labor—bad mergers.

b. Prospects—the talented can't be merged; application to conglomerates.

c. Successful mergers create new capital for new firms.

d. More new firms all the time anyway—still more without tax problems of executives and insider trading restrictions; in addition, the tax laws restrict the growth of small business, as do regulations and the costs they impose in terms of time and need for staffs of accountants and lawyers.

e. Tax stimulus to uneconomic mergers: already large firms expand for capital gains treatment, medium size sell out for capital gains treatment; absorb loss makers.

5. Positive reasons for mergers: more division of labor and economies of scale, including wider application of better management; access to the capital market, advertising, complementarity of products (e.g., better use of salesmen's time); transportation economies.

6. Truth about 19th century—higher production, lower prices—the reverse of what led to expect on basis of monopoly on the economic concept.

7. The trust movement: earliest merger device.

a. Necessary to achieve benefits of improved transportation methods, which favored larger scale manufacturing. Example: Assume a large scale plant has a manufacturing cost per unit of $1, while a small scale plant has a manufacturing cost of $10 per unit. Consider the implications if transportation cost for both is initially 50¢ per mile and then falls to 1¢ per mile.

b. Trusts represented pooling of capital to make possible replacement of small, inefficient facilities with large-scale, efficient facilities.

c. The Supreme Court in decision breaking up Standard Oil: "Much has been said in favor of the objects of the Standard Oil Trust, and what it has accomplished. It may be true that it has improved quality and cheapened the costs of petroleum and its products to the consumer. But such is not one of the usual or general results of a monopoly; and it is the policy of the law to regard not what may, but what usually happens."

Ironically, the record of Standard Oil is usually thought to be the leading evidence of the bad consequences of the trusts!

XXIV. The Predatory Pricing Doctrine

1. Statement of the doctrine: the large firm can allegedly afford losses which the small firm can't, so it allegedly temporarily slashes price to force the small firm to sell at a loss, in order to drive it out and then jack prices up to higher levels than before. Potential newcomers supposedly kept out by threat of further ruinous price cuts. All achievements of big firms in reducing prices and improving quality seen as a prelude to this kind of gouge.

2. Problems with the doctrine:

a. The narrow market case: e. g., A & P and the chain stores. The limited nature of the potential extra profit from any one location, even if it could be obtained. Most of big firm's capital *irrelevant* to what it can afford to lose in any one location. Many on just as good a footing. Exposure to competition of newcomers who haven't lost anything yet. Pouring money down a bottomless hole. Not a formula for growing rich. Actual fact is lower real prices in retailing, not higher, and brought about largely by the chains.

b. Doctrine ignores fact that in degree the large firm is larger in the same market, it must take the price cut and loss or profit reduction on a correspondingly larger volume. E. g., if "Big John" [Rockefeller] wants to make Little Joe take a loss on the latter's ten percent share, he must take a loss or a profit reduction on his *ninety percent* share.

Big John must sell below little Joe's operating costs—for as long as the latter's capacity lasts. And then, when little Joe is gone, he still can't get more than a new comer's full costs plus the going rate of return.

c. Not possible to keep small firms out by intimidation of threat of ruinously low prices—forward contracting at manufacturing and wholesaling level, niches of competition at retailing level that can't be driven out even with *permanently* lower prices, and which prevent rise in prices. Also, support from suppliers and producers of complementary goods, who stand to lose volume if higher price imposed.

3. Implication of above is that it doesn't pay a large firm to seek 100% of the market by cutting price—unless there will be a vast increase in volume. The small firm's minor market share not a sufficient reward by itself. (Fact is that the small firm has much more to gain by being aggressive in cutting price against the large firm—the latter's market represents a major potential for its expansion, while its market doesn't offer much prospect for the large firm's expansion.)

4. This is a further reason for industries usually having more than one firm, simply because it doesn't pay anyone to go for the whole market unless there is a radical expansion in that market at a lower price.

5. Historical confirmation: According to John S. McGee, in "Predatory Price Cutting: The Standard Oil (NJ) Case," (*Journal of Law and Economics*, October 1958), Standard Oil actually never practiced predatory price cutting—because it would have been unprofitable.

XXV. The Doctrine of Marginal Revenue and Higher Prices in the Single Industry

1. Example of the doctrine:

Price	Quantity	Total Revenue	Unit Cost	Total Cost	Profit
$15	100	$1500	$8	$800	$700
9	200	1800	8	1600	200

Large firm supposedly "restricts" output in order to profit more from a smaller number of units than a larger number, even though the second 100 units are independently profitable and should be produced. It allegedly takes into account *the marginal revenue* attaching to the extra units, rather than their price. The marginal revenue is the change in total revenue that accompanies a change in quantity sold. Marginal revenue takes into account the drop in price on the quantity that is already being sold. In degree that a firm is large, it will supposedly restrict production, because of its concern with the effect on the price of what it already is selling.

2. Fact: unless it has legal protection from outside competition, the firm's real choice is not between 100 at $15 or 200 at $9, but between 100 at *$9* or 200 at $9. So long as the second 100 units are profitable in their own right, they will be produced. The only question is whether they will be produced by the firm that is already producing the 100 or by another firm. In the latter case, the first firm ends up selling at $9, but only 100 units instead of 200 units.

Note:

a. No firm subject to the competition or potential competition of others can view the industry demand curve as its own. It cannot lastingly get a price higher than outsiders' costs plus an allowance for the going rate of return, as a maximum. No matter what the elasticity of the industry demand curve, the long-run demand curve to it specifically is highly elastic at any price above outsiders' costs plus an allowance for the going rate of return.

b. In the case of a new industry, founded by one firm, it might be that it will decide that it does better by getting the higher price as long as it can, and waiting for competition to reduce the price. If so, this is a further reason why there is no tendency toward the formation of a single giant firm.

c. Paradoxically, although the marginal revenue argument is directed against "big business," the actual meaning of the argument is a denunciation of big business for refusing to become still bigger. If the firm goes ahead and produces the 200 units, the marginal revenue argument will not apply. Then, however, it will be denounced for being a monopoly. If it doesn't produce the 200 units, and thereby creates the opportunity for another firm to produce some of them, it is denounced for restricting production.

XXVI. The Cartel Doctrine

1. With few exceptions (where there are very few physical sources of supply, such as is the case with diamonds), the only time cartels pay is when they serve *merely to reduce the extent of losses, i.e., raise price from a point of more severe losses to a point of less severe losses or modest profits.* This is because, in addition to the problem of deciding

which producers must curtail production how much, which is difficult enough in itself, profitable cartels have two further problems, which tend to make their success impossible:

a. The problem of controlling the investment of the profits. If the firms are profitable and want to reinvest their profits, the industry will expand and the cartel price will crash.
b. A profitable price attracts outside entrants to the field, which will make the cartel price crash. But if the cartel is not profitable, these problems do not arise, and so the cartel may succeed. If it is profitable, the only way it can succeed is if outside entrants can't enter and if the members' reinvestment policy can be controlled. In the light of these facts, the following passage from Richard Caves' *American Industry: Structure, Conduct, Performance* should not be surprising: "We even have evidence suggesting that large firms caught engaging in illegal collusion earn *lower* profits than other large firms. Perhaps collusion is most commonly attempted in situations where some adversity has depressed profits below a normal level." (p. 59, 4th ed.)

2. Cartels as a serious problem are the result of government intervention:

a. The OPEC oil cartel today. Its success was the result first of price controls and then of confiscatory taxation applied against its leading competitors, the American oil companies. In their absence, its high prices would have made these competitors extraordinarily profitable and enabled them to expand, thereby reducing prices or forcing the cartel to further restrict its output, which would have given the American industry high profits on a still greater volume, permitting further expansion, until ultimately either the price came down or the cartel was forced out of the market. The cartel's success is also due to American government policies restricting oil exploration and development, such as on the continental shelf, and in wildlife and wilderness areas. The extra oil from these sources would either reduce the price or force the cartel to reduce its own output still more. Price controls on natural gas, restrictions on the strip mining of coal, restrictions on the development of atomic power add to the demand for oil. So does the requirement that automobiles use unleaded gasoline. In the absence of these regulations, OPEC would have to restrict its own output still further in order to maintain the present price of oil. The amount of restriction of its output required would be so large as to make it not worthwhile. The major benefit of any higher price would simply go to the cartel's competitors. Our policies did most of the work of making oil scarcer, and then prevented the cartel's competitors from profiting from the high prices it was able to impose.
b. The German cartels before World War I (which were the classic case of cartelized industry) were promoted by the Imperial German Government. Mises shows in *Human Action* how social legislation raised production costs in Germany relative to those in other countries, which had not adopted this legislation. The result would have been that German manufacturers could not have sold profitably either at home or abroad. To deal with this problem, the German government enacted protective tariffs and encouraged the formation of domestic cartels, which could thus sell at high prices in the German market. At the same time, the extra profits reaped in the domestic market permitted the subsidization of German exports, which could then be sold abroad at competitive prices or even below competitive prices ("dumping"). The exports were necessary to permit Germany to import vital raw materials and food stuffs not available domestically. (See *Human Action,* Third Edition, pp. 366-368.)
c. U.S. agriculture under government price supports

XXVII. The Pure and Perfect Competition Doctrine

1. A denunciation of business as "monopolistic" for refusing to sustain unnecessary losses.

2. The meaning of pure and perfect competition (ppc): *the set of conditions required to drive price to equality with marginal cost.*

3. The meaning of marginal cost: *the extra cost required to produce an additional unit of output;* usually this is the cost of labor, materials, and fuel.

Marginal cost means different things in different contexts. Can equal full cost, or zero, or anything in between, depending on the context.

4. The alleged significance of marginal cost: a measure of value of output forgone in order to produce the output in

question. Price equal MC seen as desirable because of alleged optimization of use of resources: so long as price greater than MC, value of product gained greater than value of product lost. Thus ppc, in causing price to equal MC, seen as conditions required to optimize use of resources.

5. The treatment of fixed costs—analogous to Ricardian land rent: only properly recoverable as and when that category of plant and equipment becomes “scarce”. Any allowance for fixed costs other than in case of plant and equipment being “scarce” is “monopolistic withholding of supply”: The fish case. The machine case: A machine has the capacity to produce 1 million units of product—renders 1 million service units.

Quantity Supplied and Demanded (in thousands)	Price	Marginal Cost	Implied Machine Rent
500	$10	$8	$2
600	9	8	1
700	8	8	0

Implied machine rent justified only if quantity demanded at price of $8 is greater than 1 million units. Then machine’s services are “scarce” and deserve a price.

6. The need for the huge number of sellers and product uniformity as the principal conditions for getting sellers to drive price to marginal cost. Why rivalry seen as antithetical to competition.

7. Effects if price did equal MC

  a. In many cases, price = zero; no supply or nationalize and subsidize.
  b. Smaller industries that would operate at capacity more often.

8. The alleged lack of price competition because price not driven to MC.

The omnipresence of price competition: 200 years of lower real prices everywhere. Chrysler, American Motors—anyone driven out of business. The omnipresence of price competition even in inflation—the quest for higher productivity and the need to match others’ lesser price increases based on improvements in efficiency. The consequent need to improve one’s own efficiency.

(Accompanies Weeks 13–14)

XXVIII. The Division of Labor and the Concept of Productive Activity

A. The Doctrine That Only Manual Labor Is Productive

1. Manifestations: the IRS and "earned" vs. "unearned" income; the attitude of labor unions and their supporters; the attitude of socialist governments.

2. Will show that this doctrine rests on ignorance of the requirements of a division-of-labor society, and is both far too narrow and, in one major respect, too broad in its view of what is productive activity.

B. Money Making and Productive Activity

1. Need for money making for activity to be productive in context of a division-of-labor society—need to be able to obtain *products of others* as a result of one's labor. Must earn money to do so. Even manual labor not productive if doesn't earn money. In context of a division-of-labor society, *productive activity is activity the purpose of which is the earning of money.*

Application: the maid who works for money and the housewife who cleans the house without earning money—the significant difference.

2. If activity is not for purpose of making money, it is inherently *consumption*—in that it starts with materials and equipment, which can't be replaced. Physical production, when purpose is not money making, is a *consumptive production.*

3. Productive expenditure and consumption expenditure: expenditure for the purpose of bringing in subsequent sales receipts (implicitly at a profit) versus expenditure *not* for the purpose of bringing in subsequent sales receipts.

Practical significance of distinction: the one is self-sustaining and a source of wealth; the other is a using up of wealth. The case of the two brothers starting with an equal inheritance, one growing richer through productive expenditure, the other growing poorer through consumption expenditure.

4. Capital goods and consumers' goods; producers' labor and consumers' labor; producers' loans and consumers' loans. Purpose for which funds expended or advanced critical, not physical nature of the activity. Heavy machinery can be consumers' goods; all food and clothing are capital goods when bought for business purposes.

a. Consumers' goods that reduce expenses are still consumers' goods—a smaller consumption expenditure is still a consumption expenditure.
b. The status of government borrowing.

5. Adam Smith correctly understood these issues, even though he introduced a second, irrelevant criterion for distinguishing between productive and unproductive activity—namely, the question of whether or not there is a tangible, physical product. But Adam Smith very bad on the questions of the legitimacy of profits and interest and on the productive role of businessmen and capitalists.

C. The Marxian Exploitation Theory

1. The Smith-Marx framework.

a. See Smith, *Wealth of Nations*, p. 72, para 1 & 2 of University of Chicago Press Edition; then pp. 73-74 (quoted in *Capitalism*, pp. 476 and 477).
b. Claims labor the source of all wealth; has right to the full produce or to full value of the produce. Claims income of labor is wages; profits, interest, etc. an unjust deduction that arises with the coming of capitalism and capitalists.
c. Marx: C-M-C—equivalent to Smith's early and rude state. Allegedly no "surplus value" here; surplus value only under "capitalistic circulation"—M-C-M'.

2. Marx's theory of profits (surplus value)—attempt to explain the extent of the unjust deduction from wages.

a. The absolutist labor theory of value—exchange value of everything allegedly determined by "congealed labor content" and nothing else.
b. Implies all value added is proportionate to fresh labor added, since materials and machinery convey their labor content to the product—neither more nor less.
Thus fresh labor allegedly adds all value—the sum of profits and wages.

Corresponding Marxian terminology of "constant" and "variable" capital.

c. Wages, the value of labor, allegedly determined by quantity of labor required to "produce" labor—i.e., subsistence. Wages put there by the arbitrary power of the capitalists—the Marxian "iron law of wages." Subtraction of wage share of value added by labor, then leaves profit—"surplus value.".
d. Example and elaboration of Marx's theory:

i. 48 hours of labor in materials and machinery + 12 hours of fresh labor yield product embodying 60 hours of labor.

ii. If $1 of product value represents every hour of embodied labor, then the materials and machinery that pass into the product are worth $48, while the product itself, embodying 60 hours of labor, is worth $60. The 12 hours of fresh labor adds the whole difference in value between the product and the materials and machinery. This value difference is the sum of wages and profits together.

iii. The division of the value added, between wages and profits, says Marx, is determined by the fact that the 12 hours of fresh labor can be purchased at a price representing the number of hours of labor required to "produce" that 12 hours. If, to use Marx's own example, the worker can work for 12 hours on the basis of necessities which require only 6 hours to produce, then, says Marx, he is paid a wage of only $6. Thus the capitalist acquires 12 labor hours and the value added by 12 hours at a price corresponding to only 6 hours.

iv. Thus profits are made, says Marx, by the systematic underpayment of labor: the capitalist buys a full labor day, but pays only for the hours required to produce the worker's necessities. The hours the worker works over and above what are required to produce his necessities represent unpaid, "surplus labor time." Profits relative to wages, "surplus value" relative to "variable capital" are both expressions for "the rate of exploitation.".

v. Marx's formula for the rate of exploitation:

Rate of Exploitation = profits/wages = s/v (surplus value/variable capital) = surplus labor time/necessary labor time.

e. The exploitation theory and the Marxian rhetoric: "wage slavery" and the capitalists as the heirs to the slave owners and feudal aristocracy—meant literally. Capitalists depicted as profiting on the same basis as slave owners—the capacity of the workers to produce more than is needed for their own subsistence.
f. Implications of the exploitation theory:

i. All progress passes the workers by—improvements are either in things still beyond their reach, or, if within their reach, their wages are cut correspondingly. Thus, the workers men without a country, with nothing to lose but their chains.

ii. Things are still worse: the doctrine of progressive impoverishment: the capitalists more calculatingly greedy than earlier exploiters and the falling rate of profit leads them to constantly increase the rate of exploitation in an effort to offset it. (The falling rate of profit inferred by Marx from a growing proportion of capital in the form of "constant" capital, which adds no value. Thus the surplus value added by fresh labor has to be spread thinner, with the result that the rate of profit falls unless the rate of exploitation is increased. Example: Total capital invested in whole economy initially equals 100 = 50v + 50c. Rate of exploitation is initially 100%. Then s = 50. Rate of profit = 50s/(50v + 50c) = 50%. Now total capital grows to 200, and all the growth is in constant capital. Thus, now, rate of profit = 50s/(50v + 150c) = 25%. Capitalists need to step up the rate of exploitation to offset the fall in the rate of profit.

iii. The working day and child labor—step up the rate of exploitation by squeezing more labor out the workers for the same subsistence.

iv. Sweat the worker—reduce the labor time needed to produce necessities.

g. Influence of the exploitation theory.

i. Assumed correct by almost everyone as a description of *laissez-faire* capitalism; believed not descriptive of present-day world because of government intervention.

ii. The corresponding interpretation of modern economic history—things bad in the past because of the unrestrained greed of the capitalists; better now because of government intervention.

iii. The whole "liberal" program a reflection of the influence of the exploitation theory: laws to limit working day—only the capitalists lose; abolition of child labor—only the capitalists lose; boost pay above subsistence through unions and minimum wage laws—again, only the capitalists lose; the welfare state—progressive income and inheritance taxes, on the one side, plus social welfare spending, such as for public housing, public education, social security, socialized medicine, etc., on the other—this seen as simply taking back some of the loot from the exploiters and returning it to the victims.

D. Critique of the Smith-Marx Framework—Implications of a Correct Positive Theory of Profits

1. Under C-M-C—the early and rude state—all income is *profits*, not wages. Demand for commodities is not demand for labor—product sales revenues but zero costs of production because no M laid out to bring in M.

2. Capitalists don't deduct profits from wages; they create productive expenditure, wages, and costs, which *reduces the profit share* and raises the wage share.

3. Producers in the pre-capitalist economy were profit earners, and the fundamental producers are now, too. The standard of the guiding and directing intelligence. Columbus and his crew. The President and the State Department employees. Ford and Rockefeller.

4. The problem of profits as a labor income and the variation of profits with the amount of capital invested. Adam Smith's denial of profits as a labor income (quoted in *Capitalism* on p. 476). Variation of profit with capital not a contradiction of their attribution to labor of businessmen—the capital is the means by which businessmen implement their ideas. Variation of results with the means employed does not contradict attribution to the intelligence which guides and directs the means.

E. The Productivity Theory of Wages

1. Plausibility of exploitation theory based on ideas of worker need and employer greed—both irrelevant: the cases of the used car and the art auction.

2. Labor useful & scarce—money wage rates fall no lower than corresponds to full-employment point (occupation by occupation, place by place). Then the scarcity of labor is felt. See *Capitalism,* Figures 14–1, 14–2. and 14–3 and the surrounding disucssion on pp. 613–618

3. Such a drop in wage rates (to the full-employment point) doesn't mean subsistence by the back door—the elimination of unemployment that the fall in wage rates brings about means more production and a fall in costs of production. Both mean lower prices. Real wages actually rise with the elimination of unemployment: not only lower prices corresponding to the lower wages, but also the elimination of the burden of supporting the unemployed—thus take home pay drops less than prices.

4. Real wages depend on the productivity of labor—the output per worker. Demonstration of how productivity works:

$$\text{Average money wage rate} = \frac{\textit{Demand} \text{ for } \textit{Labor}\ (D_L)}{\textit{Supply of Labor Employed}\ (S_L)}$$

$$\text{General consumer price level} = \frac{\textit{Demand} \text{ for } \textit{Consumers' Goods}\ (D_C)}{\textit{Supply of Consumers' Goods Sold}\ (S_C)}$$

a. Money supply (and thus monetary demands for labor and goods) constant, population constant, productivity of labor rising.

b. Money supply and thus monetary demands rising, population and productivity constant.

c. Money supply and productivity rising, population constant.

d. Money supply and productivity constant, population rising.

e. Money supply constant, productivity and population rising.

f. Money supply, productivity, and population rising.

5. An algebraic demonstration of the role of productivity in determining real wage rates:

Where
W = the average money wage rate
P = the general consumer price level
D_L = the aggregate demand for labor (total business payrolls)
D_C = the aggregate demand for consumers's goods (total expenditure to buy consumers' goods)
S_L = the supply of labor employed
S_C = the supply of consumers' goods sold
then

1. The average real wage (what the worker's money wages actually buy) = $\frac{W}{P}$

2. W = $\frac{D_L}{S_L}$

3. P = $\frac{D_C}{S_C}$

By substituting equations 2 and 3 into equation 1, we obtain

4. The average real wage = $\frac{D_L}{S_L} \div \frac{D_C}{S_C}$

By following the rule of inverting and then multiplying with the second fraction, we obtain

5. $\frac{D_L}{S_L} \times \frac{S_C}{D_C}$

Finally, by changing the order of multiplication, we obtain

6. $\frac{D_L}{D_C} \times \frac{S_C}{S_L}$

The supply of consumers' goods relative to the supply of labor reflects the productivity of labor. The demand for labor relative to the demand for consumers' goods can be called the "distribution" factor. It represents the extent to which wage payments are the source of consumption expenditure versus other sources of consumption expenditure, such as dividends.

6. Real wages and the economic degree of capitalism—$\frac{M}{M'}$: the higher is $\frac{M}{M'}$, the higher is $\frac{D_L}{D_C}$ and the higher is $\frac{D_K}{D_C}$. Thus the higher is the wage share of consumption and the more rapidly rising the productivity of labor (because of the higher capital goods share of total output).

a. The increase in the supply of capital goods and the rise in the productivity of labor also depends on the efficiency of the economic system—the productivity of capital goods. The higher the productivity of capital goods, the lower is the maintenance proportion and thus the more rapid the accumulation of capital for any given higher relative production of capital goods.
b. Both the wage share, the relative production of capital goods, and the productivity of capital goods depend on the security of property and economic freedom.

7. The futility of anything but a rise in the productivity of labor as a cause of higher real wages.

a. Increases in the quantity of money.
b. Less population.
c. D_L up at the expense of D_K.
d. Less consumption on the part of non-wage earners. Limited one-time rise in real wages, but can't obtain by

force—same issue as in redistribution discussion. (Capitalists quit if no ability to consume. Can only get higher wage share by voluntary inducement to save more, which requires security of property.) Cut in government spending and taxes increasing the demand for labor more potent, but also of a one-time nature. Rise in productivity the only source capable of large, continuing increase.

8. The productivity theory of wages explains why the standard of living was so low in the past, including long hours, child labor, and bad working conditions.

9. It explains how all these things improved—the higher productivity of labor based on *respect for private property rights and economic freedom*, which led to higher saving and a higher productivity of capital goods, thus to capital accumulation and a rising productivity of labor; also to higher wage share of consumption. All in degree of respect for private property rights.

a. Hours shortened and child labor eliminated by virtue of rising real wages based on higher productivity of labor—people could then *afford* to work less and keep their children at home longer. How the desire for shorter hours then made it profitable for employers to offer shorter hours.
b. Improvements in conditions achieved in the same way—more of them pay for themselves or workers are able to bear the cost of more of those that can't pay for themselves, because now they have higher real earnings.

10. Uselessness and harm of redistribution: almost nothing to redistribute; attempt to seize it cuts production: less saving, incentives, and capital accumulation, lower $\frac{D_L}{D_C}$—chaos of socialism.

11. The harm of maximum hours and child labor legislation and of forced improvements in conditions (the kind that don't pay for themselves).

a. Forced reduction in amount of labor—e.g., $\frac{D_L}{\frac{3}{4}S_L}$ results in $\frac{3}{4}S_C$ and thus in $\frac{4}{3}P$ (because $\frac{D_C}{\frac{3}{4}S_C} = \frac{4}{3}P$). Even if weekly or family money income the same, a loss in real terms. If workers work less, get less.
b. Forced improvements in conditions equivalent to forced wage increase: unemployment, higher prices; workers who keep jobs lose, because while prices go up, their take-home pay the same; if unemployment to be avoided, the take-home wages must drop to offset the cost of the improvements. Either way, they are at the expense of the workers, who can't afford them.

12. Labor unions.

a. Artificial wage inequalities if unions limited in ability to raise wages.
b. Unemployment if raise wage rates through whole system.
c. Lower productivity of labor because of unions' opposition to labor saving machinery and worker competition, and because of featherbedding practices and misallocation of labor.
d. The unions' wrong idea of how to raise the standard of living—they seek to raise money wages, when actually the standard of living rises only through improvements in the productivity of labor, which they fight. Money wages, free competition of individuals and the fallacy of composition.

13. Effects of minimum wage laws: unemployment, lower skill and lower pay long-term, because the unemployed workers don't gain experience. Preventing the less skilled from competing with the more skilled.

F. The Division of Labor and Productive Functions

1. The specific productive function of businessmen and capitalists: *to raise the productivity and remuneration of manual labor by creating, coordinating, and improving the efficiency of the division of labor.*

a. Create division of labor: found and organize business firms—the units of the division of labor; provide capital, without which little or no vertical division of labor (and which creates and raises the wage share of consumption).
b. Coordinate the division of labor: internal management, balance among the different branches of industry (uniformity-of-profit principle).

c. Improve efficiency of the division of labor: introduce improved products and methods of production; achieve a sufficient relative production of capital goods to achieve economic progress.

2. The productive function of financial markets and institutions and of passive capitalists: promote saving, investment out of saving, and the efficiency of investment.

a. Promote saving by providing opportunity to earn a rate of return.
b. Investment the same way.
c. Promote efficiency of investment by making it possible to provide use of one's saving to others who can use them more efficiently—e.g., small businessman and the electric utility.
d. Contributes to height of relative production of capital goods and thus to economic progress. (Note: productive role here only in context of division-of-labor economy and role of capital in production).
e. If the payment of interest and dividends to passive capitalists an exploitation, then at the expense of businessmen, not the wage earners. Implication of the widows and orphans exploiting Rockefeller. But not an exploitation—all gain. Also, investors usually need to perform some labor if no government bonds or government deposit insurance. Else make minimal rate of return—safety and trustee fees.

3. The specific productive function of the stock market in view of the criticism that only the purchase of newly issued stock actually provides funds to business firms.

a. Ability to sell shares encourages buying them in the first place.
b. Holders of outstanding stock can use the funds from its sale for new business purposes—e.g., the small businessman who sells his shares of GM or IBM to obtain money to expand his store.
c. Price of stock sets terms for sale of new shares.
d. Stock market gives more power to stockholders—individually, can sell if investment bad or need the money; low stock price resulting from bad treatment of small stockholders by management makes corporate takeover more likely; compels the management to consider the interests of the small stockholders; also, low stock price makes new financing less favorable.

4. The productive function of retailing and wholesaling:

a. Need distribution system because of division of labor—the products originate in great concentrations, must be brought to all. This the basis of the need for retailing and wholesaling.
b. These institutions lower distribution costs and achieve greater variety available to consumers.

The problem of assembling the ingredients of breakfast.

The case of the 100 manufacturers and the 1000 retailers.

5. Advertising—need information because of division of labor: the sellers and buyers separate parties.

a. More benefit from the same production—toothpaste brand A and brand B; a gain even if costs higher. But extra cost always limited—advertize lower price.
b. More research and development—faster acceptance of new products; consequent encouragement of research and development.
c. Promotes competition—new entrants need it to gain exposure. Going by experience alone favors the existing suppliers.
d. Works like a bond posted with public: usually only pays to advertize good products.

SECOND COURSE

SYLLABUS AND SYLLABUS SUPPLEMENTS

COURSE OBJECTIVES

1. To provide the student with a comprehensive knowledge of the operations of a free-enterprise, division-of-labor society, with special emphasis on the phenomena of money, production, real wages and the productivity of labor, profit, saving and capital accumulation, and economic progress. The consequences of government intervention with respect to these phenomena will be considered in depth.

2. To teach the student to think of economic phenomena in terms of their long-run effects on all groups, not merely their short-run effects on those directly concerned.

OVERVIEW OF THE COURSE

The course will focus on the current or recent problem areas of the banking system, unemployment, economic stagnation, budget and trade deficits, and inflation, in the light of the contrasting analyses of the Keynesian and "Classical" schools (the latter including the Chicago and Austrian schools). Policy solutions to these problems will be explored—in particular free-market wage rates, balanced budgets with low taxes, and limitation of money-supply growth versus expansionary fiscal and monetary policy.

Two leading themes of the course will be 1) The possibility of continuous capital accumulation and economic progress based on the combination of economic freedom, private ownership of the means of production, division of labor, saving, and technological progress. 2) The ethical implication of the harmony of the rational self-interests of all men under these conditions.

BOOKS FOR THE COURSE

A. George Reisman, *Capitalism: A Treatise on Economics*. Ottawa, Illinois: Jameson Books, 1996.

B. Henry Hazlitt, *Economics In One Lesson* (paperback).

C. George Reisman, editor, *Supplementary Readings in Macroeconomics* (to be distributed in class). [The essays contained in this title appear below with references to their original sources.]

D. Paul Samuelson and William Nordhaus, *Macro-Economics* (paperback), 15th Edition, (New York: McGraw Hill, 1995).

E. (Optional) Ludwig von Mises, *Human Action* (paperback), Third Edition.

COURSE CONTENT AND READING ASSIGNMENTS

(Note: This course meets just once a week, for four academic hours. This explains why the midterm examination coincides with the seventh class session.)

Week 1

Orientation/review. The dependence of the division of labor on money. The vital connection between money making and productive activity in a division-of-labor society. Money-making and the distinction between production and consumption, productive expenditure and consumption expenditure, capital goods and consumers' goods. The quantity theory of money. The increase in the quantity of money as the cause of rising prices.

READINGS

Reisman: pp. 141–144; 441–462

Optional: Samuelson, Chapters 1 and 4

Weeks 2 & 3

The origin and evolution of money and the contemporary monetary system: from barter to media of exchange, to gold and silver commodity money; 100 percent reserve banking and fractional reserve banking; standard money, fiduciary media, and fiat money. Central banking: the Federal Reserve System and its powers of money creation. The quantity of money, the demand for money, and the business cycle.

READINGS

Reisman: Chapter 12

Samuelson: Chapter 9 (to p. 173), Chapter 10

Frederic Bastiat "The Balance of Trade" and "A Petition" in *Supplementary Readings in Macroeconomics*. [Frederic Bastiat, *Economic Sophisms*, pp. 51–60]

Optional: Adam Smith "Of the Principle of the Commercial or Mercantile System," in *Supplementary Readings in Macroeconomics*. [Adam Smith, *The Wealth of Nations*, Book 4, Chapter 1]

Week 4

The economic problem and its denial: production versus consumption—the scarcity of wealth versus the alleged scarcity of the need or desire for wealth; the making of goods versus the making of work. Opposite appraisals of the causes of depressions, and of the economic effects of machinery, worker competition, war, government spending, population growth, advertising, foreign trade, imperialism, and technological progress.

READINGS

Reisman: pp. 42–49, 54–61, 542–559

Hazlitt: pp. 7-102 (chaps. I-XIV)

Week 5

Say's Law. Monetary demand and real demand; why only more production and supply can increase real demand. Say's Law and the harmony of long-run self-interests. Say's Law and the impossibility of a general overproduction; why falling prices caused by increased production do not represent deflation.

READINGS

Reisman: pp. 559–599

Optional: James Mill, "Consumption" and "Of the National Debt" in *Supplementary Readings in Macroeconomics* [James Mill, *Commerce Defended,* reprinted in *James Mill Selected Economic Writings*]; *Optional:* Samuelson, Chapter 12

Week 6

Mass unemployment: the causes and the remedy.

Real wages and the productivity of labor. Is government intervention to promote labor unions and raise wages in the self-interest of the wage earners or is its actual effect to cause unemployment and hold down the rise in real wages?

READINGS

Reisman: pp. 613–663

Hazlitt: pp. 134-151 (chaps. XIX-XXI)

Samuelson: Chapter 14

Week 7

MIDTERM EXAMINATION

Following midterm: Aggregate production and aggregate expenditure: the classical view versus the Keynesian view.

Week 8

The role of saving in spending and income payments. Saving versus hoarding. Saving and aggregate economic accounting: the national income/net national product identity. J. S. Mill's proposition that demand for commodities is not demand for labor and the issue of double counting.

READINGS

Reisman: pp. 673–699, review of 441–447, then 699–715

Hazlitt: pp. 177-190 (chap. XXIV)

Samuelson: Chapter 5; *Optional:* Samuelson, Chapter 11

Ludwig von Mises, "Capital Supply and American Prosperity" in *Supplementary Readings in Macroeconomics.* [Ludwig von Mises, *Planning for Freedom*, pp. 195–214]

Week 9

Capital accumulation and its causes. The role of saving. The role of technological progress and the productivity of capital goods. The role of economic freedom. Critique of the secular-stagnation doctrine. National income and consumption.

READINGS

Reisman: review of 622–642

Optional: Samuelson, pp. 326–333.

Week 10

Capital, the productive process, and the rate of profit. Profit and net consumption. Net investment and the rate of profit. Net investment and the increase in the quantity of money. The nominal and real rate of return on capital. Money supply growth and production growth. The springs to profitability. The inherent monetary profitability of business in the aggregate, in the absence of financial contractions.

READINGS

Reisman: 719–787

Optional: Samuelson, pp. 326–333.

Week 11

Applications of the net consumption theory: why there is no tendency toward a falling rate of profit with capital accumulation; why falling prices due to increased production do not reduce the rate of profit. The fundamental neutrality of technological progress with respect to the rate of profit. Analysis of the effects of taxation, budget deficits, and the balance of trade on the rate of profit and interest. Implications for the theory of saving.

READINGS

Reisman: pp. 809–838

Library reading: Ludwig von Mises, *Human Action,* Third Edition (Chicago: Contemporary Books, 1966), pp. 524-537. (The library at the Orange County Center has approximately a dozen copies of this book.)

Optional library reading: Eugen von Böhm-Bawerk, *Capital and Interest,* Huncke & Sennholz translation, Vol. II, pp. 77-118. (Please note: The library at the Orange County Center has at least a dozen copies of this book too.) Also recommended but not required: Vol. I, pp. 74-121; Vol. II, pp. 257-381.

Week 12

Relationship of the net-consumption/net-investment theory to the time-preference and productivity theories. The alleged problems of underconsumption and lack of “investment opportunities.” How the demand for capital goods and labor can permanently exceed the demand for consumers’ goods and the rate of profit be positive. More on why savings cannot outrun the need for savings; the automatic adjustment of the rate of saving to the need for capital.

READINGS

Reisman: pp. 787–797, 838–859

Week 13

Keynesianism and Neo-Keynesianism. Exposition and critique of the Keynesian analysis: the unemployment-equilibrium doctrine and the IS curve; the consumption and savings functions; the diminishing marginal efficiency of capital; liquidity preference and the liquidity trap; compensatory fiscal policy and the multipliers. The economic consequences of Keynesianism.

READINGS

Reisman: Chapter 18

Samuelson: Chapters 6–8 (to p. 142)

Optional: Samuelson, Chapter 15

Ludwig von Mises “Stones Into Bread, The Keynesian Miracle” and “Lord Keynes and Say’s Law” in *Supplementary Readings in Macroeconomics.* [Ludwig von Mises, *Planning for Freedom,* pp. 50–71]

Optional: Adam Smith, “Of Public Debts” in *Supplementary Readings in Macroeconomics*. [Adam Smith, *The Wealth of Nations,* Book 5, Chapter 3]

Week 14

Inflation. Exposition and critique of alternative theories of rising prices, leading to the conclusion that the quantity theory of money is the only valid explanation. The meaning of inflation. Its roots in deficits, the welfare state, and the unemployment and easy money arguments.

Further effects of inflation: a. growth in government, including wage and price controls; b. the redistribution of wealth and income; c. the undermining of saving and capital accumulation and the productivity of labor; d. how inflation sets the stage for depression and deflation—why it is not a cure for unemployment or a source of capital; e. why inflation tends to accelerate to the point of destroying credit and ultimately money itself.

The current state of inflation.

READINGS

Reisman: Chapter 19
Hazlitt: pp. 164-176 (chap. XXIII)
Ludwig von Mises, "Wages, Unemployment, and Inflation" and "The Gold Problem" in *Supplementary Readings in Macroeconomics* [Ludwig von Mises, *Planning for Freedom*, pp. 150–160, 185–194]
Library reading: Ludwig von Mises, *Human Action*, pp. 466-478.
Samuelson, Chapter 13

FINAL EXAMINATION

(Accompanies Weeks 1–3)

Introduction: The Contextual Setting

1. Economics and the division of labor—definition of subject in Chapter 1 of *Capitalism.*
2. The division of labor and the productivity of labor—how the division of labor is essential for a high and rising productivity of labor—Chapter 4 of *Capitalism.*
3. Wealth and natural resources—why production not limited by lack of natural resources—Chapter 3 of *Capitalism.*
4. Dependence of the division of labor on the institutions of capitalism, including the price system—Chapters 5–8.
5. Influence of the division of labor on the institutions of capitalism—Chapter 9.
6. Much of this course picks up from Chapter 2—"The Role of Wealth in Human Life": limitless need and desire for wealth; natural resources no obstacle; the problem is how to go on raising the productivity of labor. Division of labor and capitalism the on-going solution to this problem, which is called "the economic problem."

II. The Division of Labor and Money

A. Specific dependence of the division of labor on money

1. Problems of double coincidence of wants—money radically widens possibilities of exchange and thus division of labor.

2. Money and economic calculations and comparisons—of methods, products, industries, and jobs—allows existence of price system and its coordinating functions with respect to the division of labor, as described in Chapter 5.

B. Money Making and the Concept of Productive Activity

1. The need to earn money to participate in the division of labor; earning money thus an essential aspect of productive activity in a division of labor economy. The vital distinction between the labor of an unpaid housewife and a paid housekeeper.
2. The purpose of money making or not money making as the distinction between production and consumption.

    a. Consumptive production—consumers' physically productive activity versus that of business
    b. Productive expenditure and consumption expenditure
    c. Capital goods and consumers' goods
    d. Classification of capital goods and consumers' goods not based on physical characteristics—machines that are consumers' goods
    e. Producers' labor and consumers' labor
    f. Why government a consumer
    g. Producers' loans and consumers' loans; nature of government borrowing

3. The concepts of imputed income and opportunity cost.

a. Fictional incomes and costs based on the idea that the saving of an expense is an income and the absence of an income is a cost. They require the introduction of counterbalancing fictional costs and incomes. E.g., the fictional income of the homeowner and his fictional cost. Fictional housewives' income. The "income" of not having cancer.
b. "Opportunity cost": the successful businessman who runs at a loss; the "gains" of closing down your research department and reducing the alternative opportunities open to you. When to buy a yacht or jump from a skyscraper.

III. Money and Spending

A. The Quantity Theory of Money: the Formula of M_1 and Velocity

1. How more M raises D: the gold mining case and the social security case
2. The quantity theory of money as the explanation of rising prices
3. Fiat money versus commodity money; the increase in fiat money and spending versus the increase in the production of goods
4. Virtual impossibility of inflation problem with gold and silver; even now, prices calculated in gold and silver coins show no rise

B. The Origin and Evolution of Money and the Contemporary Monetary System

1. How rational self-interest led to the development of money out of barter
2. How it led to the selection of gold and silver as money.
3. How paper (including checkbook) money came into being.
4. Government and the demonetization of the precious metals: the Civil War, the National Bank Act, the Federal Reserve System, World War I (including the Federal Reserve and the pyramiding of gold reserves), the New Deal, the final break with gold in the 1960s.
5. Inflation and the potential spontaneous remonetization of the precious metals.
6. Recent change in the composition of the money supply and the deficiency of the weekly reported M_1 statistics

C. The Monetary System and Banking

1. Standard money—commodity money or fiat money.
2. The monetary base.
3. Fiduciary media: transferable claims to standard money, payable on demand, and accepted in commerce as the equivalent of standard money, but for which no standard money actually exists.
4. How fiduciary media are created.
5. Fractional-reserve banking and 100%-reserve banking.
6. Limits to the private issuance of fiduciary media: the clearing difficulties of more rapidly expanding banks; the public's demand for standard money.
7. Governmental encouragement of fiduciary media.

   a. Expanding the amount of reserves—fiat money reserves and central banking.

   b. Making reserves more potent: expanding reserves—overcomes the problem of the clearing, and of the public's demand for currency. Rediscounting, deposit insurance, bank examinations, restrictions on bank competition, payments suspensions.

8. Contemporary money creation: open market operations.

Open market operations and deficits.

D. The Quantity of Money and the Demand for Money

1. Velocity as the reflection of the demand for money for holding.
2. General factors affecting the demand for money for holding—security of property and complexity of production.
3. Changes in the quantity of money as the cause of changes in the demand for money and thus the velocity of money.

   a. The effect of credit expansion on the prospects for borrowing.

   b. The ability to substitute other assets for cash holdings.

   c. The anticipation of higher prices.

   d. The effect of more money on the rate of interest, which, after a temporary drop, is to raise the rate of profit and thus to increase the demand for and reduce the supply of loanable funds.

E. The Demand for Money and the "Balance of Payments" Doctrine: A Critique

1. The meaning of the balance of trade and payments.
2. Historical origins of the concepts (Mercantilism) and notion of what is a "favorable" or "unfavorable" balance.
3. The concepts under a system of fiat money—no loss in an outflow of fiat currency.
4. Mainly fictional nature of the outflows.
5. Foreign investment as the source of an "unfavorable" balance of trade.
6. The balance under a precious metal or other world-wide standard.

   a. Principle governing the distribution of precious metal money among the various countries.

   b. Why gold mining countries export gold.

   c. The tendency of the balance toward balance.

   d. sufficiency of precious metal money to transact commerce—loss of precious metals due to not enough production of goods; potential destructive role of labor unions

7. Inflation as the cause of a gold or other reserve outflow.
8. Error of blaming the citizens.

Spending abroad does not cause a money outflow if the citizens have a demand for the money.

F. An Invariable Money

1. Variations in prices from the side of money and the side of goods.
2. The need to isolate
3. The contribution of invariable money to economic theory.

(Accompanies Weeks 4–5)

IV. Production Versus Consumption—the Macroeconomic Implications of "Scarcity"

A. Scarcity

1. The reasons for postulating a limitless need and desire for wealth.

   a. Reason and the range of knowledge and awareness, hence of action and experience. Wealth the material means of action and experience.

   b. Scope and perfectibility of need satisfactions—based on reason.

   c. Why the desire for wealth always outstrips the ability to produce it: the nature of desires and the nature of production.

2. "Scarcity"—transformation of its nature under capitalism.
3. The scarcity of labor and its ineradicability.
4. Why does unemployment exist?
5. Time preference and the scarcity of capital.

   a. Meaning and foundations of time preference.

   b. Why time preference keeps capital scarce.

   c. What makes time preference high or low.

B. Productionism

1. According to productionism, *the fundamental problem of economic life is how to expand the ability to produce in the face of a limitless need and desire for wealth.*

2. The productionist aggregate demand curve, shown in Figure 13–2 of *Capitalism* on p. 546, is based on the quantity theory of money. It is asymptotic for a constant quantity of money and corresponding constant volume of spending and shows increases in the quantity of output and labor demanded in inverse proportion to the fall in wages and prices.

C. Consumptionism

1. The belief in a fixed aggregate demand in real terms and that *the fundamental problem of economic life is how to expand the need and desire for goods in the face of an ability to produce that exceeds it.*

2. Diagrammatic exposition of the consumptionist view of the relationship between aggregate demand and aggregate supply appears in Figure 13–1 of *Capitalism*, on p. 545.

D. Manifestations of Consumptionism

1. The fear of "overproduction."

2. The fear of machinery and automation.

3. The belief in a fixed stock of work to be done in the world.

4. The belief in inherent group conflicts over fixed employment opportunities.

5. The advocacy of make-work and spread-the-work schemes.

6. The belief that the lack of wealth is an asset and the presence of wealth is a liability.

7. The belief in the beneficial effect of war and destruction.

8. The belief that government spending is a source of prosperity.

9. The belief that population growth is a source of prosperity by increasing the number of people who need and desire goods and thus enlarging the supply of consumer desires.

10. The related support for a policy of imperialism.

11. The related belief in the balance of trade/payments doctrine.

12. The belief in parasitism as a source of benefit to its victims.

13. The belief that advertising is inherently fraudulent yet economically necessary.

14. A belief in the purposelessness and irrationality of economic life.

15. The misconception of the value of technological progress.

16. The belief that increases in production are "deflationary" by virtue of tending to cause falling prices.

Consumptionism and Socialism

E. The Productionist Answers on the Above Points

V. Say's (James Mill's) Law of Markets

A. Monetary Demand and Real Demand

1. Real demand is different than monetary demand, which is simply the monetary expenditure for goods and services. It is the monetary demand adjusted for changes in the price and wage level—*it's the goods and services the monetary demand actually buys.*

2. A smaller monetary demand at one time can constitute a larger real demand than a larger monetary demand at another time, if prices are sufficiently lower. E.g., a 200 monetary demand can constitute a larger real demand than a 400 monetary demand if prices are lower by more than fifty percent.

3. According to productionism, there is no inherent limit to aggregate real demand. *It depends only on the willingness and ability of people to produce.* If they are willing and able to produce more, then, given the quantity of money and the monetary demand, the price level will drop and the real demand will be increased. The actual quantity of output demanded is determined by the aggregate supply curve, which can be shown as a vertical line SS.

4. Determination of aggregate real demand by supply is shown in Figure 13–3 of *Capitalism*, on p. 561.

5. The determination of aggregate real demand by supply—the productionist/classical position—is known as *Say's Law,* after an early 19th century French classical economist, J.B. Say, who was a leading popularizer of the ideas of Adam Smith. It's usually stated as "supply creates its own demand."

6. More output per worker or more people able and willing to work results in more output that forces down prices, thereby increasing the real demand for output. (In the case of more people able and willing to work, the larger supply of labor also forces down wage rates, thereby increasing the real demand for labor as well as the real demand for goods.) In these cases, *supply is creating real demand via its effect on wages and prices in the face of unchanged monetary demands.*

7. Real demand has been defined as *the will combined with the power of purchasing.* On this definition, it's obvious that the only thing which can make possible more real demand is more supply. (The will to purchase can be taken for granted if the power is there—for, as we have seen, our desire for wealth exceeds our ability to produce it as the power of our imaginations exceeds the capacity of our arms.)

a. More monetary demand without more supply just means higher prices and thus no additional real demand—is not sufficient to create additional real demand.

b. It takes more supply to make a larger monetary demand into a larger real demand. Thus, more supply is *necessary* for the creation of more real demand.

c. But it doesn't take more monetary demand to create a larger real demand. More supply will do it with the same monetary demand, by way of reducing prices (and, if it's a larger supply of labor that is in question, wage rates).

Thus, more supply is both necessary and sufficient for the creation of more real demand. Supply, not more money, is what counts for real demand. More money is neither sufficient nor even necessary for more real demand. Only more supply creates more real demand.

B. The Referents of Say's Law

Say's Law refers to *aggregate—economy-wide*—demand in *real* terms. It does *not* mean that if the supply of some product is increased, the supply of *that particular product* will necessarily be accompanied by more monetary demand or even by more real demand. That may happen, but need not happen. An increased supply of a particular product can actually be accompanied by a lower monetary demand and by a lower real demand for that particular product. What Say's Law actually means, and which is brought out in such a case, is that the larger supply of a product *itself constitutes a larger real demand in the economic system as a whole.*

C. The Confirmation of Say's Law by Cases Apparently Contradicting It

The potato example in barter and in money. (See Table 13–1, on p. 563.)

D. Say's Law and Economic Adjustment: Partial, Relative Overproduction, But Never General or Absolute Overproduction (see Table 13–2, on p. 565).

E. Rounding Out the Picture: Say's Law and Competition

How those who introduce improvements usually benefit from them even if the industry as a whole loses.

F. Say's Law and the Average Rate of Profit

Aggregate profit equals D_C - D_L—i.e., Net Consumption—and is independent of the rate of increase in production and fall in prices.

Production increases, profitability, and the fallacy of composition (see Table 13–3, on p. 571).

G. Falling Prices Caused by Increased Production Are Not Deflation

(Accompanies Week 6)

VI. The Unemployment Controversy

A. The Problem

Wants are limitless, production is limited only by labor, thus labor is implicitly scarce. Why is there unemployment?

B. Productionist/Classical Economics' Answer

1. Inappropriate relationship between prices and wages on the one side and quantity of money and volume of spending on the other—especially in depression context.

2. Inflation—artificial money creation—raises V, sets stage for later drop in V and reduction in M, too. When this happens, spending drops, including spending for labor. Unemployment develops. (Review the discussion in Chapter 12 of how more rapid increases in the quantity of money operate to raise the velocity of money, which then must drop back when the increases stop, moderate, or fail to accelerate. Also the discussion of the deflationary potential in a fractional reserve banking system.)

3. Unemployment, which usually comes into existence on a large scale in just this way, could be eliminated by a drop in wage rates and prices. The lesser spending could buy all that the previously greater spending bought if prices and wage rates were lower. The wage-level formula together with the price-level formula show this. For the wage-level formula, see *Capitalism*, p. 581.

4. For ease of analysis, we assume full vertical integration—e.g., that GM owns its own steel mills, iron mines, etc., etc., and similarly for all other companies. Thus wages appear as the only cost of production and consumer demand as the only sales revenue. For purposes of illustration and ease of arithmetic, assume that initially the demands for goods and labor both fall by 10 percent, creating 10 percent unemployment. Full employment and full production could be restored at the reduced levels of spending, if wages and prices fell by 10 percent.

   a. The same aggregate money demand for labor can be stretched to pay an indefinitely larger number of workers at inversely proportionate wage rates. (See *Capitalism*, Figure 13–4, p. 581.)
   b. Further: the fall in wage rates and rise in employment reduces prices—output is expanded and prices fall as the result of the larger supply; also the larger supply is produced at lower unit costs because of the fall in wage rates. Thus prices fall both because of more supply and lower production costs.

5. Major implications

   a. Average business profitability is not reduced by virtue of the fall in prices, since it is preceded by a fall in unit costs to the same extent. Roughly speaking, total business profits equal the demand for consumers' goods minus the demand for labor. If these demands are stable at the lower levels, then total profits are not affected by changes in employment and output and wages and prices.
   b. If the productivity of labor (the output per unit of labor) stays the same, average *real* wages also do not fall, and, indeed, actually *increase*, because prices fall as much as wages, and the burden of supporting the unemployed is eliminated. (Note: this refers to *average* real wages, not real wages in each and every case.)
   c. Sequence is: lower wage rates permit more employment, by stretching the ability of the same total payrolls to employ labor. More employment means more production and lower prices. Profitability is not reduced because unit costs are cut to the same extent as prices. Real wages are not reduced because prices fall and the burden of supporting the unemployed is eliminated.

6. Freedom of competition and the pursuit of self-interest by the unemployed and by employers would achieve these results by driving down wage rates.

7. The obstacles to full employment—government intervention to keep up wage rates, forcibly prevent individuals from acting for their self-interests.

   a. Minimum wage and prounion legislation.
   b. Easy relief and employer altruism.

c. Government pressure—Pres. Hoover's White House Conferences in the 1929 depression.

A Problem to Test Your Understanding

Assume that total spending for consumers' goods and labor in the economic system both fall by 20 percent from 2000 and 1800 monetary units respectively.

1. If wage rates and prices stay the same, how much unemployment will be created in percentage terms?

2. How much must wage rates and prices fall to restore full employment?

3. Assuming that total business profits equal the demand for consumers' goods minus the demand for labor, what is the magnitude of total business profits:

   a. Before the fall in total spending?
   b. After the fall in total spending but before the fall in wage rates and prices?
   c. After the fall in wage rates and prices?

4. If the productivity of labor remains the same, and during the period of unemployment the average worker was contributing ten percent of his salary for the support of the unemployed, what is the effect on average real wages of the fall in money wages and prices?

Answers to questions 1-4 appear immediately below, with 180 degree rotation.
1. 20%, 2. 20%, 3a. 200, 3b. 160, 3c. 160, 4. rise by 1/9 compared with period of unemployment

C. Unemployment and the 1929 Depression

The result of preceding inflation and a fractional reserve banking system. Deepened by government intervention preventing wage rates from falling, which caused a further contraction in investment spending, and thus in business sales revenues and the ability to repay debts. Decline in the quantity of money by one-third.

D. Unemployment, the New Deal and World War II

1. Throughout the middle and late '30s, the quantity of money and volume of spending in the economic system were stepped up by the adoption of Keynesian policies, and yet unemployment remained a massive problem, because growing labor union power raised wage rates almost as fast, with the result that growing payrolls were not able to employ correspondingly larger quantities of labor.

2. And much of the additional employment that did take place was in the form of government employment, of a make-work variety, and actually caused a drop in the standard of living of those who already were employed, since they had to produce the goods and services which the government workers consumed, and received no comparable output in return.

3. Full employment was achieved only with the coming of World War II—not because war is necessary to full employment, but because the war was financed by massive inflation of the money supply *coupled with wage and price controls.* This combination generated sharply rising payrolls and spending of all types, and wage rates and prices were prohibited from keeping pace. The result was rapidly growing quantities demanded of everything, and the emergence of shortages, including a labor shortage. The full employment of World War II was accompanied by a sharp *decline* in the standard of living of the average person, who had to work longer and harder and who got much less in the way of goods for his efforts.

4. Full employment *with prosperity* was achieved only *after* World War II, as the result of the massive reduction in the size of government spending and deficits (from 1945 to 1946, Federal Government spending fell from approximately $93 billion to approximately $45 billion and the deficit was virtually eliminated). The prosperity resulted from the release of funds from the government back to the citizens and the transfer of roughly twelve million government workers (most of the army and navy) back to private employment. The citizens now had vastly greater control of their own incomes and previously unproductive labor was now available for production. The unions could achieve wage increases (which would have been given anyway) without causing unemployment or higher prices insofar as the end of the war provided the physical means for a vast transfer of resources back to the private economy and thus for a corresponding increase in real wages. (The abolition of price and wage controls and the ending of massive inflation also played a major role in the return to prosperity.)

E. A Rational Full Employment Policy

A policy that would actually achieve full employment and would do so with growing benefit to everyone, would be the establishment of a free labor market, so that wage rates would free to adjust to changes in the demand and supply of labor, and a 100-percent-reserve gold standard, so that the spending for labor would not be subject to sudden sharp contractions.

F. More on Why Real Wage Rates Need Not Fall in Achieving Full Employment

Analysis of arguments claiming that a fall in money wages would be accompanied by some fall in real wages as well. Diminishing returns and the need for profit recovery. The elimination of the burden of supporting the unemployed and the basis for believing that the productivity of labor rises with recovery from mass unemployment.

VII. The Productivity Theory of Wages

A. An Alternative to the Exploitation Theory

1. Plausibility of exploitation theory based on ideas of worker need and employer greed—both irrelevant: the cases of the used car and the art auction

2. Labor useful and scarce—money wage rates fall no lower than corresponds to full employment point (occupation by occupation, place by place). Any further fall is against the self-interests of the employers. For then the scarcity of labor is felt. (See *Capitalism*, pp. 613–618, especially Figures 14–1, 14–2, and 14–3 on pp. 615 and 616.)

3. Such a drop in wage rates (to the full employment point) doesn't mean subsistence by the back door—the elimination of unemployment that the fall in wage rates brings about means more production and a fall in costs of production. Both mean lower prices. Real wages actually rise with the elimination of unemployment: not only lower prices corresponding to the lower wages, but also the elimination of the burden of supporting the unemployed—thus take home pay drops less than prices. (Recall discussion of elimination of unemployment.)

B. The Productivity Theory of Wages

1. Real wages depend on the productivity of labor—the output per worker.

2. Demonstration of how productivity works

Some Problems

These are problems to test your understanding of the above. (Answers can be arrived at by following out the analysis in *Capitalism.* They are also given below, so that you can check your own against them and then go back and figure out why a discrepancy, if any, exists.)

1. Assume that the quantity of money, the aggregate monetary demands for consumers' goods and labor, and the supply of labor all remain the same, while the productivity of labor and thus the supply of consumers' goods double.

    a. What is the change in the general consumer price level?
    b. What is the change in average money wage rates?
    c. What is the change in average real wage rates?

2. Assume that the quantity of money and thus the aggregate monetary demands for consumers' goods and labor both double, while the supply of labor, the productivity of labor, and the supply of consumers' goods all remain the same.

    a. What is the change in the general consumer price level?
    b. What is the change in average money wage rates?
    c. What is the change in average real wage rates?

3. Assume that the quantity of money, the aggregate monetary demands for consumers goods and labor, and the productivity of labor and supply of consumers' goods all double, while the supply of labor remains the same.

    a. What is the change in the general consumer price level?
    b. What is the change in average money wage rates?

c. What is the change in average real wage rates?

4. Assume that the quantity of money, the aggregate monetary demands for consumers' goods and labor, the productivity of labor, and the supply of labor all double.

a. What is the change in the general consumer price level?
b. What is the change in average money wage rates?
c. What is the change in average real wage rates?

5. What factor in the problems determines the change, if any, in average real wage rates?

6. What factors in the same problems determine the change, if any, in average money wage rates?

7. What factors in the above sets of problems determine the change, if any, in the general consumer price level?

Answers to questions 1-7 appear immediately below, with 180 degree rotation.

1a. halves, 1b. none, 1c. doubles; 2a. doubles, 2b. doubles, 2c. none; 3a. none, 3b. doubles, 3c. doubles; 4a. halves, 4b. none, 4c. doubles; 5. The productivity of labor. 6. Demand for and supply of labor. 7. Demand for and supply of consumers' goods

C. The Productivity of Labor and Capitalism

1. Dependence of real wages on the economic degree of capitalism—i.e., the higher is productive expenditure relative to sales revenues, the higher is the demand for labor by business relative to the demand for consumers' goods and the higher is the demand for capital goods relative to the demand for consumers' goods. Thus the higher is the wage share of consumption and the more rapidly rising the productivity of labor (because of the higher capital-goods share of total output).

2. The increase in the supply of capital goods and the rise in the productivity of labor also depends on the efficiency of the economic system—the productivity of capital goods. The higher the productivity of capital goods, the lower is the maintenance proportion and thus the more rapid the accumulation of capital for any given higher relative production of capital goods.

3. Both the wage share, the relative production of capital goods, and the productivity of capital goods depend on the security of property and economic freedom—viz., on capitalism.

D. The Productivity Theory of Wages and the Interpretation of Modern Economic History

1. The cause of low real wages and bad conditions in the past.

2. How things improved—rise in the productivity of labor the only possible cause.

a. Uselessness of more money.
b. Virtual uselessness of more monetary demand for labor from any other cause.
c. Uselessness/harm of less supply of labor.

E. The Productivity Theory of Wages and a Critique of the Intellectual Foundations of the Welfare State

1. Uselessness and harm of redistribution

a. Almost nothing to redistribute
b. Attempt to seize it cuts production: less saving, incentives, and capital accumulation, lower demand for labor relative to the demand for consumers' goods—the chaos of socialism

2. Labor unions

a. Artificial wage inequalities if unions limited in ability to raise wages.
b. Unemployment if raise wage rates through whole system.
c. Lower productivity of labor because of unions' opposition to labor saving machinery and worker competition, and because of featherbedding practices and misallocation of labor.

d. The unions' wrong idea of how to raise the standard of living—they seek to raise money wages, when actually the standard of living rises only through improvements in the productivity of labor, which they fight. Money wages, free competition of individuals, and the fallacy of composition.

3. Minimum wage laws

a. Unemployment, lower skill and lower pay long-term, because the unemployed workers don't gain experience.
b. Preventing the less skilled from competing with the more skilled.

4. Maximum hours and child labor legislation

Forced reduction in amount of labor performed—e.g., D_L divided by $3/4S_L$ results in $3/4S_C$ and 4/3P (because D_C divided by $3/4S_C$ = 4/3P). Even if weekly money income the same, there is a loss in real terms. If workers work less, get less.

5. Forced improvements in working conditions (the kind that don't pay for themselves)

Forced improvements in conditions equivalent to forced wage increase: result is unemployment and higher prices; workers who keep jobs lose, because while prices go up, their take home pay the same (in addition, they must support the unemployed); if unemployment is to be avoided, the take home wages must drop to offset the rise in the cost of the improvements. Either way, they are at the expense of the workers, who can't afford them.

(Accompanies Weeks 8–9)

VIII. AGGREGATE PRODUCTION AND AGGREGATE SPENDING

A. Aggregate Production

1. Classical economists' view of what is produced—see Figure 15–1 on p. 675 of *Capitalism*
2. Gross product, productive consumption, and net product.
3. Contemporary, Keynesian economics' view of production as merely the *gain* from production—the net product.

a. Confusion of who produces what.
b. View of the product as the gain from production leads to the view that the *total product is the final product.* For every product except the final one is subtracted from production in the next stage.
E.g., the notion that bread is the total product of wheat farmers, millers, and bakers follows from viewing the production of each of the producers as the difference between his product and his productive consumption. Thus, over Years 1 - 3 combined,

$$x_1 + y_1 - x_1 + z_1 - y_1 = z_1$$

c. Note: *production is being conceptually obliterated insofar as it is productively consumed.* Only the production of consumers' goods is considered as real.

4. Contemporary, Keynesian economics' Platonic-Heraclitean view of entities.

a. The notion that the total product in the sense of total product additions (or product differences) is the final product supports the confusion that the final product is the total product in the sense not of mere "product additions," but in the sense of *actual physical entities.*

Bread = Bread - Flour + Flour - Wheat + Wheat

and its alternative formulations:

Bread = *(Bread - Flour + Flour - Wheat + Wheat) = Bread*

Bread = Bread - Flour + *(Flour - Wheat + Wheat) = Flour* + fade out

Bread = Bread - Flour + Flour - Wheat + *(Wheat) = Wheat* + fade out

b. On this view, a loaf of bread is not conceived of as a thing that exists independently, out there in reality—that is, as a simple loaf of bread. It is conceived instead as a bundle of abstractions: bread minus flour, plus flour minus wheat, plus wheat minus zero (zero, for the sake of brevity and simplicity).
c. If all three of these abstraction are held together, as indicated by the placement of the parentheses and use of italics, then bread is conceived of as bread.
d. If the abstraction bread minus flour is placed on dim, as it were, and allowed to fade from consciousness (as indicated by its removal from within the parentheses and appearance in roman type), the result is that the loaf of bread now appears as flour minus wheat plus wheat minus zero—that is, it now appears as flour.
e. If, finally, the two abstractions bread minus flour and flour minus wheat are both placed on dim, (as indicated by their removal from within the parentheses and appearance in roman type), then the loaf of bread appears as wheat.
f. In this way, a loaf of bread appears as a loaf of bread, a quantity of flour, and a quantity of wheat.
g. It is on this basis that the value of the loaf of bread appears to count the value of the loaf of bread, the value of the flour from which it was made, and the value of the wheat from which the flour was made. And on this basis, counting the value of the bread, the flour, and the wheat separately appears to imply counting the value of the flour and wheat more than once. (See Table 15-1 on p. 681 of *Capitalism* and the equation on the next page showing how contemporary, Keynesian economics views $775 as counted by $300.)

h. Simple version: 6 "counts" 14.

6 = 1 + 2 + 3. Let 1 equal the value added by the baker, 2 the value added by the miller, and 3 the value added by the wheat farmer. Then, according to contemporary, Keynesian economics

(1) 6 = *(1+2+3),* which is the value of the bread

(2) 6 = 1 + *(2+3),* which is 1 plus the value of the flour

(3) 6 = 1 + 2 +*(3),* which is 1 plus 2 plus the value of the wheat

i. In all of these cases, 6, the value of the bread actually counts *only* the value of the bread. But it is viewed by contemporary, Keynesian economics as counting the value of the flour and the wheat as well. It could count the value of the flour and wheat in addition to that of the bread only if 6 equalled (1+2+3) + (2+3) + (3), that is, only if 6 equalled 14. Ironically, it is contemporary, Keynesian economics that double counts: it counts the bread as counting the value of the bread plus the value of the flour plus the value of the wheat. This is double counting the value of the bread, which leads to the failure to count the value of the flour and wheat, in the mistaken belief that they've already been counted.

j. What is present in contemporary, Keynesian economics is a *Platonic-Heraclitean view of entities.* It is a view of entities not as independently existing physical objects which man's mind must grasp, but as the creation of the human mind in the form of bundles of abstractions which can be put together and taken apart at will to form different entities. I call it Platonic in that it views entities as consisting of abstractions. I call it Heraclitean, in that it presents a kaleidoscopic flux, in which a thing is alleged to be simultaneously itself and other things. Instead of the Aristotelian formula that *A is A*—a thing is itself—we have the formula that *A is A+*—a thing is itself plus more than itself.

k. Contemporary, Keynesian economics' confusions about "double counting" and its belief that the final product counts the total product—that it *is* the total product—leads it to *ignore most spending in the economic system,* along with most of production. (Its confusions are supported by the confusions of many non-economists about the nature of entities and about what one buys when one buys it.)

B. Aggregate Spending

1. What is bought when it is bought?

a. The buyers of goods do not buy the means of producing the goods they buy, nor the means of producing similar goods in the future, nor the products that may be produced from those goods.

E.g., the buyer of a loaf of bread does not buy the flour, wheat, or labor services that were used to produce his loaf of bread—those things were bought by the producers at the various stages.

Nor does he buy the flour or labor services that the seller of the bread may subsequently buy, nor make the latter's research outlays, political or charitable contributions, or any other such outlay.

Nor does he buy a loaf of toast in buying a loaf of bread. He buys only the loaf of bread.

2. Absurdities of the Platonic-Heraclitean view of purchases:

a. Shadow purchases. Bread, flour, and wheat—all for the same money, all in the same wrapper, and all for the same calories. Contrast with *real* combined expenditures.

b. Amazing digestive powers.

c. The ice in the steam.

d. Why do producers need capital if it is the consumers who buy what they buy?

e. If you buy the inputs, you don't have to buy the output—you already own it; you buy the output because you *haven't* bought the inputs.

3. Need for recognition of the full parity of existence of capital goods and of expenditure for capital goods and labor.

The implicit Aristotelianism of the Classical Economists. John Stuart Mill's explicit recognition of the entity issue in his proposition "demand for commodities is not demand for labour."

4. Mill's proposition should be restated as *The Demand for A is the Demand for A.*

C. Saving and Demand

1. Saving vs. hoarding

a. Belief that consumption expenditure buys everything implies that there is nothing for savings to buy. Thus, promotes the view that saving is hoarding.
b. Saving does not mean hoarding as per Keynes and today's financial press: "leakages"; presumed effects of higher saving rate; corollary doctrine of investment out of nowhere; same idea for taxes and government spending.
c. Idea that saving is hoarding represents fallacy of composition; aggregate nominal saving implies equivalent increase in nominal value of assets, since cash hoarding by any individual just represents an equivalent dishoarding by someone else (the extent to which the money supply increases is the only exception).
d. Genuine "hoarding" (i.e., increase in need and desire to hold cash) has nothing to do with saving—represents an attempt to change composition of existing savings from assets other than cash to cash.
e. Precipitated by preceding credit expansion, which causes business firms to become illiquid and thus to have to restore their liquidity later on. Result is financial contraction and simultaneous wiping out of nominal net saving, which may become negative.

2. What is saved is spent and actually accounts for *most* spending in the economic system

a. Expensive consumers' goods
b. All the spending for capital goods—*viz.*, all the spending for goods at wholesale, all the spending for machinery, equipment, materials, components, and supplies, and all the wage payments made by business firms. These expenditures are made *by business firms, not by consumers*; they are not consumption expenditures, but *productive expenditures*—viz., expenditures made for the purpose of making subsequent sales. (Consumption expenditures, in contrast, are expenditures made not for the purpose of making subsequent sales.) The productive expenditure in payment of wages, moreover, is the source of the great bulk of consumption expenditures.
c. Thus the great bulk of spending in the economic system is productive expenditure, not consumption expenditure.
d. Productive expenditure depends on saving—on the portion ofs their revenues and incomes that people do not consume.
e. To the extent that people consume more of their revenues and incomes, and save less, their ability to make productive expenditures is less. If everyone did nothing but consume, there would be no productive expenditure. E.g., the case of buying goods from a store, whose owners used the proceeds to consume, which is followed by repeated rounds just of consumption out of sales revenues. Only additional consumption would exist in such a case. The only additional income would be *profit.*

3. The "Macroeconomic" Dependence of the Consumers on Business

—in contrast to the "microeconomic" dependence of the individual company and industry on the consumers. The two opposite dependencies are consistent in that competition is present at the microeconomic level, but not at the macroeconomic level.

a. Business as the source of its own demand and profitability: The role of productive expenditure and net consumption in the generation of aggregate sales revenues. (See *Capitalism,* pp. 725–744.)
b. No need for artificial consumption.

4. Saving increases real demand by increasing production.

5. Saving increases monetary demand by bringing about an increase in the production and supply of commodity money.

6. Saving increases consumption in the long run by bringing about an increase in the production and supply of goods.

D. Aggregate Economic Accounting on an Aristotelian Base

1. The accounting aggregates

a. What national income (Y), net national product (NNP), and gross national product (GNP) *are,* and their mutual relationships
b. The essential relationship:

$$p + w + i + r = Y = NNP = C + I$$

c. Relationship of NNP and Y to GNP.

2. Keynesian confusions

a. As shown, contemporary, Keynesian economics obliterates the role of saving and productive expenditure.
b. In its eyes, almost all of spending is consumption expenditure. The only other expenditure it recognizes is net investment or what it calls gross investment, which is actually nothing more than net investment plus depreciation allowances. The allegedly gross investment of contemporary, Keynesian economics is plant and equipment spending plus *net investment in inventories.* It is not truly gross at all.
c. Because consumption spending is quantitatively much larger than net or even gross investment, it is usually assumed that consumption spending *pays* the far greater part of national income and constitutes the far greater part of spending for goods and services in the economic system. This view is present in every depiction of national income as being determined by the sum of consumption plus net investment—e.g., the Keynesian cross.

3. An accurate conception: recognizing the role of productive expenditure

a. An accurate conception of aggregate spending and its relationship to contemporary national income accounting follows below:
KEY: s = aggregate business sales revenue, s_b = that part of aggregate business sales revenue paid by business firms and constituting part of productive expenditure, s_c = that part of aggregate business sales revenue paid by consumers and constituting part of consumption expenditure, w = aggregate wages, w_b = that part of aggregate wages paid by business firms and constituting part of productive expenditure, w_c = that part of aggregate wages paid by consumers and constituting part of consumption expenditure, d = aggregate costs deducted from aggregate business sales revenues in computing aggregate profits, C = aggregate consumption expenditure insofar as it constitutes business sales revenues or the payment of wages, B = aggregate productive expenditure insofar as it constitutes business sales revenues or the payment of wages, I= net investment.
b. On the basis of the above, it can easily be shown that most of the spending and the income payments in the economic system *are concealed under net investment,* which, in effect, is the visible portion of an iceberg. These conclusions become crystal clear if we derive the equality of national income and consumption plus net investment from the definition of national income. Thus:

(1) $p + w = Y$, by definition.

(2) $p = s - d$

(3) $s - d + w = Y$, by substituting (2) into (1).

(4) $s = s_c + s_b$,

(5) $w = w_c + w_b$

(s_c, s_b, w_c, and w_b can aptly be termed *revenue-expenditure subcomponents* of national income and net national product, in that they simultaneously represent revenue or income, when viewed from the perspective of sellers, and expenditure, when viewed from the perspective of buyers.)

(6) $s_c + s_b - d + w_c + w_b = Y$, by substituting equations (4) and (5) into (3).

(7) $s_c + w_c + s_b + w_b - d = Y$, by a change in the order of addition of the revenue-expenditure subcomponents.

(8) $s_c + w_c = C$, by definition, (i.e., consumption expenditure for goods and services purchased from business firms plus consumption expenditure in payment of wages equals total consumption expenditure)

(9) $s_b + w_b - d = I$

(10) $C + I = Y$, by substituting equations (8) and (9) into equation (7).

The full statement of the relationship between national income and net national product is:

(11) $p + w = (s_c + s_b - d) + (w_c + w_b) = (s_c + w_c) + (s_b + w_b - d) = C + I = Y$.

4. Demonstration that Productive Expenditure Minus Costs Equal Net Investment

a. The productive expenditure for buildings and equipment versus depreciation cost.
b. The productive expenditure for materials, parts, and labor versus cost of goods sold.
c. Other productive expenditures and costs are expensed expenditures and net to zero. Thus,

$$B\text{-}d = B_1\text{-}d_1 + B_2\text{-}d_2 + B_3\text{-}d_3 = I_1 + I_2 + I_3 = I.$$

E. Gross National Revenue

(12) $s + w = GNR = C + B$

From this equation, it is possible, as shown in Table 15–4, on page 707 of *Capitalism*, to go directly to national income on the left, and to net national product on the right, by subtracting aggregate business costs (d) deducted from sales revenues in computing profits. On the left, d is subtracted from s, which results in aggregate profit, p. On the right, it is subtracted from productive expenditure, which results in net investment, I.

If, in this procedure, one subtracts all costs but depreciation cost, one arrives at the contemporary, Keynesian concept of GNP. That is, one has profit gross of depreciation on the left, and “gross” investment—i.e., plant and equipment spending plus the *net* investment in inventories—on the right.

F. The Optical Illusion of Consumption as the Main Form of Spending

Table 15–3 on p. 706 in *Capitalism*, is an arithmetical example that clearly illustrates the illusion of viewing consumption spending as the main source of revenue and income payments in the economic system. (The example’s relative breakdown of national income between consumption and net investment approximates the actual data found in a typical year.)

1. Questions to test your understanding: Using the numerical data presented in Table 15–3 as an example, answer the following questions:

a. Find total sales revenue and income payments in the economic system.
b. Find the portion of total sales revenue and income payments constituted by consumption expenditure.
c. Find the portion of total sales revenue and income payments constituted by productive expenditure.
d. What portion of wages is paid by consumption expenditure?
e. What portion of wages is paid by productive expenditure?

2. Application of answers to a critique of the Keynesian multiplier doctrine.

a. The only incomes raised by the successive rounds of consumption expenditure envisioned by the multiplier doctrine would be profits, not wages. Any rise in wages, in the demand for goods at wholesale, in the demand for capital goods of any kind depends on *saving*, which the Keynesians regard as a “leakage” and as allegedly diminishing the amount of subsequent incomes.
b. See Samuelson’s multiplier discussion
c. Plug in his 1000 of initial “investment” into s_b and his implied 2000 of induced consumption into s_c.
d. State the increase in wages.
e. State the increase in profits.
f. Check your results against Table 15–5, on p. 708 of *Capitalism.*
g. Assume 500 of the “initial investment” is in the form of wage payments.

h. Repeat steps (d) and (e) above.
i. Samuelson's assumed "marginal propensity to consume" (mpc) in the table is 2/3; rework your answers to (d) and (e) on the assumption that the mpc is .75, .9.

Answers to questions 1a–e and 2d, e, g, and i appear immediately below, with 180 degree rotation.

1a. 1450, 1b. 550, 1c. 900; 1d. 50, 1e. 400
2d. zero; 2e. 3000, 2g. 500, 2500, 2i. zero, 4000; 500, 3500; zero, 10000; 500, 9500

G. Review of Capital Accumulation and thus Real Wages as Dependent on the Relative Production of Capital Goods and the Productivity of Capital Goods

1. The requirements of capital accumulation

a. Real wages depend on the productivity of labor—viz., on the output per unit of labor, which depends on the supply of capital goods per worker.
b. The supply of capital goods depends on the demand for capital goods relative to the demand for consumers' goods. This determines the relative production of capital goods, which must exceed the proportion necessary for maintenance, if capital accumulation is to take place.
c. Capital accumulation also depends on the *productivity* of capital goods—*viz.*, on the output per unit of capital goods. (See Figures 15–5 and 15–6 on pp. 710 and 711 in *Capitalism.*) This determines the maintenance proportion and the ability of any given relative production of capital goods to result in capital accumulation.
d. A sufficiently high relative production of capital goods and a constant productivity of capital goods—sustained by technological progress and innovation—causes a *continuing* increase in the supply of capital goods and thus a continuing increase in the productivity of labor and in real wages.

2. The theoretical significance of giving parity of recognition to the production of capital goods:

a. This is what makes it possible to see how more capital goods are *themselves* a source of still more capital goods and the role in capital accumulation of the productivity of capital goods, technological progress, and everything else that contributes to the productivity of capital goods—above all, economic freedom. For when more capital goods come into existence, it is clear that they are used to produce *capital goods* as well as consumers' goods and that the supply of capital goods *depends on everything that production and supply in general depend on.* These identifications are impossible if one proceeds as though all that is being produced are consumers' goods.
b. In combination with the assumption of invariable money, the recognition of the parity of existence of capital goods also makes it possible to see the role of saving in terms of force/acceleration, not simple motion.
A greater relative production of capital goods, greater saving and demand for capital goods relative to the demand for consumers' goods is not necessary for capital accumulation once a sufficiently high degree of saving and demand for capital goods exists—as seen, that's accomplished on the basis of the larger supply of capital goods in the year before, coupled with technological progress. More saving and demand for capital goods relative to the demand for consumers' goods would serve not to sustain but to accelerate capital accumulation.

H. Capital, the Productive Process, and the Generation of Sales Revenues and Costs—a First Look

a. The Diagrammatic Analytical Framework Using Figures 15–5 and 15–6, pp. 710 and 711 of *Capitalism.* Reinforcement by means of Tables 15–6 and 15–7 on pp. 713 and 714.
b. The Inverse Relationship Between National Income and Economic Progress in an Economy With an Invariable Money
c. Overthrow of the Keynesian Balanced Budget Multiplier Doctrine and the Doctrine of the "Conservative's Dilemma"

(Accompanies Weeks 10 and 11)

IX.THE NET CONSUMPTION, NET INVESTMENT THEORY OF AGGREGATE PROFIT: THE POSITIVE THEORY

All business activity is carried on for the purpose of earning a profit. What determines the average rate of profit in the economic system? Do technological progress and improvements in business efficiency raise the average rate of profit?—or, on the contrary, do they lower it by enlarging the supply of goods and thereby causing falling prices and alleged deflation? Do saving and capital accumulation imply a falling rate of profit? Does additional saving place business in the contradictory position of having more money available to invest at the very time its sales revenues are reduced because the consumers are saving instead of spending? Can there be such a thing as *too much* of an increase in production or *too much* saving? The following weeks' classes will answer these questions and satisfactorily resolve the implied paradoxes.

A. Net Consumption and the Generation of an Excess of Sales Revenues Over Productive Expenditure and Costs

1. The Nature and Problem of Aggregate Profit

a. The treatment of interest.

b. Profits at the macro level determined by different factors than at the micro level.

c. Profits as the result of the difference between the demand for products and the demand for factors of production, not the demand for and supply of capital.

d. The problem of aggregate profit: productive expenditure and the generation of equivalent sales revenues and costs.

2. Net Consumption—i.e., consumption in excess of the wage payments by business, which is financed by dividends, draw, and interest payments.

3. Net Consumption and the Generation of an Excess of Sales Revenues Over Productive Expenditure (see Tables 16–1 and 16–2, on pp. 726 and 727; Figure 16–1, on p. 729; Table 16–3 on p. 730 and Figure 16–2 on p. 732).

4. The Rate of Net Consumption and the Rate of Profit

5. Net Consumption: Its Other Sources, Wider Meaning, and Relationship to the Saving of Wage Earners

6. Confirming the Critique of the Exploitation Theory
See Table 16–4, on p. 736 for the implicit basis of the primacy of profits doctrine presented in Chapter 11.

B. The Net Consumption Theory Further Considered

1. Why Businessmen and Capitalists Cannot Arbitrarily Increase the Rate of Net Consumption and the Rate of Profit

2. Implications for the Gravitation of Relative Wealth and Income

3,. Accumulated Capital as a Determinant of Net Consumption

4. An Explanation of High Saving Rates out of High Income

5. Net Consumption and Time Preference

6. The principle of time preference

7. The foundations of time preference

8. Time preference, rationality, and freedom

C. Net Investment as a Determinant of Aggregate Profit and the Average Rate of Profit

See Tables 16–5, p. 745; 16–6, p. 747; and 16–7, p. 749; see also the equations on p. 748, which show why aggregate profit equals the sum of Net Consumption plus Net Investment.

1. The Net Investment Rate as a Determinant of the Average Rate of Profit

2. Net Investment Versus Negative Net Consumption (see Tables 16–8 and 16–9 on pp. 751 and 752)

3. The Prolongation of Net Investment Under an Invariable Money

4. Net Investment as the Result of the Marginal Productivity of Capital Exceeding the Rate of Profit

5. Net Investment as a Self-Limiting Phenomenon

6. Capital Intensification and the Tendency Toward the Disappearance of Net Investment Under an Invariable Money

7. The Process of Capital Intensification (see Table 16–10, p. 760)

D. The Addition to the Rate of Profit Caused by Increases in the Quantity of Money

See Figures 16–2 and 16–3 on facing pages 764 and 765.

1. The Impact of Increases in the Quantity of Money on the Net Investment and Net Consumption Rates (see Tables 16–11 through 16–15 in *Capitalism*)

2. Increases in the Quantity of Money and the Perpetuation of Net Investment

3. The Tendency of the Rate of Net Investment to Equal the Rate of Increase in the Quantity of Money and Volume of Spending

4. Summary Statement of the Determinants of the Rate of Profit

E. Increases in the Real Rate of Profit Dependent on Increases in the Production and Supply of Goods

1. Net Investment Without Increasing Capital Intensivity

2. Capital Saving Inventions

F. The Inherent Springs to Profitability

1. The Net Consumption Spring to Profitability. So long as net consumption exists, the only way an aggregate profit will not exist is if there is equivalent *negative net investment.* This situation is necessarily temporary.

2. The Indirect Net Investment Spring—Via Net Investment and Greater Capital Intensivity Causing a More Rapid Increase in the Quantity of Commodity Money in Conjunction with the Resulting More Rapid Increase in Production

3. The Direct, Net Investment/Greater Capital Intensivity Spring.
The potential for additional net investment represents a further "inherent spring toward profitability," in that whenever aggregate profitability is lacking, all that need occur to restore it is further net investment. At the same time, net investment *is positively encouraged by the fact that the lower is the rate of return on capital, the greater is the degree of capital intensivity that pays.*

4. Why net investment is encouraged by a lower rate of return (Note: beware the fallacy of composition in confusing this case with the case of an individual industry, in which a low rate of profit *relative to the rate of profit in other industries* discourages investment, in fact, encourages *dis*investment.)

5. The railroad tunnel case as an illustration of the rate of return as the standard for cost savings that are necessary to make more capital intensivity pay.

6. The case of methods A, B, and C, requiring different capital intensivities—see Table 16-16, p. 781 of *Capitalism.*

7. The case of the older and younger scotches

8. The effects of a lower rate of return on the profit margins and prices of more and less capital intensive industries; why it favors the expansion of the more capital intensive—see Table 16-17, on p. 782 of *Capitalism.*

9. Wage Rate Rigidities and the Blockage of the Springs

10. Note: a higher rate of return reflecting a more rapid increase in the quantity of money and volume of spending need not discourage investment. The scotch case as a demonstration: the rising volume of spending operates equally on the price and profit of the younger scotch and the older scotch, thus the less capital intensive product is not favored here. (See the subsection "Capital Intensiveness and the Monetary Component in the Rate of Profit).

X. The Net Consumption/Net Investment Theory and the Leading Alternative Theories

A. Exposition and Critique of the Productivity Theory in Its Traditional Form.

1. The meaning of the productivity theory and its illustration in terms of Roscher's famous boat and net example.

2. Problems: (a) presence of opportunity-cost doctrine (b)and what if loaves of bread forgone to obtain added fish? How calculate return? (c)Highest rate of return exists before any productivity of capital.

3. Why the productivity of capital by itself can't explain the rate of profit: lower prices of products. A case of increased output, and thus increased productivity, but no change in aggregate profitability if the aggregate monetary magnitudes are the same. Presence of the fallacy of composition.

4. But productivity in form of cost savings or quality improvements could induce net investment and in that way raise the rate of return.

5. The productivity theory's mistaken view of technological progress as the source of demand for capital and a higher rate of profit, rather than as a source of supply of capital goods; Ricardo's insights here.

B. Exposition and Critique of the Time Preference Theory in Its Traditional Form.

1. An example of the formula of the time preference theory: 10 present apples are equal in value to 11 apples to be available one year later, and to the total of the means of producing those 11 apples; in one year, the means of producing these 11 future apples become 11 present apples. Hence, factors of production worth 10 present apples become products worth 11 present apples.

2. Problems of a pure time preference theory: confusion of real and money rate of profit; the formula and the doctrine of the purchasing power premiums; the discounting approach; the marginal future unit is more valuable than the first sub-marginal present unit—Böhm-Bawerk's concession. Omission of the role of net investment and the quantity of money.

C. The Classical Basis of the Net Consumption Theory

1. Ricardo on profits rising as wages falling, and vice versa. Can be interpreted as net consumption rising or falling and productive expenditure or wage payments moving in the opposite direction in the context of invariable money.

2. John Stuart Mill on "demand for commodities is not demand for labor." Net consumption represents a demand for consumers' goods over and above the demand for labor, and a demand for commodities over and above the demand for factors of production to the same extent; this is the most fundamental source of profit—the only long-run source in an economy with a constant quantity of money.

D. Some Problems to Test Your Understanding

1. Adam Smith and Karl Marx postulated a simple state of affairs in which manual laborers produced and sold products, kept the whole sales proceeds, and did not act as capitalists, i.e., did not buy for the sake of subsequently

selling. They believed that in such circumstances all income was wages and no income was profits. They held that profits came into existence only with the development of "capitalistic circulation" (i.e., buying for the sake of selling) and were a deduction from what was originally all wages. To determine what the effect on the rate of profit would be if there were no capitalists, but just sellers of products, you are given the following information, which will test their propositions in the light of the net consumption theory: Receipts from the sale of products are 1000, all of which is consumed by the sellers and constitutes a fresh 1000 of receipts from the sale of products in the next period. Using Figure 16–2 and Tables 16–1 through 16–4 as your framework of analysis,

a. State the amount of productive expenditure present.

b. State the amount of wages paid in the production of products.

c. State the amount of money outlays to be deducted from sales revenues as costs.

d. State the amount of profits earned on the sales revenues.

e. State the amount of nominal capital in existence.

f. State the rate of return on capital.

2. Find net investment if productive expenditure for buildings and equipment by business is 1000, while total annual depreciation charges are 820, and productive expenditure for labor materials, and supplies is 2000, while cost of goods sold is 1980.

a. Find total business sales revenue from the above data, on the assumption that all wages have a counterpart in consumption expenditure.

b. Find aggregate profit in the economic system, on the assumption that net consumption is zero and thus that sales revenues equal productive expenditure alone.

c. Find net investment on the assumption that 50 of wages show up as an additional demand for capital goods accompanied by an equivalently reduced demand for consumers' goods. (You may want to use Table 16–9 as a guide to your answer.)

d. Find aggregate profit on the preceding assumption.

e. Find net investment and aggregate profit in questions 1 and 2, on the assumption that total costs are 400 higher.

Answers to questions 1a–f and 2a–e appear immediately below, with 180 degree rotation.

1a. zero, 1b. zero, 1c. zero, 1d. 1000, 1e. zero, 1f. infinite
2a. 3000, 2b. 200, 2c. 250, 2d. 200, 2e. -200, -200

(Accompanies Week 12)

XI. Applications of the Net-Consumption/Invariable-Money Analysis

A. The Analytical Framework

See Figure 17–1 on p. 811.

B. Why Capital Accumulation and the Falling Prices Caused by Increased Production Do Not Imply a Falling Rate of Profit

1. Confirmation of Fact that Falling Prices Caused by Increased Production Do Not Constitute Deflation
2. More on the Relationship Between Technological Progress and the Rate of Profit

C. Why Capital Accumulation Does Not Depend on a Continuous Lengthening of the Average Period of Production

See Figures 17–2 and 17–3 on pp. 821 and 823.

The Average Period of Production and the Limits to Technological Progress as a Source of Capital Accumulation

D. Implications for the Doctrine of Price Premiums in the Rate of Interest

E. Implications for the Process of Raising Real Wages

F. How the Taxation of Profits Raises the Rate of Profit

The Influence of the Monetary System

G. How Government Budget Deficits Raise the Rate of Profit

1. The Need to Reduce Government Spending
2. The Government's Responsibility for the Emphasis of Today's Businessmen on Short-Term Results

H. Profits, the Balance of Trade, and the Need for Laissez Faire

I. Implications for the Theory of Saving

1. Net Saving and Increases in the Quantity of Money
2. Why the Actual Significance of Saving Lies at the Gross Level
3. Net Saving and the Rate of Profit

J. "Hoarding" as a Long-Run Cause of a Rise in the Rate of Profit

Implications for the Critique of Keynesianism

K. Critique of the Investment-Opportunity Doctrine

1. Mistaken belief that the rate of profit is determined by the demand for and supply of capital, when in fact it is governed by the difference between the demand for products and the demand for factors of production (i.e., net

consumption) and by net investment and the increase in the quantity of money.

2. Error of believing that technological progress raises the average rate of profit, when in fact it is neutral (except to the extent that it increases the quantity of commodity money) and is itself an essential cause of capital accumulation.

3. Contradictory view of technological progress as both raising and lowering the rate of profit, the latter through increasing the supply of consumers' goods and causing falling prices—alleged "deflation."

4. Failure to realize the limitless need for capital and the strictly limited ability to accumulate it through saving, because of the operation of time preference.

5. Failure to realize that continued net saving in terms of money is the result of increases in the quantity of money, which correspondingly *raise* the rate of profit.

6. Exaggerated, confused view of the role of saving in capital accumulation, based on failure to analyze matters in terms of an invariable money.

7. Role of confused view of demand for consumers' goods as representing aggregate demand in conclusion that only use for additional capital goods is in the production of consumers' goods.

L. Critique of the Underconsumption/Oversaving Doctrine

1. The seeming paradox in claiming that the demand for capital goods can be greater than the demand for consumers' goods. Resolution of the paradox even in the most extreme cases. (See Tables 17-1 through 17-4 in *Capitalism.*) In such a situation, the great majority of capital goods would be employed in the production of further capital goods. All would ultimately still serve in the production of consumers' goods, but the "period of production" would be extremely long.

2. Consumption as the Purpose of Production and the Progressive Production of Consumers' Goods Over Time

3. The Measurement of the Average Period of Production

4. A Rise in the Demand for Capital Goods and a Fall in the Demand for Consumers' Goods: The Cross-Hatching of Production

Manifestations of a less capital intensive economy today in such things as thin walls of newer buildings compared with those constructed before World War II, and in products in general as not being as well made (apart from the problem of less care by workmen). Perception of less going into products is correct.

M. More on Why Savings Cannot Outrun the Uses for Savings

1. Capital Intensiveness and Land Values

2. The Housing Outlet and Consumer Interest

3. The Automatic Adjustment of the Rate of Saving to the Need for Capital

(Accompanies Week 13)

XII. EXPOSITION AND CRITIQUE OF KEYNESIANISM

A. The Essential Claims of Keynesianism

1. The denial of the fact that a fall in wage rates and prices can achieve full employment. Call for government budget deficits as the solution. Keynesianism and Consumptionism. Implied opposition of the Keynesian doctrine to the quantity theory of money.

2. The reasons for Keynesianism's influence: the hostility to a free market in labor—the influence of the exploitation theory. The isolated position of economists. The earlier abandonment of classical economics, especially the wages fund theory and the view of saving.

3. Neo-Keynesianism: Pigou and the Pigou effect. Weakness of Pigou's position. The latest incarnation of Neo-Keynesianism.

B. The Keynesian System: The Unemployment Equilibrium Doctrine and Its Basis; the IS Curve and Its Elements

1. The meaning of the unemployment equilibrium—see *Capitalism*, p. 868, Figure 18–1. Same essential idea as Consumptionism.

2. The meaning of the IS Curve: *the relationship between the "marginal efficiency of capital" (the rate of profit), on the one side, and the volume of output and employment, on the other, for equilibria of investment and saving.*

3. The IS Curve claims that as output and employment expand, the rate of return on capital falls. The Keynesians claim that at the point of *full employment* and its corresponding output, the rate of return would either be negative or, if not negative, at least unacceptably low—somewhere below 2% is the usual estimate. See *Capitalism,* p. 869, Figure 18–2.

4. Derivation of the Keynesian aggregate demand curve and the unemployment equilibrium from the IS curve—see *Capitalism,* p. 870, Figure 18–3.

5. The meaning of the Keynesian argument is that full employment can't exist, because if, somehow, it did, the rate of profit would be too low. Businessmen would then start to hoard, and the hoarding would reduce output and employment until the rate of profit was raised back up to an acceptable level. This is supposed to be the reason why a fall in wages and prices is incapable of achieving full employment: the problem is, allegedly, that the physical output corresponding to full employment simply imposes an unacceptably low rate of return on capital. The level of wages and prices is thus held to be irrelevant.

6. Derivation of the IS Curve from a. the production function, b. the saving function, c. an equality of saving and investment, d. the marginal efficiency of capital schedule. See *Capitalism*, pp. 867-875, especially Figure 18-4, on p. 871.

7. A fall in wages and prices is held to be incapable of achieving full employment, because all of the relationships above are supposed to hold true *in physical terms.* N_f of employment means Y_f of output, means S_f of saving, requiring I_f of investment, which causes too low a rate of return. These same physical relationships allegedly hold irrespective of the wage and price level. Specifically, at a lower wage and price level, no more physical investment is profitable (yields more than 2%) than before. See *Capitalism,* p. 874, Figure 18-5 and the surrounding discussion.

Thus, there allegedly still can't be an outlet for saving in excess of this given physical amount of investment. And thus there still can't be an output greater than the one that produces such a level of saving, nor, finally, a volume of employment greater than the one that produces such a level of output. Full employment can't exist or be maintained because it would produce a physical volume of output out of which there would be a physical volume of saving requiring a physical volume of investment that would put the rate of return below the minimum acceptable rate. (See Keynes, *General Theory of Employment, Interest, and Money,* p. 261—quoted in *Capitalism,* p. 875.)

8. The fall in wages and prices and the pile up of funds in the "liquidity trap."

9. The Grounds for the MEC Doctrine—why the "marginal efficiency of capital" (rate of profit) is supposed to fall: (see *Capitalism,* pp. 875–876.)

a. Rising purchase prices of capital assets as net investment increases—the additional net investment perceived as an additional demand for capital assets, which raises their purchase price.

b. Lower selling prices of products as more capacity comes on stream as the result of additional net investment.

c. Operation of law of diminishing returns; see Keynes on these points: *General Theory* p. 136—quoted in *Capitalism*, pp. 875–876.

10. The Keynesian solution: "fiscal policy," i.e., federal budget deficits, to absorb the allegedly excess saving at full employment—see *Capitalism*, pp. 876–878.

C. Critique of the Keynesian Analysis

1. The declining MEC argument and the fallacy of context dropping. The ability of *lower wages and prices* to achieve full employment is the context. The three reasons advanced for the declining MEC as net investment increases contradict this context.

a. Lower, not higher, purchase prices of capital assets.

b. Lower costs of production to offset lower selling prices.

c. Increasing returns to capital, not decreasing returns as employment expands.

The first of the three reasons claims that a fall in wages and prices could not achieve full employment because a *rise* in wages and prices would not.

The second claims that a fall in wages and prices could not achieve full employment, because if there were no fall in costs, but only in selling prices, the rate of profit would be reduced.

The third reason claims that a fall in wages and prices cannot achieve full employment because if what occurred as wages and prices fell was an increase in capital relative to labor as employment increased, there would be diminishing returns to capital. The actual fact is that an increase in employment means *increasing* returns to capital, because it means more labor relative to capital. If ever capital were "too abundant," the surest cure would be more labor—more employment rather than less.

2. The Keynesian claim that a fall in wages and prices cannot achieve full employment, because at full employment the rate of return on capital would be too low, implies that *the rate of return is lower in the recovery from a depression than it is in the depression.*

3. The Keynesian argument claims that in a depression saving and net investment are at their maximum limit, and that the problem is that full employment requires that they be carried still further. Actually, in a depression, saving and net investment are extremely low or even *negative.*

4. Our previous discussion of the determinants of the rate of profit showed that the rate of profit and net investment *are positively related*, i.e., that more net investment and more profits go together virtually dollar for dollar, because while profits are the difference between sales and costs, net investment is the difference between productive expenditure (which is almost equivalent to sales, since it embraces the expenditure for capital goods and for labor by business) and those same costs.

5. The actual reason the rate of profit is so low or negative in a depression is the same as the reason net investment is so low or negative—namely, that productive expenditure has fallen, taking sales revenues with it, while costs, especially depreciation costs, fall only with a lag. The restoration of net investment would be accompanied by a rise in aggregate profits virtually dollar for dollar and would thus sharply raise the rate of profit.

6. The restoration of net investment is prevented by *the failure of wage rates to fall.* When wage rates fall, the costs of individual investments will be sharply lower. Until wage rates fall, investment expenditures are postponed. In this way, as previously shown, the failure of wage rates to fall operates to deepen the depression, because it causes the postponement of investment expenditures, the consequent wiping out of profitability, and thus of the ability of business firms to repay their debts. This, in turn, causes more bank failures, a further reduction in the quantity of money and velocity of circulation, and thus necessitates greater wage cuts than would have been the case if they had come quickly.

7. Further Errors in the Keynesian Analysis: The contradiction between the marginal-efficiency-of-capital doctrine and the multiplier doctrine; critique of the "paradox-of-thrift" doctrine; critique of the saving function; critique of the liquidity-preference doctrine; critique of the balanced-budget multiplier.

D. Critique of the Keynesian Policies

1. Budget deficits.

a. Promote expansion in size of government—if more government spending is the goal, then any and every government program appears justified—see Keynes, *General Theory*, p. 129, p. 131; quoted in *Capitalism*, pp. 35, 544
b. Actually, budget deficits are *deflationary,* unless financed by inflation of the money supply; if not so financed, they threaten government bankruptcy, and thus a fall in the velocity of circulation of money and a contraction of the money supply insofar as it is backed by government debt.

2. Inflation

a. In the absence of a gold standard, which the Keynesians totally oppose because of the obstacles it puts in the way of money creation and deficits, deficits are in fact financed by the creation of money.
b. The Keynesians also desire the creation of additional money insofar as they believe that it can succeed in lowering the rate of interest. (If the rate of return is not already at its irreducible minimum, the Keynesians believe that increasing the quantity of money can push it lower and in the process stimulate additional investment, employment and output—i.e, they believe that in such circumstances the creation of more money permits a movement down and to the right on the IS curve.)
c. As the discussion of inflation will show, the creation of money by the government, or with the encouragement of the government, is the essence of the inflation problem—inflation *is* the government's creation, or sponsorship of the creation, of money at a rate more rapid than would be possible under a gold standard.
d. The consequence of deficits and inflation is *capital decumulation, a lower productivity of labor, and lower real wages. It is also a lower real rate of return on capital*—for reasons to be explained under the head of inflation.

3. Price and wage controls are the classic response to inflation. They in turn cause total economic chaos and culminate in a totalitarian socialist dictatorship. (See chaps. 7 & 8 in *Capitalism.*) Because the Keynesian policies lead to the inflation that results in price and wage controls, price and wage controls must be considered one of the consequences of those policies.

4. The Keynesian policies of deficits and inflation are not only not necessary for the achievement of full employment, but *do not achieve it.*

a. Indeed, deficits, by themselves, apart from the creation of money, actually cause more unemployment, by virtue of their deflationary effects noted above.
b. As shown in the discussion of unemployment, earlier in the term and in Chapter 13 of *Capitalism,* even when combined with inflation of the money supply, much, most, or even all of the extra spending can be nullified by wage increases that are just as rapid or even more rapid.
c. Throughout the middle and late '30s, the quantity of money and volume of spending in the economic system were stepped up by the adoption of Keynesian policies, and yet unemployment remained a massive problem, because growing labor union power raised wage rates almost as fast, with the result that growing payrolls were not able to employ correspondingly larger quantities of labor.
d. And much of the additional employment that did take place was in the form of government employment, of a make-work variety, and actually caused a drop in the standard of living of those who already were employed, since they had to produce the goods and services which the government workers consumed, and received no comparable output in return.
e. Also as shown in previous discussion and in Chapter 13 of *Capitalism,* full employment was achieved only with the coming of World War II—not because war is necessary to full employment, but because the war was financed by massive inflation of the money supply *coupled with wage and price controls.* This combination generated sharply rising payrolls and spending of all types, and wage rates and prices were prohibited from keeping pace. The result was rapidly growing quantities demanded of everything, and the emergence of shortages, in-

cluding a labor shortage. As previously explained, the full employment of World War II was accompanied by a sharp decline in the standard of living of the average person, who had to work longer and harder and who got much less in the way of goods for his efforts.

f. As previously pointed out, full employment *with prosperity* was achieved only *after* World War II, as the result of the massive reduction in the size of government spending and deficits (from 1945 to 1946, Federal Government spending fell from approximately $93 billion to approximately $45 billion and the deficit was virtually eliminated). The prosperity resulted from the release of funds from the government back to the citizens and the transfer of roughly ten million government workers (most of the army and navy) back to private employment. The citizens now had vastly greater control of their own incomes and previously unproductive labor was now available for production. The unions could achieve wage increases (which would have been given anyway) without causing unemployment or higher prices insofar as the end of the war provided the physical means for a vast transfer of resources back to the private economy and thus for a corresponding increase in real wages. (The average wage earner could have more because the government took less not only from him, but also from his employer, who could now afford to pay him more without increasing his total costs.)

5. Paradoxically, the Keynesian policies reduce the rate of return on capital.

a. This is implied in the very attempt to neutralize or seize current savings, whether by taxing them away or by absorbing them in budget deficits which will never be repaid. The savings that are seized or absorbed for the most part *come out of the rate of return.* Taking them away is tantamount to taking away part of the rate of return itself.

b. This result is evident in inflation, when both saving in real terms and the rate of return in real terms become negative, and people turn to hoarding as the result of the Keynesian policies themselves—a hoarding of the precious metals.

6. The insincerity of the Keynesian policies:

a. Even if the analysis were correct (which it certainly isn't), why not try to raise the rate of return by reducing taxes on the rate of return? Only after all taxes on the rate of return had been eliminated, would it be legitimate to talk of a problem in the private economy of too low a rate of return.

b. The doctrine of the "euthanasia of the rentier" (See *The General Theory*, pp. 375-378—quoted in *Capitalism,* pp. 891–892.) All along the problem of capitalism has been presented as the rate of profit being too low for full employment. Now it turns out that it's *too high!*

(Accompanies Week 14)

XIII. INFLATION

A. Confusions Resulting From the Definition of Inflation as Rising Prices

1. Too many explanations, causing ignorance in any particular case.

2. Implication of the responsibility of businessmen.

3. Implication of price and wage controls as the solution.

4. Implication of limiting inflation by expanding the quantity of money.

Alternative definition of inflation in terms of the increase in the quantity of money.

B. Validation of the Quantity Theory of Money as the Explanation of Rising Prices

1. The demand/supply test using the formula for the general consumer price level.

2. By the nature of the formula, the price level can rise only by virtue of more D or less S.

3. Reductions in supply must be ruled out as a cause of an inflationary rise in prices because:

   a. Supply has actually increased.
   b. Even where supply has decreased, the overwhelmingly greater part of the rise in the price level has been the result of more demand.
   c. Reductions in supply could explain a sustained, significant rise in prices only if material civilization were in the process of rapidly disappearing, which it isn't.
   d. A decrease in supply is often itself merely an indirect consequence of a rapidly rising aggregate demand, rather than being an initiating cause of rising prices.
   e. Decreases in supply do not produce the range of price increases people associate with inflation.
   f. Decreases in supply do not produce the effects on the relations between debtors and creditors that people associate with inflation.
   g. To say that decreases in supply cause inflation is to imply that increases in supply cause deflation and, therefore, depression and poverty. This is a self-contradiction because more supply causes prosperity, not poverty.

4. Thus, the problem of inflation is exclusively one of rising aggregate demand.

5. A rise in aggregate demand is the result of an increase in the quantity of money: recall the examples of the gold mining case and of the issuance of social security checks from Chapter 12 and the discussion of the ways in which more M raises V.

6. Governmental responsibility for inflation.

   a. The forced abandonment of gold and the creation of fiat standard money through the open market operation.
   b. The encouragement of fractional reserve banking and fiduciary media: expanding the amount of reserves through the open market operation and making reserves more potent.

7. The implied solution for inflation: *take the ability to create money out of the government's hands:* make the monetary unit something the government cannot create—viz., *gold.*

C. Alternative Explanations of Rising Prices: The Cost Push Doctrines

1. The cost-push doctrine: the attempt to blame rising prices on rising costs of production. Variants of the cost-push doctrine: wage-push, profit-push, the wage-price spiral, crisis-push.

2. The roots of the cost-push doctrine: the belief that more demand causes more production and supply and can only raise prices at the point of full employment ("demand-pull inflation"). The belief that in the absence of full employment another explanation of rising prices must be found. Rising costs selected as the explanation because in first

instance costs often do determine prices.

3. The logical deficiency of the cost-push doctrine: explaining prices on the basis of costs means explaining them on the basis of other prices and ultimately on the basis of mere arbitrary power.

4. The cost-push doctrine is equivalent to blaming inflation on falling supply. All the objections raised against falling supply as an explanation of inflation apply to it.

5. Critique of the wage-push variant:

a. If demand did not rise, wage push would burn itself out in mounting unemployment. The total cumulative effect of wage push would be limited and probably could not stop prices from actually falling.
b. Wage push is a continuing phenomenon only because of governmental decisions to increase the money supply and expand demand in an effort to avoid or fight the unemployment otherwise resulting from wage push. Wage push is thus actually a consequence of an expanding quantity of money and more demand.
b. Confirmation by the experience of the 1980s.

6. Critique of the profit-push variant.

a. Even a protected legal monopolist can raise his price only if the demand for his product is growing. In order to be associated with a problem of inflation, the growth in demand for the monopolist's product must be part of a growth in economy-wide demand.
b. The actual effect of the profit motive is to expand production and thus reduce prices; this confirmed even by the rise in prices in paper money.
c. Inflation is associated with high profits. This is because an expanding money supply and demand increase sales revenues. The increase in profits is purely in terms of paper money and is usually accompanied by a decline in real profits: the inventory case.

7. Critique of the crisis-push doctrine.

Confusion of non-repeatable, particular price increases with sustained general price increases.

D. Alternative Theories of Rising Prices Continued: The Velocity Doctrines

1. The basic velocity doctrine: the attempt to blame increases in aggregate demand on a higher velocity of circulation of money rather than on a larger quantity of money.

2. Critique of basic velocity doctrine.

a. Velocity not an entity or cause of anything; reflects desire to hold money in reserve.
b. This desire mainly determined by rate of increase in the quantity of money, as explained previously; thus rise in velocity itself mainly a reflection of increase in quantity of money—more rapid the increase, the less is the desire to hold money, and thus the greater is velocity.
c. Independent changes in demand for money and velocity slow and gradual, and largely offset by more complexity of production involving more stages of payment and by more production.

3. Critique of the inflation-psychology doctrine:

a. Inflation psychology not a primary—the product of the fact of inflation; quickly diminishes in the face of a serious attempt to reduce inflation, as the experience of 1980s confirms.
b. Largely describes same factors as make for higher V; but also operates from the side of supply, in the anticipations of sellers: higher wage rates and prices than corresponds to current D. To this extent, like cost-push and with the same limits. Implication here of inflation causing unemployment via wages and prices outrunning rise in D.

4. More on inflation psychology: can appear to lead life of own—can continue for a while even if government sharply cuts back or stops inflating for a while; people go on with low cash holdings or reduce them further, and go on raising prices in expectation of being bailed out by more inflation. At this point, a crisis necessary to break inflation psychology—government must not validate inflationary expectations, not bail people out as demand appears inadequate, as credit fails to materialize and cash holdings prove inadequate. Appearance of crisis easily leads to resumption

of more rapid expansion of money—to stop, mitigate, or turn the crisis around; can lead to undoing of paper money by making inflation worse than before, producing still more rapidly rising prices and still worse inflation psychology on the next round, with problem getting worse and worse as time goes on. Validating inflation psychology not possible on the gold standard.

5. The credit-card doctrine:

a. Thesis: reduce need to hold M—raise V.

b. Largely *apparent* reduction in need to hold M: American-Express-type card: hold checking balance instead of currency, *two* cash holdings instead of one (American Express's and yours); probably acts to *reduce* V.

c. Sometimes credit cards can reduce the need to hold cash: Visa and Mastercards; here we have lines of bank credit—guaranteed loans. Don't need to hold cash for case of finding something and not being able to borrow; now sure to be able to borrow. But what makes possible this great extension in lines of bank credit is ability to expand M—an instance of more M reducing need to hold M and thus raising V. Confirms quantity theory.

d. credit cards and lines of bank credit can certainly exist without inflation, but only on basis of *savings*, where origin is drop in consumption of the savers; thus, if not based on more M, not inflationary.

6. Consumer installment credit and credit in general—inflationary if from more M; not, if financed by saving.

7. Consumer "greed"—vague: might refer to some goods bid up, but then others down; no hoards to draw down and if were, why does greed mean spending them?; desire for higher living standards *reduces* prices, not raises—more production.

E. The Meaning of Inflation

1. The alternative theories confirm the quantity theory of money: whole problem of inflation in government's expansion of M, which causes more D.

2. Hence, definition of inflation as: *an increase in the quantity of money caused by the government*, or, equivalently: *an increase in the quantity of money more rapid than the increase in the quantity of gold and silver*.

3. This definition explains all the symptoms of inflation:

a. A sustained significant rise in prices (without material civilization disappearing).
b. A rise not only in the general price level but the whole range of prices.
c. Debtors gaining at the expense of creditors.
d. High nominal profit and interest rates.
e. A low demand for money for holding.

4. This definition shows how to stop inflation: stop the government from creating money in excess of gold and silver reserves.

5. Critique of definition of inflation as rising prices:

See points 1 - 4 under (A) on p. 105, above, plus the fact that this definition makes no distinction between higher prices due to more D or less S—hence no ability to explain *all* the symptoms of inflation described under 3a - 3e, immediately above.

6. Difference in definitions is as important as right or wrong understanding of a disease: know what it is that produces all the symptoms and what needs to be dealt with to stop them versus attempting to deal directly with an isolated symptom.

F. The Deeper Roots of Inflation: Connection of Inflation with Budget Deficits

1. Deficits not inflationary if financed by selling bonds to the "public"— i.e., private individuals and non-bank corporations; here just demand diversion: government spends instead of private borrowers, who are deprived of the funds the government borrows.

2. But bankruptcy at end if such borrowing a regular policy.

Further problems with deficits: capital diverted to consumption—economic progress slows or is reversed; rising tax burden to service debt further contributes to process of decline; private consumer borrowing also disrupted—e.g., the mortgage market; for these reasons, and others (i.e., incompatibility with principles of representative government and creation of class of public annuitants supported by others' industry), long-standing opposition has existed to public debts (see Adam Smith, *Wealth of Nations*, chapter "Of Public Debts"—also von Mises, *Human Action*, pp. 224-228).

3. If the government had no ability to create money, then, in weakening the government's credit and threatening bankruptcy, borrowing from the public would actually be *deflationary:* under a fractional reserve banking system in which government debt serves as part of the assets of the banking system, it would be a threat to the quantity of money; also prospect of government bankruptcy would lead to rise in demand for gold and its exportation.

4. What makes government deficits inflationary is the ability to finance them by the creation of new and additional money.

This exists today at the Federal level (but not at the state or local level); hence Federal deficits are inflationary; mechanisms of money creation in connection with deficits already shown: create deposits and reserves, on basis of which banking system can create still more money in purchase of additional government bonds or in granting private loans.

5. Ability to create money makes it impossible for Federal government to go bankrupt in the technical sense—always has money available to pay its debts, and also raises its tax revenues in the process (at least absolutely and often relatively, as well); as far as debt held by Federal Reserve (central bank), even payment of interest is nominal, since most of it is turned back to the treasury.

Even though it can't go bankrupt technically, the government has probably long been bankrupt in the sense of being unable to repay its debt *in the same purchasing power in which the debt was contracted.*.

6. Inflation possible without current deficits in the government's budget—e.g., Fed can buy up existing government debt and thus create reserves and deposits; also, within—fairly narrow—limits the banking system might expand fiduciary media somewhat further under supporting framework the government has provided, but soon a problem of need for more reserves and more currency in circulation, which can come only from the government's creation of additional standard money.

7. *The essential element in any major inflation is government's creation of new and additional standard money.*

8. Desire for deficits implies opposition to the gold standard, since a gold standard would make bankruptcy the price of deficits, because it would deprive the government of the ability to create money and thus bail itself out; deficits unlikely under representative government where the price is this high; no end to deficits until the government loses the power to create money. Proposals for constitutionally balanced budgets make avoidance fairly easy and could be evaded. Under the American system of division of powers, they necessarily lack an enforcement mechnaism.

G. The Motives for Deficits and Inflation

1. To foster the view of government as Santa Claus—apparent free benefits from government. Cost, in form of rising prices, not seen as connected—blame shifted to business. How public thinks of government even now. Government vastly larger because of its ability to inflate—benefits seen, but costs not.

2. To be able to finance wars, as well as the welfare state, without the public being aware of the actual cost.

3. The belief that deficits and inflation are necessary to prevent or combat unemployment, which is the essential teaching of Keynesian economics; this belief provides major reinforcement for the free benefits idea: the benefits are allegedly paid for by the elimination of unemployment, and much more besides—via the "government spending multiplier".

4. The belief that creating money and lending it out is equivalent to creating additional capital and lowers the rate of interest—the businessman's version of the welfare state.

5. Deeper explanation of most of these points is *the influence of the socialist ideology*.

a. Continuing expansion in size of government is movement toward socialism. Also view of government as Santa Claus conforms to socialists' belief that the individual is helpless and that the government is all wise and

all powerful.
b. A hostility to profits and interest—Keynes' "euthanasia of the rentier"—also underlies the desire for credit expansion and the reduction of the rate of interest; but even without this, the desire for credit expansion manifests the socialist ideology insofar as it is a desire for a "free benefit."
c. The unemployment problem also is largely an indirect result of the influence of the socialist ideology, for the labor legislation that causes unemployment is the result of the influence of the exploitation theory.

H. The Further Effects of Inflation

1. The growth of government under the influence of inflation-financed deficits and the free benefits idea.

2. Greater frequency and duration of wars in the belief not only that they do not have to be paid for, but are an actual source of prosperity.

3. Increased hostility to profits and interest because of the increase in nominal profit and interest rates, while the public suffers.

4. Price controls—as a method of controlling inflation.

5. Relative wealth and income effects:

a. People with fixed assets or on fixed incomes; the hypocrisy of helping the poor with inflation-financed programs.
b. The problem of lags and of incomes slow to adjust—an important deficiency of price indexes.

6. Effects on saving and capital accumulation.

a. Reversal of safety—traditionally safest investments made the least safe in terms of purchasing power; what purchasing power of the dollar made to depend on; risk effects on the average person: save less, hoard gold and silver, invest less efficiently—e.g., buy house on credit; at the same time artificially created speculative opportunities for the very nimble in commodity, real estate, and possibly stock speculation; diversion of efforts from productive work to artificially induced speculative activity.
b. Tax effects—recall the inventory case; now the depreciation case.
c. The prosperity delusion of inflation.

i. Of stockholders in above type case.

ii. Poverty coverup provided by seeming interest incomes.

iii. Wage earners' lagged idea of purchasing power and consequent overconsumption.

d. Malinvestment—wasteful use of capital—stemming from artificially low interest rate.
i. Mises on false appearance of capital available for more capital-intensive projects.
ii. Low interest rate relative to rate of profit: wasteful inventory accumulation.
iii. Low interest rate relative to rate of price increases: wasteful housing and real estate investment; potential for wasteful investment in anything, the stronger inflation becomes.
iv. Discrimination against long term investments: if allow for rise in replacement cost, means higher prices or lower dividends now, before much of the inflation; which discourages such investments.
Note: in reducing the productivity of existing capital goods malinvestment further reduces or restricts the supply of capital goods, because the capital goods of the future are the products of the capital goods of the present.
e. The abstraction (withdrawal of wealth) effect: spenders of the new and additional money draw goods out of the system without putting goods in to earn the money they spend; thus corresponding loss to producers; loss of capital if new money spent preponderantly by consumers; probable malinvestment to extent spent for business purposes by firms not otherwise able to attract funds.
General consequences.

i. All five effects operate against capital accumulation.

ii. The reversal-of-safety, tax, malinvestment, and abstraction effects also operate to reduce the real rate of return on capital as well; reduction in real r comes in conjunction with *less* capital formation, not abundance of capital as advocates of credit expansion believe.

iii. Implication of gains of debtors less than loss of creditors—net reduction in real rate of return on investment as such.

iv. Impairment in growth of productivity of labor as the result of less capital formation because lower relative production of capital goods and less efficiency in their use—so real wages held down or reduced; real wages also held down because demand for labor depends on savings, whose growth is retarded relative to growth in consumer demand and rise in prices.

7. How inflation, especially in the form of credit expansion, sets the stage for standard, deflationary-type depression.

a. Raises V—so superinflates demand. Higher V sustainable only so long as inflation continues. V may even need to accelerate. (Stabilization of V means slowdown in rate of increase in spending and sales revenues, hence reduction in monetary component in rate of profit. Hence profit squeeze in face of prevailing high interest rates.) Also, cash holdings run down in expectation of continuation of same or greater rate of growth in sales revenues. If M fails to accelerate, then profit squeeze and cash shortage develop.
b. Inflation (credit expansion) encourages debt by making rate of interest low relative to rate of profit and to rise in prices—raises ratio of debt to incomes and asset values already superinflated by rise in V.
c. In the ways shown under point 6, above, inflation undermines real capital and thus availability of real credit.
d. And as part of (c), above, it encourages investments whose profitability exists only because of inflation.
e. Because of all this, if inflation stops, slows down, or even fails to accelerate sufficiently, both a profit squeeze and a "credit crunch" develop. The latter occurs because capital has been diverted to projects whose profitability in whole or in part rested on inflation and the growth in sales revenues it inspired, and on the low rate of interest relative to the rate of profit that it caused. That capital is now not available. The diversion of capital shows up in the fact that in the absence of sufficiently large fresh doses of credit expansion, existing capital funds are made inadequate by the rise in wages and materials prices caused by initial injections of new money. This creates the potential for insolvencies and bankruptcies: surge in credit demand, to carry on business at higher wages and materials prices, and reduced credit supply, as the same cause makes funds more urgently required internally, leading suppliers of funds to supply less or themselves become demanders of funds. This situation makes some refinancings impossible, with the result that some firms can't pay debts. Further result is a sudden need for cash by creditors whose own solvency is threatened because debtors can't repay. Consequence is that V starts to fall, accompanied by inventory and other asset liquidations to raise cash. Sudden losses as investments whose profitability was based on inflation are no longer profitable; nominal profitability of all investments reduced by slower growth in D; all can be turned into losses by drop in D.
f. Revenues, incomes, asset values now stable or declining with huge debt incumbrance based on expectation of their rising—result: many debts not payable; further results: further credit tightening and drop in V—calling in of doubtful loans, need to raise cash as debts constituting one's assets go bad, while the debts constituting one's liabilities remain firm.
g. Bank failures as too many business and consumer debts go bad; this means actual *reduction* in quantity of money—deposits and notes of a failed bank lose their money character.
h. Less M further reduces spending and operates to reduce V further, thus compounding the problem—i.e., more business failures and still more bank failures; process like a row of dominoes falling over; ultimate stopping point: reduction of M to standard money; process descriptive of early '30s, with successive waves of bank failures.

8. Unemployment.

a. Unemployment of depression and deflation due to inflation, because they are the result of inflation.
b. Inflation the preventive of unemployment only in the sense that more drugs are the preventive of withdrawal symptoms for an addict; no unemployment without inflation if don't start the inflation in the first place.
c. Inflation a cure for unemployment only in context where not necessary—i.e., if no unions, etc., and so wages could fall and eliminate unemployment that way—or a very limited cure in context where unions showing re-

straint because of existing large scale unemployment and fear of adding to it.

d. If wages not free to fall and so eliminate unemployment that way, inflation will also not eliminate it—wages start rising with rise in demand, because of

i. Removal of threat of greater unemployment.

ii. Red flag of higher nominal profits produced by rising demand.

iii. Rising prices of goods in limited supply and then rising prices because of rising wages.

e. Inflation a direct cause of unemployment insofar as it ultimately leads wages to rise more rapidly than demand—in anticipation of price increases over the life of employment contracts—and insofar as it brings about a fall in real wages which labor unions are unwilling to accept: i.e., the problem of the declining productivity of labor and the failure of the demand for labor to keep pace with the demand for consumers' goods.

9. Inherent accelerative tendencies of inflation, capable of culminating in the destruction of money and the division of labor; basic problem: government has the power to expand M; use of that power creates problems whose apparent solution is still more rapid expansion of M.

a. Continued growth of welfare state and deficits, with inflation to finance the deficits:

i. Natural philosophical basis of growth in welfare state.

ii. Help victims of previous extensions of welfare state.

iii. Decreasing real revenues of the government.

iv. Lags in tax collections.

b. Accelerate to paper over credit crunches and so prevent recession or depression.

c. Recessions as inflationary fueling periods—more rapid money supply expansion to prevent recession from turning into depression; then, when clear depression avoided, money comes pouring out.

d. Possible acceleration to make good general ravages of capital—e.g., an inflation-financed "reindustrialization plan."

e. Adoption of escalators—indexing.

i. Wages to cost of living; multiply price increases; cause larger unemployment or more rapid increase in M to ratify them.

ii. Tax rates, depreciation.

iii. Social security, government bonds.

Government has smaller revenues and larger outlays as result of (ii) and (iii) and thus is likely to create more M.

f. Acceleration on account of interest: when rates rise high enough to protect creditors, they impoverish debtors, creating demands for more rapid inflation to enable debtors to pay; then creditors losing again; process repeats itself until creditors realize no interest rate in paper money is sufficient; then destruction of credit; chance for quantum leap in inflation, with government creating money to make up for loss of private credit.

g. Acceleration on account of wage increases: every time wages rise more rapidly than the demand for labor, government must either allow unemployment to develop or accelerate the increase in the quantity of money; then wages rise still faster.

h. Accelerate to avoid profit reduction due to stabilization of V.

i. Continuous acceleration of inflation leads to destruction of money: becomes unacceptable when people know they must lose by taking it; then, possibility of no money; then no significant division of labor, no modern economic system.

I. The Current State of Inflation

1. The 1990 slowdown and the development of deflationary psychology.

2. The inflationary recovery and the fear of renewed inflation psychology.

3. The impending choice: will the government be willing to allow another major recession to develop to prevent this renewal?

4. Overcoming a recession/depression and ending inflation in the long run by using gold to increase the quantity of money.

a. Make gold, at its market price, legal tender for paper-money debts. Rise in price of gold then automatically creates the equivalent of additional paper money and thereby raises sales revenues and reduces the debt burden. This is compatible with large gold holdings relative to the spending of gold, i.e., low gold velocity, which can make possible the avoidance of a later contraction of spending in terms of gold.

b. At same time, exempt the rise in price of gold from capital gains taxation and make contracts written in gold fully enforceable. This will ensure major rise in demand for gold and in its price.

c. Government collection of some revenues in gold, e.g., a growing proportion of the tariff, phased in over a period of a few years. (Could be payable with checks on 100-percent-gold-reserve banks, which could be established for this purpose.)

d. A creditors' protection bill to limit present creditors' loss.

e. Finally, at high enough price of gold, make paper dollar fully redeemable in gold and give remaining gold reserves to banks to enable them to redeem checking deposits in full.

STUDY/REVIEW QUESTIONS FOR GEORGE REISMAN'S
CAPITALISM: A TREATISE ON ECONOMICS

INTRODUCTION

1. Which schools of economic thought have been the main supporters of capitalism?

2. Which schools of economic thought have been the principal allies of these schools?

3. Who were the leading members of the classical school?

4. Which schools of economic thought preceded the classical school? Which of them was closest to the classical school? Which of them has the most contemporary influence?

5. Who were the most important members of the Austrian school?

6. Explain the leading difference between classical economics and Austrian economics.

7. Describe the role of Marxism and socialism in the abandonment of classical economics.

8. Explain how the abandonment of classical economics in the nineteenth century contributed to the success of anticapitalist ideas in the twentieth century.

9. Which schools of economic thought have been opposed to capitalism or essential features of it? Which of these have been the most important since the 1930s?

10. Explain the role of Marshall's doctrine of the representative firm in leading to the conclusion that large-sized firms usually cannot gain by cutting their prices.

11. Explain what is meant by the partial equilibrium approach of Alfred Marshall in contrast with the general equilibrium approach of classical and Austrian economics.

12. How has the partial equilibrium approach led to the breakup of economics into "microeconomics" and "macroeconomics"?

13. What is the theoretical substance of most textbooks on "microeconomics"?

14. What is the theoretical substance of most textbooks on "macroeconomics"?

15. Describe the shortcomings of mathematical economics.

16. Describe the special status of von Mises in the defense of capitalism.

CHAPTER 1. ECONOMICS AND CAPITALISM

PART A. THE NATURE AND IMPORTANCE OF ECONOMICS

1. What is economics, according to the instructor?

2. What are some frequent alternative definitions of economics?

3. How does the individual live under a division of labor—that is, for whom does he produce and from whom does he obtain the goods he consumes?

4. "The importance of economics derives from the importance of wealth." Discuss.

5. Why is the importance of wealth not sufficient to establish the importance of economics?

6. Would Robinson Crusoe be able to produce more if could salvage some books on economics?

7. How does the existence of the division of labor as the system of producing wealth necessitate the science of economics?

8. To what extent does the population of the present-day world live in division-of-labor societies?

9. To what extent has the history of the world been characterized by the existence of division-of-labor societies? In what century and what country did the division-of-labor society of the present-day world first develop? What society represented the greatest development of the division of labor prior to modern times? What happened to that society?

10. "What makes the science of economics necessary and important is the fact that while human life and well-being depend on the production of wealth, and the production of wealth depends on the division of labor, *the division of labor does not exist or function automatically*."

11. Explain the potentially destructive effects on the division of labor of public opinion that is fashioned in ignorance of economics and what such a situation is analogous to.

12. Describe what the consequences of the destruction of the division of labor would be on human life and well-being, especially what would happen to population figures and why.

13. Explain the rapid growth in population figures around the world over the last two hundred years, after centuries of stagnation, on the basis of the higher productivity of labor resulting from the division of labor.

14. Describe the important applications of economics, according to the instructor, apart from the very survival of a division-of-labor society and all that depends on it. Be sure to deal with the following aspects:
   a. What major present-day problems can be solved on the basis of a knowledge of economics?
   b. What kind of important applications does economics have to the understanding of history and current events?
   c. Describe the implications of economics for ethics.

d. What are its applications to understanding one's place in the world and the kind of world one lives in?
e. What are its applications to business? What is its most important application to business?
f. What is the relationship of knowledge of economics to the defense of individual rights.
g. Who needs to know economics?

PART B. CAPITALISM

1. What is capitalism?

2. What is the relationship of the division of labor to capitalism?

3. "Economics, as the science which studies the production of wealth under a system of division of labor, is actually the science which studies the production of wealth under *capitalism.*" Discuss.

4. Describe the philosophical foundations of capitalism and economic activity, without which they could not develop or only minimally develop. Be sure to deal with the following aspects:
   a. philosophical convictions pertaining to the reality and primacy of the material world of sensory experience
   b. the philosophical conviction that the world operates according to definite and knowable principles of cause and effect
   c. the extent of conceptual awareness of the future
   d. the individual's identification of himself as a self-responsible causal agent with the power to improve his life
   e. the relationship between property rights, on the one side, and the principles of causality and "secularism" on the other
   f. peace and tranquility, respect for individual rights, limited government, and economic and political freedom
   g. great entrepreneurship
   h. The ability of economic science to influence people's thinking so that they will favor capitalism and sound economic policy.

5. What is the meaning of freedom?

6. What is the meaning of physical force?

7. What does the *initiation* of physical force mean?

8. Why does fraud represent the initiation of physical force?

9. Why is the existence of government necessary to the individual's freedom in relation to other private individuals?

10. What kind of government is necessary if the individual is to have freedom in relation to the government?

11. Why must freedom be defined not merely as the absence of the initiation of physical force, but, in addition, in order to highlight its most crucial aspect, the absence of the initiation of physical force specifically by, or with the sanction of, *the government*.

12. Describe the essentials of the relationship of the government of the United States to the concept of freedom both over the course of most of its history and at the present time.

13. Explain how freedom is the foundation of both personal and economic security.

14. Explain how the existence of freedom implies the existence of peace.

15. Contrast peace as the accompaniment of freedom with the "peace of slaves and cowards."

16. "The existence of the social security system is a leading consequence of the belief that in order to achieve economic security, one must violate economic freedom and establish a welfare state. It also provides essential evidence about what is wrong with that belief." Discuss.

17. "Economic freedom and political freedom—property rights and human rights—are indivisible; they are, in fact, merely different aspects of the same thing." Illustrate in terms of the freedoms of speech and press.

18. Using illustrations, compare and contrast the rational and the anarchic concepts of freedom. Be sure to deal with the following aspects:
   a. the fundamental facts of reality that the rational concept of freedom incorporates and takes for granted
   b. what the rational concept then focuses on as having to be absent in order for freedom to exist
   c. the anarchic concept's obliteration of the distinction between two sorts of obstacles to the achievement of a goal or desire: "obstacles" constituted by the ordinary facts of reality, including other people's voluntary choices, and obstacles constituted by the government's threat to use physical force

19. "On the basis of the anarchic concept of freedom, it is claimed that freedom is violated any time there is anything that, for whatever reason, a person cannot do, from flying to the moon, to being able to afford a house or a college education that is beyond his reach, to committing murder." Discuss.

20. "The anarchic concept of freedom is implicitly accepted by conservatives and fascists, as well as by anarchists and hippies." Illustrate.

21. "Such acts as murdering one's mother-in-law or speeding through red lights and thereby threatening the lives of others, are so far from representing freedom that their *prohibition* is what actually constitutes freedom." Discuss.

22. "The anarchic concept of freedom is present in the assertion of Communists and socialists that their freedom of speech is violated because they are threatened

with arrest for attempting to disrupt the speech of an invited speaker by shouting him down or by speaking at the same time." Discuss.

23. "A prohibition on arbitrarily shouting 'fire' in a crowded theater should not be construed as any kind of limitation on the freedom of speech, let alone a justified limitation. On the contrary, in the case of a live theatrical performance, the freedom of speech is violated precisely when someone does arbitrarily shout 'fire.'" Discuss in the light of the rational concept of freedom.

24. "The freedom of the press is violated and censorship exists not when a newspaper refuses to publish a story or a column that, for any reason, it regards as unworthy of publication, but when it is prepared to publish a piece and is stopped from doing so by the government. A private newspaper cannot commit censorship. Only the government can commit censorship." Discuss in the light of the rational concept of freedom.

25. "The freedom of travel is *not* violated when an individual wants to travel somewhere but lacks the ability to pay the cost of doing so. On the contrary, it is violated when he *has* the ability to pay the cost, and wants to pay it, but the government stops him—say, with a wall around his city (as existed until a few years ago in East Berlin), a passport restriction, or a price control on oil and oil products that creates a shortage of gasoline and aviation fuel and thus stops him from driving and the airlines from flying." Discuss in the light of the rational and anarchic concepts of freedom.

26. "State laws that impose residency requirements for the receipt of welfare violate the freedom of travel, because they stop people from traveling in the knowledge that they will have no source of funds when they reach their destination." Discuss in the light of the rational and anarchic concepts of freedom. In your answer, be sure to explain how striking down such requirements represents violating the freedom of taxpayers, according to the rational concept of freedom.

27. "What makes the anarchic concept of freedom so destructive is the fact that in divorcing freedom from the context of rationality, it not only seeks to establish a freedom to initiate physical force, as in the case of the anarchic concept of the freedom of travel, but also, on the basis of the consequences of such a perverted concept of freedom, provides seeming justification for the violation of freedom as a matter of rational principle." Discuss.

28. "The anarchic concept of freedom leads to the belief that freedom of speech is incompatible with the communication of thought. The rational concept of freedom, on the other hand, establishes freedom of speech precisely as the safeguard of the communication of thought." Discuss.

29. "In recent decades, the government's energies and efforts have more and more been diverted from the protection of the individual's freedom to the violation of it." Discuss.

30. "The growth of government corruption is the result of the decline of freedom." Discuss.

31. "To the degree that they exist, freedom and the pursuit of material self-interest, operating in a rational cultural environment, are the foundation of all the other institutions of capitalism." Explain with respect to the following:
   a. private ownership of the means of production
   b. saving and capital accumulation
   c. the development of the division of labor
   d. the development of exchange and money
   e. financial self-interest and the profit motive
   f. economic inequality
   g. economic competition
   h. the price system
   i. economic progress
   j. the harmony of rational self-interests

32. Use the economic history of the United States as an illustration of the answer to the preceding question.

33. Explain why economics and capitalism are controversial. Be sure to include an account of the following:
   a. the various attacks that are frequently made on economic activity and capitalism and their effect on legislation and government intervention in the economic system
   b. the prevailing prescientific worldview in the realm of economics
   c. economics versus unscientific personal observations
   d. economics versus altruism
   e. economics versus irrational self-interest
   f. economics versus irrationalism

34. It is usually argued that science must be "value free." In opposition to this view, name some leading values that science rests upon and without which it could not be pursued.

CHAPTER 2. WEALTH AND THE ECONOMIC PROBLEM

1. Explain the meaning of wealth.

2. Explain how the concept of wealth differs from the concept of money.

3. Does the production of more wealth in the economic system necessarily mean a larger total monetary value of that wealth?

4. What does a larger total monetary value of wealth fundamentally depend on?

5. In what circumstances would a connection exist between the quantity of money and the amount of

wealth? Describe the connection.

6. Are monetary aggregates such as GDP or GNP measures of the amount of wealth produced or indicators of the quantity of money in existence? Discuss.

7. Explain what is meant by economic goods in contrast to free goods.

8. Explain why air, sunlight, and rainfall are free goods rather than economic goods.

9. Are stocks and bonds wealth? Explain.

10. Are licenses wealth?

11. What is the effect of licenses on the production of wealth?

12. Are patents and copyrights wealth?

13. What is the effect of the expiration of a patent or copyright on the production of wealth?

14. What is the long-run effect of the existence of the system of patents and copyrights on the production of wealth?

15. Are slaves wealth in a society that allows slavery?

16. What is the effect of slavery on the production of wealth?

17. Name the concept that embraces the market value of stocks, bonds, licenses, etc.

18. Define (economi
  a. goods.

19. When did petroleum and uranium become economic goods and thus wealth?

20. Explain what was required before petroleum and uranium could become economic goods and thus wealth.

21. Is iron ore on Mars wealth? What would be required to make it wealth?

22. Could shale oil become wealth? What would be required to make it wealth?

23. Were deposits of iron, copper, or any of the metals wealth to the men of the Stone Age?

24. Compare the extent to which the land and mineral deposits of North America constitute wealth today versus the extent to which they did so for the American Indians.

25. Explain why desert land on which crops could successfully be grown if the land was irrigated is generally not an economic good or wealth.

26. What is meant by "imaginary goods"? Give examples.

27. What is meant by goods of the first order? The second order? The third order? Give examples.

28. "The source of the goods-character of things is ultimately *within us.* Goods derive their character as goods by virtue of their ability to benefit human beings." Discuss.

29. "The fact that more people are employed today in the various service industries than in manufacturing, mining, and agriculture shows that our economic system no longer revolves around the production of wealth." Explain why this conclusion is false.

30. "Economics is concerned with services only insofar as they are necessary to the production, enjoyment, or acquisition of wealth, or depend on the use of wealth. Economics is not at all concerned with the rendition of services apart from their connection with wealth." Discuss, being sure to give examples of the rendition of services with which economics is unconcerned.

31. In what way does its fundamental concern with the production of wealth lead economics to be concerned with explaining the exchange ratios at which services might be exchanged for services?

32. "Economics is the science which studies the allocation of scarce means among competing ends. It is not a science of wealth." Explain what is wrong with this view.

33. Name the leading classical economists. What was their view of the essential subject matter of economics?

34. "The ultimate source of the importance of the division of labor and capitalism, and of the science of economics, is *wealth*." Explain.

35. Why it is incumbent upon economics to provide philosophical validation for the production of wealth being a central, continuing concern of human existence?

36. How does man's possession of the faculty of reason imply a limitless need for wealth on his part?

37. Describe the extent of man's need for wealth merely in order to serve his needs for nutrition and health, i.e., what kinds of goods nowadays make an important contribution to the meeting of these needs?

38. Describe how reason gives man the ability to use wealth progressively to enhance the exercise of the capacities he shares in common with lesser species. Illustrate in terms of the capacities for locomotion, sight, and hearing.

39. Describe the contribution of wealth to the satisfaction of man's so-called higher needs, such as music, art, and science, whose existence and satisfaction is the result of his possession of reason.

40. Describe how man's nature as a rational being introduces additional, "higher" dimensions in the satisfaction of his "lower" needs such as nutrition.

41. Explain how man's desire for novelty and variety stands in the service of his life.

42. Explain how even when no practical applications ever result directly from the things that are desired, such as the paintings or sculptures that a millionaire desires to add to his collection, their being desired still produces important practical results.

43. Illustrate in contemporary terms the proposition of

Adam Smith that "the desire of food is limited in every man by the narrow capacity of the human stomach; but the desire of the conveniences and ornaments of building, dress, equipage and household furniture seems to have no limit or certain boundary."

44. What kind of philosophical convictions must be present to induce people to desire additional wealth strongly enough to go out and actually produce it?

45. "The fact that the need and desire for wealth are limitless does not mean that when people devote themselves to satisfying that need and desire, as in the nations of modern capitalism, they go through life with a sense of endless frustration, seeking more than they can ever hope to obtain." Explain how, on the contrary, the pursuit of ever more wealth should be expected to contribute powerfully to human happiness.

46. "Progress is the natural result of the use of reason as a constant." Discuss.

47. Explain the contribution of economic progress to human happiness in connection with the fact that as rational beings we are aware of the future in the present.

48. "According to the doctrines of cultural relativism and conspicuous consumption, the concept of economic progress can have no objective meaning." Explain.

49. "How man succeeds in relation to the physical world provides an objective standard by which to judge the value of cultures." Discuss.

50. Explain the basis for claiming that the automobile, for example, is objectively an advance over the horse and buggy, and radio objectively an advance over the telegraph and tom tom, while television is objectively an advance over radio, and color television is objectively an advance over black and white.

51. On the basis of what standard does the earning of wealth *deserve* to bring prestige?

52. Explain why the attempt to substitute the gaining of prestige for the incentive of gaining wealth ends up bringing the opposite of prestige to those who would accept the substitution.

53. Explain how the fact that in our culture many people want to own such goods as horses, canoes, bows and arrows, and so on, and in some cases prefer units of these goods to units of more advanced goods serving the same needs, is both consistent with the objective superiority of the goods of modern capitalism and further exemplifies the principle that man's need for wealth is limitless.

54. "In the name of being able to see, hear, move, or do anything that our senses, limbs, and minds enable us to do—in short, in the name of being able to live as human beings—the division of labor and capitalism and the values that underlie them—namely, reason, science, technology, individual rights, limited government and economic freedom, and private ownership of the means of production—deserve to be upheld." Discuss.

55. "The same principle that establishes the objectivity of the economic advances of modern capitalism directly establishes the objectivity of the superiority of modern capitalist civilization as such, in comparison to any other form of civilization. Here the attribute that serves as the standard is the ability to acquire and apply knowledge." Discuss.

56. "It should go without saying that capitalist civilization—modern Western civilization—is open to men of all races, as the brilliant success of Japan and several other Oriental nations dramatically illustrates. It is not the civilization of the white man, but of all men who wish to prosper and are prepared to adopt reason as their fundamental means of doing so. Those who view it, whether with pride or with hatred, as the civilization of the white man only are implicitly racists, in that they view civilization and culture as being racially determined. The fact is, of course, that civilization and culture, above all, modern capitalist civilization, is a body of knowledge and values that is accessible to all of mankind." Discuss.

57. State and illustrate the law of diminishing marginal utility.

58. Explain the two foundations of the law of diminishing marginal utility.

59. "The concept 'most important of our wants that a good is capable of satisfying' must be understood as *a variable range*, whose extent depends on the quantity of the good we possess." Explain and illustrate.

60. "The marginal wants that a good serves should be thought of as being the least important of the most important wants that its supply suffices to serve." Explain and illustrate.

61. "The utility of the marginal unit of a supply determines the utility of *any* of the units of that supply at that moment." Illustrate in terms of the frontiersman example.

62. Explain why, despite the views of Galbraith, the law of diminishing marginal utility is perfectly consistent with the fact that man's need for wealth is limitless. (Describe the three grounds for this conclusion.)

63. Explain how the law of diminishing marginal utility resolves the classical economists' paradox of value—i.e., the seeming paradox constituted by the fact that goods of apparently the lowest utility, such as diamonds, are normally more valuable in exchange than goods of apparently the highest utility, such as water.

64. Explain how determination of price by cost is an instance of the operation of the law of diminishing marginal utility.

65. Describe how the law of diminishing marginal utility helps to explain the pattern of demand that prevails in the economic system at any given set of prices of goods. In your answer be sure to describe the nature of the equilibrium that emerges.

66. Why is it mistaken to describe the equilibrium to which reference is made in the preceding question, in terms of an equal proportionality between price and marginal utility everywhere?

67. Show how the principle of diminishing marginal utility helps to explain the phenomenon of partial, relative overproduction and underproduction described by Say's Law.

68. "In essence, our desire for wealth outstrips our ability to produce it by virtue of the limitless range of the mental in comparison with the physical and thus by virtue of the fact that the range of our imaginations is always incomparably greater than the power of our arms." Discuss.

69. Explain why the relationship described in the preceding question remains true no matter how much we may augment the power of our arms by means of tools and machinery.

70. Explain what economists mean by "scarcity."

71. Contrast the meaning of scarcity in a capitalist society with its meaning in a precapitalist society.

72. Explain why scarcity under capitalism is the cause of the progressive elimination of scarcity in the sense experienced in a precapitalist society.

73. Explain what is meant by time preference.

74. Explain what, according to the principle of time preference, is analogous in the valuation of temporally more remote future goods and the perception of spatially more remote physical objects.

75. Does time preference mean that if it is December, an individual in Minneapolis should be expected to value a bathing suit that will be available to him in the coming January more highly than one that will be available to him in the coming July? Explain.

76. Is it consistent with the principle of time preference to value the first unit of a future supply above the second unit of a present supply? Explain.

77. Explain how the ascending price structure of commodity futures is consistent with the principle of time preference.

78. Explain how the principle of time preference is implied in the very nature of valuing something.

79. Explain why the nature of human life implies time preference.

80. Explain how time preference prevents the existence of profit and interest from always resulting in saving and the accumulation of additional capital.

81. Illustrate how time preference manifests itself in the extent to which individuals make provision for the future relative to their current consumption.

82. Other things being equal, how would you expect the size of the savings of an individual with a higher degree of time preference to compare with the size of the savings of an individual with a lower degree of time preference?

83. What is meant by the two dimensions of the scarcity of capital goods?

84. Give examples of different degrees of capital intensiveness in the production of products.

85. Compare different industries in their degree of capital intensiveness.

86. Describe the effect of time preference on the methods of production used, the kinds of products produced, and the relative size of various industries.

87. Explain how the existence of time preference operates to keep capital in its "vertical dimension" permanently scarce.

88. Describe the extent to which capital would have to be accumulated before the scarcity of capital in its vertical dimension could be overcome.

89. "It is always necessary to leave undone an incalculable range of potential improvements whose execution would require a more abundant accumulation of capital in its vertical dimension than exists." Discuss.

90. Describe the relationship between time preference, on the one side, and the degree of rationality and economic freedom in a society, on the other.

91. Explain the relationship between wealth and human labor.

92. What is meant by a product? A producer?

93. Explain why the concept of labor is not limited to manual labor in a division-of-labor society. What other type of labor is very important, which achieves its effects by working through the manual labor of others?

94. "Man does not create the matter that natural resources represent, but he does create their *wealth-character*." Explain.

95. "The scarcity of wealth implies a more fundamental *scarcity of labor.*" Explain.

96. Explain how the scarcity of labor is manifest in the fact that virtually everyone would like to enjoy an income many times greater than the income he is presently capable of earning.

97. Why would it be necessary physically to produce five times as much if the average member of society were to have five times the real income (i.e., buying power) that he now has. (Why wouldn't giving everyone five times the money income make possible this greater real income?)

98. To have all the goods and services we would like to consume, approximately how much labor would we have to perform on average per week, in the present state of technology, in order to produce it?

99. "The supply of labor that people can provide falls radically short of the supply whose products they would like to have." Explain.

100. Describe the extent to which the scarcity of personal services adds to the scarcity of labor.

101. "Each of us is easily capable of forming desires

whose fulfillment requires the labor of multitudes, and yet by the laws of arithmetic, the average member of any society can never obtain more than the labor, or products of the labor, of just *one* person." Discuss the implications for the scarcity of labor.

102. If labor is fundamentally scarce, why is there ever a problem of mass unemployment?

103. Explain why the scarcity of labor is *ineradicable,* i.e., is not eliminated either by a larger supply of labor or by a higher productivity of labor.

104. "The fundamental and essential nature of economic life is this: the need and desire for additional wealth are there and the nature-given means of producing it are there; all that is lacking is the ability of human labor to transform the nature-given means of production into additional wealth." Discuss.

105. What is meant by "the economic problem"?

106. What are the underlying foundations of the economic problem?

107. What is an important subsidiary problem that is also frequently referred to as the economic problem?

CHAPTER 3. NATURAL RESOURCES AND THE ENVIRONMENT

PART A. NATURAL RESOURCES

1. Describe the currently prevailing view on the relationship of production to the supply of natural resources.

2. Explain in what sense man creates natural resources and how, since the beginning of the Industrial Revolution, he has actually enlarged their supply right along with the increase in the supply of products.

3. "From the upper limits of the atmosphere, to its center, 4,000 miles down, the earth is a solid ball of natural resources." Discuss.

4. What does the increase in the supply of useable, accessible natural resources depend on? Explain.

5. "The energy shortage proved the existence of a growing scarcity of natural resources in nature." Discuss. (In your answer, be sure to present an alternative explanation of "the energy crisis.")

6. Explain what is meant by "the law of diminishing returns." Describe an important phenomenon analogous to the law of diminishing returns and which rests on the logic of human choice.

7. Explain how the existence of continuous economic progress and the law of diminishing returns can be logically reconciled.

8. "The law of diminishing returns confirms the fact that the fundamentally limiting factor in production is always human labor." Discuss.

9. "Allowing fertile land to lie idle is economically wasteful." Discuss in the light of the discussion of the law of diminishing returns.

10. "The fact that, as a rule, only one-third of the oil physically present in a petroleum deposit is ever extracted, is evidence of economic waste." Discuss this contention in the light of the discussion of the law of diminishing returns.

11. "The law of diminishing returns implies that economic progress is necessary *to maintain the standard of living,* not just to raise it." Discuss.

12. Explain the implications of the discussion of the law of diminishing returns for the value of government irrigation and flood control projects.

13. "Atomic waste disposal and the strip mining of coal should be prohibited because they destroy the future usefulness of the land sites involved." Discuss in the light of the law of diminishing marginal utility.

14. "In order to avoid the waste of valuable raw materials, we must recycle tin cans, paper products, and so forth as much as possible." Explain the errors of this claim.

15. "American retailers are wasteful in giving shoppers fresh paper bags with every purchase. In the name of economy, they should adopt the practice common in many parts of Europe of requiring shoppers to bring their own bags." Explain the errors of this claim.

16. "Driving at fifty-five miles an hour consumes less gasoline for the same distance travelled than does driving at sixty-five miles an hour. Thus, it is only economic common sense to drive at fifty-five miles an hour." Explain what is wrong with this claim.

17. Explain what is meant by "conservation by the market."

18. "In the early years of this century, logging companies often cut down forests without bothering to replant. This proves the destructive nature of the profit motive." Present the alternative explanation of deforestation that is provided in *Capitalism.*

PART B. THE ECOLOGICAL ASSAULT ON ECONOMIC PROGRESS

1. "In the last two centuries, loyalty to the values of science, technology, and capitalism has enabled man in the industrialized countries of the Western world to put an end to famines and plagues, and to eliminate the once dread diseases of cholera, diphtheria, smallpox, tuberculosis, and typhoid fever, among others." Discuss.

2. Describe the effects of industrial civilization on life expectancy in the Western World since the 18th Century, and in the United States since 1900.

3. Describe the effects of the use of man-made power on the productivity of labor, the average standard of living, and human life expectancy.

4. Describe the effects of industrialization on the quality of drinking water, and on air quality in large towns and cities in comparison with the past.

5. Describe the effects of man's economic activity on the survival of species other than man. Describe the effects on *human* survival.

6. Explain the economic logic underlying the near extinction of the buffalo and why the preservation of large numbers of buffalo would represent an enormous economic waste.

7. Compare and contrast the concepts of economic efficiency and "energy efficiency." Explain how they can mean opposite things.

8. "The environmental movement is characterized by pathological fear of industrial civilization and of science and technology." What examples can be cited in support of this claim?

9. Describe the environmental movement's attitude toward man-made power.

10. What is meant by the doctrine of intrinsic value? How does it contrast with the doctrine that the source of the goods character of things lies within human beings?

11. Describe the ethical perspective of the environmental movement in the light of its endorsement of the doctrine of intrinsic value.

12. How does the doctrine of intrinsic value imply a view of human beings as being inherently destructive, and the more so as they come to be guided by the values of reason, science, and technology?

13. Explain how the exact same set of facts, such as the clearing of a piece of land and its conversion into a housing tract can be described both as an improvement in the environment and as destruction of the environment, on the basis of the two different ethical standards of the supreme value of human life and the doctrine of intrinsic value.

14. "From the perspective of the doctrine of intrinsic value, the lives of spotted owls, snail darters, and gnat catchers are as valuable as the lives of human beings, and so is the existence of hillsides, deserts, and jungles." Discuss.

15. Explain the contention that production necessarily tends to improve the environment. (Be sure to describe both the underlying ethical perspective and the relevant fundamental economic principles that support the statement.)

16. Explain and illustrate in what sense the environmental movement holds individuals responsible for the actions of a collective.

17. If the environmental movement had existed in the early 19th century, what sort of arguments might it have raised against the settlement of the Midwest?

18. "Provided they are not allowed to use force, the voluntary, self-interested actions of individuals always tends to accomplish incomparably more good than harm. Such harm as occurs, which is not intended and for which no individual is actually responsible, should be regarded as an act of nature, which individuals should then be left free to deal with." Discuss.

19. Explain what is meant by the doctrine of "externalities."

20. Describe the implications of the externalities doctrine for the kinds of benefits one might claim the right to payment and for the kinds of costs one might be held accountable.

21. If individuals are not be able to demand payment for *all* the benefits they give to others, and are not to be held accountable for *all* the costs they impose on others, explain what principle can serve as a narrower standard.

22. Explain how the failure of socialism has contributed to the environmental movement's distrust of science, technology, and the power of human reason.

23. "The ecology movement is an attempt to resurrect the essential doctrines of socialism concerning the consequences of the uncontrolled, self-interested actions of individuals." Discuss.

24. What basic political-economic conditions would be required for man to deal successfully with global warming (if in fact it were to come) and the inevitable climate changes, such as the next ice age, that sooner or later will be produced by nature itself?

25. Explain the essential differences between the concepts of economic progress and economic growth.

26. Describe the role of contemporary education in promoting the influence of the ecology movement.

27. Describe an essential cause of the inability of contemporary education to succeed in the task of educating.

28. Explain the role of the cultural devaluation of man in the success of environmentalism.

CHAPTER 4. THE GAINS FROM THE DIVISION OF LABOR

1. Explain what is meant by the division of labor.

2. Describe how the individual lives in a division-of-labor society, in terms of the extent to which others are the physical beneficiaries of his labor and the extent to which he is the physical beneficiary of the labor of others.

3. Explain how the division of labor increases the amount of knowledge that is used in the production of products. (Illustrate in terms of the example of the "census of knowledge" in third-world societies and our own.)

4. What is meant by "the multiplication of knowledge" in a division-of-labor society?

5. Explain how the multiplication of knowledge makes possible the production of products that would otherwise be impossible.

6. "The division of labor makes it possible for geniuses to specialize in science, invention, and the organization and direction of the productive activity of others, thereby further and progressively increasing the knowledge used in production." Discuss.

7. "An important advantage of the division of labor is that individuals at all levels of ability can concentrate on the kind of work for which they are best suited on the basis of differences in their intellectual and bodily endowments." Explain and illustrate.

8. Explain and illustrate what is meant by the geographical gains from the division of labor.

9. Describe the effects of the division of labor on the ability of any geographical area to exploit its natural resources.

10. Describe the various ways in which the division of labor increases the efficiency of the processes of learning and motion that are entailed in production.

11. Describe four ways in which the division of labor underlies the use of machinery in production.

12. In the light of knowledge of the gains derived from the division of labor, explain why 18th Century England was the first country to experience the Industrial Revolution.

13. "What a division-of-labor society represents is the organization of the same total sum of human brain power in a way that enables it to store and use vastly more knowledge than would otherwise be possible." Discuss.

14. "The effect of a division-of-labor society is not only to increase the total of the knowledge that the same amount of human brain power can store and use, but also to bring that knowledge up to a standard set by the most intelligent members of the society." Explain.

15. "While man always possesses the faculty of reason, a division-of-labor society is necessary if he is to use his rationality efficiently in production." Discuss.

16. "The division of labor increases the efficiency with which man is able to apply his mind, his body, and his nature-given environment to production." Discuss.

17. Explain why the division of labor is an essential precondition for the achievement of a high and steadily rising productivity of labor.

18. "The division of labor is the essential framework for the ongoing solution of the economic problem." Discuss.

19. "Whoever, in the words of von Mises, prefers wealth to poverty and life and health to sickness and death, is logically obliged to value the existence of a division-of-labor society and all that it depends on." Discuss.

20. "The widely held notion that life in society requires the sacrifice of the individual's self-interest is totally mistaken in regard to a division-of-labor society." Discuss.

21. Explain how in the light of knowledge of the gains from the division of labor, the ethical principle of respect for the persons and property of others has a rational basis in the requirements of the individual serving his own material self-interest.

22. Explain why in a division-of-labor society, the individual's material self-interest is served to the extent that others are secure in their persons and property from the initiation of force.

23. "The claim that a division-of-labor society is incompatible with the well-rounded development of the individual, in accordance with the ideals of the Renaissance, is nonsensical. It is precisely in a division-of-labor society that the average worker, for the first time in all of human history, has the opportunity of actually becoming something of a Renaissance man." Discuss.

24. "A dull job performed for money is almost always less dull than one performed merely for the sake of a given physical result." Explain.

25. Describe how even the otherwise most monotonous, repetitious types of factory work might be given an important measure of challenge and excitement if a fuller measure of capitalism existed.

26. "The proportion of interesting and challenging jobs in the economic system has steadily increased with the progress of the division of labor." Discuss.

27. "While it is true that alienation is a growing problem in present-day society, it is not because of, but *in spite of* the existence of the division of labor." Discuss.

28. Define production and producer.

29. Define labor.

30. Explain what is meant by "land" as the term is used in economics.

31. Explain what is meant by "consumption," in the physical sense.

32. Describe the twofold relationship that exists between production and consumption.

33. Explain and illustrate what is meant by the concepts of productive consumption and reproductive consumption.

34. Explain and illustrate what is meant by the concept of unproductive consumption.

35. Explain and illustrate how in the context of a division-of-labor, monetary economy, the concepts productive consumption and reproductive consumption become synonymous.

36. Explain and illustrate what is meant by the concept of capital goods in the physical sense.

37. Explain what is meant by the concept of capital. (What form does this concept take in a division-of-labor, monetary economy?)

38. Why must a substantial portion of production be devoted to the production of capital goods in order to maintain the supply of capital goods?

39. What must be true of the portion of production devoted to the production of capital goods, in order to have capital accumulation?

40. Why is the supply of capital goods of importance to production?

41. How does a greater efficiency in the utilization of labor and existing capital goods serve to increase the supply of capital goods?

42. Explain why production with capital goods always represents an indirect, more time-consuming process of production as compared to production without capital goods.

CHAPTER 5. DEPENDENCE OF THE DIVISION OF LABOR ON CAPITALISM

PART A. THE NATURE OF THE DEPENDENCIES

1. Explain why, by the very nature of the leading benefits it provides, namely, the multiplication of knowledge and the gains from the existence of geniuses, a division-of-labor society depends on the institution of private ownership of the means of production. (Hint: the connecting links are separate, independent knowledge and the consequent need for separate independent action and production.)

2. Explain the fundamental incompatibility of socialism and collectivism with a division-of-labor society. In your answer, bear in mind the socialist prescription of "central planning," viz., the whole of society functioning as one, indivisible unit in the conduct of the economic system.

3. Explain why socialism in fact always represents contradictory, partial planning, not any form of coordinated central planning.

4. Describe how capitalism is characterized by economic planning on the part of all of the individual participants in the economic system—businessmen, wage earners, and consumers.

5. Explain how the virtually omnipresent private economic planning that goes on under capitalism could have been overlooked by the great majority of today's intellectuals and media and the significance of this fact.

6. Explain the error underlying the use of the expression "economic planning" as a synonym for *government* planning.

7. Describe how the economic planning of individuals under capitalism is based on prices and how the resulting economic calculations provide a standard of action for the planner under capitalism.

8. Explain why the standard of action that the consideration of prices and costs provides to the planner under capitalism, is *objective* in the light of his desire to obtain more wealth.

9. Explain and illustrate how prices serve to coordinate and harmonize the plans of each individual under capitalism with the plans of all other individuals in the economic system.

10. Explain the dependence of the price system on the profit motive and the freedom of competition.

11. Explain the dependence of the profit motive and the freedom of competition in turn on private ownership of the means of production.

12. Explain why in a division-of-labor society exchange must exist on a massive scale and be a central feature of economic life.

13. Explain the dependence of a division-of-labor society specifically on *monetary* exchange and how the absence of money would make impossible the existence of any substantial degree of division of labor. In your answer, be sure to explain the dependence on money with respect both to the problem of the double coincidence of wants and the matter of economic calculation.

14. In the light of its essential role in the division of labor, appraise the truth of the frequent contention that "money is the root of all evil."

15. Explain how saving is vital to the development of the division of labor.

16. Explain what is meant by the "the division of payments," how it is essential to the vertical aspect of the division of labor, and how it depends on saving.

17. Explain the role of economic competition with respect to the organization of the division of labor.

18. Explain the role of the freedom of competition with respect to safeguarding a division-of-labor society from possible extortion by the members of individual vital industries.

19. Explain why economic inequality is a virtually inevitable result of economic freedom.

20. Explain how the imposition of economic equality represents the destruction of the individual's ability to regard himself as a causal agent and thus must radically reduce production both under the division of labor and under any other arrangement.

21. Explain how economic inequality enables less capable individuals to compete with more capable individuals.

PART B. ELEMENTS OF PRICE THEORY: DEMAND, SUPPLY, AND COST OF PRODUCTION

1. What is meant by the concepts demand and supply in classical economics?

2. What is meant by these concepts in contemporary economics?

3. State the law of demand.

4. Explain three reasons why the law of demand exists.

5. Explain the difference between a change in quantity demanded and a change in demand.

6. Describe the kinds of factors that cause changes in demand.

7. What is meant by the elasticity of demand?

8. Explain the use of the total spending/total revenue criterion in distinguishing between demands that are elastic, inelastic, or unit elastic.

9. Why do cases of close substitutes and luxury goods represent examples of demands that are likely to be elastic?

10. Why do cases of poor substitutes and necessities represent examples of demands that are likely to be inelastic?

11. What is the leading example of a unit elastic demand, and why?

12. Use the concept of elasticity of demand to explain the differing effects of improvements in output per worker on the number of workers employed in an industry in different circumstances.

13. Use the concept of elasticity of demand to explain the possible impact on a company's profits of charging a higher or lower price.

14. Explain why elasticity does not remain constant even over the length of the same demand curve.

15. Explain why, even though the basic case is that of a vertical supply line reflecting a given quantity that sellers are prepared to sell at the best price they can obtain, supply curves often slope upward and to the right.

16. Explain why the marginal utility of sellers is actually not a significant reason for upward sloping supply curves.

17. Explain why the law of diminishing returns is usually not relevant to upward sloping supply curves in the short run.

18. Explain in what context the apparent determination of price by supply and demand curves actually represents determination of price on the basis of cost of production.

19. Why is it incorrect to try to derive supply and demand curves by observing changes in price and quantities demanded and supplied over time?

20. Explain why cases in which both prices and quantities demanded rise over time do not contradict the law of demand.

CHAPTER 6. DEPENDENCE OF THE DIVISION OF LABOR ON CAPITALISM II: THE PRICE SYSTEM AND ECONOMIC COORDINATION

PART A. UNIFORMITY PRINCIPLES

1. What is the uniformity-of-profit principle and how does it work?

2. How does the uniformity-of-profit principle counteract, delimit, and prevent the mistakes of relative overinvestment and overproduction and relative underinvestment and underproduction, and thus promote coordination in the relative size of the various branches of production?

3. How does the uniformity-of-profit principle give consumers the power to change the pattern of production, i.e., to cause industries to expand or contract?

4. Explain why insofar as goods are produced in a free market to which various people object—such as allegedly nonnutritious breakfast cereals, automobiles without seatbelts or airbags, trashy or pornographic literature, alcoholic beverages, cigarettes, and so on—the logical targets of the complaints are the consumers, even though the actual targets are almost always the manufacturers.

5. How does the uniformity-of-profit principle operate to bring about a progressive increase in production?

6. If the uniformity-of-profit principle implies increas-

ing production and falling prices,, why do we almost always observe rising prices instead of falling prices? Is this a contradiction of the uniformity-of-profit principle?

7. What do claims about "planned obsolescence" imply about the operation of the uniformity-of-profit principle? Are such claims well founded? Explain.

8. How do cost cuts operate to expand production in the economic system?

9. How does successfully anticipating changes in consumer demand operate to increase the gains from economic progress?

10. What is a minimum price control? What is a maximum price control?

11. Use the uniformity-of-profit principle to trace the effects of repealing a minimum price control, such as those on many agricultural commodities. What would be the initial effect on price and profitability? The subsequent effects?

12. Use the uniformity-of-profit principle to trace the effects of repealing a maximum price control, such as rent control or a price control on oil and gasoline. What is the initial effect on price and profitability? The subsequent effect? Has the repeal of price controls on oil worked out differently than the theory indicates?

13. Explain why it is reasonable that people are able to borrow money to the extent that they already have money.

14. Explain why there is a tendency toward the existence of a uniform price for the same good throughout the world.

15. Is this principle contradicted by the existence of tariffs?

16. Explain how the existence of this principle operates to minimize the effects of local supply failures and to prevent famines.

17. Explain how the operation of this principle could have mitigated the effects of the Arab oil embargo. Explain what prevented it from doing so.

18. Explain why the belief that if a country has lower tariffs than its trading partners it is at a disadvantage, is equivalent to the belief that if the winds and the ocean currents run toward it and cause its inbound transportation costs to be less than its outbound transportation costs, it is at a disadvantage.

19. Explain why there is a tendency for the price of a good in the present to equal its expected price in the future.

20. Explain how the existence of this principle operates to minimize scarcities over time.

21. In the light of this principle, appraise the role of commodity speculation.

22. Explain how a price control can turn a scarcity of a storable good into a famine.

23. Explain why speculators as a class cannot profit from price increases caused by their own activity.

24. Explain why there is a tendency toward a uniformity of wage rates for workers of the same degree of skill and ability.

25. Does the operation of this principle require that forty-year olds be willing to change careers for ten or twenty percent pay differences? Why not?

26. How does the uniformity-of-wages principle give the consumers the power to determine the relative size of the various occupations?

27. Explain what kind of factors introduce permanent inequalities in wage rates at any given level of skill and ability.

28. Explain why there are permanent inequalities of wage rates between unskilled, skilled, and professional-level workers.

29. Explain the effects of a rise (fall) in the demand for the products and services of skilled labor relative to unskilled labor on the wages of the two groups. What does this imply about the role of the consumers in setting wage rates?

30. Explain why the wages of star performers can exceed the wages of other workers practically without limit and not result in any increase in supply. What does set the limit to the wages of star performers?

31. It is frequently claimed that capitalism discriminates against blacks by paying them less than whites for doing the same work, and by denying them entry into the better paying jobs. Appraise this claim in the light of the uniformity-of-profit principle and the uniformity-of-wages principle.

32. It has been claimed that capitalism discriminates against blacks by charging them higher rents for the same housing and higher prices for the same goods. Appraise this claim in the light of the uniformity-of-profit principle

33. Explain how cost of production indirectly and directly influences the prices of products.

34. Explain why cost of production cannot be an ultimate explanation of prices, but leads back to supply and demand as the ultimate explanation.

PART B. ALLOCATION PRINCIPLES

1. Explain which kinds of prices are directly determined by supply and demand and which are determined directly on the basis of cost of production.

2. Explain the role of the quantity of money and consumer preferences in the determination of prices based on supply and demand.

3. Explain the significance of prices of consumers' goods determined by supply and demand
   a. in preventing shortages
   b. in serving the self-interests of buyers as well as sellers, and of poor buyers as well as rich ones
   c. in determining the distribution of goods and services in limited supply

4. Explain the significance of prices of factors of production in limited supply in regard to points (a), (b), and (c) of the preceding question and with respect to the allocation of the factors of production among the competing uses for them.

5. Explain how the factors of production are allocated to their most important uses.

6. Explain how the concept "most important uses" is actually a variable range determined by the supply of the factor available.

7. Explain how a free market operates to maximize gains and minimize losses in connection with increases or decreases in the supply of a factor of production.

8. Explain how price controls during the Arab oil embargo led to submarginal uses of oil being able to go on obtaining supplies at the expense of far more important uses of oil.

9. Explain how cost calculations operate to lead each product to be produced by methods that least impair production in the rest of the economic system.

10. Explain how price controls during the Arab oil embargo prevented the economic system from adopting a rationally planned response to the reduction in oil supplies.

CHAPTER 7. DEPENDENCE OF THE DIVISION OF LABOR ON CAPITALISM III: PRICE CONTROLS AND ECONOMIC CHAOS

PART A. PRICE CONTROLS AND SHORTAGES

1. Explain how the definition of inflation as being rising prices implies that businessmen are responsible for inflation.

2. Present two alternative definitions of inflation (which are virtually equivalent to one another).

3. Why are rising aggregate demand and falling aggregate supply the only two possible direct causes of a higher price level? Why must falling supply be ruled out as a cause of the rising prices of the last 60 years?

4. Describe the process by which an increasing quantity of money raises aggregate demand and thus prices.

5. Explain why the imposition of price controls to combat inflation is analogous to an attempt to deal with expanding pressure in a boiler by means of manipulating the needle in the boiler's pressure gauge.

6. "Price controls not only do not stop inflation, but *combine* with inflation to produce a different and worse set of consequences than inflation alone would produce." Discuss.

7. Explain what is meant by a "shortage."

8. Explain how the concept of a shortage differs from that of scarcity.

9. Explain why in a free market scarcities do not result in shortages.

10. Explain why scarcities can result in shortages only when they are accompanied by price controls.

11. Explain how price controls can create shortages even when supplies of goods are at record-high levels.

12. Explain how the combination of inflation plus price controls easily results in large and growing shortages of practically everything.

13. Give an illustration of how shortages cause scarcities.

14. Why is it that in a free market, so far from there being shortages, the typical case is that a seller is in a position to supply more than his present number of customers, even when the overall supply of the item is strictly limited for the time being.

15. Explain why price controls, especially when accompanied by inflation, operate to reduce the supply of goods produced.

16. Explain why rent controls first destroy the housing of the poor.

17. Explain how price controls in a local market operate to deprive that market of supply.

18. Describe the role of price controls in causing the natural gas crisis of 1977.

19. Describe the role of price controls in causing the agricultural export crisis of 1972–73.

20. Explain how price controls foment international hostility and thus serve to promote wars.

21. Explain why price controls that are expected to remain in force for several more years reduce the supplies of goods held in storage.

22. Explain why private hoarding is not responsible for the existence of shortages.

23. Explain why private speculation is not responsible for the existence of shortages even in cases in which suppliers do withhold supplies, in anticipation of the relaxation or repeal of a price control in the near future.

24. Recall your previous answer (to a question on Chapter 6) explaining why speculators cannot gain by

attempting to artificially raise the price of something and then sell their supplies at the higher price they themselves have caused.

25. Explain the argument that it would be legitimate for producers in the position of the oil companies in the 1970s to band together to withhold supplies in a deliberate effort to have the controls repealed. Explain also why this did not actually happen and is very unlikely ever to happen, given the state of knowledge and the attitudes of today's businessmen.

26. Explain why in contrast to the case of most goods, price controls on natural resources in the ground are likely to result in a withholding of supplies.

27. Explain how a control on the wage rate of any particular type of labor operates to reduce the supply of that type of labor.

28. Explain how a price control on any particular product of a factor of production, such as milk for drinking, which is made from raw milk, operates to reduce the supply of that product even if the price of the factor of production is also controlled.

29. Practically, the very day on which rent controls were imposed in Los Angeles, apartment-house owners began to convert their units to condominiums. Explain why. Can the landlords reasonably be blamed for this?

30. Explain in what way price controls are tantamount to a prohibition of supply.

31. Explain the likely effect of the combination of price controls and inflation on electric utilities and other regulated industries.

32. Describe the general level of knowledge concerning the cause of shortages.

33. Describe the level of knowledge implied by the New York City law declaring that rent controls could not be lifted until the vacancy rate in the City had first climbed to a certain substantial level.

34. Explain the effect of inflation on nominal profits.

35. Explain the effect of inflation on real profits.

36. "The claim of the city government of New York that in refusing to keep up their buildings landlords were 'milking' their properties is an attempt of the guilty to prosecute the innocent." Discuss.

37. Describe what is meant by the "destructionist mentality."

38. Explain the effect on the tenants and consumers of electricity and oil products, if the landlords, electric utilities, and oil companies that serve them were richer. How well understood are these connections in New York City? In the United States as a whole?

39. Explain why in an inflationary environment, the upward repricing of inventories already on the shelves is in the long-run interests of the consumers as well as the producers.

40. Describe the essential claims made or implied in the campaign against the profits of the oil companies in the early 1970s.

41. Describe the essential facts omitted in the above-mentioned campaign against the profits of the oil companies.

42. Describe the claims made in the more recent attack on the prices and profits of the pharmaceutical companies and important facts omitted in those claims.

43. In the 1970s, the oil companies were widely blamed for having caused the oil shortage. Explain what the oil companies would have had to do in order actually to cause the oil shortage.

44. Describe the ways in which the U.S. government, acting largely under the influence of the ecology movement, has operated to reduce the supply of oil and increase the demand for it.

45. Describe the ways in which the policies of the U.S. government have been responsible for the success of the OPEC cartel. Be sure to include in your answer a discussion of how the competitors of a cartel would normally be the major beneficiaries of its reduction of production and how price controls served to insulate the cartel from competition.

46. Describe the policy of the American oil companies with respect to the increase in the supply of oil.

47. Explain how the profit motive has necessitated that the oil companies strive to increase the supply of oil.

48. "The accusation that the oil companies were responsible for the oil shortage embodies a triple injustice." Explain.

49. What is the gain that oil companies derive from having independent service station owners?

50. Explain how the existence of an oil shortage, caused by price controls, was the cause of efforts by the oil companies to deprive their independent service station owners of supplies.

51. What are the fundamental and radical distinctions that are ignored in the claim that in setting their prices private firms are engaged in a process of price control, with the result that the only choice left is between selfish, private price controls and benevolent, government price controls?

PART B. FURTHER EFFECTS OF PRICE CONTROLS AND SHORTAGES

1. Explain why price controls and shortages deprive the buyers of economic power over the sellers and place the latter in a more powerful position with respect to ignoring the wishes of the buyers than if they

(the sellers) were protected legal monopolists.

2. Explain why price controls and shortages give producers a motive to reduce the quality of their products.

3. Explain how price controls and shortages launch a spiral of mutually reinforcing hatreds between buyer and seller. Illustrate in terms of rent controls in New York City and the treatment of customers during the gasoline shortage.

4. Explain how repeal of rent controls would restore harmony between landlords and tenants.

5. Explain how price controls and shortages create an impetus to higher costs.

6. Explain how price controls result in more than one controlled price being imposed on producers of the same good and the administrative chaos this results in. Illustrate in terms of the price controls on crude oil.

7. Explain how price controls and shortages introduce chaos into the distribution of consumers' goods to individuals.

8. Explain how price controls and shortages introduce chaos into the geographical distribution of goods among local markets.

9. Explain how the existence of a shortage prevents a larger supply from reducing the price of a good.

10. Explain how the severity of shortages in particular localities can depend on the time of year in which the price controls are imposed.

11. Explain how small bureaucratic adjustments in the controls can cause major swings in supply between different geographical markets.

12. Explain how price controls and shortages introduce chaos into the distribution of factors of production among their various uses and make it possible for some products of a price-controlled factor of production to be faced with extremely severe shortages, while other products are faced with only minor shortages. Illustrate in terms of the oil shortage.

13. Explain how the position of the various products in the preceding question can suddenly be reversed by minor changes in the uncontrolled prices of complementary factors of production, by small bureaucratic changes in the price controls, or by anything that results in the slightest changes in the relative profitability of the various products of the factor of production.

14. Explain the relevance of the season of the year in which price controls are imposed to the extent to which different products of a factor of production are faced with shortages. Illustrate in terms of the oil shortage.

15. "Price controls and shortages create tremendous instability in supply. The supply of everything subjected to controls becomes subject to sudden, massive, and unpredictable shortages." Discuss.

16. Explain why price controls and shortages cause hoarding and how hoarding makes shortages more severe.

17. "Under price controls, the most vital and urgent employments of a factor of production are prevented from outbidding not only its most marginal employments, but, from the standpoint of a free economy, employments that could not even qualify as submarginal." Discuss.

18. Explain how the abolition of price control puts an end to hoarding.

19. "The effect of a shortage of any particular commodity is to cause the unsatisfied demand for that commodity to spill over and add to the demand for other commodities." Discuss.

20. "Selective" or partial price controls, that is, price controls imposed merely on certain goods only, are contrary to any rational purpose the government might have in imposing them." Illustrate in terms of the effects of a price control on milk.

21. Explain how selective or partial price controls actually raise prices. Be sure to include a discussion of the effects on the efficiency of production.

22. Explain what is wrong with the claim that price controls "save people money."

23. Explain why rent control on part of the supply of rental housing has the effect of raising rents on the part of the supply that remains free of rent controls.

24. Explain how rent controls and the housing shortages they cause have the potential for bringing about the compulsory assignment of boarders to homes and a system of internal passports so that it requires the government's permission to move to various places within one's own country. Illustrate in terms of the conditions of Soviet Russia.

25. Why have rent controls in the United States not resulted in the kind of conditions described in the preceding question?

26. Why does rent control serve to increase the effective cost of constructing new rental housing?

27. Explain how rent controls contribute to the imposition or increase in local sales and income taxes.

28. "The effect of the immediate abolition of rent controls would largely be that the present 'beneficiaries' of rent control simply have to change places with an equally large but generally unrecognized class of victims of rent control." Discuss. (Be sure to attempt to identify the kinds of victims of rent control.)

29. Explain why the effect of repealing rent controls in an otherwise unregulated housing market would not be to make people sleep in the streets.

30. Explain how government housing regulations can result in people having to sleep in the streets.

31. Explain why the victims of rent control are suffering substantially more hardship than the 'beneficiaries' of rent control would suffer if rent controls were repealed.

32. Explain why there are no beneficiaries of rent con-

trol in the long run.

33. Explain how the repeal of our price controls on oil reduced the price received by the OPEC cartel.

34. Explain how the windfall profits tax on the oil industry, enacted in conjunction with the repeal of price controls, contributed to subsequent widespread bankruptcies in the oil industry.

PART C. UNIVERSAL PRICE CONTROLS AND THEIR CONSEQUENCES

1. Explain why price controls tend to spread until all prices and wages in the economic system are controlled—i.e., why partial price controls lead to universal price controls.

2. Explain why the shortages of individual goods that exist under universal price controls tend to be far more severe than the shortages that exist under partial or selective price controls. Illustrate in terms of the case of Soviet Russia.

3. Explain how excess demand under price controls builds up even though people's incomes are controlled.

4. Explain how shortages under universal price controls destroy production. (Recall the various ways previously discussed of how shortages do this and also explain the new and further ways that shortages under universal price controls have this result.)

5. Explain how universal price controls and the shortages they create result in chaos in the allocation of capital and labor among the various branches of production in the economic system.

6. Explain why, under universal price controls, the shortage facing any given industry may not be capable of being overcome, irrespective of any increase in the industry's output.

7. "As the result of the shortages created by universal price controls, capital and labor can be withdrawn from any industry and placed in any other industry, and there is no effect on the rate of profit anywhere."

8. Explain why, under universal price controls and shortages, even though the consumers want more of one good and less of another, say, more shoes and fewer shirts, the producers can go ahead and do the exact opposite and yet suffer no financial penalties.

9. Describe the extent of chaos that is possible in the relative production of consumers' goods under universal price controls. Illustrate in terms of the conditions of Soviet Russia.

10. Explain how the chaos in the relative production of capital goods that results from universal price controls and shortages undermines the subsequent ability to produce, including the subsequent ability to produce capital goods. Illustrate in terms of the conditions of Soviet Russia.

11. Explain why the reduction in the ability to produce capital goods tends to result in a cumulative, self-reinforcing decline in the ability to produce.

12. Explain how universal price controls result in a labor shortage, and the effects of a labor shortage on production.

13. Explain how the combination of inflation and shortages promoted a delusion of prosperity in the United States in World War II.

14. Describe the government's typical response, in the way of the assumption of added powers, to the chaos resulting from price controls and shortages.

15. Describe the U.S. government's response to the chaos that resulted in connection with price controls on oil and the resulting oil shortage.

16. Explain why the government's assumption of the further powers required to deal with the economic chaos caused by universal price controls and shortages represents the de facto socialization of the economic system.

17. Explain von Mises's distinction between "socialism on the German or Nazi pattern" and "socialism on the Russian or Bolshevik pattern."

18. "Nazi Germany was a socialist country. However, Sweden is not a socialist country, nor was Great Britain or Israel when they were governed by socialist parties." Discuss.

19. Explain why a "mixed economy" is more appropriately described as a "hampered market economy."

20. Provide several examples of genuinely socialist economies, including some of those that were socialist only for the duration of World War II.

CHAPTER 8. SOCIALISM, ECONOMIC CHAOS, AND TOTALITARIAN DICTATORSHIP

PART A. THE CHAOS OF SOCIALISM

1. Explain what characterizes an economic system as fundamentally capitalistic or as socialistic.

2. In the light of the above distinction, is Sweden a socialist economy or, in the words of von Mises, "a hampered market [viz., capitalist] economy"? How about Israel? Great Britain under the Labour Party?

3. Explain once more the distinction von Mises makes between Russian-style socialism and German-style socialism, or between socialism on the Bolshevik pattern and socialism on the Nazi pattern.

4. Provide examples of the two types of socialist economies in the twentieth century.

5. "The essential economic identity between socialism and universal price controls consists in the fact that both of them destroy private ownership of the means of production and its offshoots the profit motive and the price system." Discuss. (Hint: Explain how price controls effectively destroy private ownership of the means of production in the context of a division-of-labor society in the very fact of destroying the right to bid and ask prices.)

6. Describe the kinds of problems a socialist government must face in trying to plan the production of a simple item, such as shoes. In your answer, be sure to explain why decisions about all of the choices that arise in connection with planning the production of shoes are important not only from the standpoint of the consumers of shoes, but, no less, from the standpoint of the production of all other goods.

7. "In planning the production of shoes, or any other individual item, a socialist government is logically obliged to consider its effect on the production of *all other items in the economic system.*" Explain.

8. "The insuperable difficulty of socialist planning is that under socialism, it is necessary to plan the production of the entire economic system as an indivisible whole. That would be the only rational procedure. But the planning of the economic system as an indivisible whole is simply impossible." Discuss in terms of the kind and number of items that the individual planner would have to keep in mind and over what period of time.

9. Explain how under capitalism the economic system *is* planned in the light of the magnitude of knowledge indicated in the preceding question, but the knowledge is held in small portions by large numbers of individuals and is manifested in prices, which then serve to coordinate the plans and actions of all the various individuals.

10. Explain why unanticipated events, such as a train wreck, a snowstorm, even unanticipated favorable events, such as a better-than-expected harvest, require the replanning of the entire economic system.

11. Describe how a socialist economy would have to go about such replanning.

12. Describe how a capitalist economy goes about such replanning.

13. The essential problem of socialism is that it requires economic planning to take place without benefit of a division of intellectual labor. Discuss.

14. "It follows from the preceding, that in reality, the actual planning of socialist countries must be undertaken by separate government ministries, each responsible for different industries or regions. Even the individual factories undertake part of the planning process." Discuss.

15. "The—necessarily—decentralized planning of socialism causes chaos. Because without a price system—without the foundation and mainspring of the price system, i.e., private ownership of the means of production and the profit motive—the individual planners must operate at cross purposes." Explain and illustrate.

16. Describe the effect on the ability of an industry to carry out its plans successfully when its suppliers are disinterested monopolists, which is the case under socialism, where there are no profit-and-loss incentives and no freedom of competition.

17. What was meant by the Soviet quota system?

18. How was the Soviet quota system similar to the conditions that exist under universal shortages?

19. Illustrate how the lack of precision of the Soviet quota system further contributed to economic chaos.

20. What facts pertaining to socialism's lack of ability to plan gave rise to the Soviet quota system?

21. Explain why a labor shortage is a necessary feature of socialism.

22. Explain why shortages of consumers' goods are a necessary feature of socialism.

23. Explain why as a result of government ownership of the means of production, no one is free to produce on his own initiative and to regard his own intelligence and judgment as the ultimate authority for his action.

24. Explain how its attempted monopoly of intelligence and initiative is the cause of socialism's anarchy of production.

25. "Under socialism very few new ideas are thought of, fewer still are implemented, and virtually none at all are of benefit to the plain citizen." Discuss. (In your answer, compare and contrast capitalism and socialism with respect to the number of chances they offer for new ideas being tried in production, and with respect to the incentives to develop and implement such ideas, as well as with respect to the need to serve the buying public in deciding which new ideas to implement.)

26. "Under socialism, the plain citizen is no longer the customer, 'who is always right,' but the serf, who must take his rations and like it." Discuss in the light of the importance of profit-and-loss incentives and the freedom of competition in the satisfaction of the citizen's wants.

27. "A socialist government has no compelling reason to supply the plain citizen with anything more than is necessary to prevent an uprising." Discuss.

28. "In contrast to the politicians, democratic or totalitarian, the people who really do work to improve the economic conditions of the general public, who—literally—stay up nights thinking of ways to provide them with such things as grocery stores, more and better shoes and means of transportation, and everything else they may possibly want, are *capitalists,* who are continually motivated by the prospect of making or losing

a fortune and who can act on their own initiative." Discuss.

29. "The only kind of technological developments that a socialist government is interested in are those which are of value to its rulers: above all, improvements in weapons production and in the kinds of things that add to the rulers' prestige, such as 'sputniks'—or pyramids." Discuss in the light both of the economic powerlessness of the plain citizen under socialism and the fundamental moral-political postulate of a socialist society respecting the individual's status as a means to the ends of society.

30. Explain why it is impossible significantly to develop military technology, or any other aspects of technology of special interest to the state, while repressing civilian technology.

31. What is the significance of your answer to the preceding question for the ability of a free society to develop superior military technology in the long run in comparison with a slave society?

32. Why does the ability of the civilian economy to benefit from military technology depend on the existence of a capitalist economic system?

33. "Without the aid of capitalist countries, socialism must revert to feudalism. In the long-run, it is incompatible with the existence of an extensive division of labor." Discuss. (In your answer, be sure to explain whether or not conditions in the Soviet Union and its dependence on outside aid contradicted or confirmed these propositions.)

34. Explain how the inefficiencies of the Soviet Union explained its inability to accumulate capital despite a reputedly very high degree of concentration on the production of capital goods.

35. "Capital accumulation under socialism is possible only at the cost of human life, on the scale imposed by Stalin." Discuss.

36. What is meant by "market socialism"?

37. "Under market socialism, profits will serve as a 'parameter,' that is, as a guide to what to do—though, of course, no one will actually profit from doing what he is supposed to do." Discuss.

38. How is socialism to achieve a price system according to the market socialists?

39. The absurdity of market socialism can be grasped most simply by starting with the existence of capitalism and then imagining two alternative things to occur: (1) the government imposes price and wage controls, (2) the government obtains the power to expropriate any firm's or individual's capital and turn it over to any other firm or individual at its discretion." Discuss.

40. "The debate over market socialism is now closed and the correctness of von Mises's position definitively established." Discuss.

PART B. THE TYRANNY OF SOCIALISM

1. "Where the government owns all the printing presses and meeting halls and is the sole employer, freedom of press and speech is impossible." Discuss.

2. "Wherever socialism has actually been enacted, as in the Communist-bloc countries and Nazi Germany, violent and bloody means have been used to achieve it and/or maintain it. And where socialist parties have come to power but abstained from wholesale violence and bloodshed, as in Great Britain, Israel, and Sweden, they have *not* enacted socialism, but retained a so-called mixed economy, which they did not radically or fundamentally alter." Are these phenomena accidental or necessary? Discuss in the light of what is implied by the nationalization of all of the means of production.

3. Why does it take the Communists to establish socialism, while the social democrats are unwilling to take the necessary steps?

4. "The maintenance of socialism requires a reign of terror." Discuss in the light merely of the requirements of effectively enforcing a system of price controls.

5. Explain why black market activity under Russian-style socialism implies the theft of state property and under both Russian and German-style socialism, the crime of *sabotage* as well.

6. Why is it dangerous to be a production manager under socialism?

7. "The fundamental fact driving socialism to a reign of terror is the incredible dilemma in which the socialist state places itself in relation to the masses of its citizens." Discuss in terms of the promises versus the necessarily hateful reality of socialism, and the requirements of remaining in power in such conditions. Be sure to relate your answer to the phenomena of repression, periodic purges, and hysterical propaganda.

8. How do the policies pursued by Gorbachev, and his removal from office, relate to the preceding quotation?

9. How is forced labor implied in the very idea of socialist planning?

10. Explain what factors bring about forced labor under socialism even though it cannot plan. (In your answer, be sure to explain the essential role of labor shortages.)

11. Describe the factors causing or intensifying labor shortages under socialism.

12. Describe the extent of forced labor in the Soviet Union.

13. Describe the circumstances that almost led to the establishment of forced labor (on the home front) in the United States in World War II.

14. "Socialism is a system of aristocratic privilege and a court society."
   a. Describe the extent of aristocratic privilege in the Soviet Union, in terms of housing, the possession of automobiles, and access to shops.
   b. Explain how the existence of a system of aristocratic privilege is compatible with the slogan "from each according to his abilities to each according to his needs."
   c. Describe the factors, both economic and in terms of fundamental moral-political principle, that positively generate a system of aristocratic privilege under socialism.

15. "A socialist society does have some incentives. But the incentives are geared entirely to the achievement of the values of the rulers. There are no incentives to the achievement of the values of the plain citizens." Discuss. (In your answer, be sure to include the analogy to the system of incentives that exists in an army.)

16. Describe the status of intellectuals under socialism.

17. Explain why, while private slave owners in the days of slavery were at least motivated to treat their slaves with the same consideration they gave their livestock, forced labor under socialism goes even beyond slavery and results in mass murder.

18. How can private ownership of the means of production be established in the formerly socialist countries? Explain the essential requirements.

CHAPTER 9. THE INFLUENCE OF THE DIVISION OF LABOR

PART A. PRIVATE OWNERSHIP OF THE MEANS OF PRODUCTION

1. Describe the fundamental ways in which private ownership of the means of production benefits *nonowners* of the means of production.

2. State the above benefits in terms of the supply of what one buys and the demand for what one sells.

3. To what extent are the benefits of privately owned means of production to nonowners generally recognized? In your answer, be sure to develop the implications of the following: (a)the assumption that if you are in favor of private ownership of the means of production and of respecting the rights of the owners of the means of production, you yourself must be a wealthy capitalist or in the pay of such capitalists; (b) the assumption that blue collar districts will vote for leftwing candidates, while pro-free–enterprise candidates can be expected to do well in high-income areas; (c) the way to fight the spread of communism is to make more people into capitalists.

4. "Prevailing ideas concerning the benefit from ownership of the means of production derive from the era predating the establishment of a division-of-labor society and have not been reexamined since that time." Discuss.

5. "The benefit of privately owned means of production to nonowners is the greater and more rapidly increasing, the more the property rights of the owners are respected." Discuss.

6. Describe the benefits that owners of the means of production derive from them that nonowners do not.

7. Describe how much is available from the significant-sized capitalists for redistribution without directly and immediately encroaching on their capitals. Explain the effect of redistribution that is at the expense of capital.

8. Explain whether or not a policy of the redistribution of wealth and income is of benefit to nonowners.

9. "People should welcome government ownership of business enterprises because then the business firms become theirs." Discuss.

10. Explain why the alleged citizen owners of government enterprises, like the Post Office and Amtrak, cannot derive the special benefits of ownership that are derived from privately owned means of production.

11. Explain the distinction between profit management and bureaucratic management and why government operations are properly characterized by the latter while, in the absence of government intervention, business enterprises are characterized by the former.

12. Explain the benefits derived by *nonheirs* from the institution of inheritance and why the imposition of inheritance taxes is against the interests of everyone, not just the heirs.

13. Explain the case, *from the point of view of the average wage earner*, for initially concentrating tax cuts on the incomes of businessmen and capitalists rather than on the incomes of wage earners.

14. Explain the special hostility to private ownership of land.

15. Explain how the economic history of the period 1250–1750 appeared to lend support to the belief that landowners were the only long-run beneficiaries of economic progress.

16. Explain how private ownership of land and respect for the property rights of landowners in fact operates to reduce the economic significance of land rent.

17. Confirm your answer to the preceding question by describing the major extensions of private ownership of land that took place in the hundred years from 1750–1850.

18. Further confirm your answer to the same question by showing how limitations on private ownership of

land and interference with the property rights of landowners is the essential factor responsible for the sharp rise in oil "rents" in the last generation.

19. Explain how environmentalism operates systematically to increase the economic significance of land rent and, if unchecked, must ultimately bring back the same kind of economic situation as existed in the pre–Industrial era—i.e., the existence of a small minority of wealthy, landowners and a subsistence standard of living for almost everyone else.

20. Explain how private ownership of land in a market economy operates to eliminate the stain of violent appropriations of land that may have occurred in the past.

21. "The conditions of a non–division-of-labor society are necessarily those of recurring conflict and warfare, with successive waves of newcomers again and again forcibly displacing the previous inhabitants." Explain why.

22. Explain and criticize the policy of land reform.

23. Explain why it is not necessary for a country to have sovereignty over land and natural resources in order for its citizens to benefit from that land and natural resources.

24. Describe the benefits of foreigners' development of a country's natural resources to the inhabitants of that country.

25. Explain why a policy of economic freedom and respect for the property rights of foreign as well as domestic investors is essential to the economic development of the backward countries.

26. Explain what policy on the part of its government would give the maximum possible benefit of the land and natural resources of any given territory to the people of the world as a whole. Discuss the implications of this for a country's being able to remain at peace.

27. Explain what is meant by the "Argentine delusion" in connection with the collectivist view of the ownership of natural resources.

PART B. ECONOMIC INEQUALITY

1. Explain why in a division-of-labor society, the proposition that one man's gain is another man's loss does not apply.

2. Is there such a thing as an actual distribution of wealth? Explain.

3. Explain how the notion of a distribution of wealth leads to the conclusion that it is unjust for one person to produce more than another.

4. Explain why, both in their origin and in their use, great business fortunes are a source of gains to everyone who participates in the economic system. (Be sure to include in your answer a description of what is required in terms of financial arithmetic to accumulate a great fortune and what is required to go on earning a high rate of profit over a long period of time.)

5. Illustrate your answer to the preceding question in terms of Henry Ford's accumulation by the end of his life of $1 billion after having started out with about $25,000.

6. "Relative rates of growth or decline in accumulated wealth are the result of a combination of relative rates of profit and relative degrees of saving out of profits." Discuss.

7. If it is true that 10 percent of the population owns 90 percent of the wealth of the country, what is the significance of that fact?

8. Describe the Marxian doctrine on economic inequality.

9. Explain the essential differences between economic inequality under capitalism and economic inequality under feudalism.

10. What are the essential differences between a slave owner and a slave, on the one hand, and an employer and a poor, hungry wage earner, on the other,
   a. in terms of the relationship of the slave owner and employer to the cause of the worker's suffering
   b. in relationship to what is required to keep the worker at his job
   c. in relationship to the ability of the worker to exploit the best of the opportunities open to him

11. "Galbraith's views on the nature of freedom are out of *1984*. He claims that what we think of as constituting freedom is in fact slavery." Discuss.

12. How are lack of employment opportunities itself the result of the violation of freedom?

13. "The feudal nobility were in fact not landowners at all in the proper sense of the term. Their position was more analogous to that of hereditary commanders of military bases." Discuss.

14. In what ways does socialism, rather than capitalism, represent a revival of the conditions of feudal-type inequality?

15. Explain how the law of diminishing marginal utility is used to justify attempts to equalize wealth and income, e.g., by means of progressive taxes.

16. Explain the essential fallacies present in the use of diminishing marginal utility to justify the seizure of others' wealth or income.

17. On what basis can human beings be *selfishly* concerned with the well-being of the rest of mankind? What are the limits to such concern?

18. "The solution to the problem of massive, overwhelming poverty on a global scale, cannot be charity. On the contrary, it is *the science of economics,* which is truly *the humanitarian science.*" Discuss.

19. Explain once more what is meant by the doctrine

of external benefits or externalities.

20. "As an attempt to wring benefits for others from sacrificial victims, by means of force, the external-benefits doctrine destroys the basis of the existence of benefits to others being a value to an individual, and is thus a self-nullification." Discuss.

21. According to Paul Samuelson, "Abilities are much more equally distributed than are incomes . . . . While human traits seldom differ by more than a factor of 3, high incomes today are more than 100 times greater than the lowest." Explain why the "distribution" of income and wealth is more skewed than the normal curve and what is involved in the assumption that the "distribution" of wealth and income should follow the normal curve.

22. Explain what is meant by the equality-of-opportunity doctrine.

23. Explain what would have to be done to achieve the equality of opportunity.

24. What are opportunities? How abundant are they? Can they be created by individuals? If so, how?

25. How extensive must employment opportunities be, given man's limitless need for wealth and the fact that production is limited only the availability of labor?

26. What is meant by the freedom of opportunity?

27. How do violations of the freedom of opportunity explain the side-by-side existence of limitless employment opportunities and mass unemployment?

28. Explain how, on the basis of the principle that the individual creates his own opportunities, it is possible for a child born to poor parents ultimately to far outstrip in his accomplishments practically everyone else.

PART C. ECONOMIC COMPETITION

1. Explain the essential difference between economic competition and competition in the animal kingdom.

2. Explain why, in the nature of the case, there are no long-run losers as the result of economic competition.

3. What is the effect of competition among food growers and pharmaceutical manufacturers on the hungry and the sick?

4. Explain how individuals end up benefitting *even from the very improvements in production that initially cause them a "loss"*—for example, the case of the blacksmiths who were displaced by the automobile.

5. "The effect of competition is an upward ratcheting of standards accompanied by continual efforts to match and exceed the rising standards." Discuss.

6. Compare and contrast the short-run loss periods for unskilled workers, skilled workers, and those who lose invested fortunes as the result of economic competition.

7. Can anyone legitimately claim that economic competition reduces his standard of living?

8. In what way do those who denounce economic competition as the "law of the jungle" implicitly support the real law of the jungle?

9. Explain how economic competition, rather than being in conflict with economic security, is in fact an essential foundation of economic security.

10. Explain how the hardships of those who lose their jobs as the result of economic competition would be alleviated if there were more freedom of competition rather than less.

11. Compare and contrast the law of comparative advantage with the pyramid-of-ability principle. Show how both principles are integrated into a wider principle of the harmony of interests.

12. Does population growth represent a competitive conflict of interests? Discuss.

13. Does freedom of immigration represent a competitive conflict of interests?. Discuss.

14. Would the existence of a fixed quantity of money and a corresponding fixed volume of spending represent a situation in which there was a genuine conflict of interests? Discuss.

CHAPTER 10. MONOPOLY VERSUS FREEDOM OF COMPETITION

1. Contrast the rational and the anarchic concepts of freedom with respect to what constitutes a violation of freedom.

2. Present the contrasting interpretations of the meaning of "freedom of competition" that arise on the basis of the rational and the anarchic concepts of freedom.

3. Describe the kind of thing that constitutes a violation of the freedom of competition (a) according to anarchic concept of freedom of competition, (b) according to the rational concept of freedom.

4. High capital requirements
   a. constitute a violation of the freedom of competition
   b. exist as the result of the freedom of competition
   c. are the result of the fact that other producers in the industry, who are probably using large amounts of capital in their operations, are charging low prices; their low prices necessitate that to be profitable, one must have low costs of production, which, in turn, are achieved by the employment of large

sums of capital
d. all of the above
e. none of the above
f. (b) and (c) but not (a)

Discuss and justify your answer.

5. Explain what is meant by the political concept of monopoly.

6. Describe the relationship of the political concept of monopoly to the rational concept of freedom in general and the rational concept of the freedom of competition in particular.

7. Explain whether monopoly arises from within the economic system or is externally imposed, according to the political concept of monopoly.

8. How does the political concept of monopoly relate to the original meaning of monopoly as an exclusive grant of government privilege?

9. According to the original meaning of monopoly, the British East India Company was a monopoly because
a. it was the only company conducting trade between England and India
b. it was the only company legally allowed to conduct trade between England and India

10. List the leading present-day examples of monopoly according to the political concept.

11. Name some examples of exclusive government franchises.

12. Explain why exclusive government franchises constitute monopolies according to the political concept of monopoly.

13. What is essential to the monopoly constituted by exclusive government franchises is the fact that
a. there is only one seller
b. the market is reserved to the exclusive possession of that seller by means of the initiation of physical force

14. For many years, Alcoa was the only supplier of aluminum ingot in the United States.
a. Explain whether this fact made Alcoa a monopoly according to the political concept of monopoly.
b. Explain what made it possible for Alcoa to be the sole supplier.

15.
a. If the freedom of competition resulted in only one electric or gas company supplying a given area, would that make that company a monopoly according to the political concept of monopoly? Explain.
b. What would such a company have to do to achieve and maintain its position?

16. Are exclusive private franchises, such as McDonalds, monopolies according to the political concept? Explain.

17. Explain how licensing laws create monopolies according the political concept of monopoly.

18. Name some examples of monopolies created by licensing laws.

19. Explain how the fields controlled by licensing laws can be monopolies even though they contain numerous sellers—i.e., identify where the element of exclusivity is and what maintains it.

20. Describe the effects of licensing-law monopoly
a. on the quantity of services received by the buyers
b. on prices
c. on the incomes of the sellers
d. on the incomes of those excluded from the field

21. Describe the usual justifications that are given of licensing laws.

22. Explain the effect of licensing laws on lower-income consumers insofar as they (the licensing laws) serve to raise the minimum level of service that can be provided.

23. Describe the effects of liberalizing or abolishing medical licensing
a. on the ability of the poor to afford medical care
b. on the ability of everyone to afford the services of the more highly qualified medical practitioners

24. Explain how a free market would meet the legitimate objectives of the licensing laws.

25. What fundamental advantage would the absence of licensing offer to individuals that is not possible under licensing? Give examples.

26. "The existence of freedom carries with it the possibility that people will make wrong and even foolish choices. But there is no alternative. That possibility exists *with or without freedom.* The great advantage of freedom is that each individual has the right to make his own choices and need not be bound by the ignorance or stupidity of others." Discuss in relation to medical licensing.

27. In the light of the uniformity-of-profit principle, explain the effect on the cost of hospital stays if licensing requirements and other government regulations in connection with the establishment and operation of hospitals were abolished.

28. Contrast the meaning of "the right to medical care" in the light of the rational and anarchic concepts of freedom.

29. Explain how the present high cost of medical care is the result of the violation of the right to medical care understood in the light of the rational concept of freedom.

30. Explain why protective tariffs constitute monopoly legislation according the political concept of monopoly.

31. Explain how protective tariffs create monopolies even though many thousands of domestic producers may still compete with each other under them—i.e., identify the parties against whom the market is monop-

olized by protective tariffs.

32. Explain and illustrate how monopoly legislation can protect the less efficient many against the competition of the more efficient few, or even just one.

33. "Monopoly exists, and the freedom of competition is violated, not because there happens to be just one seller in a market, when all have the legal right to enter, but when there are millions in the market, and all *but one* are allowed to enter, with that one otherwise able and willing to enter. For example, a monopoly would exist in the automobile market even if it were comprised of thousands of small automobile companies and everyone in the world were allowed to enter it with the single exception of the original Henry Ford! Such exclusion of Ford would constitute a monopoly, in violation of the freedom of competition." Discuss.

34.
   a. Would such exclusion as described above constitute a monopoly even if Ford's entry were to mean that he would then become the sole seller of automobiles?
   b. Explain why, according the political concept of monopoly, Ford's becoming the sole seller would not constitute a monopoly.

35. Explain how minimum-wage and prounion legislation operate to monopolize markets in favor of more-skilled workers and to exclude the less able and the disadvantaged from the market. In your answer, be sure to explain how minimum-wage and prounion legislation
   a. prevent less-efficient workers from competing with more efficient workers in terms of labor cost per unit
   b. attract the competition of relatively more skilled workers to the field

36. Explain how prounion legislation operates against the interests of less skilled workers even insofar as it serves to raise the wages of relatively more-skilled categories of workers.

37. Explain how minimum-wage and prounion legislation create situations in which employers are free to indulge their personal prejudices in deciding which workers to employ.

38. Explain why minimum-wage and prounion legislation have had particularly harmful effects on blacks, especially teenagers, and have often resulted in lifelong unemployment and welfare dependency.

39.
   a. Enumerate the laws that serve to increase housing costs.
   b. Explain how such laws, coupled with high government-imposed minimum housing standards for health and safety, serve to cause homelessness.

40. Explain how government-imposed minimum housing standards on a local basis have the unintended effect of worsening the housing conditions of the poor elsewhere.

41. Explain why government-owned and government-subsidized enterprises represent monopolies according the political concept of monopoly.

42. Explain how public education represents monopolization of a major part of the education market against the competition of private education.

43. Compare and contrast public education and unregulated private education in terms of their potential to achieve improvements in the quality of education and safeguard against deterioration in the quality of education.

44. "The position of private education today, and that of education as a whole, is analogous to what the position of the automobile industry would be if the production of all the low- and medium-priced models were in the hands of the government, which subsidized their production to the point of giving these models away for nothing—indeed, of compelling every adult to accept one for nothing—while the privately owned portion of the automobile industry were confined to the production of very expensive models, and essentially prohibited from cutting its costs." Discuss.

45. Explain why, according the political concept of monopoly, the antitrust laws constitute promonopoly legislation—i.e., represent the reservation of markets to the exclusive possession of a limited group by means of forcibly excluding potential competitors.

46. Explain why socialism represents the most extreme form of monopoly.

47. Explain and illustrate how the effect of monopoly is often to enable high cost producers to survive, rather than securing exceptionally high profits for anyone.

48. Explain whether patents and copyrights constitute promonopoly legislation and, if not, why not.

49. Describe and explain the long-run effect of the abolition of patents and copyrights on prices.

50. Describe the essential foundation and consequences of monopoly according the political concept.

51. "It follows from the political concept of monopoly, that the program of the announced enemies of monopoly should not be, as it has been for many years, the government's growing control over big business or the breakup of big business. Rather, it should be the progressive elimination of government intervention into the economic system." Discuss.

52. What is meant by monopoly according to the economic concept of monopoly?

53. According to the economic concept of monopoly,
   a. where does monopoly originate?
   b. what is the government's relationship to monopoly?

54. "According to the economic concept of monopoly, the essential feature of monopoly is the 'oneness' of the seller, irrespective of how he has achieved his position." Discuss.

55. Explain how the economic concept of monopoly can be construed in such a way that it embraces hardly anything or almost everything,

56. Describe the extent to which monopoly was held to exist
   a. before the 1930s
   b. since the 1930s.

57. Explain the concepts of "oligopoly" and "monopolistic competition" and describe their role in broadening the perception of the prevalence of "monopoly."

58. Describe the extent to which full-bodied competition—viz., "pure–and–perfect competition" is now held to exist.

59. Name the two essential requirements for the existence of "pure–and–perfect competition."

60. Explain how the acceptance of the contemporary theory of the comparative extent of monopoly and competition has led to a rewriting of economic history to account for the fact that competition was traditionally considered to be the norm.

61. Explain how the fact that after the Civil War fewer producers remained in many branches of industry was nevertheless accompanied by an increase in the number of producers in actual competition with one another.

62. Describe the doctrine of the tendency toward the formation of a single giant firm controlling the entire economic system.

63. Explain the role of this doctrine in the further doctrine of the alleged inevitability of socialism.

64. Describe how, according to this doctrine, the last day of capitalism is supposed to differ from the first day of socialism.

65. Describe the influence of this doctrine in the beliefs of many antisocialists and in the enactment of the antitrust laws.

66. Explain how the alleged tendency toward the formation of a single giant firm contradicts the essential nature of the gains derived from the division of labor.

67. Explain why the only place that centralized control over all the means of production has been established is under socialism.

68. Explain why a combination of the resort to physical force and a spirit of self-sacrifice on the part of the regime is necessary to the continuation of the state's monopoly of the means of production under socialism.

69. "The experience of socialism confirms the fact that monopoly is a political phenomenon, not an economic phenomenon." Discuss.

70. Explain how the phenomenon of bad mergers confirms the fact that there is no tendency toward the formation of a single giant firm under capitalism.

71. Explain why the formation of conglomerates, containing separate divisions each with its own management, would not be a feasible means of overcoming the conflict between a megacombine and the essential gains from the division of labor.

72. Explain how similar considerations serve to frustrate the combination of firms even within the same industry.

73. Explain how successful mergers serve to provide the basis for the formation of new firms, if not in the industry where a given merger occurs, then in other industries.

74. Describe another, even more important factor that is operative in mergers being accompanied by the continued existence of numerous other firms, and which serves to keep the proportion of the total capital of the economic system in the hands of the merged firms from growing.

75. Describe how taxation and government regulation limit the formation and/or growth of new firms.

76. Describe how the tax laws have encouraged uneconomic mergers.

77. Explain how the absence of the prohibition of insider trading would promote the formation of new firms.

78. Explain the effects of insider trading
   a. on buyers, sellers, and holders of a stock when the insider trading represents buying with knowledge of favorable developments
   b. on buyers, sellers, and holders of a stock when the insider trading represents selling with knowledge of unfavorable developments

In both cases be sure to isolate the parties who might have grounds for complaint and appraise the justice of their claims.

79. "If the gains of the insiders, who know what they are doing, must be transferred to those who do not, the latter will not be able to keep those gains for very long. For they will have no basis on which to argue for the retention of their unearned, accidental gains from society as a whole. If knowledge is not an adequate basis for earning a profit that others do not earn, the mere accident of owning the right stock at the right time can hardly be such a basis." Discuss.

80. Describe the kinds of conditions that make for economically sound mergers. In your answer, by sure to explain why conditions for an economically sound merger can exist beyond the achievement of economies of scale.

81. Describe the major post–Civil War changes in transportation and transportation costs and how they gave a competitive advantage to large-scale manufacturing over small-scale manufacturing and thereby created the need for widespread mergers.

82. Explain the role of the trusts in effecting the mergers referred to in the preceding question. (In your answer, be sure to also explain the legal considerations

that led to the use of trusts in order to achieve mergers.)

83. In broad outline, describe what happened to output and prices, including real prices, in virtually every industry in the United States between 1870 and 1914.

84. Explain what would have happened to output and prices if the trusts had been a promonopoly development, as is usually believed.

85.

a. Describe how the 1911 Supreme Court decision that broke up Standard Oil acknowledged the improvements in quality and price that Standard Oil had achieved for the consumer.
b. Describe the Court's grounds for the breakup nonetheless.
c. Describe the extent to which presumably educated opinion, such as that found in history textbooks, newspaper editorials, and novels and plays, shares the Court's acknowledgement of the achievements of Standard Oil or rests on the belief that the Court based its decision on a diametrically opposite set of facts.

86. Explain what is meant by the predatory pricing doctrine.

87. Describe its influence in the appraisal of the achievements of big business.

88. Describe the conditions in which the attempt to practice predatory pricing would—totally contrary to what the doctrine takes for granted—serve to actually *increase* the price received by the intended target.

89.

a. Describe the condition that must be present in order for a firm practicing predatory pricing to be able to succeed in imposing a lower price on the intended target.
b. Describe the possible costs that achieving this condition can entail for the firm. What critical factor will determine the extent of these costs? How long can they last?

90. Describe the usually unrecognized but nonetheless extremely powerful interests that are created on behalf of the continued existence of the small competitor, if it is the case that as soon as he is driven out the large firm can sharply increase its price, while so long as he remains in business, the price is held below the level of his costs. Could this lead to attempts to subsidize the losses of the small competitor for the purpose of keeping the predator's price low? Discuss.

91. If it is the case that the large, predator firm will slash its price as soon as it is confronted with a small, competing firm, describe how people are placed in a position in which they can use that very knowledge to profit precisely by forming small competing firms against whom the predator will slash price.

92.

a. Explain why that to the extent that the predatory big and rich firm is larger in the same market, it must take the price cut and the resulting loss on a correspondingly larger volume than the small and poor firm.
b. Describe the conditions in which the small firm can be in a better position to withstand its relatively smaller losses than is the large firm.
c. Explain to what extent, if any, matters are fundamentally changed if the large firm has lower unit costs than the small firm—i.e., does this change the principle that its profit reduction is a multiple of the smaller firm's profit reduction to the extent that its volume in the same market is greater?

93.

a. Explain the distinction between operating costs, fixed costs, and total costs.
b. Explain why practicing predatory pricing would necessitate setting one's price below the target's *operating* costs, not his total costs, and then keeping them there for the life of his plant and equipment.

94. If the predator firm does not want to go to the expense implied in answer to the preceding question, what is its alternative?

95. Explain why neither sustaining losses or major profit reductions for years in order to drive out one's small competitors, nor buying out the small competitors at premium prices, can actually pay. (In your answer, be sure to describe the price that one would need to charge in order to recoup, versus the price that one must accept and could have had without attempting to practice predatory pricing.)

96. "The permanent, long-run price that the large firm can obtain is limited by the costs of production—the full costs—of potential new entrants, together, of course, with an allowance for the competitive rate of profit on their capital. These costs set an objective limit above which the price cannot be maintained in the absence of legal protection from competition—namely, that provided by monopoly according to the political concept. As a result, the large firm cannot in fact later on charge the premium price that is necessary to recoup the profits it must forgo or the additional expense it must incur." Discuss.

97. If the large firm must accept a price that is limited by outsiders' costs, describe the extent of its gains if it should succeed in capturing the business of its small competitors. Is it worth it to the large firm to pursue such limited gains?

98. Explain why it follows from the answer to the preceding question that more than one company in an industry is the normal case.

99. Explain what condition must be present to make it worthwhile for a large, low-cost firm that already does the bulk of an industry's business to cut its price below what is required to enable its smaller rivals to stay in business, if merely gaining their volume is not sufficient.

100. Even if the condition explained in answer to the preceding question is present, what effect would the possession of patent protection on the process or processes that gave the large firm its cost advantage probably have in deciding whether or not to go for 100 percent of the market?

101. Explain why in fact a small firm has a far greater incentive to price aggressively against a large firm, rather than the large firm against the small firm. Try to relate your answer to the case of Compaq versus IBM. @QUESTION = Compare and contrast the claims of predatory pricing made against the old Standard Oil Company with the present-day claims of "dumping" that are made against Japan. What is the same and what is different in the claims.

102. Explain why in the nature of the case, Japan's success in exporting cannot be attributed to selling below its costs nor to subsidies on the part of its government.

103. Explain why, despite widespread belief to the contrary, it is not reasonable to attribute Japan's economic success to guidance of its economy by its Ministry of International Trade and Industry.

104. Describe the kind of assumptions that make attribution of economic success to government interference seem plausible.

105. Explain what is meant by the chain-store variant of the predatory pricing doctrine and how it differs from the predatory pricing doctrine as that doctrine has been considered up to now.

106. Explain why the overwhelming bulk of the larger capital of a chain of stores, or other multi-market firm, is *irrelevant* to the size of the losses it might rationally be willing to sustain on a temporary basis in order to become the sole seller in a local market and thereafter forever reap a premium profit in that market. (In your answer, be sure to describe the kind of calculation that would have to be made to arrive a rational limit to such temporary losses.)

107. Explain the implication of your answer to the preceding question for the size of the firms that would be in a position to match even the largest chains in the ability to sustain temporary losses.

108. Explain the effect of losing any part of the capital one had calculated that it was reasonable to lose in an effort to secure a monopoly position in a local market, on one's ability to meet the competition of a newcomer who had made the same calculation but had not yet lost any of his capital.

109. Explain the implications of your answer to the preceding question for the ability of firms to practice such a policy successfully. (Be sure to include in your answer consideration of the need of any firm that practiced such a policy to recoup its losses by thereafter having to charge higher prices than those who had not practiced the policy would have to charge.)

110. Explain how selling under long-term contract can provide the small competitor of a large, would-be practitioner of predatory pricing automatic protection against such practice and can do so even while allowing customers to decide not to actually buy the quantities they have contracted for.

111. How does the kind of arrangement referred to in the preceding question make the predator finance the small firm's costs in order to gain its business?

112. While long-term contract pricing may often not be feasible at the level of retailers' customers, explain what kind of market factors operate to protect small retailers from being dislodged even by permanently lower prices charged by larger firms, and how this contributes to preventing the larger firms from raising their prices.

113. Describe the ways in which the implications of the predatory-pricing doctrine represent an inversion of economic history with respect to

a. the movement of real prices in retailing and elsewhere over the last 130 years or so, i.e., since the days of the general store, whale oil, and the local blacksmith shop

b. the basis of the growth of the chains and big business in general—i.e., was it greater efficiency and providing better products at lower costs of production, or the ability to succeed at price gouging?

114. Explain what a large firm bent on cutting off vital supplies to a small competitor (which is the doctrine of predation with respect to suppliers) would have to be able to do to succeed in cutting him off; that is, explain how many suppliers the small firm needs, how many the large firm must close off, and how much it has to offer each of them in comparison with what the small firm can presently offer or may be able to offer in the future.

115. Describe any similarity you see between your answer to the preceding question and the relationship of the losses or profit reduction of a large firm attempting to practice predatory pricing against a small firm in the same market.

116. Explain why the prospect of the large firm charging high prices in the event it succeeds in cutting off vital supplies to its small competitors should make suppliers allies of the small competitors.

117. Explain why if there existed only a small number of suppliers that the large firm needed to tie up in order to deny supplies to its smaller rival(s), that would not make matters easier for the large firm.

118.

a. Describe the story of the South Improvement Company and Standard Oil's alleged involvement in it.

b. Present an alternative hypothesis to explain the events of the story, assuming they actually occurred.

119. Explain and illustrate the concept of marginal revenue.

120. On the basis of the concept of marginal revenue, explain the claim that to the degree that a firm is large relative to the size of the market it serves, it is motivated to restrict its production to a quantity of product that is less than what in some sense it "should produce."

121. Explain why, given the elasticity of demand for the product of the industry, the smaller is a given firm relative to the industry as a whole, the more motivated it is alleged to be to expand its production and cut the price of the product.

122. "A large firm can be denounced both for monopolistically restricting supply if it does not produce the extra output that supposedly should be produced, and for being a monopolist if it does produce that extra output." Discuss.

123. Assume that the increment of output that supposedly should be produced is profitable in its own right; that is, is profitable when considered apart from the effect of its production on the price of the quantity that is already being produced. Explain why in such a case, a large firm that must experience the price reduction on its present quantity, does not have the alternative of deciding between a larger industry-wide quantity at a lower price and a smaller industry-wide quantity at a higher price, but only between whether *it* will produce the larger quantity at the lower price or a smaller quantity at the lower price while some other firm produces the additional quantity.

124. "Where competition is physically possible and is peaceful—that is, in which the same or a similar good is capable of being produced by others without violation of anyone's intellectual property rights—and is legally free, the decision of any seller or group of sellers to produce less, or not to produce at all, cannot lastingly establish a selling price that is above the cost of production, plus allowance for the going rate of profit, of potential competitors." Discuss.

125. "The cost of production of potential new entrants constitutes an objective given that limits one's price. One's only choice is to sell either a smaller volume at that cost-limited price or a larger volume at that cost-limited price or a still larger volume at a lower price. But one cannot get a higher price." Discuss.

126. "If one allows for the time that may be required for new firms to enter a field, one can say that irrespective of the elasticity or inelasticity of the demand for the product of an industry as a whole, *the elasticity of the demand for the product of any individual firm*, however large, *is virtually infinite if it charges a price above outsiders' costs plus allowance for the going rate of profit*." Discuss.

127. "Under the freedom of competition the elasticity of demand for the product of any individual company or group of companies at a price above outsiders' costs plus allowance for the going rate of profit, is determined by the sum of the elasticity of demand for the product of the industry as a whole *plus the elasticity of supply of competitors and potential competitors*." Discuss.

128. In the light of your answer to the preceding question, explain how it can be that while the demand curve facing the industry as a whole may be almost perfectly inelastic, or, indeed, actually be perfectly inelastic, as in the case of table salt, the demand curve facing any individual firm in the industry tends to be perfectly elastic at a price above outsiders' costs plus allowance for the going rate of profit.

129. Explain why legal freedom of entry is an essential foundation of competitive price determination and how its absence serves to make it possible for individual firms to set price on the basis of consideration of the industry's elasticity of demand, above the point of outsiders' costs plus an allowance for the going rate of profit.

130. Compare the role of cost of production and elasticity of demand in determining the prices normally charged for necessities and spare parts. In your answer, be sure to indicate how high prices would be in such cases if they were determined on the basis of a consideration of the industry's elasticity of demand.

131. Describe the role of formal or informal contractual agreements in making cost of production rather than the elasticity of demand the determinant of prices.

132. Explain how contractual agreements tying price to cost of production can contain a major element of variability to make them conform to changes in market conditions.

133. Explain how contractual agreements can serve to make *buyers* the major beneficiaries of any supply reductions and price increases that sellers might otherwise be motivated to bring about.

134. Explain why even if there were just one producer of table salt, it would probably not be possible for him even temporarily to take advantage of the inelasticity of demand for table salt by reducing his production and raising his price.

135. Explain why even though when the excise tax on cigarettes is increased, the price immediately rises and is accompanied by relatively little decline in the quantity of cigarettes demanded, it would not pay an individual tobacco company or combination of all the present tobacco companies taken together to attempt to raise price by the equivalent of an excise tax increase.

136. Describe the role of the potential competition which can take place between producers at different stages of the productive process in limiting price to outsiders' cost of production plus an allowance for the going rate of profit. Illustrate in terms both of the tobacco industry and the oil industry.

137. Compare and contrast the views of Ricardo and Böhm-Bawerk on the role of cost of production versus the (marginal) utility attached to goods by buyers, as the determinant of prices.

138. Explain why in cases in which cost of production rather than considerations of the elasticity of demand determines prices, there is no implication that cost of production can make anything *more valuable* than corresponds to its marginal utility, but only that it can make something *less valuable* than corresponds to its direct marginal utility.

139. Explain Böhm-Bawerk's contention both that it is correct to say that costs govern value and that in such cases marginal utility is what more fundamentally governs value, by virtue of governing the costs.

140. "The notion that cost of production has no significant explanatory role in economics does not come from Böhm-Bawerk and Wieser, but from Jevons." Discuss.

141. Explain in what respect Ricardo was incorrect in conceding that the price of vintage wines was determined by demand and supply rather than by cost of production.

142. "After devoting chapter after chapter to developing a theoretical analysis that is entirely dependent on the concept of marginal revenue, Samuelson and Nordhaus are surprised to find that it is largely irrelevant to the real world and that they have no theory to explain the actual facts of pricing." Discuss.

143. What are the advantages a firm derives from setting its price on the basis of
  a. its own cost of production if it can assume that its cost is no higher than its competitors' or potential competitors' costs?
  b. its competitors' or potential competitors' costs of production if its own cost of production is lower than theirs.

144. "Absence of knowledge of the connection between prices and costs, and the belief that the price of each and every product must be determined by the specific demand for and supply of the product—by its own independent marginal utility—is what has led contemporary economics (a) to the expectation that without the presence of a vast number of individually insignificant firms, sellers will be in a position to exploit the product's elasticity of demand, (b) to regard big business per se in a way that should be reserved for one or a few firms operating under monopolistic legal protection against competition, but not when operating under the freedom of competition, (c) in the last analysis, to find that its theory simply does not fit the facts and that it has no applicable theory." Discuss.

145. Explain why the adoption of lower-cost methods of production, even when protected by patents, soon serves to reduce prices somewhere—if not in the industry where introduced, then in another industry or industries.

146. Explain in what ways the prices of other goods serve to limit the price that it is profitable to charge for a good produced under patent or copyright protection.

147. Explain why the prices of patented or copyrighted products are typically set on the basis of cost of production, though with the addition of a substantially greater-than-usual profit margin.

148. Explain why it is generally a sound business policy to reinvest the proceeds of an extremely high profit margin and rate of profit in order to earn a larger amount of profit on the strength of a lower profit margin and rate of profit applied to a greater volume of sales and quantity of capital invested in the production of the good (or more advanced versions of the good).

149. Explain how the ability to practice price discrimination would make it possible to price life-saving patented drugs in a way that did not deprive the marginal buyers of their life's savings.

150.
  a. Explain the effect of today's methods of paying for medical care on the elasticity of demand for patented drugs and thus on the price that drug companies find it profitable to charge for them.
  b. Explain why it is difficult to practice price discrimination in the sale of patented drugs within the United States today.

151. Explain the potential role of pricing under long-term contract in connection with the feasibility of unregulated private ownership of the various utilities, such as electricity, water, and gas, telephone and sewage services, and the provision of bridges and tunnels.

152. Are privately owned fire-fighting services economically feasible? What would prevent their charging extremely high rates, especially in emergencies?

153. Are privately owned streets economically feasible? How could they be financed?

154.
  a. Explain what is meant by eminent domain.
  b. Explain the apparent dilemma eminent domain presents in connection with the principle of respect for individual rights.
  c. Explain what relatively simple steps would be necessary to eliminate most of the practical substance of this dilemma within a short period of time. (In connection with your answer, be sure to explain the basis of the very different reaction people are likely to have in response to a letter from the government telling them it wants to build a road through their property, and a letter from an oil company saying it would like to drill for oil on their property.)
  d. Explain how the need for eminent domain could probably be eliminated if, say, 50 or 75 years, were given for the expiration of that power.

155. Explain what is meant by a cartel.

156. Describe the effects that are widely expected to exist if cartels are not prohibited or at least regulated by the government.

157. Explain why, apart from the handful of cases such as diamonds, in which there are very few physical sources of supply, the only time cartels can suc-

ceed under capitalism is when they serve merely to reduce the extent of losses, i.e., raise a price from a point of more severe losses to a point of less severe losses or modest profits. (In your answer, be sure to describe the two problems that exist for a profitable cartel, that are likely to lead to its undoing, but which are not present in the case of a cartel that is not particularly profitable.)

158.
  a. Explain what limits the prices that the few successful cartels in mining can charge in a free economy.
  b. Explain why, in a free economy, such cartels are under continuous pressure to improve their methods of production and lower their costs and the real prices they charge.

159. "What is true of the price charged by a successful cartel is that at any given time it is higher than would be the case if the same known physical quantity of the good were found in widely scattered deposits. The effect of this higher price is to slow down the rate at which the limited known supplies are consumed. Thus, von Mises is correct in describing the higher prices charged by such cartels as tantamount to a form of conservation." Discuss.

160. "Cartels as an economic problem are the result of government intervention, and where they are formed or maintained on this basis, they represent part of the genuine and very serious problem of monopoly." Discuss. In your answer, deal with
  a. the case of the Imperial German cartels
  b. the case of present-day American agriculture
  c. the OPEC oil cartel

161. Explain in what way contemporary economics' doctrine of pure-and-perfect competition represents a trivialization of the economic concept of monopoly.

162. Describe the influence of the doctrine of pure-and-perfect competition on contemporary antitrust policy.

163. Compare and contrast pure-and-perfect competition with competition as it is normally understood, with respect to the subject of business rivalry.

164. Explain what is meant by "the tribal premise."

165. Explain the implications of the tribal premise for "society's" alleged rights in connection with private ownership of the means of production.

166. Describe the circumstances in which "society's" alleged right to 100 percent of every seller's inventory and to the benefit of 100 percent use of his plant and equipment is to be limited.

167. Explain what is meant by the rationing theory of prices.

168. Describe contemporary economics' view of costs.

169. Explain and illustrate what is meant by marginal cost and why contemporary economics considers it the only relevant cost from its perspective.

170. Explain why the concept of marginal cost normally excludes the cost of existing factories and machines.

171.
  a. Explain what is meant by scarcity prices.
  b. Describe what is meant by "supply" in the context of the pure-and-perfect-competition doctrine.
  c. Describe what is meant by "demand" in the context of the pure-and-perfect-competition doctrine.
  d. Explain why all prices, according to the collectivist, tribal view that underlies the pure-and-perfect-competition doctrine, should be set at whatever point is required to give the buyers the full supply in the above sense and to limit their demand to the size of the supply.

172. Explain why the pure-and-perfect-competition doctrine regards the equality of price with marginal cost as representing a social optimum.

173. Explain whether the "imperfect competitor"—viz., the "monopolist," the "oligopolist," or the "monopolistic competitor"—sets his price at the point of equality with marginal cost, and, if not, why not.

174. Illustrate the alleged sin of the "imperfect competitor" in terms of
  a. the example of the primitive fishing village whose fleet has a superabundant catch
  b. the earning of a royalty or profit by virtue of the use of an idea
  c. the earning of depreciation on existing plant and equipment whose services do not qualify as scarce

175. Explain why the earning of depreciation charges is held to be improper short of capacity operation of the plant and equipment in question.

176. Explain how the claim that depreciation cost should not be recovered until the services of the plant and equipment in question becomes scarce applies in cases of firms that possess capacity of different grades of efficiency.

177. Describe the similarity between the Ricardian land rent theory and the circumstances in which contemporary economics believes the recovery of fixed costs to be proper.

178. Describe what competition is needed to accomplish, according to contemporary economics, and how, in accordance with that objective, it defines pure-and-perfect competition.

179. Give an example that illustrates the satisfaction of the various requirements of pure-and-perfect competition.

180. Explain why such examples are rarely if ever given.

181.
  a. Explain contemporary economics' stress on the need for a large number of individually insignificant sellers as an essential condition of leading profit-seeking businessmen to drive price to equality with marginal cost.

b. Why would such a seller have an inducement to cut his price whenever it was greater than marginal cost, while a significant-sized seller would not?
c. Explain the role of product uniformity in making price cuts appear profitable in such circumstances.

182. Explain the implications of having to set prices equal to marginal costs for the prices charged by airlines and railroads whose planes or trains have empty seats; by movie theaters, baseball stadiums, and opera houses that have empty seats; by toll bridges not confronted with traffic heavy enough to cause jams.

183. How are Samuelson and Nordhaus prepared to deal with cases such as those just mentioned?

184. Explain what the effects would be on the amount of fixed capacity and the ability quickly to meet increases in demand if marginal-cost pricing were applied throughout the economic system.

185. "The standard of 'efficiency' used to justify the doctrine of marginal-cost pricing is one according to which the economy of Soviet Russia was more efficient than that of the United States, because even though there was less of everything in Soviet Russia than in the United States, what there was, was used more fully." Discuss.

186. "Ironically, what the pure-and-perfect-competition doctrine seeks is the abolition of competition among producers and its replacement with a competition among consumers resembling the conditions of the animal kingdom." Discuss.

187. Explain in what way the pure-and-perfect-competition doctrine is to the left of Marxism.

188. In what way do Harberger's findings concerning the meager negative impact of "monopoly" confirm the proposition that the pure-and-perfect-competition doctrine represents a denunciation of big business for refusing to sustain unnecessary losses.

189. Explain why the supporters of the pure-and-perfect-competition doctrine accuse capitalism of lacking price competition. What is their notion of price competition?

190. Explain why in fact, properly understood, price competition is an omnipresent feature of capitalism.

191. Explain how price competition exists even under conditions of inflation.

192. Compare and contrast actual price competition with the view of price competition held by contemporary economics.

193. Explain what it is that leads a competitor to cut his price in the knowledge that others will quickly match his cut.

194. Explain how it can be to the rational self-interest of a large firm to cut its price in response to a fall in demand, even though the industry demand curve is highly inelastic and other firms will quickly match its cut. (Hint: think of the height of its cost of operating presently idle capacity relative to the operating costs of less efficient rivals with active capacity.)

195. Explain how Alfred Marshall's doctrine of the "representative firm" serves to blind contemporary economists to the existence of situations of the kind described in the preceding question.

196. Explain what leads contemporary economics to the conclusion that the only possible gain for a large producer in cutting his price is the same gain that would exist if there were only one producer.

197. "The supporters of the pure-and-perfect-competition doctrine are aware of the fact that their doctrine is inapplicable to reality, but are not troubled by this fact." Discuss.

198.
a. Explain how cost of production operates to set many prices far below what they would be if they were determined on the basis of the direct marginal utility of the good concerned.
b. Explain how cost of production operates to establish prices at a point that is above what they would be if producers did in fact have to regard their plant and equipment and intellectual property as not deserving to command an allowance in the price of the product because their renditions of service were not scarce.
c. Explain how setting prices above what they would be if producers had to regard their plant and equipment and intellectual property as not deserving to command an allowance in the price of the product, serves in the long run to keep prices below what they would otherwise be and to progressively reduce real prices.

CHAPTER 11. THE DIVISION OF LABOR AND THE CONCEPT OF PRODUCTIVE ACTIVITY

PART A. THE ROLE OF MONEYMAKING IN PRODUCTIVE ACTIVITY

1. Describe the influence of the doctrine that productive activity is synonymous with manual labor—i.e., state who are the leading parties that accept the doctrine and what prominent activities of a capitalist society it implies are unproductive.

2. Explain how the doctrine is a heritage from the non–division-of-labor societies of old.

3. Explain why, in the context of a division-of-labor society, money making is an essential aspect of productive activity.

4. Explain why bank robbery does not qualify as productive activity even though it may bring in money to its practitioners.

5. Explain why in the context of a division-of-labor so-

ciety, activity that physically results in the production of a product represents consumption if it is not carried on for the purpose of earning money.

6. Define productive expenditure and consumption expenditure and explain and illustrate why the distinction between them is important.

7. Define capital goods and consumers' goods and explain what is the essential difference between them.

8. Explain why machines are not necessarily capital goods. Give examples of machines, tools, and implements that are everyday consumers' goods.

9. Explain why government is essentially a consumer and its expenditure, consumption expenditure.

10. Explain the difference between producers' labor and consumers' labor and why the distinction is important. What is the leading example of consumers' labor today?

11. Explain what is meant by producers' loans and consumers' loans and why the difference between them is important.

12. Explain why government borrowing represents consumer borrowing.

13. Describe an essential difference between government borrowing and private consumer borrowing.

14. Define capital and distinguish it from the broader concept of wealth.

15. Define investment.

16. Explain and illustrate how the concept of capital value differs from the concept of capital.

17. Explain the relationship between productive expenditure and capital value; explain why not all productive expenditure results in capital value.

18. Explain why expenditures for consumers' goods that are necessary to keep one alive and able to work do not qualify as productive expenditures. (In your answer, be sure to include an analysis of the effect of such a procedure on the calculation of a person's net income and thus of his gain from working.)

19. Explain whether consumption expenditures imposed by the earning of an income, such as a working mother's employment of a housekeeper, should be counted as a productive expenditure and a cost of earning the income.

20. Explain why consumption expenditures of a kind that save money, such as the purchase of a home in comparison with renting or the purchase of a washing machine in comparison with using a laundromat, should not be treated as productive expenditures on the grounds that they are income producing.

21. Should government expenditures that increase the capacity of the citizens to pay taxes be regarded as productive expenditures? Discuss.

22. Should workers employed in a charity's fund raising activities be regarded as producers' labor? Discuss.

23. Explain why expenditures for education should not normally be regarded as productive expenditures.

24. Explain why improvements in an individual's personal capacities, including his ability to earn an income, should not be regarded as capital or any kind of wealth.

25. Explain how the artificial capital constituted by the market value of slaves in a society that sanctions slavery operates to prevent the formation of genuine capital. Illustrate in terms of the economic differences between the North and South in the period before the Civil War.

26. What two criteria did Adam Smith use in distinguishing between productive and unproductive labor? Why is one of them misleading and irrelevant? Discuss.

27. Explain what is meant by the concept of imputed income and describe the contradictions to which it leads.

28. Explain what is meant by the doctrine of opportunity cost and the contradictions to which it leads.

29. Does the fallaciousness of the opportunity-cost doctrine imply that alternative uses for factors of production do not influence costs or that indeed they do, insofar as they influence the formation of the money prices of the factors of production.

PART B. THE PRODUCTIVE ROLE OF BUSINESSMEN AND CAPITALISTS

1. Describe the productive functions of businessmen and capitalists.

2. Explain how businessmen and capitalists (a) create division of labor, (b) coordinate the division of labor, and (c) improve the efficiency of the division of labor.

3. Describe the productive role of financial markets and financial institutions. Be sure to explain the effect both on the accumulation of capital and on the efficiency with which capital is used if financial markets and financial institutions did not exist.

4. Explain the productive role of the stock market in view of the fact that most of its activity does not center on the market in new issues and thus the direct channeling of funds from stock purchasers to business firms.

5. Explain how the existence of the division of labor is what makes retailing and wholesaling necessary.

6. Describe the productive role of retailing.

7. Describe the productive role of wholesaling.

8. Explain how it is possible, without any injustice being committed, for the retail price of a good to rise at the same time that the price paid to the farmers or manufacturers who physically make the good falls.

9. Explain how the existence of the division of labor is what makes advertising necessary.

10. Explain the productive role of advertising.

11. Explain why there is an important gain from advertising even in conditions in which its use leads to a rise in the price of the product being advertised.

12. Explain why there is a limit to any rise in price that advertising might ever cause.

13. Explain why normally advertising serves to reduce prices.

14. Explain how advertising serves to promote the introduction of new and improved products. In your answer, be sure to explain advertising's effect on the extent to which it pays to engage in research and development.

15. Explain in what way the expenditure for advertising is comparable to a seller's posting a bond with the public.

16. Explain why advertising does not dictate what people consume.

17. Explain the statement that advertising pays only when it is for products that people will like when they try them.

PART C. BUSINESSMEN AND CAPITALISTS: CLASSICAL ECONOMICS VERSUS THE MARXIAN EXPLOITATION THEORY

1. Describe the essential claim of the Marxian exploitation theory.

2. Name and briefly describe two leading doctrines of classical economics that are closely associated with the exploitation theory.

3. Briefly describe how the abandonment of classical economics in the late 19th century led to the promulgation of major anticapitalistic doctrines in the 20th century.

4. Explain why Adam Smith can properly be called the father of the Marxian exploitation theory.

5. Describe and illustrate Smith's confusion between labor and wage earning. (Quote him on the subject.)

6. Explain why Smith denies that profits could be an income attributable to the labor of those who make profits.

7. Name some everyday cases in which profits obviously are an income attributable to the performance of labor on the part of those who make them, and explain how the doctrine of "opportunity cost" serves to obliterate this fact.

8. Describe conceptual framework of the exploitation theory, as presented by Adam Smith. In your answer, be sure to explain Smith's "primacy-of-wages doctrine" and what that doctrine implies about the status of profits and the effect on the income of wage earners of the coming of capitalism and capitalists.

9. Explain how Adam Smith viewed the effect of private ownership of land on the incomes of wage earners.

10. On the basis of what you have learned earlier in this chapter, and in Chapters 6 and 9, explain the actual effect of the activities of businessmen and capitalists and private ownership of land on the real incomes of wage earners.

11. Compare and contrast Smith's view of an alleged "early and rude state of society" and the alleged effects of the coming of capitalism and capitalists with Marx's *C–M–C* and *M–C—M'* sequences.

12. Explain why *profits*, rather than wages, are the original and primary form of income.

13. Explain why businessmen and capitalists are not responsible for the coming into existence of the phenomenon of profit, but rather for the coming into existence and subsequent increase in the relative size of the phenomena of productive expenditure, wages, and costs, and for the reduction in the proportion of income that is profit.

14. Explain what is meant by the "primacy of profit" as opposed to the "primacy of wages."

15. Explain how, while important passages in Adam Smith's *The Wealth of Nations* support the primacy-of-wages doctrine, the doctrine of John Stuart Mill that "demand for commodities is not demand for labor" opposes it.

16. "Ricardo's doctrine that profits fall as wages rise and rise as wages fall pertains to *nominal* profits and wages in the context of an *invariable money,* and is perfectly consistent with real wages and real profits rising together, as Ricardo's own example clearly demonstrates." Discuss.

17. Explain how, when taken in conjunction with J. S. Mill's proposition that "demand for commodities is not demand for labor," Ricardo's doctrine that profits fall as wages rise and rise as wages fall actually supports the primacy-of-profit doctrine and the harmony of interests of wage earners and capitalists, rather than class warfare.

18. Explain how precisely the conditions of Adam Smith's "early and rude state of society" and Marx's "simple circulation" support the proposition that profit is an income due to the performance of labor.

19. Explain how under the more complex conditions of modern society and of Marx's "capitalistic circulation" profit continues to be a labor income, indeed, the income of the most important workers.

20. Compare the underlying standard of attribution used in your answer to the preceding question with

that normally employed in fields outside of economic activity, such as history.

21. Explain how the proposition that profits are a labor income is consistent with their variation with the size of the capital invested.

22. Explain how using their variation with the size of the capital invested to deny the attribution of profits to the labor of businessmen and capitalists implies that hardly any production can be attributed to labor in any form and thus contradicts Adam Smith's proposition that labor is the source of all wealth.

23. Explain the implications of the primacy-of-profit doctrine and the application of the normal principle of attribution to the economic realm, for the doctrine of "labor's right to the whole produce." When is this right satisfied under capitalism?

24. Explain the implications of the primacy-of-profit doctrine and the normal principle of attribution, for the treatment of the subject of "passive" recipients of dividends and interest. If the receipt of these incomes represented an exploitation of labor, be sure to explain who the exploited parties would be and what important groups the category of "exploiters" would include.

25. Explain why in fact there is no genuine exploitation in the case described in the preceding question and how the so-called passive incomes can in fact be the result of the application of potentially limitless amounts of labor.

26. Explain why the magnitude of income requiring no labor of any kind in order to be earned would be extremely small under laissez faire capitalism and how government intervention makes such income economically significant.

27. Explain whether Böhm-Bawerk, who is regarded as the leading critic of the exploitation theory, supports the primacy-of-profit doctrine or the primacy-of-wages doctrine.

28. Compare and contrast the labor theory of value held by the classical economists with the labor theory of value held by Marx. In your answer, be sure to deal with the differences between the two with respect to the role of (a) scarcity, (b) the time factor, (c) the rate of profit, (d) differences in wage rates between countries and occupations.

29. Explain how the labor theory of value held by the classical economists can be harmonized with recognition of the productive role of businessmen and capitalists.

30. Explain what is meant by the "iron law of wages."

31. Compare and contrast the version of the iron law of wages propounded by the classical economists with the version propounded by Marx with respect to (a) the cause of the alleged tendency of real wages toward minimum subsistence, (b) the closeness of the alleged connection, and (c) the possibility of escaping the alleged connection altogether.

32. Explain why the "iron law of wages," as propounded by the classical economists, could seem reasonable in the early 19th century, when Ricardo wrote.

33. Describe the revisions that must be made in classical economics in order "to transform it from a source of support for the exploitation theory into a source of complete and total opposition to the exploitation theory.

CHAPTER 12. MONEY AND SPENDING

The Quantity Theory of Money

1. What does the quantity theory of money claim?

2. State the quantity theory of money in terms of an algebraic formula. Explain the meaning of each of the terms of the formula.

3. Illustrate the quantity theory formula in terms of specific assumptions about the size of its various terms.

4. How large is the M_1 money supply currently? How much of it represents currency and coin and how much of it represents checking deposits?

5. Estimate the current size of the M_1 money supply after allowing for additions resulting from the existence of "sweep accounts" and from the fact that a growing proportion of money market mutual funds has become indistinguishable from checking accounts. (The Federal Reserve Bank of St. Louis provides estimates on the size and growth of sweep accounts since they became significant after the end of 1993. The *Federal Reserve Bulletin* regularly reports the size of money market mutual funds. Varying assumptions may be made about the extent to which these funds have become the full equivalent of checking deposits since the end of 1993. Attempt to form an estimate on the basis of the best further information you can obtain about this subject.)

6. How large is gross domestic product (GDP), formly gross national product, (GNP) at the present time?

7. To what extent does GDP represent consumer spending?

8. Why should government spending be counted as consumer spending?

9. Why should expenditures for owner-occupied housing be counted as consumer spending?

10. How large is income velocity (or approximately, consumption velocity) at the present time?

11. Describe two other measures of velocity.

12. Describe how an increase in the quantity of money operates to increase the volume of spending in the economic system.

13. Explain the essential difference between the factors determining the increase in the quantity of a gold

money and that of an irredeemable (i.e., fiat) paper money.

14. Explain rising prices on the basis of an increasing quantity of money.

15. Present the preceding explanation in terms of formulas both for the volume of consumer demand spending and the general consumer price level.

16. Explain the meaning of demand and supply as used in the price level formula.

17. Assume that over a decade the quantity of money and volume of spending double, while production and supply increase by 50 percent. How great is the percentage rise in the general consumer price level?

18. The price level formula shows demand as a numerator and supply as a denominator. In the light of this formula can you think of any way in which the average price at which goods are sold could rise without the demand rising or the supply falling?

19. Explain why it is far more likely for prices to rise under a system of fiat paper money than under a system of commodity (i.e. gold or gold and silver) money.

20. Explain why gold and silver moneys were often accompanied by long periods of *falling* prices, as in the generation preceding the discovery of the California gold fields and the generation from 1873–1896.

Origin and Evolution of Money and the Contemporary Monetary System

1. Describe the essential condition that must be present for a barter exchange to take place and how in the absence of this condition some of our more intelligent ancestors began to resort to indirect exchanges.

2. What goods have served as media of exchange in the course of history?

3. Describe how a medium of exchange evolves into money.

4. Describe how for a time cigarettes developed into a kind of quasi-money in some parts of Europe after World War II. Explain how this phenomenon led nonsmokers to become eager to accept cigarettes in exchange for their goods and smokers not to smoke.

5. Explain why, historically, gold and silver in particular came to be money as civilization developed.

6. Describe how the process of a medium of exchange developing into money is cumulative and self-reinforcing.

7. "The precious metals came to be money because they are the most suitable commodities for most people to save." Discuss.

8. Explain how the growing use of gold and silver as media of exchange favored their use as a medium in which to write contracts and state debts and how this further encouraged their use as media of exchange and thus promoted their development into money.

9. Over what period of time did gold and silver coin serve as money in the Western world?

10. Describe the process by which paper currency and checkbook money came into existence.

11. Could paper money have come into existence without a preexisting commodity money to which it was considered a secure claim payable on demand?

12. Describe the critical role played by the National Bank Act of 1863 in fostering the use of paper money in the United States in place of gold coin.

13. The great bulk of the American people's gold came into the government's hands
   a. in World War I, as the result of a wartime amendment to the Federal Reserve Act of 1913
   b. in 1933, when the New Deal ordered all privately held monetary gold to be turned into the Federal government

14. What did the Federal Reserve's possession of the gold previously held by the private banking system make possible?

15. Why did virtually everyone continue to accept dollars after 1933, even though they were no longer redeemable in gold?

16. Explain why even though the law required the Federal Reserve to hold substantial gold reserves against the dollars it created, for many years this requirement did not impose an effective limit on the Fed's ability to increase the supply of dollars.

17. Describe the process by which the excess gold reserves of the Fed were gradually eliminated and what happened as their exhaustion threatened.

18. Explain why abandonment of external convertibility of the dollar at the rate of $35 per ounce was inevitable, given the rate at which the U.S. government wanted to increase the supply of dollars.

19. Describe what has happened to the price of gold since 1971, when the U.S. government abandoned the last vestige of the policy of redeeming dollars at the rate of $35 per ounce.

20. Describe the legal status of gold ownership by American citizens from 1933 to the present.

21. Explain the potential that is created for a spontaneous remonetization of gold under conditions of substantial inflation. Explain how this potential would be greatly increased if it were legal for businessmen to discriminate between precious metal coins and paper currency of the same face value.

22. What is meant by "fiduciary media"?

23. What, in contrast, is meant by standard money?

24. What is standard money under a gold standard? What is standard money today?

25. What is meant by the "monetary base"?

26. What is the relationship of standard money to the monetary base?

27. "Fiduciary media" represent claims to debt that cir-

culate as money." Disuss.

28. What is the present magnitude of fiduciary media in the United States? What portion of the present money supply is this?

29. Describe the process by which fiduciary media come into existence.

30. "An alternative way of viewing fiduciary media is that of the fractional-reserve principle." Explain.

31. Explain why the opposite system to fiduciary media is the 100-percent-reserve system.

32. Describe the relative roles of standard money and debt as backing for paper currency and checking deposits under the 100-percent and fractional-reserve systems.

33. "The 100-percent-reserve principle applies only to checking deposits and banknotes, not to savings deposits or time deposits." Explain.

34. Describe how fractional reserve banking possesses a *deflationary* potential that, once unleashed, tends to be self-reinforcing and cumulative, ultimately capable of wiping out all fiduciary media.

35. Explain the applicability of the forces described in answer to the preceding question to the 1929 depression.

36. What prevents the deflationary potential of fractional reserve banking from being unleashed today? What does this portend for inflation?

37. Explain how a 100-percent-reserve monetary system would make the money supply absolutely independent of the failure of any debtors and thus make sudden, drastic reductions in the money supply virtually impossible.

38. Describe the factors that would greatly limit the creation of fiduciary media in a banking system that was free of government interference.

39. Describe, in contrast, the various ways in which government policy has promoted fractional reserve banking over the course of many years.

40. Short of prohibiting fiduciary media, what policy could the government follow that would entail simply removing all support it gives to their existence? Is there anything of relevance to such a policy to be found in President Jackson's specie circular?

41. What is meant by the Federal Reserve's "open-market operation"?

42. What is the role of the open-market operation in increasing the quantity of money?

43. What is the connection between the open-market operation and government budget deficits?

The Quantity of Money and the Demand for Money

1. Explain what is meant by "the demand for money" and its relationship to the velocity of circulation of money.

2. Explain the relationship between the demand for money and the security of property and why this relationship is very different under a commodity money system (i.e., a gold money) and fiat paper money.

3. Explain the relationship between the demand for money (velocity) and the development of financial markets and financial institutions.

4. Explain the effect on the demand for money (velocity) of improvements in transportation and the development of clearing houses.

5. "In the context of an economic system with developed financial institutions and financial markets, saving operates to *raise* the velocity of circulation of money." Present two reasons for this conclusion and describe how it contrasts with the view that saving is hoarding.

6. "In the conditions in which the velocity of circulation of a gold money rises, there is unlikely to be any fall in the purchasing power of gold as a result." Explain why not. (Is the velocity that rises in connection with economic development likely to be mainly income velocity.)

7. Describe each of the four reasons why the more rapidly the quantity of money increases, the less is the demand for money likely to be and thus the greater is the (income or consumption) velocity of circulation likely to be.

8. Explain the connection between increases in the quantity of money and the rate of interest, both in the short run and in the long run.

9. "To avoid rapid destruction of the monetary system, there is no practical alternative but to allow the rate of interest to follow the rate of profit on up as the quantity of money increases." Discuss.

10. "Interest is the price of money. Thus, the larger the money supply, the lower must be the rate of interest." Discuss.

11. What is a more precise description of interest than the "price of money," and which is consistent with the rate of interest being higher as the result of more rapid increases in the quantity of money?

12. Explain how higher interest rates make it worthwhile to lend out smaller sums of money for shorter periods of time, sums which it otherwise would not have paid to lend out.

13. Explain why, despite the relationship referred to in the preceding question, a reduction in the rate of profit and interest that might result from a higher rate of saving should *not* be presumed to increase the demand for money and thus reduce the velocity of money.

14. Explain the changes in the velocity of circulation of money in the period 1929–1945 in the light of the relationship between velocity and changes in the quantity of money.

15. Explain the changes in the velocity of circulation of money in the period 1946–1981 in the light of the

relationship between velocity and changes in the quantity of money.

16. Explain the changes in the velocity of circulation of money in the period 1981 to the present in the light of the relationship between velocity and changes in the quantity of money.

17. "The present monetary situation is highly unstable, possessing as it does the potential both for major inflation and for major deflation." Discuss.

18. Explain why the deadly alternative referred to in the preceding question would not exist if the policy of inflation had not been resorted to in the first place.

The Demand for Money: A Critique of the "Balance of Payments" Doctrine

1. Explain what is meant by the "balance of trade."

2. Explain what is meant by the "balance of payments."

3. Explain how these doctrines imply international economic conflict.

4. Which school of economists first propounded these doctrines?

5. Explain why from the perspective of economic history and the history of economic thought, the concepts of the balance of trade and the balance of payments can be taken as interchangeable.

6. Describe the historical context in which the doctrines originated and the original, essentially military objective which a "favorable" balance was supposed to achieve.

7. Describe the wider, economic objectives that a "favorable" balance was supposed to achieve.

8. "On the Mercantilist view of things, in the absence of government intervention to secure a favorable balance, the balance of trade (payments) was determined on an essentially accidental basis." Discuss.

9. "On the mercantilist view of things, imports had the potential of completely draining a country of its money supply." Discuss.

10. "Mercantilism has a very contemporary ring to it in terms of the economic objectives it is thought necessary for governments to promote." Elaborate.

11. "Mercantilism's treatment of the balance of trade (payments) as being the fortuitous outcome of the unrelated actions of individuals is also shared by most contemporary writers and commentators on the subject." Illustrate.

12. "Concern with an unfavorable balance of trade or payments under a gold standard may have some plausibility, but under the conditions of a fiat paper money it makes no sense whatever." Discuss.

13. "To some extent the position of the dollar as an international money entails some actual loss of dollars to abroad each year, but such loss, for from being a proper source of worry, simply represents a modest lessening of the degree of domestic inflation of the money supply." Discuss.

14. "The far greater part of what is recorded as an unfavorable balance of payments does not in fact represent an actual outflow of money, but an increase in short-term foreign lending to the citizens of the country, or to its government. These are developments which are actually favorable from the point of view of economic well-being." Explain.

15. "The various items in the accounts are not independent, but rather are mutually interconnected. For example, the so-called unfavorable balance of trade (the excess of imports over exports) that the United States has experienced in recent years is precisely the result of the excess of receipts by the United States over outlays in the vital area of lending and investing." Explain why it is in the very nature of foreign investment that it be accompanied by a so-called unfavorable balance of trade in the country receiving the investment.

16. "The purchase of imports does not represent any significant carrying out of money from the United States or any reduction in total, overall spending for goods and services in the United States. On the contrary, the imports represent new and additional wealth brought into the United States, where they are added to the supply of domestically produced goods and made available for purchase by the same total expenditure of money that would otherwise take place." Discuss.

17. "The rise in the foreign exchange value of a country's money that foreign investment in the country causes not only does not cause unemployment in that country, but actually tends to be accompanied by *less* unemployment." Explain.

18. "The prohibition or forced reduction of auto and steel imports would reduce unemployment in those industries but, in the absence of wage rate reductions, increase unemployment in the rest of the economic system." Explain.

19. Describe the unfavorable results likely to accompany the reduction or elimination of foreign investment and the excess of imports over exports that is the accompaniment of net foreign investment.

20. "What is called a favorable balance of trade can in fact be fully as much unfavorable as an allegedly unfavorable one is favorable." Explain.

21. Explain how foreign investment brings about an excess of imports over exports in the country receiving the investment under the conditions of an international gold standard.

22. Explain the principle governing the distribution of the world's money supply among the various individual countries under an international gold standard.

23. What is the implication of the principle cited in an-

swer to the preceding question for the balance of payments of a country whose economic system grows (declines) relative to that of the rest of the world?

24. Explain the effect of the presence or absence of gold mines on a country's balance of payments under an international gold standard, namely, why a country with extensive gold mines would most likely experience an "unfavorable" balance of payments, while a country without them would most likely experience a "favorable" balance of payments.

25. "Other things being equal, under an international gold standard, *the balance of trade and payments of all countries always tends toward balance.*" Explain why.

26. Explain how under an international gold standard, labor union activities operate to reduce a country's share of the world's money supply in comparison with what it would otherwise be.

27. Explain the effect of labor union activities on the height of money wage rates that can accompany full employment in a country that operates under an international gold standard.

28. Explain how the growth rate of a country's economy relative to that of the rest of the world operates to determine that country's share of the world's money supply under a system of fiat moneys.

29. Explain how under an international gold standard, the creation of fiduciary media in any one country operates to cause a drain of gold from that country.

30. "What explains an 'unfavorable' balance of payments in the sense of an actual outflow of money from a country is that the citizens of the country have an insufficient demand for that money to keep it in the country. In such circumstances it is futile to try to do so by blocking this or that category of imports or encouraging this or that category of exports." Explain.

31. "When the citizens of a country do have a demand for its existing quantity of money, no amount of outlays to abroad will for very long deprive them of any part of that quantity of money." Explain.

32. "Imagine that a new foreign aid bill is passed [in the U.S.] and, as part of it, an army of tax collectors is dispatched into the streets to seize money from every passerby and from every shopkeeper and businessman. The money, we can imagine, is then loaded into armored cars, rushed to nearby airports, and then flown to various foreign capitals." Will this foreign aid be at the expense of the cash holdings of the American people? Or will its effect very soon be a combination of decreased American imports and increased American exports and borrowings from abroad until American cash holdings are restored to approximately their former level?

33. In the light of your answer to the preceding question, discuss the observation of Adam Smith that "the attention of government never was so unnecessarily employed, as when directed to watch over the preservation or increase of the quantity of money in any country."

34. "What needs to be understood in connection with the balance of trade and payments viewed as source of changes in the quantity of money in a country is that the change in the stock of money in people's pockets, like the change in the stock of food in their refrigerators, is fully within their control and that their decisions about changes in the stock determine the relationship between the receipts and outlays, not that the relationship between the receipts and outlays determines the change in the stock." Discuss.

35. In the light of the analysis of the balance of trade/payments doctrine, explain how in a free market unilateral tariff reduction by one country and a resulting surge in its imports would soon be followed by a diminution of the increase in its imports and an increase in its exports.

36. Explain what the lasting advantage of the tariff reduction would be.

37. Explain why an essential requirement of being able to adapt to the consequences of a temporary outflow of money is the absence of labor legislation.

38. In the light of the analysis of the balance of trade/payments doctrine, explain what would happen if one country pursued a policy of free trade, while all other countries absolutely prohibited the importation of its goods.

Invariable Money

1. "Changes in prices can reflect changes taking place on the side of money as well as changes taking place on the side of goods. This is certainly the case whenever there is inflation or deflation." Discuss.

2. "The variability of the value of money coming from the side of money applies even to a pure gold or silver standard—that is, to a 100-percent-reserve gold or silver standard." Explain.

3. "In order for a money to serve as an *invariable standard of value,* it would have to be such that changes in prices would reflect exclusively changes operating on the side of goods, not money." Explain.

4. What did Ricardo believe would be necessary in order for gold to serve as an invariable standard of value?

5. What would be necessary for gold to be an invariable standard of value according to *Capitalism?*

6. Under such an invariable standard of value, explain what all changes in the general price level would reflect.

7. What would be the relationship between supply changes and price level changes under such an invariable standard of value?

8. What would be the elasticity of aggregate demand under such an invariable standard of value?

9. At what level would price changes reflect demand changes under such an invariable standard of value?

10. What is Hazlitt's attitude, at least implicitly, toward an invariable money?

11. Does the concept of invariable money imply that every measure of velocity must remain unchanged, or only velocity in relation to the demand for products?

12. In what way does use of the concept of invariable money as a tool of analysis represent the adoption of a procedure analogous to that of mechanics? Explain.

13. In what way is the assumption of an invariable money necessarily made, at least implicitly, by everyone who thinks about economic phenomena?

14. Explain how the concept of invariable money and recognition of the fact that money is not of invariable value sheds light on the respective roles of a system of fiat paper money and the businessman's profit motive in the causation of the rising prices we see almost all around us.

15. Describe the uses that will be made of the concept of invariable money in the chapters to follow.

CHAPTER 13. PRODUCTIONISM, SAY'S LAW, AND UNEMPLOYMENT

PART A. PRODUCTIONISM

1. Define the terms "productionism" and "consumptionism."

2. Describe various other leading economic doctrines with which productionism is closely associated.

3. Explain a leading philosophic basis for consumptionism that has become increasingly more influential in recent decades.

4. Explain how businessmen are often led to accept a consumptionist view of things on the basis of misinterpreting their experience.

5. Illustrate in contemporary terms the proposition of Adam Smith that "the desire of food is limited in every man by the narrow capacity of the human stomach; but the desire of the conveniences and ornaments of building, dress, equipage and household furniture seems to have no limit or certain boundary."

6. In what special sense can one legitimately say that a lack of desire for wealth constitutes an economic problem?

7. What kind of philosophical convictions must be present to induce people to desire additional wealth strongly enough to go out and actually produce it?

8. What is the fundamental basis in human nature for the desire for goods outstripping the willingness and ability to produce goods? Why does this relationship continue no matter what the advances in the ability to produce?

9. What is the fundamental basis in human nature for man's *need* for goods having no limit?

10. Explain why there is an inherent, ineradicable scarcity of human labor.

11. Illustrate the scarcity of labor in relation both to the goods we would almost all like to have and the personal services we would like to have.

12. Explain the proposition that we could work ourselves into the hospital from exhaustion long before we could produce all the goods we would like to have.

13. On the basis of consumptionism, explain why the adoption of labor-saving machinery is held to be a cause of unemployment. Illustrate your answer with the use of diagrams.

14. Explain why, on the basis of consumptionism, it is often held that there is only a fixed stock of work to be done in the world and that it is necessary to "make work." Give some examples of "making work."

15. How does the notion of a limited demand for goods lead to the belief that there is an inherent conflict among groups for limited employment opportunities?

16. How does the notion of a limited demand for goods lead to the belief that war is a source of prosperity? Illustrate your answer with the use of diagrams.

17. How does the notion of a limited demand for goods lead to the belief that the presence of great wealth in a country is a liability, and that its absence is an asset?

18. How does the notion of a limited demand for goods lead to the belief that government spending is a source of prosperity?

19. What is the actual effect of government spending on employment and prosperity?

20. Explain how the notion of a limited demand for goods leads to the belief that increases in population are a source of prosperity. Explain why the ideal role that the larger population should play, according to this view of things, is that of consumers, not producers.

21. Explain the actual relationship between increases in population and aggregate demand.

22. How does the notion of a limited demand for goods lead to the belief that a country can gain from following a policy of imperialism?

23. How does the notion of a limited demand for goods lead to the belief that the gain from foreign trade is in exporting, not importing?

24. Why does consumptionism imply that advertising is inherently fraudulent?

25. What is the actual relationship between advertising and aggregate demand?

26. How does the notion that falling prices are deflation represent support for consumptionism?

27. Compare and contrast the productionist and consumptionist views on the economic value of technological progress in relation to capital accumulation.

28. Describe the absurdities of the doctrine of secular stagnation with respect to the role of technological progress in relation to capital accumulation.

29. Explain what is meant by the consumptionist's dilemma in connection with the consequences of technological progress?

30. Explain how consumptionism presents parasitism as a source of benefit to its victims.

31. How has acceptance of the consumptionist premise led serious people to support socialism?

32. In the light of his views on the economic effects of war and pyramid building, explain whether you would classify Keynes as a productionist or as a consumptionist.

PART B. SAY'S (JAMES MILL'S) LAW

1. Explain the distinction between monetary demand and real demand and in what circumstances a smaller monetary demand can constitute a larger real demand.

2. Explain how increases in production and supply create real demand.

3. Explain why *only* increases in production and supply create real demand, i.e., why increases in monetary demand are not sufficient to create additional real demand, and why increases in production and supply are both necessary and sufficient to create more real demand.

4. Explain the importance of keeping in mind that Say's Law refers to *aggregate* real demand.

5. Demonstrate how even in the case of an inelastic industry demand for an individual good, such as potatoes, in which an increase in supply reduces the volume of goods received by the producers in the industry concerned, there is nonetheless an increase in aggregate real demand that is precisely equivalent to the increase in aggregate supply in the economy as a whole.

6. Show why the losses of the potato growers are more than offset by the gains of producers in the rest of the economy when the supply of potatoes increases.

7. Explain how even though an industry as a whole may lose when its supply increases, the individual producers within the industry who are responsible for the increase in supply can nevertheless gain.

8. Explain how the potato growers, who initially lose as the result of the doubling of the supply of potatoes, are able to gain from the improvement in the ability to produce potatoes.

9. Describe the process of adjustment, which ends with those who remain in potato growing coming out ahead, the ex-potato growers coming out ahead, and those who were non-potato growers from the beginning coming out ahead.

10. Explain in what sense the initial increase in the supply of potatoes represents an *underproduction* of goods other than potatoes.

11. Explain why if the production of *everything*—from matches and salt to swimming pools and yachts—suddenly doubled overnight, as much underproduction would exist as overproduction.

12. "'Overproduction' is always partial and relative, never general and absolute." Discuss.

13. Explain how the economic system benefits from an increase in the ability to produce goods with which people may already be sated, such as table salt.

14. Explain how the concentration of an increase in the ability to produce in the particular industry in which it originates often represents a less efficient use of the improvement than is possible if that particular industry expands less than the full amount by which the improvement would allow it to expand, and allows other industries to expand instead.

15. Explain why what appears as an overproduction in an individual industry would often cease to appear as an overproduction if other industries could increase their production sufficiently.

16. Explain how the adoption of improvements in the ability to produce can be accompanied by gains to all who adopt them, while the accompanying losses to the industry as a whole are suffered by the producers who fail to adopt the improvements.

17. Explain what is meant by the fallacy of composition.

18. Explain in what sense the belief that a fall in general business profitability is the result of too much production reflects the fallacy of composition.

19. Explain why the general profitability of business is independent of the level of physical production of ordinary goods, that is, of goods other than the monetary commodities gold and silver on a precious metal standard. Explain why, at the same time, the profitability of an individual industry is not independent of its level of physical production.

20. What does the general profitability of business in the aggregate basically depend on?

21. Explain why depressions are not the result of any kind of excess of production, but of a monetary contraction.

22. Explain how the fallacy of composition is present in the belief that what is necessary for the existence of more demand is greater need.

PART C. UNEMPLOYMENT

1. Explain why unemployment exists despite the fact that there is an inherent, ineradicable scarcity of labor and despite the fact that all that is necessary to the creation of more aggregate demand is more aggregate supply.

2. Explain how in a free labor market the existence of unemployment automatically tends to reduce money wage rates to the level required to achieve full employment.

3. Explain how government interference is responsible for the perpetuation of mass unemployment.

4. Explain how government interference precipitates mass unemployment by bringing about a drop in payroll spending.

5. Explain what held back the fall in wage rates in the early 1930's, how this led to a further collapse in investment spending and profitability, more bank failures, and a deepening of the depression.

6. Explain why, when wage rates fall to the necessary level, payroll spending tends to increase, rather than remain the same.

7. Would continuous economic progress hold back investment because investments made in the future would be more efficient than investments made in the present?

8. Explain why the prospect of falling prices due to economic progress should *not* be expected to result in a postponement of consumer spending.

9. Explain why full employment was not achieved under the New Deal in the 1930s, despite a policy of large-scale money creation and rapid increases in total spending.

10. Explain why, in principle, a policy of inflation is unlikely to achieve full employment.

11. Explain what made possible the achievement of full employment in World War II.

12. Explain why any additional employment achieved by a policy of inflation and deficits is likely to represent a *decline* in the standard of living of most people.

13. Describe the effects of the full employment achieved in World War II on the standard of living of most Americans.

14. Explain why many people *believed* that World War II represented a period of prosperity.

15. Explain how *the return to peace* is what made possible full employment with prosperity.

16. Explain how full employment could be achieved and maintained through abolishing government interference in the labor market and establishing a 100-percent-reserve gold standard.

17. Explain how real wages can rise in connection with the fall in money wages that is necessary to achieve full employment.

18. Compare and contrast the views of the author with those of von Mises on the subject of the effect on real wages of the process of eliminating unemployment through free competition.

19. Explain why depressions are not caused by excess inventory accumulation.

20. "Excess inventories and depressions are both the result of the same cause, namely, inflation in the form of credit expansion." Explain.

21. In what sense can inventories be viewed as deficient rather than excessive in a depression—that is, how would a larger volume of inventories serve to stave off bankruptcies?

CHAPTER 14. THE PRODUCTIVITY THEORY OF WAGES

PART A. THE MARXIAN EXPLOITATION THEORY

1. Explain what is meant by the Marxian exploitation theory.

2. Describe Marx's "absolutist" version of the labor theory of value. Explain how it differs from the labor theory of value of the classical economists.

3. Explain how Marx's version of the labor theory of value implies that all value is added exclusively by fresh labor.

4. Explain the implications of Marx's doctrine for such cases as the greater value of aged wine over newly fermenting grape juice.

5. Describe Marx's version of the "iron law of wages." Explain how it differs from the classical economists' version of the iron law of wages.

6. Describe Marx's "rate of exploitation formula."

7. What is Marx's explanation of the existence and magnitude of profit and all other forms of "surplus value"?

8. Explain Marx's doctrine of the progressive impoverishment of the masses. Describe the various ways in which the capitalists are supposed to increase "the rate of exploitation" and what allegedly drives them to it.

9. Explain why, according to the Marxists, the wage earners under capitalism are essentially in the same economic position as slaves or serfs.

10. Explain the influence of the exploitation theory on the interpretation of modern economic history—i.e., on the explanation of why conditions were very bad in the past and what made them improve.

11. Show point for point how the Marxian exploitation theory underlies the present-day "liberals'" beliefs concerning minimum-wage, prounion, maximum-hours and child-labor legislation. Show how it underlies their views concerning confiscatory taxation and social welfare spending.

PART B. THE PRODUCTIVITY THEORY OF WAGES

1. What facts make the exploitation theory appear plausible?

2. Explain why the need of wage earners to work and their willingness to work for minimum subsistence if necessary is *irrelevant* to the wages they must actually accept. (Recall the case of the late model car owned by someone who can no longer afford to keep it.)

3. Explain why the desire of employers, like any buyers, to pay less rather than more, i.e., lower wages rather than higher wages, is also irrelevant to the wages the workers must actually accept.

4. Explain why the rational self-interest of employers and all other buyers is not to attempt to pay the lowest price they can imagine or would desire, but merely the lowest price that is simultaneously *too high* for any other employer or buyer who would otherwise obtain the labor or good in question.

5. Explain how money wage rates are determined by the limited supply of labor on the one side and the quantity of money and volume of spending in the economic system on the other.

6. Explain why the fall in wage rates required to eliminate unemployment does not represent the possibility of subsistence wages, but rather tends to raise real take-home wage rates.

7. Explain how real wage rates are determined primarily by the productivity of labor. Using the formulas for the price and wage level, illustrate in terms of the effect on average real wages of (a) a doubling of the productivity of labor while the quantity of money and the monetary demands for consumers' goods and labor remain unchanged, (b) a doubling of the monetary demands for consumers' goods and labor while the productivity of labor remains unchanged, (c) a doubling of the quantity of money and the monetary demands for consumers' goods and labor accompanied by a doubling of the productivity of labor.

8. In the light of the formulas for the price and wage level and the critical role of the productivity of labor, explain how phenomena which begin by reducing money wage rates, such as immigration or a larger labor force due to population growth or the participation of more married women, as well as the elimination of unemployment, need not reduce real wage rates but can actually raise real wage rates.

9. Explain how a rising productivity of labor is essential if a rise in money wage rates is to represent a rise in real wage rates.

10. Explain what is responsible for rising money wage rates for any labor force whose size does not diminish.

11. "Improvements in the productivity of labor raise real wages by reducing prices not by raising money wages." Discuss.

12. Explain why it is that as real wages have risen, so too have money wages.

13. Explain how the productive contribution of businessmen and capitalists is manifested precisely in the determination of the exchange value of products largely by the quantity of labor required to produce them.

14. Show mathematically how, starting with the formulas for the price and wage level, real wage rates are expressible as the product of the productivity of labor times the "distribution factor." Explain the meaning of the "distribution factor."

15. Explain the connection between real wages and the supply of capital goods per worker.

16. Name the two main determinants of the supply of capital goods.

17. Explain the meaning of "the economic degree of capitalism" and state the two ways in which real wages vary in the same direction as it does.

18. Explain the relationship between the economic degree of capitalism and the productivity of labor and real wages by way of the determination of the relative demand for and production of capital goods.

19. Describe the relationship between the economic degree of capitalism and real wages by way of the "distribution factor."

20. Describe the role of saving in capital accumulation.

21. Explain the role of technological progress in capital accumulation.

22. Explain the reciprocal relationship between technological progress and capital accumulation.

23. Explain the effect on real wages of the activities of businessmen and capitalists insofar as these groups are motivated to save and productively expend and to improve the methods of production.

24. Explain the role of free trade and of economic freedom in general in the accumulation of capital. Name the concept that subsumes both economic freedom and technological progress as causes of capital accumulation.

25. Explain why under the conditions of an invariable money an increase in saving and the relative demand for capital goods stands in the same relationship to capital accumulation as does force to acceleration in physics.

26. Explain the rapid economic progress of Japan and other East Asian countries in the light of the theory of capital accumulation presented in this chapter. Present your analysis in terms of Figures 14–4 and 14–5.

27. Explain the relative stagnation of the American economy in the last generation in the light of the theory of capital accumulation presented in this chapter. Present your analysis in terms of Figures 14–4 and 14–5.

28. Explain the stagnation or retrogression of socialist economies, notably Soviet Russia, in the light of the theory of capital accumulation presented in this chapter. Present your analysis in terms of Figures 14–4 and 14–5.

29. Explain how the ultimate foundations of capital accumulation and a rising productivity of labor and real wages are freedom and reason.

30. Describe the leading ways in which government intervention undermines capital accumulation and real wages.

31. Explain why capital accumulation under capitalism is nonsacrificial.

32. Rebut the argument that capital accumulation which comes about by virtue of a rise in the demand for capital goods at the expense of the demand for labor is against the interests of the wage earners.

33. Explain the bad economic conditions of the average worker in Great Britain in the early years of the Industrial Revolution in a way that is consistent with the nonsacrificial character of capital accumulation under capitalism.

34. In the light of the productivity theory of wages, explain the low real wages, long hours of work, and poor working conditions that characterized much of the nineteenth century.

35. In the light of the productivity theory of wages, explain not only how real wages rose, but also how the hours of work shortened, how child labor disappeared, and how working conditions improved over the course of the last two centuries.

36. Explain what is meant by "the fable of the company towns."

37. Explain why the rise in the productivity of labor is the only possible cause of a sustained, significant increase in real wage rates.

38. Explain the futility of attempting to raise real wage rates by almost all of the possible methods of raising money wage rates, i. e., by means of

a. increasing the quantity of money and volume of spending in the economic system,

b. decreasing the supply of labor available to work,

c. increasing the demand for labor at the expense of the demand for capital goods, (

d. increasing the demand for labor by means of taxation the proceeds of which is used to pay wages.

39. Explain the limited context in which it is possible to raise real wage rates by means of raising the demand for labor and thus money wage rates.

40. Explain how a reduction in government spending and taxation could make a significant one-time contribution to raising real wage rates by means of raising the demand for labor. Describe a more important, continuing contribution of cutting government spending and taxation to raising real wage rates.

41. Explain the destructive consequences of efforts to "redistribute" wealth and income in the light of the productivity theory of wages.

42. Explain the error of believing that the existence of profits signifies an ability to pay higher wages. In your answer, be sure to explain how the profits in question may already have been expended for productive purposes and what distinctly different concept profits are being confused with.

43. "The general public and the labor unions are mistaken in believing that raising money wage rates is the means of raising real wage rates." Discuss.

44. Explain the nature of the connection between the productivity of a given individual's labor and his ability to earn higher money wages. Be sure to explain the specific aspect of the individual's productivity of labor that does explain his ability to earn higher wages and the aspect that does not explain it.

45. Explain the effect of a higher productivity of labor on the part of any given individual or group of individuals on the money incomes of those with whom they compete.

46. Explain the lack of direct connect between the average productivity of labor in the economic system and average money wage rates.

47. Explain the effect (or lack of effect) both on average money wage rates and on average real wage rates if all individuals increase their productivity of labor to the same extent, e.g., by a factor of two.

48. Explain how increases in the productivity of labor in some contexts, such as the adoption of the piece work system, can result in a reduction in the average wage rates of the category of workers concerned. Explain how it nevertheless operates to raise the average of real wage rates in the economic system as a whole and, in the long run, the real wage rates of the specific group of workers whose money wage rates have fallen.

49. If all wage earners in the economic system increase the productivity of their labor, but do so in unequal degrees, explain the effect on both the money wages and the real wages of those whose productivity increase is below average; likewise, for those whose

productivity increase is above average.

50. Describe the indirect connection between a higher average productivity of labor and higher average money wage rates under a system of commodity money, such as the gold standard.

51. "The efforts of individuals, who must operate under the freedom of competition, to raise their real wages by means of earning more money are perfectly reasonable, fully consistent with the productivity theory of wages, and serve to raise the average level of real wage rates. However, the attempt to raise the average money wage rate of wage earners as a group, by means of violating the freedom of competition, serves to cause unemployment and lower real wages." Discuss.

52. Explain the consequences of prounion legislation in the light of the productivity theory of wages.

53. "The effect of labor unions is either to raise the wage rates of some groups of workers artificially while more than equivalently reducing the real wage rates of other groups of workers, or else it is to cause unemployment." Discuss.

54. "Labor unions are an antilabor institution in that they actively combat the rise in real wages by combatting the rise in the productivity of labor." Discuss.

55. Explain and criticize the labor unions' conception of how the standard of living of the average worker is increased.

56. "Even when the labor unions recognize a connection between the productivity of labor and wages, the connection they seek to establish is wrong, in that they seek to connect a higher productivity of labor to higher money wages rather than to lower prices." Discuss. (Be sure to include in your discussion the implications of the unions' views for the wages of groups like workers in the computer industry, where there has been an enormous rise in the productivity of labor, and groups like waiters in restaurants, where there has been virtually no rise in the productivity of labor for many generations.)

57. Explain the consequences of minimum-wage legislation in the light of the productivity theory of wages.

58. Explain the consequences of maximum-hours legislation in the light of the productivity theory of wages.

59. Explain how maximum-hours legislation reduces real wages even when hourly wage rates are increased to offset the reduction in hours, leaving weekly wage rates unchanged.

60. Explain the consequences of child-labor legislation in the light of the productivity theory of wages.

61. Explain the consequences of forced improvements in working conditions in the light of the productivity theory of wages.

62. In the light of the productivity theory of wages, explain the effect on real wages of freedom of competition in the employment of women and members of minority groups despite a possible reduction in the money wage rates of those already employed.

63. Explain the very different effects of the competition of women and members of minority groups in the face of prounion and minimum-wage legislation and racial and sexual quotas.

64. Explain the relationship of the productivity theory of wages to the classical economists' doctrine of the wages-fund theory.

65. Explain why John Stuart Mill's recantation of the wages-fund doctrine was not justified.

66. Explain the essential differences between the productivity theory of wages and the so-called *marginal*-productivity theory of wages.

67. Explain the difficulties encountered in attempting on a case by case basis to derive the value of a factor of production from the product that is lost when a unit of a factor of production is withdrawn.

CHAPTER 15. AGGREGATE PRODUCTION, AGGREGATE SPENDING, AND THE ROLE OF SAVING IN SPENDING

1. "The volume of spending in the economic system is a measure of the quantity of money that exists, not of the volume of wealth that is produced." Discuss.

2. Explain why the use of price indexes to adjust the volume of spending for changes in the price level, does not make possible any kind of precise measure of what is produced.

3. Describe what the concept of gross product includes according to the author and the classical economists.

4. Explain what is meant by productive consumption.

5. Explain what is meant by the *net* product according to the author.

6. Explain why what contemporary economics describes as the gross product is actually a highly netted product.

7. Explain what is meant by the error of "double counting" according to Samuelson and other contemporary economics textbook authors.

8. Explain how Ackley, Samuelson, and the others come to the conclusion that to claim that both bread *and* flour, or both automobiles *and* steel, are produced is to claim that more is produced than is in fact produced.

9. Explain Samuelson's and the others' concept of what it is that one produces when one produces a product such as a loaf of bread or an automobile.

10. Explain how this concept of one's product leads to the conclusion that the total product of the economic system is essentially just the production of consumers' goods, i.e., of "final products."

11. "*The Statistical Abstract of the United States* and all other publications reporting the production both of consumers' goods and of the capital goods necessary to their production are guilty of the error of double counting, according to contemporary economics." Discuss.

12. Describe the mental processes that lead to the conclusion that a final product, such as bread, counts all the intermediate products whose production is necessary to its production.

13. Explain why the mental processes referred to in the preceding question rest on a Platonic-Heraclitean view of the nature of entities.

14. Explain why, according to the author, the belief that the value of the final product counts the value of the intermediate products in addition to its own value rests on a twofold violation of the laws of arithmetic and entails a double counting of the value of the final product.

15. Explain what is meant by productive expenditure. (See Chapter 11, if you have forgotten.)

16. Explain what is meant by consumption expenditure. (See Chapter 11, if you have forgotten.)

17. Describe the nature of the confusions many people have in connection with what a person buys when he buys a consumers' good.

18. Explain how the confusions referred to in the preceding question reinforce the view that saving is synonymous with hoarding.

19. What is meant by the proposition that "the demand for *A* is the demand for *A*"?

20. How does the proposition that "the demand for *A* is the demand for *A*" relate to John Stuart Mill's proposition that "the demand for commodities is not the demand for labor"?

21. Explain what is meant by "shadow entities and shadow purchases." Illustrate by distinguishing between a real purchase of bread, flour, and wheat in a supermarket, and the purchase of bread alone.

22. Explain how the notion that in buying the final product one buys the labor and capital goods necessary to its production contradicts the fact that businessmen need capital in order to buy the means of production.

23. Explain why the fact that buying the output is proof that one has *not* bought the inputs.

24. "The demand for consumers' goods is not only not a demand for factors of production, but is *in competition* with the demand for factors of production." Discuss.

25. Describe what would happen to the demand for factors of production if the sellers of consumers' goods used the whole of their sales proceeds to consume.

26. "If wealthy businessmen decide to withdraw funds from their firms in order consume in the form of buying yachts, say, the effect will be to cause an increase in the demand for capital goods and labor by the yacht-building industry. Nevertheless, the *total* demand for capital goods and labor in the economic system will now be less to the extent that the purchase of yachts has taken the place of the purchase of capital goods and labor." Explain.

27. "A rise in the demand for consumers' goods at the expense of the demand for factors of production increases the proportion of the demand for factors of production that is made by the consumers' goods industries while reducing the overall size of the demand for factors of production in the economy as a whole." Discuss.

28. Explain why the only income of any significance that could be increased by virtue of the repeated rounds of consumption expenditure depicted in the multiplier process would be profit income, not wage income.

29. Explain what is meant by "saving."

30. Explain why people of limited education and with no business experience are especially prone to confuse saving with hoarding.

31. Describe how the fallacy that saving is hoarding is prominent among Keynesian economists and the financial press.

32. Explain the connection of the fallacy that saving is hoarding and thus economically depressing, to the notion that investment spending comes out of nowhere and is expansionary.

33. Describe the closely related fallacy in connection with the way in which government spending and taxes are frequently viewed.

34. Explain why the belief that saving is hoarding represents the fallacy of composition when it is applied to the economic system as a whole.

35. Explain why hoarding—i.e., an increase in the demand for money for holding—when it actually occurs is the cause of a *reduction* in savings.

36. "When it occurs on a significant scale, 'hoarding' has nothing to do with any attempt to save or to save more; nor does it originate with consumers. Rather, it represents the attempt of business firms and investors to convert previously accumulated savings from their usual form of physical assets or claims to physical assets, into cash, in an effort to become more liquid." Discuss.

37. Explain how "hoarding" operates to increase the degree of liquidity in the economic system—i.e., the ratio of the quantity of money to such magnitudes as current liabilities—and finally to put an end to the de-

sire further to increase cash holdings.

38. Explain how inflation and credit expansion create the potential for a sudden rise in the demand for money for holding.

39. Describe how what is saved is not only spent, but is the source of *most* spending in the economic system. (In your answer, be sure to feature the role of saving by business firms out of their sales revenues, i.e., the extent to which their sales revenues are used to make productive expenditures rather than consumption expenditures.)

40. Starting with the fact that approximately 98 percent of supermarkets' sales revenues serve to cover costs, estimate the ratio of productive expenditures made at all the various stages of production connected with supplying food, to consumption expenditures for food.

41. Explain the effect of saving on the demand for houses and expensive consumers' goods in general.

42. Describe the extent to which wages are paid out of saving and productive expenditure versus consumption expenditure.

43. "Saving and productive expenditure not only far exceed consumption expenditure, but are the *source* of almost all consumption expenditure." Explain.

44. "Financially the individual business firm is vitally dependent on the consumers, but from the perspective of the economic system as a whole, it is the consumers who are vitally dependent on business." Discuss.

45. Explain the proposition "money comes to goods."

46. Explain what is meant by the propositions "business is the source of its own demand and profitability" and "there is no need for artificial consumption."

47. Explain what is meant by the proposition that saving is the source of an increasing aggregate demand in both real and monetary terms.

48. Explain what is meant by the proposition that saving is the source of rising consumption. Illustrate in terms of the recent history of Japan.

49. Describe the effects on aggregate consumption of the use of savings to pay wages.

50. Explain what is meant by the consumption illusion of contemporary national-income accounting.

51. Explain why the equality between national income (i.e., the sum of profits plus wages), on the one side, and net national product (i.e., the sum of consumption expenditure plus net investment), on the other, is in fact an identity in which the only difference between the two sides is a change in the order of addition of the exact same revenue-expenditure subcomponents.

52. Explain why net investment equals productive expenditure minus business costs—the same costs as are deducted from sales revenues in calculating aggregate profits.

53. Explain how it is that most spending in the economic system is concealed under the heading of net investment.

54. Explain what is meant by the "gross national revenue" (GNR).

55. Explain what item must be subtracted from GNR to go to national income, on the one side, and to net national product, on the other?

56. What must be subtracted from GNR to go to GNP?

57. Explain why recognizing the separate existence of the demand for capital goods, and the separate, distinct production of capital goods, is necessary in order to understand that an additional supply of capital goods serves to increase the supply of capital goods as well as the supply of consumers' goods.

58. Explain how the failure to recognize the separate existence of the demand for capital goods and the corresponding separate production of capital goods leads both to an inadequate appreciation of the role of saving in capital accumulation and to a corresponding overemphasis on the role of saving in capital accumulation.

59. Explain how the failure to recognize the separate existence of the demand for capital goods and the corresponding separate production of capital goods also prevents recognition of the role of technological progress as a cause of capital accumulation in serving to maintain the productivity of the increasing supply of capital goods.

60. Explain why in the light of the analysis of Figures 15–5 and 15–6 the relationship between national income and economic progress and prosperity is *inverse* in the context of an economic system with an invariable money.

61. Explain why in the light of the analysis of Figures 15–5 and 15–6 national income is basically the counterpart just of consumption expenditure.

62. Explain the mechanism by which economic progress raises *real* incomes in Figure 15–6.

63. Explain what is meant by the "balanced-budget multiplier" of the Keynesians.

64. Explain how recognition of the inverse relationship between national income and economic progress and prosperity serves to overthrow the doctrine of the balanced-budget multiplier.

65. Explain what is meant by the doctrine of the "Conservatives' Dilemma."

66. Explain how recognition of the inverse relationship between national income and economic progress and prosperity serves to overthrow the doctrine of the conservatives' dilemma.

CHAPTER 16. THE NET-CONSUMPTION/NET-INVESTMENT THEORY OF PROFIT AND INTEREST

PART A. THE POSITIVE THEORY

Net Consumption

1. Describe the treatment of interest in relation to profit in Chapter 16.

2. "The amount of profit in the economic system is essentially the difference between the demand for the products of business and the demand for factors of production by business." Discuss.

3. Explain why the determinants of the average rate of profit in the economic system as a whole are different than the determinants of the rate of profit of an individual company.

4. Explain the different significance of an individual company earning a given high rate of profit, such as 50 percent, and the average rate of profit in the economic system being that high.

5. Why is the interest rate on government bonds probably not a good indicator of the average rate of profit in the economic system?

6. What is meant by *net consumption?*

7. What is meant by *net investment?*

8. Given that profits in the economic system equal aggregate sales revenues minus aggregate costs, show why the algebraic difference between profits and net investment is business sales revenues paid by consumers minus productive expenditure in payment of wages, i.e., net consumption.

9. Describe the role of productive expenditure both as a source of business sales revenues and as the source of business costs.

10. If productive expenditure were the only source of business sales revenues, what would be the implications for the amount and rate of profit in the economic system?

11. Define net consumption in terms of the difference between business sales revenues and productive expenditure. Why is that equal to the portion of business sales revenues that is paid by consumers minus the portion of productive expenditure that goes for the payment of wages?

12. Define net consumption in terms of the difference between the demand for the products of business and the demand for factors of production by business. Why is that equal to the difference between the demand for consumers' goods from business minus the demand for labor by business?

13. "The principal source of net consumption is the consumption expenditure of businessmen and capitalists, made possible by dividend, draw, and interest payments." Discuss.

14. "Dividend and draw payments, to the extent that they are consumed, are the source of business sales revenues that have no counterpart whatever in productive expenditure and thus the generation of business costs. Thus they are the source of sales revenues exceeding productive expenditure and costs." Discuss.

15. "Interest payments by business, to the extent that they are consumed, are the source of business sales revenues in excess of the productive expenditure and costs that we are considering." Discuss.

16. Explain the role of net consumption in generating an excess of demand for products (sales revenues) over demand for factors of production (productive expenditure) in Tables 16–1 and 16–2.

17. In Figure 16–1, explain the connection between productive expenditure in any given year and the aggregate costs of the capital goods and consumers' goods that appear in the following year.

18. What in Figure 16–1 determines the allocation of any given year's total productive expenditure between the production of the capital goods and consumers' goods of the following year, and thus the specific aggregate costs of the capital goods and consumers' goods of the following year?

19. What are the two overall categories of demand for the products of business in every year of Figure 16–1? What are the two basic sources specifically of the demand for consumers' goods each year—that is, what are the two basic sources of the money the consumers spend each year?

20. Identify what it is in Figure 16–1 that allows business to sell each year for more money in toto than it expends in buying the factors of production.

21. Explain the relationship of Table 16–3 to Figure 16–1.

22. How does Table 16–3 treat productive expenditure in relation to business sales revenues and business costs?

23. Why is net consumption the source of aggregate profit in Table 16–3?

24. Why is net consumption the source of an aggregate profit in Figure 16–1?

25. How does Figure 16–1 differ from Figure 15–5?

26. How does aggregate profit differ from national income? How does the expenditure counterpart of profit differ from the expenditure counterpart of national income?

27. How does Figure 16–2 differ from Figure 16–1? How does Figure 16–2 make possible a calculation of the average *rate* of profit in the economic system as well as its overall amount?

28. How does it happen that in every year of Figure 16–2, business both spends all of its cash and yet ends

up with exactly the same amount of cash with which to begin operations in the following year?

29. What is the aggregate amount and average rate of profit in every year in Figure 16–2?

30. Describe other possible sources of net consumption besides the consumption expenditure of businessmen and capitalists.

31. Explain why, in addition to its previous formulations, net consumption also equals total consumption expenditure that constitutes sales revenue *or* wages, minus total wages paid in the economic system.

32. Explain why it is reasonable to assume that all the wages paid by business have a counterpart in the demand for consumers' goods from business, even though wage earners save.

33. In the light of Table 16–4, explain how a rise in the amount and rate of net consumption raises the amount and rate of profit. Explain what would happen to the amount and rate of profit if all businessmen were to consume 100 percent of their sales proceeds.

34. Explain the implications of your answer to the preceding question for the analysis of Adam Smith's and Karl Marx's contention that in a society without businessmen and capitalists, in which manual workers produced and sold products none of the sales proceeds from which they productively expended and all of which they consumed, all income would be wages and no income would be profits.

35. Explain why businessmen and capitalists cannot arbitrarily increase the rate of net consumption and the rate of profit.

36. Explain why capital tends to gravitate into the hands of those businessmen and capitalists whose rate of consumption relative to their accumulated capitals is below average and out of the hands of those whose rate is above average.

37. Describe the two principles operating to determine the growth and decline of individual fortunes relative to the total wealth of the economic system.

38. Explain the influence of accumulated capital on net consumption and thus why net consumption exists even in the face of general business losses.

39. Explain how seeing the consumption of businessmen and capitalists as determined mainly by their accumulated capital helps to explain the relationship between *relatively* high incomes in the economic system and high rates of saving, and, at the same time, the lack of relationship between rising *average* real incomes and the rate of saving.

40. What is meant by time preference?

41. How does a high or low time preference in a society affect the rate of net consumption and the rate of profit?

42. Explain why the absolute temporal extent of the present and future—i.e., whether the present is taken as the coming year, month, week, or day, and the future as everything beyond it, has no bearing on the role of the rate of net consumption in determining the annual rate of profit.

43. "The role of time preference in determining the rate of profit is indirect, not direct." Discuss.

44. "Other things being equal, because of the effect on time preference, the average rate of profit and interest will be the lower, the freer and more rational is a society." Explain by way of the effect on the rate of net consumption.

45. In the light of your answer to the preceding question, explain why the effect of the activity of revolutionary bandits and plundering government officials who rail against the existence of profit and interest is actually to raise the average rate of profit and interest.

Net Investment

1. Explain the distinction between productive expenditure and costs.

2. "Much of productive expenditure is added to asset accounts; much of cost represents subtractions from asset accounts." Illustrate.

3. Explain why net investment is the difference between productive expenditure and costs.

4. Explain why, on the basis of their very mathematical definitions, aggregate profit and net investment are closely related.

5. Explain why, on the basis of their mathematical definitions, the difference between aggregate profit and net investment is net consumption.

6. Demonstrate how, starting with the fact that aggregate profit equals aggregate sales revenues minus aggregate cost, it also equals the sum of net consumption plus net investment.

7. Explain what is meant by the net consumption rate?, the net investment rate?

8. Explain how the average rate of profit in the economic system equals the sum of the net consumption and net investment rates.

9. Explain what is meant by "secondary productive expenditure."

10. Explain how net consumption is reduced and conceivably could become negative as the result of the saving of wage earners being used to finance secondary productive expenditures.

11. Explain why the existence of negative net consumption is unlikely.

12. Explain how net investment makes possible the existence of an aggregate profit even if net consumption is negative.

13. How does an increase in productive expenditure for plant and equipment with a life of many years affect net investment?

14. How does an increase in productive expenditure for plant and equipment that requires several years in its construction affect net investment.

15. Describe the various ways that net investment can exist by virtue of a change in the disposition of a given aggregate amount of productive expenditure between various subcategories of productive expenditure.

16. Explain what is meant by an invariable money.

17. Explain how the existence of net investment can be indefinitely prolonged under the existence of an invariable money.

18. Explain why, for example, the process of substituting the production of 12-year old scotch for the production of 8-year old scotch entails a rise in the aggregate amount both of profit and net investment in the economic system.

19. Describe how the shifting of productive expenditures from points less remote from the making of sales to points more remote from the making of sales operates to reduce aggregate costs in the economic system.

20. In connection with your answer to the preceding question, explain the effect on the amounts of net investment and profit in the economic system.

21. Explain what is meant by the expression the marginal productivity of capital as used in *Capitalism.*

22. Explain how if the marginal productivity of capital exceeds the rate of profit, incentives are created that serve to increase the amount of net investment and the amount and rate of profit in the economic system.

23. Explain why the marginal productivity of capital, in the sense in which the expression is used in *Capitalism*, and the rate of profit tend to equalize.

24. Explain why, under the conditions of an invariable money, the ability of net investment to add to the rate of profit is an inherently self-limiting phenomenon.

25. Explain why, under the conditions of an invariable money, it becomes progressively more difficult to keep net investment in being in the face of any given rate of profit.

26. Present two reasons why, under the conditions of an invariable money, the rate of profit comes to equal the rate of net consumption alone.

27. Explain why, under the conditions of an invariable money, the effect of net investment is to bring about a subsequent rise in net consumption and reduction of productive expenditure.

28. "Under an invariable money, savings and capital would be accumulated up to a certain ratio to income, and then, in the absence of a fall in time preference, further accumulation would cease." Discuss.

29. Explain how the increase in the quantity of money operates to perpetuate the existence of net investment.

30. Explain why the increase in the quantity of money tends to bring about an addition to the nominal rate of profit that is approximately equal to itself.

31. Explain why the net investment rate tends to equal the rate of increase in the quantity of money.

32. Explain why the rate of increase in production and supply adds an approximately equal percentage to the real rate of profit.

33. Explain what is meant by "springs to profitability."

34. Describe the various "springs."

35. Describe the various ways in which a lower rate of profit encourages capital intensivity.

36. Explain how wage-rate rigidities operate to block the operation of the most powerful spring.

37. Does the increase in the quantity of money that is the by-product of economic progress operate to reduce the degree of capital intensiveness of the economic system? Discuss.

PART B. THE NET-CONSUMPTION/NET-INVESTMENT THEORY AND ALTERNATIVE THEORIES

1. Describe the explanation of the rate of profit/interest that is provided by the productivity theory. Be sure to include Roscher's famous example of the boat and net.

2. Explain the productivity theory's view of the role of diminishing returns and technological progress in connection with the rate of profit/interest.

3. Diminishing returns and technological progress determine
   a. the rate of profit/interest
   b. the rate of capital accumulation in real terms

4. Among the difficulties encountered by the productivity theory of profit/interest are
   a. a reliance on the doctrine of opportunity cost
   b. the problem of having to subtract mathematically incommensurate quantities, such as loaves of bread forgone versus extra fish produced
   c. a confusion of more physical output with more money revenue
   d. the fact that the rate of profit is highest before there is any capital or productivity of capital
   e. all of the above
   f. none of the above

5. "The productivity of capital goods, such as a boat and net, can explain a virtually corresponding addition to the profits of an individual enterprise if it is alone in adopting the more productive method; even then, it cannot explain the existence of an addition to the aggregate profits of the economic system, because equivalent losses on the part of other firms are implied." Discuss.

6. "If all firms in the economic system employ more

productive methods of production based on the use of more capital, no addition to aggregate profits or the average rate of profit is implied." Explain and illustrate in terms of everyone adopting the more productive boats and nets in the conditions of an invariable money.

7. Describe the two *indirect* connections that can exist between the adoption of more productive methods of production and a positive contribution to the rate of profit/interest via
   a. the effect on the rate of increase in the quantity of commodity money
   b. the effect on net investment

8. Describe the two reasons why the general marginal net productivity of physical capital goods conceived of in terms of abstract units of wealth, such as the productive consumption of each unit *K* of capital goods resulting in an output equivalent to *2K* of capital goods, is far higher than the average rate of profit/interest.

9. Describe the explanation of the rate of profit/interest that is provided by the time preference theory in its traditional form.

10. "According to the time preference theory, profit/interest exists because factors of production are future goods, which are purchased at a "discounted value" in comparison to present goods of the same kind and number, and then mature or ripen into present goods, which shake off that discount and sell at the full value appropriate to present goods." Discuss.

11. "Rothbard's exposition shows that the time-preference theory in its traditional form shares with Böhm-Bawerk's critique of the exploitation theory the error of regarding the wage earners as the real producers of the products, rather than, as is in fact the case, the businessmen and capitalists." Discuss.

12. "The basic formula of the time-preference theory in its traditional form does not demonstrate what it is supposed to demonstrate. Starting with 9 present apples and ending with 10, 20, or 5 present apples a year later simply does not tell us the rate of return that is actually earned in production." Discuss.

13. What assumption does the time-preference theory make about the prices of present goods? Explain why this assumption does not hold up in the conditions of an invariable money accompanied by changes on the side of production and supply. Use Figure 16–2 as the basis of examples showing why not.

14. What error does the time-preference theory share with the productivity theory in connection with the relationship between a greater or smaller physical product and sales revenues?

15. "The supporters of the time-preference theory in its traditional form are led into the contradiction of regarding increases in production as the cause both of an increase and a decrease in the rate of profit." Explain.

16. Explain and illustrate why it is an error to take the value of consumers' goods as a fixed starting point and to assume that changes in the rate of profit/interest affect only the value of the factors of production used to produce them.

17. "The prices of factors of production are determined by supply and demand no less than the prices of consumers' goods; the rate of discount (viz., profit) then emerges as the result of *differences* between the demand/supply situation in the market for products and the demand/supply situation in the market for factors of production." Discuss, being sure to relate demand and supply differences to net consumption and net investment.

18. Describe the result of Böhm-Bawerk's recognition that whoever has savings of any kind thereby demonstrates that he values the last unit of wealth that he devotes to the future above an additional unit of wealth that he might devote to enjoyment in the present, and thus, to this extent, has *a preference for future goods over present goods*.

19. Explain why the role of time preference in determining the rate of profit/interest is not eliminated by the fact that at the margin individuals may value units of future goods above units of present goods.

20. Describe what is required to view Ricardo's proposition that "profits rise as wages fall and fall as wages rise" as implying the net consumption theory.

21. Explain how the above interpretation is reinforced by John Stuart Mill's proposition that "demand for commodities is not demand for labor," which Ricardo accepted.

CHAPTER 17. APPLICATIONS OF THE INVARIABLE-MONEY/NET-CONSUMPTION ANALYSIS

1. Describe how capital accumulation can take place with no accompanying fall in the rate of profit.

2. Describe how production can increase and prices fall both with no accompanying fall in the rate of profit and no greater difficulty of repaying debts being present.

3. Explain why, in the conditions of an invariable money, a fall in the rate of profit should be associated with an *acceleration* of the rate of capital accumulation and fall in prices, rather than with capital accumulation and falling prices per se.

4. Explain how the habit of focusing almost exclusively on the production of consumers' goods, as though all that were produced were consumers' goods, leads to the belief that the only source of capital accumulation is more saving.

5. Explain how the fallacy of composition contributes to the conclusion that the effect of capital accumulation is a lower rate of profit.

6. "Falling prices caused by increased production and supply are preceded by falling unit costs to the same extent." Explain.

7. Explain why a fall in the rate of profit that results from a fall in the rate of net consumption differs profoundly from a fall in the rate of profit that results from a financial contraction and deflation.

8. "The fact that a fall in the rate of net consumption entails a rise in saving and productive expenditure, extensive net investment and the formation of new capital giving rise to a higher degree of capital intensiveness, and makes possible a correspondingly greater availability of credit, characterizes it as the very opposite of a period of deflation or financial contraction. In a deflation or financial contraction, productive expenditure falls, net investment becomes negative, capital values decline, and credit becomes largely unobtainable." Discuss.

9. Explain why the process of falling prices resulting from increased production and supply is actually almost certain to be accompanied by a growing ability to repay debt rather than by an increased difficulty of repaying debt.

10. Explain how the fall in the rate of profit that is the accompaniment of launching or accelerating the process of capital accumulation by means of a fall in the rate of net consumption, is in part reversed by the consequences of that capital accumulation.

11. "Just as technological progress is not required as an 'outlet' for capital goods accumulated merely by means of saving, but is itself the source of capital goods, so in its relation to the increase in the supply of commodity money it is not an outlet for net investment, but is itself the source of net investment." Discuss.

12. Describe Ricardo's essential insight concerning the nature of capital accumulation.

13. Why is a fall in the rate of profit caused by a fall in the rate of net consumption unlikely to be accompanied by a rise in the demand for money for holding, as is the case when the rate of profit falls because of a financial contraction/deflation?

14. Explain and illustrate why it is that with the passage of years, the cumulative proportion of the capital goods and labor in existence in any given base year that directly or indirectly serves in the production of consumers' goods continually grows, while the proportion continuing to serve indirectly in the production of capital goods and thus of consumers' goods in the still further future continually declines.

15. Using Figures 16–2 and 17–3, explain how the average period of production or length of the structure of production can be expressed.

16. Explain why a continuous lengthening of the period of production is not necessary for the existence of capital accumulation.

17. Use the concept of the average period of production to explain why technological progress by itself is limited in its ability to bring about capital accumulation and why an economic system with a longer average period of production is in a better position to implement technological advances.

18. Explain how the taxation of profits raises the rate of profit.

19. Explain how budget deficits financed by borrowing from the public operate to raise the rate of profit.

20. Explain why the goal of increasing saving and capital formation through balancing the government's budget depends on cutting government spending rather than raising taxes.

21. Describe how government intervention has contributed to an emphasis on short-term results.

22. Describe the connection between chronic budget deficits and the negative balance of payments between the United States and Japan.

23. Describe how greater economic freedom and respect for property rights in the United States is necessary to maintain America's world role.

24. "In the absence of increases in the quantity of money, net saving in terms of money would tend to disappear." Discuss.

25. Explain why the actual economic significance of saving lies at the gross level, rather than at the net level.

26. "Rather than reduce the rate of profit, continued net saving is the product of forces that add to the rate of profit." Discuss.

27. Explain how hoarding operates as a long run cause of a higher rate of profit rather than a lower rate of profit.

28. Describe the extent of the outlets for investment.

29. Explain what is meant by underconsumptionism. Describe its basic error.

30. Explain how the demand for capital goods and labor can radically and permanently exceed the demand for consumers' goods.

CHAPTER 18. KEYNESIANISM: A CRITIQUE

1. Explain the implications of the proposition that unemployment can be eliminated by a fall in wage rages and prices for the position of economists vis-a-vis labor legislation and in the minds of those who accepted the Marxian exploitation theory.

2. Describe the essential claims of Keynesianism with

respect to the ability of a fall in wage rates and prices to achieve full employment.

3. Explain the implications of your answer to the preceding question for the need of economists to fight for the establishment of a free market in labor.

4. Describe what, according to Keynesianism, is the solution for mass unemployment.

5. On the basis of your answers to the preceding questions, explain why Keynesianism was a source of intellectual relief for many economists.

6. Explain the contention that Keynesianism is incompatible both with common sense and with the love of liberty.

7. Explain why Keynesianism is incompatible with the quantity theory of money.

8. Describe the developments that had taken place in economic theory in the two generations prior to the appearance of Keynes that undercut his critics' ability to present strong counterarguments.

9. Explain what is meant by neo-Keynesianism and how it differs from Keynesianism. (In your answer, be sure to explain who was A. C. Pigou.)

10. Explain whether or not neo-Keynesianism differs from Keynesianism with respect to the conclusion that a free economy cannot have full employment.

11. Explain why the neo-Keynesians are led to conclude that reductions in wage rates and prices can have only a relatively modest impact on the increase in employment and output.

12. Explain why Pigou's doctrine is even weaker than the Keynesians themselves recognize.

13. In the 14th Edition of their book, Samuelson and Nordhaus state: "The basic difference between classical and Keynesian approaches can be found in differing views about the behavior of aggregate *supply.* Keynesian economists believe that prices and wages adjust slowly, so any equilibrating forces may take many years or even decades to operate. The classical approach holds that prices and wages are flexible, so the economy moves to its long-run equilibrium very quickly. . . . While the classical economists were preaching that persistent unemployment was impossible, economists of the 1930s could hardly ignore the vast army of unemployed workers . . . . Keynes emphasized that because wages and prices are inflexible, there is no economic mechanism to restore full employment and ensure that the economy produces its potential. . . . In the Keynesian model, aggregate supply slopes upward, implying that output will increase with higher aggregate demand as long as there are unused resources." (pp. 464–67; similar views are expressed in the 15th Edition, on pp. 602–603.)

a. Describe Samuelson's departure both from Keynesianism and traditional neo-Keynesianism in his explanation of the cause of unemployment, i.e., in terms of whether unemployment is caused by wage-rate rigidities or by the alleged inelasticity of the aggregate demand curve.
b. Explain whether or not it is true to say, as Samuelson does, that "The classical approach holds that prices and wages are flexible, so the economy moves to its long-run equilibrium very quickly." Did the classical economists maintain that wages and prices are flexible in the face of minimum-wage and prounion legislation and similar government interference?
c. Explain whether or not it is true to say, as Samuelson does, that the classical economists preached "that persistent unemployment was impossible." Did they maintain this proposition in reference to conditions in which government interference prevented the necessary adjustment of wage rates and prices or only to conditions in which wage rates and prices were free of government interference?
d. Is Samuelson accurate in claiming that "Keynes emphasized that because wages and prices are inflexible, there is no economic mechanism to restore full employment and ensure that the economy produces its potential." Or was Keynes position that there is no way for a free economy, which *has* flexible wages and prices, to achieve full employment?
e. In what way does Samuelson's position represent an unadmitted capitulation to the claims of classical economists?

14. Explain what is meant by the Keynesian doctrine of the unemployment equilibrium?

15. Compare and contrast the Keynesian aggregate demand curve with the consumptionist aggregate curve.

16.
a. Explain whether the basis of the Keynesian aggregate demand curve is the claim of many union leaders that wage rate reductions result in proportionate reductions in consumer spending.
b. Explain why it does not follow that wage rate reductions, while reducing the spending of the individual wage earner, reduce total spending on the part of wage earners.
c. Explain why the fall of wage rates to their equilibrium level is in fact almost certain to be accompanied by a rise in total payroll spending and in productive expenditure as a whole.

17. Explain what is meant by the Keynesian "IS" curve.

18. Explain the relationship between the IS curve and the Keynesian aggregate demand curve.

19. State the Keynesian argument for an unemployment equilibrium in terms of the alleged effect of full employment on the rate of profit.

20. Explain whether the Keynesian argument for an unemployment equilibrium depends on the assumption that the minimum acceptable rate of return for lending and investing is specifically 2 percent.

21. Explain what is meant by each of the following: (a) the production function, (b) the saving function, (c) the equilibria of investment and saving, (d) the mar-

ginal efficiency of capital schedule.

22. Explain the derivation of the IS curve from the functions and schedules described in answer to the preceding question.

23. Explain why in terms of the relationship Keynesianism alleges between the "marginal efficiency of capital" and the volume of investment in physical terms, reductions in wage rates and prices result in proportional reductions in total spending.

24. Describe the unemployment equilibrium in terms of the alleged relationship between the portion of their incomes that people attempt to save at the point of full employment and the amount of profitable investment that can take place.

25. Explain the three grounds for the MEC doctrine.

26. Explain what is meant by "fiscal policy."

27. Explain how fiscal policy, in the form of chronic government budget deficits, is supposed to be the solution for the unemployment equilibrium, according to Keynesianism. In your answer, be sure to explain the effect budget deficits are supposed to have on the marginal efficiency of capital at the point of full employment.

28. Present an environmentalist analogy to the Keynesian doctrine of the unemployment equilibrium and fiscal policy as the solution for it.

29. Explain the criticisms of each of the three grounds for the MEC doctrine. Be sure to describe the logical fallacy committed by the Keynesians in each instance.

30. Explain why the Keynesian claim that a fall in wage rates and prices cannot achieve full employment, because at full employment the rate of return on capital would be too low, is a claim that the rate of return in the recovery from a depression is lower than it is in the depression.

31. "A major reversal of economic reality on the part of the Keynesian analysis is its belief that in a depression saving and net investment are at their maximum possible limits, and the problem is that full employment requires that they be carried still further. The actual fact is, however, that far from being at their maximum limits, saving and net investment are extremely low or even *negative* in a depression." Discuss. (In your answer, be sure to explain why saving and investment are negative in a depression.)

32. Explain why the marginal-efficiency-of-capital doctrine constitutes a *reversal* of the actual relationship between net investment and the rate of profit in the context of a business cycle, i.e., why more net investment accompanying the return to full employment would result in a *rise* in the rate of profit, not a fall.

33. Describe the contradiction between the marginal-efficiency-of-capital doctrine and the multiplier.

34. Explain why a fall in wage rates is the requirement for the restoration of net investment and profitability along with full employment.

35. Explain the effect on business profits if wage rate reductions were accompanied by reduced total wage payments, and the saving of funds were used to buy plant and equipment.

36. Explain what is meant by the paradox-of-thrift doctrine.

37. Explain why the paradox-of-thrift doctrine rests entirely on the central notion of the Keynesian analysis that there is room in the economic system for only a strictly limited amount of profitable investment.

38. Explain why there is no such thing as saving being a mathematical function of income. (In your answer be sure to explain the relationship of saving to the increase in the quantity of money and what would happen to saving if the quantity of money stopped increasing.)

39. Explain what is meant by "liquidity preference."

40. Present the arguments advanced by the Keynesians for expecting a 2 percent minimum to the rate of return at which people are willing to lend or invest and what is supposed to happen to the size of cash holdings once the rate of return gets that low.
   a. Explain why, in a free economy the rate of profit and interest would almost certainly be above 2 percent.
   b. Explain why if the rate of return somehow did get so low that people attempted to hoard, that very fact would operate to raise the rate of return.
   c. Explain why, in answer to the Keynesian arguments in its favor, 2 percent does not in fact constitute a necessary floor to the rate of return.

CHAPTER 19. GOLD VERSUS INFLATION

PART A. INFLATION OF THE MONEY SUPPLY VERSUS ALTERNATIVE THEORIES OF RISING PRICES

1. State the popular definition of inflation.
2. State the alternative definition of inflation presented in *Capitalism.*

3. Explain why the definition of inflation as rising prices results in people having no ready idea of what causes inflation in any given case except the greed of businessmen.

4. Explain why the definition of inflation as rising prices implies that price controls are the solution for inflation.

5. State and explain the formula for the general consumer price level.

6. Explain why the formula for the general consumer price level limits the direct, immediate explanation of rising prices to either a rise in aggregate demand or fall in aggregate supply.

7. Describe the effect of supply on prices in the United States and practically all other countries over the last fifty years.

8. Explain why where falling supply has contributed to rising prices, its role has been relatively minor.

9. Explain why reductions in supply as the cause of rising prices imply the rapid disappearance of material civilization.

10. Explain how falling supply is itself often the by-product of rapid increases in aggregate demand.

11.
a. Explain why falling supply cannot explain the range of price increases that exists under inflation.
b. Explain how, on the other hand, rising aggregate demand does explain the range of price increases that exists under inflation.

12.
a. Explain why rising prices caused by falling supply are incompatible with the debtor/creditor effects associated with inflation.
b. Explain how it is possible for debtors actually to be worse off than creditors as the result of rising prices caused by falling supply.
c. Explain how, unlike rising prices caused by falling supply, rising prices caused by rising aggregate demand are fully compatible with the debtor/creditor effects associated with inflation.

13. Explain why the belief that falling supply is a cause of inflation implies the overproduction doctrine.

14. Summarize the seven reasons why falling aggregate supply must be eliminated as the cause of an inflationary rise in prices, leaving only rising aggregate demand (and, underlying it, a rising quantity of money).

15. What assumptions lead people to believe that the rising prices of the last two generations could not have been caused by rising aggregate demand, but only by rising costs of production or the greed for higher profits.

16. Explain why the cost-push doctrine is mathematically equivalent to blaming rising prices on falling supply.

17. Explain the effect of wage increases imposed by labor unions on unemployment if there is no increase in the quantity of money and thus in aggregate demand.

18. Starting from a position of full employment, explain to what extent could labor unions succeed in raising wage rates before bringing about an unemployment rate comparable to that of the great depression, if there is no increase in the quantity of money and thus in aggregate demand.

19. Explain how, over the same period of time that the unions were driving up wage rates, *prices* could actually fall substantially.

20. "Labor unions are not a significant cause of rising prices, but of unemployment." Discuss.

21. "In order for "wage-push" to have a sustained significant effect on the general consumer price level, it must be sustained by an increasing quantity of money and rising aggregate demand." Discuss.

22. Explain how the increase in the quantity of money and rising aggregate demand encourages "wage push"—indeed, calls it into being when it otherwise would not exist.

23. "The intellectual zone of explanation of rising prices previously regarded as belonging to the wage-push doctrine should henceforth be regarded as having been annexed by the quantity theory of money." Discuss.

24. Explain what is meant by the "profit-push" doctrine.

25. Explain why in the absence of increases in demand even a protected legal monopolist, while almost certainly charging very high prices, would not charge continually *rising* prices.

26. Explain why even if a protected legal monopolist were faced with a rising demand for his particular product, no rise in the general consumer price level would be present in the absence of a rise in *aggregate* demand.

27. Explain why, apart from the case of protected legal monopolists, the normal operation of the profit motive is steadily to *reduce* prices, not increase them.

28. Explain how an increasing quantity of money and rising aggregate demand creates an association between rising prices and higher nominal profits.

29. Explain and illustrate what is meant by the "crisis-push" doctrine.

30. Explain why, in the absence of increases in the quantity of money and aggregate demand, supply crises while causing dramatic increases in the prices of some goods, would result in numerous price reductions, including reductions in prices that constitute costs of production.

31. Explain why any given supply crisis is unable to explain more than a one-time delimited rise in the general consumer price level.

32. Explain why, in the absence of increases in the quantity of money and aggregate demand, any given supply crisis should usually be expected to be followed by a reduction in the general consumer price level, probably all the way to the point of where the price level was before the crisis. Also explain why the public generally does not expect such a result.

33. "In order to explain a rising price level on the basis of supply crises, one would have to find not only replacement crises for the ones that have been solved,

but additional crises as well. And in the next year, one would have to find replacements for this larger number of crises, along with still more additional crises; and this would have to go on from year to year at a compound rate." Discuss.

34. Name the two errors of the crisis-push doctrine and their underlying error in thinking.

35. Explain what is meant by the wage-price spiral.

36. Explain why, in the absence of increases in the quantity of money and aggregate demand, any wage-price spiral would quickly burn itself out. Illustrate your answer in terms of the experience of the early 1980s with respect to the provisions of union contracts.

37. Explain what is meant by the "velocity" doctrine.

38. Describe the relationship of the velocity doctrine (a) to the role of the increase in aggregate demand in raising prices and (b) to the role of the increase in the quantity of money in raising prices.

39. Explain why increases in velocity caused by factors other than the increase in the quantity of money are unlikely to result in increases in the general consumer price level.

40. Briefly describe the four ways in which increases in the quantity of money operate to raise velocity and thereby further contribute to the rise in prices.

41. Explain why all that is required than to reduce velocity is to cut back on the rate of increase in the quantity of money.

42. What has happened to velocity since the early '80s. Why?

43. "The intellectual zone of explanation previously claimed by the velocity doctrine should henceforth be regarded as annexed by the quantity theory of money." Discuss.

44. Explain what is meant by inflation psychology.

45. Explain what causes inflation psychology.

46. Explain how inflation psychology operates from the side of supply and what the limits of such operation are.

47. Explain how inflation psychology makes inflation into a cause of unemployment.

48. Explain what is required to eliminate inflation psychology.

49. Explain why the elimination of inflation psychology may need to be accompanied by a financial crisis.

50. Explain why inflation psychology would not be a problem under a gold standard.

51. Explain what is meant by "the credit card doctrine."

52. Explain how the use of credit cards serves actually to *reduce* the velocity of money rather than increase it, despite the fact that people no longer need to hold as much currency as they otherwise would.

53. Explain why insofar as the possession of credit cards may contribute to a rise in velocity, by representing guaranteed lines of credit, the rise in velocity is to be attributed to the ability of the banking system to increase the quantity of money. (In your answer, be sure to explain what has made possible the widespread granting of such substantial lines of credit and to distinguish between the effect of lines of credit extended on the basis of accumulated savings and lines of credit extended on the basis of the ability to increase the quantity of money.)

54. Explain what is meant by the consumer-installment credit doctrine.

55. Explain under what circumstances the granting of credit (whether consumer-installment credit or otherwise) does not serve to increase aggregate demand and under what circumstances it does serve to do so.

56. Explain why the incurrence of debt is not inflationary in and of itself.

57. Explain what is meant by the consumer-greed doctrine.

58. Explain what is wrong with the consumer-greed doctrine with respect to
   a. overgeneralization,
   b. its assumption concerning the connection between "greed" and the demand for money for holding, and
   c. its assumption concerning the effect of the desire for a higher standard of living on prices.

59. Explain what is required to make "consumer greed" translate into a lower demand for money for holding rather than a higher demand for money for holding.

60. "As far as the explanations of rising prices other than the quantity theory of money contain any kernel of validity at all, it is only as an extension of the quantity theory of money." Discuss.

61. Explain why the undue increase in the quantity of money, which is what underlies the rise in prices, is the result of government action.

62. Explain why all of the knowledge concerning the cause of rising prices presented in this book can be summarized in a definition of inflation as *an increase in the quantity of money more rapid than the increase in the supply of gold and silver*, which is to say, *an increase in the quantity of money caused by the government*.

63. Contrast the definition of inflation in the preceding question with the definition as rising prices, with respect to:
   a. the information conveyed concerning the cause of rising prices
   b. the ability to understand the causation of the full range of symptoms associated with inflation
   c. the ability to distinguish between rising prices caused by more demand and rising prices caused by

less supply
d. the information conveyed about how to stop inflation
e. the ability to raise further questions about the causes and effects of inflation

PART B. THE DEEPER ROOTS AND FURTHER EFFECTS OF INFLATION

1. Explain the nature of the connection between inflation and government budget deficits.

2. Explain why government budget deficits in and of themselves are not inflationary.

3. Explain what is required to make government budget deficits inflationary.

4. Explain why under a gold standard, government budget deficits can actually be deflationary.

5. Explain how inflation could go on while the government operated with a budget surplus.

6. Explain why only the budget deficit of the federal government can be inflationary at the present time, not those of state or local governments.

7. Explain how the ability of the federal government to create new and additional money prevents it from going bankrupt in the technical sense no matter how large its debt becomes.

8. Explain why, despite the previous question, the federal government has probably long been bankrupt in the sense of an inability to repay its debt in terms of the same purchasing power in which the debt was contracted.

9. Explain why depriving the government of the power to inflate the money supply—i.e., establishing a gold standard—is essential to its operating with balanced budgets.

10. Describe the motives and rationale for budget deficits and inflation under the following headings:
   a. the welfare state,
   b. inflation and war finance,
   c. inflation and the "easy money" doctrine,
   d. inflation as the alleged cure for unemployment.

11. Explain the underlying influence of the socialist ideology in your answers to the preceding question.

12. Explain how the government's ability to inflate the money supply destroys peoples' understanding of the fact that the government is supported by them and leads them to believe instead that they are supported by the government.

13. Explain how the government's ability to inflate the money supply has contributed to the growth in the size of the government relative to the economic system.

14. Explain why the practice of inflation and budget deficits is in conflict with the principle of representative government.

15. Explain how inflation operates to redistribute wealth and income. In your answer, be sure to include a discussion of the differing effects of inflation on those whose selling prices and incomes rise relatively early and those whose selling prices and incomes rise relatively late.

16. Explain how those who introduce the new and additional money gain at the expense of others.

17. Explain why the poor and the elderly are among the worst victims of inflation.

18. Explain how inflation makes the traditionally safest types of investments the least safe.

19. Explain what the safety of fixed income or asset investments comes to depend on under a fiat paper money system.

20. Explain how in making the traditionally safest types of investments the least safe, inflation undermines capital formation.

21. Explain how inflation operates to increase the effective rate of taxation on business investments. Illustrate your answer in terms of the effect on profits earned on inventories and profits earned on investment in plant and equipment.

22. Explain how inflation operates to raise the effective rate of taxation on interest incomes.

23. Explain how inflation operates to raise the effective rate of taxation on capital gains.

24. Explain how inflation contributes to the decline of the government-managed infrastructure.

25. Explain and illustrate what is meant by the prosperity delusion of inflation, and how it contributes to overconsumption and the undermining of capital.

26. Explain how even after people stop regarding themselves as enriched by inflation, inflation continues to promote overconsumption.

27. Show how inflation transfers wealth from lenders to borrowers in the case of home mortgages, and why this contributes to overconsumption.

28. Explain how inflation in the form of credit expansion operates to reduce the rate of interest relative to the rate of profit, while at the same time operating to raise the rate of interest.

29. Explain what is meant by malinvestment and how the situation described in the preceding question fosters malinvestment.

30. Explain and illustrate how inflation in the form of credit expansion makes investments that actually lose in real terms appear to be profitable nonetheless, and to be profitable in fact to some investors.

31. Describe the kind of malinvestment that von Mises attributes to credit expansion.

32. Explain how malinvestment further impairs capital formation in reducing the efficiency with which existing capital goods are used.

33. Explain how the existence of malinvestment confirms the proposition that inflation does not raise all prices at the same time and to the same extent.

34. Explain what is meant by the withdrawal-of-wealth effect and the ways in which it contributes to the undermining of capital formation.

35. Describe the ways in which inflation operates to reduce the real rate of return on capital at the same time that it impairs capital formation.

36. Explain why the fact that inflation reduces the real rate of return on capital as such implies that the gains of debtors resulting from inflation are less than the losses of creditors. (Illustrate your answer with examples drawn from malinvestment in inventories and housing.)

37. Explain how inflation operates to impoverish wage earners by virtue of its effects on the productivity of labor and on the so-called distribution factor. In conjunction with your answer, explain the effect of inflation on

a. the demand for capital goods relative to the demand for consumers' goods and the degree of capital intensiveness in the economic system
b. the efficiency with which existing capital goods are employed
c. the demand for labor relative to the demand for consumers' goods

38. Explain why efforts on the part of labor unions to resist the fall in real wages caused by inflation result in unemployment.

39. Explain how in the long run inflation operates to prevent common stock prices from keeping pace with the prices of consumers' goods.

40. Explain how inflation gives rise to the phenomenon of an inflationary depression—i.e., a rapidly increasing quantity of money and rapidly rising prices accompanied by widespread insolvencies and bankruptcies.

41. Explain how inflation, especially in the form of credit expansion, sets the stage for a financial contraction and deflation. In your answer, be sure to explain

a. how inflation brings about an increase in the volume of spending and in sales revenues and incomes that is more than proportional to the increase in the quantity of money
b. the effect of inflation on the degree of liquidity in the economic system, i.e., on the ratio of cash holdings to current liabilities
c. how inflation, especially in the form of credit expansion, encourages the incurrence of debt
d. what must happen, in view of your answers to the preceding questions, to the demand for money for holding and to the ability to repay debts if and when inflation stops
e. what can happen to the solvency of banks and thus to the quantity of money, in view of your answer specifically to the previous part of this question

42. Explain how the ending of inflation can result in numerous investments suddenly becoming loss making, even before a major decline in demand sets in.

43. Explain how the stoppage of credit expansion results in a "credit crunch" and in an increase in the demand for money for holding.

44. Explain how the mere slowing down or failure of credit expansion to accelerate sufficiently can result in a credit crunch.

45. "The failure of inflation to accelerate sufficiently can also cause the demand for money for holding to increase, and thus velocity to decrease, insofar as the demand for money for holding has become unduly low based on the expectation of a more rapid acceleration of inflation than turns out to be the case." Discuss.

46. Explain why in order to produce a credit crunch and the onset of a depression, it is not necessary that credit expansion result in an actual rise in wage rates and materials prices.

47. Explain what is meant by gold clauses.

48. Explain why under a fractional reserve gold standard, inflation of the supply of paper money that is redeemable on demand in gold can lead to a *reduction* in the quantity of money insofar as it is considered as the equivalent of gold, and thus to a reduction in the ability to repay debts containing gold clauses.

49. Explain how in the conditions described in the previous question, efforts to increase the supply of money, and the prospect that they will succeed in the future, can bring about a reduction in the quantity of money in the present.

50. Explain why the policy of the Hoover Administration of running what for the time were major budget deficits, and the policy of the Federal Reserve of attempting to increase the supply of dollars in order to reduce interest rates and to finance the deficits, may have served to intensify the deflation and depression of the early 1930s.

51. Explain how the policy of inflation and consequent devaluation against gold may have served to reduce the volume of international trade in particular in the early 1930s.

52. Explain the effects of an increase in the supply of Mexican pesos that causes a more-than-proportionate devaluation of the peso against the dollar on the ability of Mexican firms to pay their dollar debts. Does such an increase in the supply of pesos represent a deflationary inflation?

53. Explain why, indirectly, inflation and credit expansion must be blamed for the mass unemployment that results from financial contraction, deflation, and depression.

54. "Given the existence of inflation, it is true that its

continuation and acceleration can forestall the development of mass unemployment. But this no more makes inflation a means of preventing unemployment than narcotics are a means of preventing sickness and debilitation." Discuss.

55. Explain why in the face of the existence of strong monopoly labor unions, inflation is ineffectual as a remedy for existing unemployment.

56. Explain why those who are reemployed on the various make-work projects that almost always accompany any attempt to eliminate unemployment by means of inflation, are employed at a loss to the rest of the population.

57. Describe the special conditions in which a resumption of inflation can achieve substantial reemployment.

58. Describe the negative features of such a policy.

59. Describe an alternative means of achieving reemployment.

60. Explain why the resumption and continuation of inflation is bound to be accompanied by substantial unemployment sooner or later.

61. Explain how it is possible for mass unemployment to come into existence in the midst of major inflation, e.g., for an unemployment rate of 25 percent, to come into existence alongside an annual rate of price increases of 50 percent.

62. Describe the ultimate limit of accelerating inflation.

63. Describe the three stages that inflation goes through according to von Mises before reaching its ultimate limit.

64. Explain why, in the absence of an acceleration of inflation, there must be a fall in the rate of increase in spending.

65. Explain why, in the absence of an acceleration of inflation, there must be a fall in the rate of profit.

66. Explain why, in the absence of an acceleration of inflation, the gains experienced by debtors at the expense of creditors as the result of inflation wear off.

67. Explain why the underlying premises of the welfare state, which lead to the policy of inflation in the first place, logically call for more and more rapid inflation as time goes on.

68. Explain the role of inflation in fostering the belief that Washington, D. C., a city that is economically insignificant in terms of what it produces or contributes to production, is nevertheless capable of bailing out the economies of such major cities as Detroit, Newark, and New York, indeed, the economies of entire states and multistate regions.

69. Explain and illustrate how inflation comes to be demanded as the means of solving problems largely created by inflation. Be sure that your answer covers the following matters:

a. rescues and bailouts
b. government aid to the elderly
c. government aid to the mortgage market
d. the government's real revenues
e. papering over credit crunches and profit squeezes

70. Explain how recessions can serve as inflationary fueling periods.

71. "Price indexing does not provide any means for dealing with the problem of lags between the rise in the prices one must pay and the prices or income that one receives. At most it can enable an individual to catch up with the rise in prices. But it does not compensate people for the loss of purchasing power they experience in the intervals before catching up." Discuss.

72.

a. Name the leading areas in which price indexes are currently in use in the United States.
b. Name some additional areas that are likely candidates for the use of price indexes in the future.
c. Explain how in all of these areas the use of price indexes operates to make inflation accelerate.

73. Describe the operation of the "wage ratchet" in connection with the acceleration of inflation.

74. Describe the operation of the "interest ratchet" in connection with the acceleration of inflation.

75. Explain the limits of the interest ratchet and why, when they are reached, the potential is created for a quantum leap in the rate of inflation.

76. Explain what brought about the deceleration of inflation in the 1980s.

77. Describe the effects of the deceleration of inflation on the real estate market and on related financial institutions.

78. Explain the effect of the deceleration of inflation on inflation psychology.

79. Explain why the reacceleration of inflation from 1982–1987 was accompanied by a greater desire to own balances of money than had existed in the late 1970s.

80. Explain how the effect of the very sharp reacceleration of inflation in 1985 and 1986 served to defeat the purpose of those who had advocated the reacceleration in order to reduce the foreign exchange value of the dollar.

81. Describe the changes in money supply increase that precipitated the severe recession of 1990-92.

82. Explain why, on the basis of the factors determining the demand for money for holding, in the absence of a renewed substantially more rapid rate of increase in the money supply in the years 1991–93, the economic system would likely have gone into a major depression.

83. Explain why the very rapid increases in the quantity of money in 1991–93 drove short-term interest rates to levels not seen since the 1950s.

84. Describe the two camps into which government policy makers divided in response to the recession of 1990–92.

85. "The government's response to the depression or near-depression of 1990–1992 confirms that recessions and even virtual depressions nowadays do indeed represent inflationary fueling periods." Discuss.

86. Is the Federal Reserve System a private institution or a government agency? Discuss.

87. How rapidly must prices be rising for an administration to have substantial political support for reducing inflation at the risk of a double digit unemployment rate? Discuss.

88. To what extent can prices be expected to rise on a compound annual basis over the next decade? Discuss.
  a. Describe the factors making for a more rapid rate of increase.
  b. Explain what is necessary to restrain those factors.
  c. Can the government be expected to continue to do what is necessary to prevent the reappearance of growing inflation psychology?

89. If the government were willing to do what is necessary to prevent such reappearance, how would the situation differ from the pre–New Deal days in which limited inflations were always brought to a sharp halt and followed by a depression?

90. Continuing the preceding question, is any fundamental difference introduced by virtue of the government's present ability to go on increasing the quantity of money indefinitely, at any rate it deems necessary, whereas it lacked such ability under the fractional-reserve gold standard of the pre–New Deal days? Discuss.

91. Explain how if inflation were to accelerate out of all bounds, it would end up destroying the existing monetary unit.

92. Describe the conditions under which if inflation were accelerated to the point of destroying the monetary unit, it could destroy the existence of money as such, and what the consequences would be for the existence of the division of labor and all that depends on the division of labor.

93. State and discuss the leading historical example of the destruction of money and the resulting consequences.

94. Explain what conditions must be present in order to introduce a new monetary unit to replace a monetary unit that has been inflated out of existence.

95. While a new mark could be introduced following the German hyperinflation of 1923, on the basis of convertibility to the dollar, it might not be possible to introduce a new dollar on the basis of convertibility to the mark or yen if the United States were to experience hyperinflation. Discuss.

PART C. GOLD

1. Explain how the widespread ownership of gold and silver coins would serve as a guarantee against the destruction of money as the result of hyperinflation.

2. Explain why if not prevented by government interference, inflation at the rate experienced in the United States in the 1970s leads to the growing ownership of precious metals. In your answer, be sure to explain why inflation at such a rate deprives the customary forms of investment, including common stock ownership, of their real profitability.

3. Explain how in the absence of government interference to prevent it, inflation operates to bring about a spontaneous remonetization of the precious metals.

4. Describe what it would be necessary for the government to do or avoid doing that would foster the spontaneous remonetization of the precious metals. Your answer should cover the following aspects:
  a. the taxation of transactions in precious metals
  b. the enforceability of contracts payable in precious metal
  c. the importation of precious metals
  d. the ability of merchants to practice discrimination between paper money and precious metal coins of the same face value

5. "Fiat money can be maintained in existence only by the forcible suppression of the competition of gold." Discuss.

6. Explain why the requirement that paper money be redeemable in gold at a fixed, known rate is not a form of price control.

7. Describe positive measures the government might take with respect to the following, that would foster the remonetization of the precious metals:
  a. the minting of precious metal coins
  b. the collection of taxes
  c. the sale of government assets
  d. the protection of creditors from large-scale depreciation of the paper money

8. Present the case for a 100-percent-reserve gold standard in terms of its ability to prevent both inflation and deflation. In your answer, be sure to explain
  a. why the falling prices that would probably exist under the standard, would not be deflationary either with respect to the height of the rate of profit or with respect to the ability of business firms and individuals to repay their debts and
  b. why the 100-percent-reserve gold standard would actually serve as the strongest possible guarantee against deflation on the basis of its effect on the possibility either of sudden substantial increases in the demand for money or sudden substantial decreases in the supply of money.

9. Explain why adopting a fractional-reserve gold standard, in order to enable the quantity of money to grow more rapidly than the quantity of gold, implies the need for an ever declining fractional gold reserve.

10. Explain why the rate of increase in the supply of gold itself is likely to be greater under a 100-percent-reserve system than under any fractional-reserve system in which the fraction of gold is fixed.

11. Describe the effects of a 100-percent-reserve gold standard on
   a. the risk of currency depreciation on the part of countries that had it
   b. international investment
   c. the possibility of government budget deficits
   d. the size of government
   e. the frequency and duration of wars
   f. the risk of arbitrary redistribution of wealth and income
   g. saving and investment
   h. the taxation of profit and interest income

12. Contrast the 100-percent-reserve gold standard with a fractional reserve gold standard in terms of conformity to the law of the excluded middle as to whether a given sum in the possession of a bank depositor or note holder represents cash held at the bank or a loan made to the bank.

13. Explain the argument that legislation requiring 100-percent-reserve banking in connection with checking deposits and banknotes would not constitute government interference, but only an exercise of the government's proper powers.

14. Discuss the claim that fractional-reserve banking and the issuance of fiduciary media increase the volume of capital and credit that exists in the economic system. Present the arguments for reaching the opposite conclusion and show how, even if the claim were correct, any loss of capital and credit entailed in the abolition of fiduciary media could be far more than compensated for by reduction in the national debt.

15. Explain why a 100-percent-reserve gold standard implies an important monetary role for silver and some significant role for subsidiary token coins.

16.
   a. Explain why the modest issue of fiduciary media is required in connection with the issue of subsidiary token coins, such as pennies and nickels.
   b. Explain why the effect of fiduciary media in this case is not to reduce the value of the precious metals, but, if anything to add somewhat to their value.
   c. Explain why no significant credit expansion could occur in connection with the issue of fiduciary media in this case.

17. Explain how the adoption of a 100-percent-reserve gold standard at a sufficiently high price of gold could serve to end inflation once and for all and, at the same time, prevent a major depression from developing as the result of the sharply higher demand for money for holding that would result from the cessation of all further inflation.

18. Explain the potential danger in connection with the U.S. first obtaining a disproportionate share of the world's gold and then losing back a major portion of it, and how the dangers could be avoided.

19. Explain how the adoption of a 100-percent-reserve gold standard at a sufficiently high price of gold would both establish a high degree of financial liquidity and reduce the burden of debt in the economic system.

20. Describe the connection between the high degree of financial liquidity that establishment of a 100-percent-reserve gold standard could achieve and the ability to bring to carry out the large-scale reduction in government activity and spending entailed in dismantling the welfare state. In your answer, be sure to explain the important parallel provided by the experience of the immediate post–World War II era, and why this time the positive results of could be even more dramatic.