FREEDOM AND ECONOMIC GROWTH

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"People must come to accept private enterprise not as a necessary evil, but as an affirmative good."

—EUGENE BLACK
President, World Bank

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IS SOCIALISM THE ANSWER?

Prof. G. Carl Wiegand*

Millions go hungry in Asia, Africa and Latin America not because the world cannot produce enough rice and grain, but because the leaders of mankind are blinded by ideologies and a strange confusion of values. Neither capital nor natural resources assure economic growth.

Switzerland is poor in natural resources and its climate is harsh, yet the Swiss enjoy one of the highest srandards of living in the world, thanks to a happy combination of hard work, private initiative, a high regard for privaie property rights, and a well developed sense of social responsibility. Brazil, on the other hand, which in terms of natural wealth is potentially one of the richest countries in the world, is heavily dependent upon foreign aid, and more than 50% of the Brazilian people suffer from malnutrition.

The German "miracle,"—the rise within 15 years from utter devastation to a high degree of prosperity—was not the result of foreign aid, which actually amounted to less than the billions carried away in the form of reparations, nor of natural resources, but of sound economic policies and a strong belief in private initiative and personal freedom, a conviction which was slowly and painfully acquired during fifteen years of economic regimentation.

What makes Malaya prosperous and keeps the Indonesian masses near the starvation level? Both countries are

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rich in tin, rubber and oil, but Malaya's currency is stable and the country attracts foreign investments, while the Indonesian Rupiah sells in the free market at about 25% of its official value. Malaya believes in economic freedom and respects private property right;, while Indonesia hampers private initiative, nationalises or confiscates private property, and in the end fails to carry through its grandiose economic blueprints.

One hundred and fifty years ago, India was richer and economically more developed than Japan. The opposite is true today. During the past decade alone, Japan's national income increased three times as fast as that of India. Can this difference really be explained only by the fact that India lived for almost 200 years under British colonial rule, while Japan was able to retain her independence?

Five hundred years ago, the great nations of Asia were more powerful and far richer than the nations of Europe. Yet 200 years later the Europeans were well on their way to make themselves the master:: of five continents. The world was not conquered by superior resources and greater fighting power, but by a new spirit of private initiative, of respect for hard work and for material values. which Europe had not known during the Middle Ages, and which much of the world lacks today.

How can the people of Asia, Africa and Latin America capture the secret which has made possible the economic and social advance of Europe and North America during the past 150 years? They cannot import socio-economic systems like potted plants and expect them to grow. All they can hope for is to gather the seeds of carefully selected ideas, plant them in their own soil and slowly raise a new plant, a combination of proven foreign ideas and indigenous strength. Foreign influences can be stimulating, but they can also have a sterilizing effect. An imported machine civilization can easily destroy traditional cultural values, and in the end produce social chaos and economic stagnation rather than material progress. Japan did not copy Europe. It assimilated certain ideas and forms and shaped them to

its own needs. Free enterprise, capitalism and economic progress are not based on "cocacolanization."

Far more dangerous for an underdeveloped country, than an attempt to copy too literally economic institutions which proved effective in the socio-economic development of other countries, is the tendency among many foreign economic advisers of today and the leaders of many under-developed countries to promote ideas, which, although politically expedient from the point of view of the ruling politicians, have proven conspicuous failures in the more developed countries, and which are manifestly inapplicable to underdeveloped countries. This holds equally true of the totalitarian brand of economic planning, which has turned one-third of the world into an ill-fed prison, as well as of the Keynesian and welfare state types of socialism which have retarded the economic recovery of post-war Britain, and, in more recent years, have been chiefly responsible for the relative decline in economic strength of the United States.

Totalitarianism and welfare state socialism promise economic growth and "freedom from want." Yet neither can achieve both, and in the end both may prove unable to provide either, because both philosophies spring from a basic misunderstanding of human nature. Men is more than an economic being which can be satisfied in the long run with bread and circuses. The communists boast of the rapid industrialisation of Russia, but fail to mention the continued poverty of the masses and the suppression of basic freedoms. The welfare state advocates speak of "freedom from want" as a basis for democracy and a shield against communism, and seemingly fail to see that their slogan involves a semantic confusion, because they do not really believe in "freedom," but rather in a policy under which the individual surrenders his freedom in return for economic security provided by a more or less powerful state. This is obviously not a new idea, even though it is presented as such to the historically illiterate masses of the 20th century. The same desire for economic security which we witness today prevailed during the troubled years of disintegration of the Roman empire, and developed gradually into the system of feudalism and serfdom of the Middle Ages. The slaves and serfs of yesteryears, if theirs was a good master, enjoyed a considerable degree of economic security. But good masters have a tendency of turning into tyrants, and who assures the moderu would-be serf that his new master, the all-powerful state, will remain benevolent. The millions of kulaks killed in the course of Stalin's economic reforms, and the twenty m on Chinese who perished as part of the cost China paid for its industrialisation are silent and gruesome monuments to the new philosophy of "freedom from want." No one enjoys greater economic security than the inmate of an American jail, who has been sentenced to life imprisonment. All his material needs are looked after by state. But how many people in the underdeveloped countries would trade their personal freedom, however desperate their economic misery, for the relatively high standard of living of an American prison?

To expect the totalitarian state to increase materially the average standard of living is contrary to all logic, even if Russia did not provide ample evidence against this naive faith in totalitarian benevolence. Like any organism, the leviathan state must continuously add to its own power: guns instead of butter; moon-rockets instead of adequate housing. Because of its very nature, the total state cannot permit the individual to grow in either personal freedom or economic strength.

All this is different, we are told, in the case of the socialistic welfare state, as if Fabian socialism had not been disproven by the post-war socialist experrments of the British Labour Party, from which the British economy has not fully recovered to this day. Intellectuals throughout the world like to challenge the ethics of free enterprise, which are supposedly based on greed and an asocial selfishness, and to uphold the, ethics of socialism. But quite aside from the utter failure of socialism to provide the economic progress it promises, its ethical arguments are based on an illusion. Socialism has all the weaknesses and none of the strength of either totalitarianism or free enterprise. While it lacks

the brutality of the totalitarian state, it also lacks its strength which makes possible forced economic growth at the expense of individual freedom and wellbeing. On the other hand, socialism paralyzes the dynamic powers of free enterprise, which during the 19th ceniury provided Europe with a rapidly rising standard of living, a tremendous increase in economic power, and an unprecedented expansion of personal liberties. The modern socialists no less than the advocates of communism are the 20th century followers of Mobbes, the great defender of 17th century absolutism, who argued, just as the modem planners argue today, that man is inherently asocial and unable to use his purchasing power rationally, so that we need a strong stale to curb the individual and regulate production and consumption.

Nor will the socialists, statist-interventionists and economic planners learn from the failures of their past cxperiments. They are like the man who believed that he could fly, but broke a leg when he jumped from a secqnd storey window. "I just didn't have enough altitude," he argued. and when his leg had healed, he jumped from the sixth floor and was killed. When a billion dollars spent on some economic experiment proves an utter waste of money. the economic planners assure the voters that they would succeed. if they could only spend ten billion dollars.

By far the largest recipient of American aid is not India, Korea, or any other underdeveloped country. but the highly mechanised and scientifically operated American farm industry. In the 1961-62 fiscal year alone farm subsidies will amount to $5 bill., compared with the total net income of American farmers, including the subsidies of $12.7 bill in 1961. But government aid, planning and steadily increasing regimentation has not cured the ills of American agriculture. Here is what the President of the American Farm Bureau Federation, one of the two large farm organisations in America, has to say: "America has been known as the land of opportunity, but opportunity depends upon freedom and freedom means individual responsibility—not the rule of force by government. The government interventionist abandons freedom of choice because he is contemptuous of the ability of individuals to know what is best for them The result is that those who favour government intervention soon recognise the market price system as their principal target and'set out to replace it with price fixing and controls."

Mahatma Gandhi realised the dangers of the all-powerful state, when he wrote: "While apparently doing good by minimising exploitation, the state does the greatest harm to mankind by destroying individuality which is the root of all progress. The state represents violence in a concentrated and organised form. . . The state is a soulless machine; it can never be weaned from violence to which it owes its very existence." Nor did Gandhi believe in the planned socialist state: "Controls give rise to fraud, suppression of truth, intensification of the black market and to artificial scarcity. Above all, it unmans the people and deprives them of initiative; it undoes the teaching of self-help they have been learning for a generation. It makes them spoonfed." How different Prime Minister Nehru: "Without social freedom and a socialistic structure of society and the state, neither the country nor the individual could develop. . . . . A real government by the people and for the people can only be established when the masses hold power, that is under socialism when all the people really share in the government and wealth of the country."

Mr. Nehru's philosophy—and this philosophy is shared by many American economists and politicians—rests on two false premises: that a totalitarian or socialist state is actually a "people's republic" in which the people have a choice; and that the people, rather than the ruling bureaucracy,—or the state as a moloch—enjoy the wealth of the country.

Collectivism is nothing new. It was overthrown in Europe and North America in three bitter struggles: the Glorious Revolution of 1688 in England, the American Revolution of 1776, and the French Revolution of 1789. In each case, the power passed from the ruling aristocracy and its proliferating bureaucracy to the entrepreneurial middle class, and it was this step which precipitated the rapid economic growth of Europe and North America. Modern totalitarianism and socialism have all the earmarks of the European absolutism and mercantilism of 300 to 400 years ago the replacement of social conscience by jingoistic nationalism, the gloriiication of the state, the contempt for the individual, the disregard for agriculture, the emphasis upon fiscal and monetary manipulations, a naive economic pragmatism which neglects economic forces.

The very same ideas which Europe and North America had to defeat before their economies could develop. are presented today to the underdeveloped countries, including India, as the recipe by which to achieve economic growth.

THE REAL PATH OF ECONOMIC DEVELOPMENT

Few nations have been successful in developing an industrial system until they were able to produce agricultural surpluses. The industrial revolution of England followed and coincided with a rapid development of agriculture. The farm surpluses necessary to feed the growing industrial population require a gradual change from a primitive local self-sufficiency to the production of marketable surpluses. Land reforms, which are at present widely advertised as the solution of Latin America's problems, may or may not meet the needs of increased production. When the large estates of eastern Germany, which due to scientific farming and centuries of careful tending produced before the war large surpluses, were distributed among the workers and deserving party members, the production dropped sharply, and before long the communist regime found it necessary to unite the individual farms into cooperatives with the peasant, like the serf of yester-years, prohibited from leaving the land. In theory, the new collectives could have been operated as efficiently as were the former private estates, but in reality they are not, and eastern' Germany, which was a good exporter before the war, is now dependent upon food imports despite a sharp decline in the total population and in the **per capita** consumption.

The tendency in underdeveloped countries to overlook the importance of agriculture as a basis, if not a prerequisite for industrial and economic growth in general, is in part at least the result of a prejudice dating from the colonial rule. The new nations no longer wish to be merely the producers of raw materials, the handmaidens of industrial nations. Dr. Raul Prebisch, one of Latin America's best-known economists, has built a whole theory of economic development upon this assumpttion, forgetting completely that until the end of the last century, the major portion of United States

exports consisted of two farm products: cotton and wheat, and that even today farm exports account for about one-fourth of United States exports. The expansion of farm production even during decades of declining prices, did not prevent, but actually made possible the industriaiisation of the United States.

Since the United States is today the most highly industrialised and mechanised nation and enjoys the highest standard of living, the leaders of many underdeveloped nations jump to the conclusion that their economic problems can be solved if they can only build enough modern factories. This is a dangerous illusion. The steel production does not necessarily determine "the tempo of progress of the economy as a whole", as India's Second Five-Year Plan assured. The demand for steel is not self-generating, neither is the demand for machinery. Industrialisation requires a peculiar type of skilled worker, quite different from the skilled artisan, and a market for finished industrial products. Neither can be developed overnight, and stronger the cultural ties of a peasant-handicraft culture, the greater the difficulty of producing modern industrial workers and demand for machine-made products. Europe required centuries to achieve the transition. To speed this cultural process through government fiat, as the totalitarian countries have attemped, causes a profound cultural shock and indirectly retards economic development.

The case against heavy industries, created by the government and financed through heavy taxation or inflation, is particularly obvious in India with its very large supply of cheap labour, and its acute shortage of investment capital. Economic logic calls, for the time being at least, for labour rather than capital-intensive industries. It requires at least $10,000 in capital investments to provide one job in an automated steel plant, compared with $ 100 to $ 200 in cottage industries. Some 100,000 steel plows at $ 20 each will do far more for India's economic development than a $2 million machine tool.

This raises the whole problematic question of capital formation and investments. One may well question a recent statement by one of India's highest government officials that "there is only one factor of growth missing, and that is capital." Even though capital is admittedly important, the lack of certain psychological, cultural and social prerequisites is probably a far more critical and difficult handicap. There are four ways in which investments can be financed: through private savings, private foreign investments, government funds obtained through taxation or through the printing press; and finally through foreign aid or inter-government loans. It is a widely held misconception that the four are complementary. The inter-American "Alliance of Progress" is based on this illusion. The four sources of investment capital can be complementary under ideal conditions, but in reality they are often mutually destructive. Private domestic capital formation and private foreign investments go hand-in-hand. Traditionally one depends upon the other. Public investments, on the other hand, whether financed through taxation or through inflation, are likely to hamper—contrary to post-Keynesian doctrine—both private capital formation and private foreign investments, unless great care is taken not to undermine private capital formation through heavy taxation and to discourage private investments through direct government competition. Unfortunately, modern economic planners are rarely satisfied to use public funds to prepare the basis on which a private economy can develop. Instead of building roads, schools, irrigation systems, and enforce social and economic order, modern economic planners build steel mills and power plants in direct competition with private enterprise, and yet they wonder why private enterprise seeks greener pastures in other countries.

Foreign aid can provide a sound basis for economic development, but the temptation of inter-governmental loans being used to expand the public sector at the expense of the private sector is obvious. The leaders of many underdeveloped countries and certainly many American experts, trained in Keynesian theories and raised in the spirit of the "New

Deal," are basically distrustful of private enterprise and too impatient to permit the development of a free economy by logical stages. They build steel mills before the peasant has learned to use a steel plow, they build super-highways instead of all-weather feeder roads even though the price of the cheapest car is equal to the average **per capita** income for ten years. When Mexico, and more recently Colombia, nationalised the remaining private power plants, in which American investors held a substantial stake, the foreign exchange needed to pay off the American owners was obtained through a loan from Washington. Instead of being used to build more power plants, American aid was used to spread socialism. Why should private investors, under such circumstances, risk their capital?

Investment policies in underdeveloped countries suffer from a basic defect in economic reasoning. Instead of starting with the available resources and planning their most effective allocation, much of what passes as economic planning in underdeveloped countries is concerned with production goals, usually far beyond the available supply of capital and skilled workers. While there is an old saying that some men succeed better than others because they attempt more, and the fraudulent check-passer may succeed better for a while than is more honest neighbour, in the long run he is likely to get into trouble; and inflating the currency in order to achieve utopian production goals, like passing bad checks, is a form of fraud, as the two great scholastic writers, Buridan and Oresme already warned more than 500 years ago. Nor does inflation pay in the long run. It hampers private capital formation, drives existing private capital abroad or into sterile treasure hoards, and scares away foreign investors.

Of all the dangerous socio-economic theories which have found wide currency in recent years, probably the most deadly is the idea, which always appeals to spend-happy politicians, that a nation need not worry about the effect of rising prices on the balance of payments as long as the national income continues to grow at a rapid rate. As

THE ECONOMIST wrote recently: "One cannot believe the governments of the United States and Britain will labour under artificial and irrational restraints on their economic growth,"—meaning,,the maintenance of a sound balance of payments position. In order to import machinery essential to economic growth, underdeveloped countries must export and they will find their foreign markets vanishing, if their prices rise above world market prices. The "growth-through-inflation" formula is undermining the strength of the United States, and it makes impossible the economic development of India except on a totalitarian basis and at a cost in human dignity and well-being far greater than even Mahatma Gandhi could have anticipated when he called the state a "soulless machine' which "can never be weaned from violence."

The views expressed in this booklet do not necessarily represent the views of the Forum of Free Enterprise.

"Free Enterprise was born with man and shall survive as long as man survives."

—A. D. SHROFF

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