

BOOKS

How the Dismal Science Got Its Name: Classical Economics and the Ur-Text of Racial Politics

by David Levy

University of Michigan Press • 2001 • 320 pages
\$52.50 hardcover; \$21.95 paperback

Reviewed by Karen I. Vaughn

For about a century and a half, economics has been known as the “dismal science.” While perhaps few remember that it was Victorian writer Thomas Carlyle who coined the term, the phrase invokes sympathy from those who find economic theory difficult and mundane. What most people do not appreciate, however, is the reactionary, even abhorrent context within which Carlyle made his famous pronouncement.

In this important book, David Levy provides an exhaustive and authoritative account of that context. Levy exposes a shocking truth: the Victorian literary opposition to political economy had less to do with the dreariness of economic theory than it had with the consequences of the free-market economy. That is, these Victorians (including in addition to Carlyle, John Ruskin and, to some degree, Charles Dickens) despised the flourishing of a market economy because it provided more goods to the lower classes and fostered equality of persons regardless of class or race.

Levy’s thesis is as surprising as it is provocative. Generations of students have been taught that the Victorian critics of capitalism were the good guys, the defenders of the working class against the cruelties of early capitalist exploitation. By calling attention to the miserable condition of the working classes in Britain through essays, letters, and novels, they were demonstrating a humanitarian concern absent among economists of their day. Levy shows that the underlying view of humanity and society

that motivated these Victorian critics was not so appealing as we were led to believe. Often pointing to the Middle Ages as a paragon, they believed that society was composed of a natural hierarchy wherein the lower orders are to be cared for by their betters to whom allegiance and deference is owed. At the bottom of the social hierarchy were the Irish and blacks, whom they considered subhuman and incapable of self-governance.

The unapologetic proslavery views of Carlyle and Ruskin come as a shock to the modern reader. While not completely unknown to literary scholars, such ideas tend to be wrapped in a blanket of silence. Levy removes the blanket and exposes such writings as Carlyle’s, “Occasional Discourses on the Negro Question” (1849). In this odious essay about Jamaican former slaves, Carlyle claims that blacks are incapable of managing freedom. They live only for pleasure and are content to eat pumpkins rather than to work to grow the West Indian spices that the “gods ordained” should be their lot. Emancipation of Jamaican slaves, he argues, has left them bewildered and unwilling to work. The only solution is to re-enslave them while reforming the laws to encourage more benevolent masters.

While the call for re-enslavement was extreme, Carlyle’s view of blacks was central to the critics of capitalism. They argued that rather than worry about the conditions of far distant subhumans such as Jamaican blacks, it is more important to be concerned about the plight of the fully human, if low-status, British working class. Capitalism, they argued, renders British laborers worse off than black slaves (a claim that Levy proves false), and so their improvement takes precedence.

Such reactionary ideas did not go unchallenged. Levy shows that at this time, slavery was opposed by a coalition between utilitarians (including the classical economists) and Evangelical Christians. Despite their differences, both groups believed that there was a single human nature, implying a universal equality among men. They also held that the utilitarian greatest-happiness principle was

equivalent to Christianity's golden rule. Slavery violated both precepts because, on the one hand, slaves were suffering unhappiness and redressing their ills would increase utility, and, on the other, no one would choose to be enslaved himself, so no one has a right to enslave others. Thus the hard-hearted economists and enthusiastic Evangelicals turn out to be the true humanitarians of the Victorian age.

This review can barely scratch the surface of Levy's scholarship. For instance, there is no room to do justice to his claim that Dickens's novel *Hard Times* must be read in conjunction with Harriet Beecher Stowe's *Uncle Tom's Cabin* to fully understand the nuances of the text. The same is true for the essay in which Levy explores the implications of Adam Smith's contention that humans are the only species that trades, and that trade is a function of speech and reason. Hence, Levy argues, Smith's system of economics shows trade to be the logical starting point of economic theory and not rational choice, an insight almost lost to twentieth-century economists.

While the arguments of this fascinating book can be difficult and the reasoning sometimes elusive, the importance of the message and the light it sheds on the relationship between the foundational assumptions of economic theory and a benevolent view of human association make it well worth the reader's effort. □

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Ayn Rand and Business

by Donna Greiner and Theodore Kinni
Texere • 2001 • 209 pages • \$22.95 hardcover

Reviewed by Douglas B. Rasmussen

What sort of book is this? Perhaps the best answer is to say that an alternate title could be: *Ayn Rand for Dummies*. Indeed, that might be a better title, for the book is a *very* elementary introduction to Rand and her thought. It is well written

and organized, providing an accurate account of the basic tenets of Rand's philosophy. Moreover, the book offers the right combination of personal vignettes, scandal, and inspiration to satisfy the beginner who wants to be entertained as well as informed. It thus serves well as a book that one might give someone who has finished one of Rand's novels and now wants to know *a little* more.

The book is divided into three parts. Part one, "Ayn Rand and Objectivism," provides an account of Rand's life, her affair and breakup with Nathaniel Branden, and the rudiments of her philosophy. Part two, "Randian Work," describes in eight brief chapters the central virtues of Rand's ethical egoism. These chapters home in on "Rand's ideas regarding the personal characteristics of effective people." Part three, "Randian Management," explores the implications of Rand's thought for managing and leading organizations—in effect, for managerial ethics.

The presentation of Rand's philosophy, as well as the central virtues of ethical egoism, never strays far from Rand's language, and there is no attempt, beyond the usual contrasting of egoism with altruism, to place Rand's thought in an intellectual context. The reader never learns of works that are sympathetic and supportive of the rejection of altruism—for example, such works as Henry Veatch's *Rational Man* (1962) or David Norton's *Personal Destinies* (1976). Rand is thus made to appear as *entirely* original, as if no one else ever shared her commitment to the ethical centrality and sanctity of individual human life.

Though integrated nicely with examples from Rand's fiction, the discussion of the virtues does not consider their place in the lives of "effective people." Are the virtues— independence, integrity, honesty, justice, productiveness, and pride—practiced only because they are means to individual well-being, or are they also practiced for their own sake because they are constituents or expressions of such living? Also, do effective people ever have a place for treating others as more than merely means to their well-

being? What is the place of friendship in Rand's ethics? Finally, Rand seems to portray rationality in theoretical terms only with little discussion of what practical reason, much less practical wisdom, might be. Can this view of rationality be reconciled with ethical individualism?

Perhaps these questions are unfair, because laymen might not be expected to ask such questions. Yet, after nearly 30 years of teaching ethics, I have always found the beginner capable of probing questions, and it is here that the authors fall down. They do not sufficiently discuss problems and ambiguities in Rand's ethics so as to allow the reader to understand or appreciate her positions. In effect, they treat their audience like dummies.

However, the book purports to do more than educate laymen. It seeks to tell the world something new and substantial about Rand's thought, particularly as it pertains to managerial ethics. We are told the following: that employees are not chattel; that voluntary cooperation is more effective than coercion; that employees ought to be judged by objective criteria; and that the principle of trade applies to both sides of the employer-employee relationship. Further, we are told that the human mind is the ultimate source of knowledge and wealth and that all progress, spiritual as well as material, stems from the innovators—those who use their minds.

All of those statements are true, and Rand certainly made or implied them. But none of this is new. There have been many works in business ethics using Rand-inspired insights. Robert McGee's *Business Ethics and Common Sense* and Tibor Machan's *Commerce and Morality* come to mind. Further, the relationship between these statements and the moral vision that is the United States can be found in Douglas Den Uyl's *The Fountainhead: An American Novel* (1999). *Ayn Rand and Business* is certainly not in this league.

The penultimate chapter, "Leading With Purpose," does offer something new, namely that insights from Rand's ethics can be used to manage people in business. We are told

that purpose and focus are crucial to a successful business organization, for they unify effort and bring about productiveness. But there is nothing terribly profound here. It can be found in almost any organizational behavior text or management course. □

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The Lochner Court, Myth and Reality: Substantive Due Process from the 1890s to the 1930s

by Michael J. Phillips

Praeger • 2001 • 224 pages • \$72.95 hardcover

Reviewed by George C. Leef

L*ochner v. New York* is an often-mentioned but misunderstood 1905 Supreme Court decision that lends its name to this excellent analysis of constitutional jurisprudence by Michael J. Phillips. Phillips, professor emeritus of business administration at Indiana University, has written probably the best book by a non-lawyer on any aspect of constitutional law, and the best survey of the *Lochner* line of cases by anyone. This book is a penetrating revisionist history of a key period in our legal history.

Briefly, in *Lochner* the Supreme Court struck down a New York statute that limited the number of hours bakers could work. The majority held that the freedom to contract for as much work as a man chose was within the "liberty" protected by the Fourteenth Amendment and that paternalistic health and safety rationales advanced by the government did not save the statute. The decision elicited a furious dissent from Justice Oliver Wendell Holmes, who argued that the Court was usurping state prerogatives. "The 14th Amendment does not enact Mr. Herbert Spencer's *Social Statics*," Holmes grumbled.

Lochner wasn't the first time the Court had declared unconstitutional statutes that interfered with liberty and property, but that name has been applied to a line of cases in which the Court, employing an approach

later dubbed “substantive due process,” defended individual rights against government encroachment. That philosophy came to an end during the New Deal, when the Court, with an augmented number of “liberals,” upheld coercive New Deal programs. Ever since, law students have heard that *Lochnerism* was a terrible mistake. Justices like Holmes and Louis Brandeis have been elevated to constitutional deities, while the defenders of individual rights have been pilloried.

Phillips correctly notes that there is a lot of myth in the standard account of the *Lochner* period. His study of the Court’s decisions leads him to conclude that there was nothing like the uniform obstruction of “progressive” legislation that most people believe occurred during that era. Interventionist legislation sometimes lost, but sometimes it was upheld. Thus the Court doesn’t deserve as much blame—or credit—as it is customarily given, depending on your point of view.

More important, Phillips’s analysis of the particular decisions leads him to conclude that “some of the cases in which [the Court] did strike down governmental action were more justified than is generally believed.” He demonstrates that the statutes in question were largely the sort of counterproductive special-interest legislation that we have come to expect from legislatures. In striking down such measures, the Court was not acting against the common good, but for it.

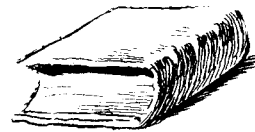
One of the most valuable parts of the book is the author’s demolition of the canard that in the “substantive due process” cases, the Court was simply acting as an agent for business interests. Phillips refutes that bit of anti-capitalist posturing by noting that in most, if not all, of the cases where legislation was struck down, the Court was certainly not siding with business. For example, in *Louis K. Liggett Co. v. Baldridge* (as in the *Lochner* case), the Court invalidated an obviously anticompetitive statute. Phillips writes, “Pennsylvania’s ostensible effort to protect the public health looked suspiciously like an effort by in-state pharmacists to block competition from chain stores.”

In the course of his analysis, Phillips produces a delightful byproduct—a reassessment of the supposed brilliance and consistency of the Court’s famed dissenters Holmes and Brandeis. Brandeis especially has been revered by leftists for his dissents in cases like *New State Ice v. Liebmann*. Read the chapter “What Motivated the Old Court?” and watch the lustrous Brandeis halo turn to junk before your eyes.

Also worthy of close attention is Phillips’s chapter “The Question of Unequal Bargaining Power.” The standard defense given by interventionists for minimum wage and other supposedly pro-labor statutes is that the government must intervene to “equalize bargaining power” where one party is said to have an “unfair” advantage. Phillips takes a fairly sharp sword to that idea. He points out that while an individual, whether a manual laborer or a Harvard Law School graduate, doesn’t have much “bargaining power” regarding employment offers, competition among prospective employers ensures that workers are paid according to their productivity. That the *Lochner* Court didn’t bite on the “unequal bargaining power” sucker bait, while the New Deal Court did, is a mark in favor of the former and against the latter.

Phillips concludes that the decisions of the *Lochner* era are best explained by a commitment, if imperfect, to the idea that freedom ought to be preserved unless there is a compelling reason to interfere with it. I’d love to see many law students confound their professors in constitutional law with the points raised by this book when they arrive at the “substantive due process” cases. □

George Leef is the book review editor of Ideas on Liberty.



The Elusive Quest for Growth: Economists' Adventures and Misadventures in the Tropics

by William Easterly

MIT Press • 2002 • 356 pages • \$17.95 paperback

Reviewed by John T. Wenders

As this is being written, the television talking heads are imploring us “not to walk away” from Afghanistan and to “invest” billions there instead. Before buying into that idea, everyone should read this book by a former World Bank economist whose forthrightness has evidently cost him his job.

Early on, Easterly makes the following observation about foreign investment in Zambia: “I start with a comparison of what Zambians’ actual average income would have been, \$2 billion of aid later, if [all aid had gone into investment, and investment had gone into growth] as predicted. Zambia today would be an industrialized country with a per capita income of \$20,000, instead of its actual condition as one of the poorest countries of the world with a per capita income of \$600 (which is one third lower than at independence).”

No single statement more cogently exemplifies the tragic and ironic history of Western attempts to lift the lesser developed countries from their poverty by top-down, government-directed financial aid. No matter where it has been tried, or what methods have been used, it has been a dismal failure. Easterly’s book tells us some of the reasons why.

In the past, attempts to alleviate Third World poverty “ranged from foreign aid to investment in machines, from fostering education to controlling population growth, from giving loans conditional on reforms to giving debt relief conditional on reforms. None of these has delivered as promised.” To illustrate, Easterly points to the failure to recognize that incentives are what drives successful economic activity. Throwing capital and machines at an economy failed for a simple reason: the capital did not come as a

result of someone’s perception of a market for its output. The cart was before a non-existent horse. Incentives create capital; capital without a market is useless.

When throwing physical capital at lesser-developed countries failed miserably, attention turned to increasing human capital—education—with similar results. From 1960 to 1990 the median rate of secondary-school enrollment more than quadrupled, and the median college-enrollment rate has increased more than seven times. “What has been the response of economic growth to the educational explosion? Alas, little or none.”

Easterly’s explanation is threefold. In economies with extensive government intervention, those with the most education either go into government or turn to lobbying the government for favors, both largely redistributive rather than productive. Further, much of the increased investment in education came from government-mandated schooling, which was just as useless as throwing capital at an economy. In many instances, mandatory schooling actually took children away from productive work. Finally, much of the investment in education is simply worthless. In Pakistan, for example, teaching positions are often dispensed as patronage, cheating is rampant, and teachers cannot pass the exams they administer.

Next, trying to create better incentives for growth, international institutions began making loans conditional on policy reforms. Instead of aid for investment, it was bribery for reform. The failure of incentive lending is confirmed by the admission that the debts cannot be repaid because the loans were unproductive to begin with. “Debt forgiveness grants aid to those recipients that have best proven their ability to misuse that aid, [and] governments will have too strong an incentive to keep borrowing in the expectation that their debt will be forgiven,” Easterly writes.

He argues that government might, theoretically, aid the development process. His discussion of the externalities of knowledge and technological change is correct. But it is an unproven stretch to jump from what an all-powerful, well-meaning, benevolent gov-

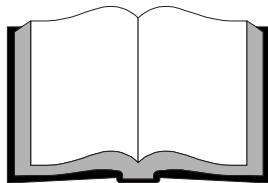
ernment *could* do to what a real-life government *will* do, especially in light of the government corruption and meddling that Easterly himself describes in detail. He discusses how bureaucracies are corrupt, subvert markets, and create incentives that kill growth, especially in lesser-developed countries where decades of top-down foreign aid have solidified government's hold on the economy. The incentive of many in those governments is to promote policies flatly inconsistent with economic development.

Our author, nevertheless, remains hopeful, even though he often feels "like the clueless advising the helpless." This reviewer is less hopeful. As Mancur Olson has shown, in the absence of revolution, or defeat in war, government sclerosis seldom reforms itself.

Easterly's conclusion that government should stay out of the marketplace is certainly correct. However, many of the problems he cites, like high inflation, black-market premiums, high budget deficits, and negative real interest rates, are merely signs of governments obsessed with redistribution, not production. He naively presumes that corruption just happens. The idea that it emanates from unconstrained government power doesn't seem to occur to him.

Like many economists who study economic development, Easterly has been mugged by reality. Now that he has left the World Bank, I hope his next book will go beyond illustrating how aid to foreign governments *has failed* and focus on why it always *will fail*. □

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Dogs and Demons: Tales from the Dark Side of Japan

by Alex Kerr

Hill and Wang • 2001 • 320 pages
\$27.00 hardcover; \$15.00 paperback

Reviewed by Victor A. Matheson

D*ogs and Demons*, by expatriate writer Alex Kerr, is another attempt to explain the malaise into which Japan has fallen over the past decade. Japan's real-estate and stock-market bubbles have burst with prices falling to one-quarter their previous highs; the Japanese government's budget deficits dwarf even those run by the United States during the '80s and early '90s; and a banking crisis looms over any possible economic recovery. Why?

Kerr places blame for Japan's troubles on the pervasive and powerful government bureaucracy that creeps into every facet of Japanese life. This unelected administration has had devastating effects on the environment, the culture, and the economy, and threatens to mire the country in a future of unpayable debt.

Japan's oversized construction industry is at the center of the country's problems. The sheer scale of this sector is astounding. As a percentage of the GDP, construction investment constitutes 18.2 percent of the Japanese economy compared to less than half that in the United States. By 2000 Japan was spending 9 percent of its GDP and nearly 40 percent of its government budget on public works, levels roughly ten times that of the United States. It has run out of beneficial projects to undertake and proceeds with projects of questionable value. The public-works sector of the economy has "succeeded" in encasing 55 percent of Japan's coastline in concrete and damming up 97 percent of its rivers. Japan is literally building "the road to nowhere."

Bureaucratic momentum has kept these massive expenditures in place. While nearly all politicians realize the cost these public works place on the nation as a whole, no local official is willing to give up his slice of pork.

Indeed the economies of many rural communities depend almost entirely on government largess.

The book works best as a tale about what government does well and what it does not. The title derives from a quote by the court painter of the emperor of China. When asked what was the hardest thing to paint, he replied “dogs” and when asked the easiest he responded “demons.” In other words, it is harder to manage the commonplace than the exotic. In Kerr’s words, “Basic solutions to modern problems are hard, but pouring money into expensive showpieces is easy.” Japan is a country full of modern concert halls without performers, futuristic sports stadiums without teams, and fantastic art museums without collections. Most important, these monuments are without paying visitors. Public subsidies allow for the creation of these edifices even when the costs far outweigh any potential benefits.

Japan’s difficulties have parallels in the American economy. The U.S. government spent millions creating large-scale low-income housing projects in the ’60s. The Department of Housing and Urban Development was notoriously unsuccessful, however, at creating workable neighborhoods. Similarly, the massive transformation of the American professional sports infrastructure over the past decade has often resulted in beautiful new facilities surrounded by acres of barren parking lots. It is easier to build the shining stadium than that comfortable sports bar on the corner.

The failure of Japan’s economy to revive despite massive capital spending also casts doubt on the ability of Keynesian fiscal policy to revive a stagnant economy. Market-oriented economists have long argued that fiscal stimulus is doomed to failure over any extended period. Since expansionary fiscal policy must be financed by sale of government bonds, this borrowing naturally drains money from private capital markets. Thus government borrowing crowds out private investment. Indeed, while outsiders may gasp at the absurdly low nominal interest rates in Japan (the official interest rate is a minuscule one-tenth of 1 percent), when

combined with widespread deflation, real interest rates in Japan are actually quite high.

Sadly, the book itself doesn’t draw such lessons. For a work claiming to discuss the economic collapse of Japan over the past decade, the author displays an extraordinary lack of knowledge about even the most basic economic principles. For example, Kerr confuses nominal and real interest rates, leading him to conclude that the relatively low American savings rate is actually better for accumulating retirement assets than the high savings rates in Japan. Even low nominal interest rates provide a high level of future purchasing power when prices are falling.

Furthermore, Kerr generally tries to prove his hypothesis by anecdote and story rather than by hard evidence. While this strategy makes for interesting reading, it does little to persuade a skeptical reader of the validity of his ideas.

For those with a dedicated interest in the rise and fall of modern Japan, this book poses many interesting questions and has numerous fascinating stories to tell. Those looking for convincing answers to those questions, however, will be disappointed. □

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In Defense of Global Capitalism

by Johan Norberg

English translation by Roger Tanner.

Timbro • 2001 • 291 pages • \$11.95 paperback

Reviewed by Donald J. Boudreaux

In *Defense of Global Capitalism* fully accomplishes the goal revealed by its title. Here, Swedish historian and political writer Johan Norberg adeptly explains why free trade and free markets achieve not only “economic” successes (such as improved living standards for everyone) but, also, successes in areas not typically regarded as economic (such as cultural enrichment).

Remarkably compact given the amount of material covered, Norberg here engages

almost every argument against free trade. And he does so with admirable fairness, giving each anti-trade argument its best possible rendition.

Norberg corrects several misunderstandings and exposes many canards. Among these are the following:

Globalization increases the wealth of already-rich nations by impoverishing poor nations. Norberg reports that between 1965 and 1998 “the richest one-fifth of the world’s population increased its average income from 8,315 to 14,623 dollars, i.e., by roughly 75 per cent. For the poorest one-fifth of the world’s population, the increase has been faster still, with average income rising during the same period from 551 to 1,137 dollars, i.e., more than doubling. . . . [W]orld poverty has fallen more during the past 50 years than during the preceding 500.”

Globalization promotes increasing inequality of wealth. He points out that the Gini coefficient—a widely accepted means of measuring wealth inequality—has, for the whole world, fallen by ten percent between 1968 and 1997. Wealth inequality across the world has declined with globalization’s advance. But Norberg makes a more basic and vital point: “Only those who consider wealth a greater problem than poverty can find a problem in some [people’s] becoming millionaires while others grow wealthier from their own starting points.”

Globalization threatens democracy. He presents data showing that, while in 1950, 31 percent of the world’s population lived in democratic societies, today 58.2 percent do. More fundamentally, he astutely recognizes that what the antiglobalization crowd “really see threatened is the use they would like to make of democracy, namely as a means of augmenting governmental power.”

Globalization is both desired and promoted by giant, multinational corporations. Norberg answers this pet allegation of the anti-free-trade crowd by calling attention to the obvious: “What free trade has done is to expose corporations to competition. It is above all consumers that have been made

freer, so that they can ruthlessly pick and choose even across national boundaries, rejecting those firms that do not come up to scratch. Historical horror stories of companies *de facto* governing a society always come from regions where there has been no competition.”

Western corporations mistreat their employees in developing countries. Norberg again reports revealing facts: “In the poorest developing countries, someone working for an American employer draws no less than eight times the average national wage! In middle-income countries, American employers pay three times the national average. Even compared with corresponding, modern jobs in the same country, the multinationals pay about 30 per cent higher wages. Foreign firms in the least developed countries pay their employees, on average, twice as much as the corresponding native firms. . . . The same difference applies to working conditions. ILO, the International Labour Organization, has shown that it is the multinationals, especially in the footwear and garment industries, that are leading the trend towards better workplace and working conditions.”

Globalization hurts the environment. Relying heavily on the data-rich researches of Julian Simon and Bjørn Lomborg, Norberg summarizes the empirical data on environmental quality: the doomsayers are not only wrong; they are spectacularly wrong. Indeed, the only places in the world where pollution is a growing problem are countries that refuse to integrate themselves into the market. He also makes the significant point that pollution is not the product only of commerce and industry. Pollution exists, in much more devastating concentrations, in noncommercial and nonindustrial countries.

My only complaint is that the book’s production quality is mediocre. I encourage an American publisher to bring out a higher quality version of this truly excellent case for freedom and free trade. □

Donald Boudreaux is chairman of the economics department of George Mason University, former president of FEE, and monthly columnist for Ideas on Liberty.