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AMERICAN CAPITALISM'S NEW TESTAMENT

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George F. Gilder, *Wealth and Poverty*, Basic Books, New York, 1981.

The reign of conventional Keynesianism, as a philosophy of economic policy and a practical guide to redistributive justice, is over, at least in America. It was dethroned partly by the inexorable flow of events in the real world of business and politics, and partly by the increasingly feeble results of the applications of its doctrines. Lacking the dignity even to await the last rites, the schools contending for the succession already have an impressive record of public diatribe to their credit. The principal battle has been between the post-mortem neo-Keynesians, who continue to put their primary reliance on fiscal interventionism to stabilise the level of aggregate demand, and the "new" monetarists who assert the sufficiency of credit control via the money supply to influence demand conditions in desired directions. From time to time the two pretenders cease their own public quarrels to join forces against a third, much punier set of rivals—the handful of North-American followers of the Latin-American school of structuralists who are even more interventionist than the Keynesians but who target their policy prescriptions at the industry, and even at the enterprise level, with a view to creating the supply-side conditions for economic growth. Structuralism put its primary emphasis on assuring the growth of productive capacity through state intervention to break the institutionalized barriers to economic development imposed on peripheral economic regions via a division of labour determined by the metropoles. It therefore was never a serious contender, in America, with the two demand-side pretenders for the succession. The same is certainly not the case for the newest supply-oriented school of thought to throw down the gauntlet.

Collapse of the Keynesian Consensus

After the Second World War Keynesianism was institutionalized in Britain and in Canada. But in the U.S. its acceptance was belated, and its effective period of operation much shorter—a fact which explains the greater ease with which it was overthrown. During the brief period when it was accepted in the U.S., it worked for reasons that had little to do with its inherent logic.

Keynesianism was premised on the notion that government spending in excess of tax receipts would, in the face of industrial excess capacity, eliminate unemployment and increase national income without generating appreciable inflation. That, in the U.S., for all practical purposes, came to mean the combination of, in Seymour Melman's expression, Pentagon Capitalism and the "key currency" status of the dollar. Pentagon Capitalism meant the emergence of a gargantuan system of corporate welfare in which leading sectors of American industry, particularly concentrated in the northeast, were guaranteed financial viability without reference to efficiency or managerial competence in anything beyond the cultivation of political and military connections. The "key currency" system meant that part of the cost of maintaining the flow of corporate largesse was passed on to America's chief trading partners abroad. As American "Keynesianism" worked, the U.S. government ran budget deficits, attributable in no small measure to the costs of military procurement at home, while the U.S. economy ran balance of payments deficits due to the export of fund for private investments and, increasingly throughout the 1960's, for military spending abroad. Since the U.S. dollar was *the* international medium of exchange, other countries absorbed the outflow of dollars from the U.S. into their foreign exchange reserves, and then re-lent them to the U.S. in the form of purchases of American government treasury bills. And since the issue of treasury bills financed much of the government deficit, the circle was complete. Easy fiscal policy (deficit spending) and easy money went hand-in-hand with rapid income growth; for the normally inflationary consequences could be diffused abroad as other countries absorbed the U.S. excess liquidity.

Confidence in the system eroded rapidly as the Vietnam War deepened and the pile-up of overseas claims on the U.S. treasury got proportionately greater. Financial shocks followed — the gold rush of 1968, Nixon's suspension of convertibility of the dollar into gold and the accompanying trade offensive in 1971, and the final collapse of international managed money in 1973. In the wake of the 1973 debacle the western world was haunted by the spectre of stagflation —declining productivity, rising unemployment, *and* rising prices. Within the U.S. the response among policy makers and academic economists was disciplined confusion. On the one hand *rigor mortis* Keynesians of the Chrysler school saw the solution in more-of-the-same-with-a-difference, in a perpetual government bail-out system for corporate incompetence despite the danger that, with the loss of the dollar's international status, the results would mean the institutionalization at home of the inflation formerly diffused abroad. On the other hand the new monetarists, with their star rising, and backed by Wall Street and Club of Rome advocates, preached economic conservatism and the paramount virtues of a stable dollar value of financial contracts even at the expense of zero or very slow real growth. In one fundamental sense, new monetarists and the Keynesians were Tweedledum and Tweedledee, both nagging at the level of aggregate demand but differing on how to control it, on how much to control it, and on the relative importance of unemployment and inflation as social ills. The more vociferous their public antagonisms, the clearer it became that the differences between them, including the question of the relative futility of their policy prescriptions, were of degree rather than of kind. Hence when the supply siders came on the scene, they took the country by storm. While the old right had largely acquiesced in the philosophy of a government-corporate plutocracy, the new right stood for the moral rearmament of American capitalism around the altar of the free market mechanism. While the conservative Old Right fought to defend the entrenched powers of big industrial and financial interests, especially in the northeast, the radical New Right articulated the aspirations of the moral majority of small- and medium-size enterprises, particularly in the South and West.

Economics for the Moral Majority

The moral majority of enterprises inhabit a world that is radically different from that in which members of Pentagon Capitalism and other facets of the corporate welfare system dwell. Large firms have their financial viability guaranteed by the state, either by general demand-management policies, or, in the case of firms within the military-industrial complex, directly. In both cases firms can be relatively indifferent to cost, including the cost of credit, of labour, and of managerial incompetence; for additional costs can be passed on more or less at will to their customers, be they the state or the population at large. But moral majority firms have no such guaranteed annual incomes. They lack both the political key to entry into the military-industrial complex, and the market power to price on a simple cost-plus basis. Hence the reality of their plight when high and rising interest rates hamper their capacity to raise working capital or carry inventories, when a rising tax bite chomps off the surpluses necessary for self-financing of their capital requirements, and when unions or minimum wage laws prevent them from shifting the burden back down onto the shop floor.

Central to the supply-side creed are the reaffirmation of Say's Law and the entrepreneurial spirit. Say's Law states that the act of supplying commodities to the market simultaneously generates enough purchasing power in the form of payments for labour, resources, or services that went into the production process, to clear the resulting products off the market—ie, supply creates its own demand. If true, then this would obviate the need for government demand-management policies, and undercut the moral as well as the economic rationale of the welfare state. At the same time, exultations of the entrepreneurial role reaffirm the frontier spirit of American business, and provide the moral majority of firms with a much-needed shot in the political arm in the face of the entrenched power of the old corporate plutocracy. The resulting combination produced the mobilization of the moral majority behind the doctrine of supply-side economics and, in uneasy alliance with the Old Right, the capture of the levers of political power—and as well the imaginations of the American "middle class."

Supply-side doctrines are much more than economics. Supply-siders articulate a philosophy that welds a protestation of faith in the entrepreneurial spirit with a reaffirmation of the traditional values of suburban America badly in need of a fillip to carry it out of the post-Vietnam doldrums. Supply-side economics then is the writ of America the beautiful at the enterprise level. It taps simultaneously the healthy current of traditional American political culture that distrusts big government and the bureaucratic decision-making process, and the unhealthy undercurrent of contemporary American political reflexes that yearns for the 1950s when good guys and bad guys had their roles well defined, and America walked tall on the world stage. Thus the supply siders, in conjunction with Ronald Reagan, assumed the position of moral and political leadership of Middle America left vacant by the respective demises, physical and metaphysical, of John Wayne and the Green Berets. What the supply side was lacking was a Good Book in which its gospel could be recorded in readily accessible form. Into that spiritual and epistemological void stepped George Gilder and his New Testament of the New Right, reiterating that

> faith in man, faith in the future, faith in the rising returns of giving, faith in the mutual benefits of trade, faith in the providence of God are all essential to successful capitalism. (p. 73)

Moral Foundations of the New Right

Gilder sets himself a task previous commentators on American business and economic life had demonstrably failed to do, namely "to capture the high adventure and redemptive morality of capitalism" (p. X), and thus to rescue it from the array of sins—ecological brigandage, sexism, racism, exploitation, and moral vacancy—imputed to it by the left (p. 7). Predictably he sees a socialist conspiracy everywhere, "in auditoria and parish parlours, among encounter groups of leftist intellectuals" (p. 3) and, presumably, behind the curtain in American boardrooms and, in the final sanctuary of America's most endangered species, under the beds of the nuclear family. To demonstrate the "moral value of capitalism" he feels it is essential to sell the notions that the American frontier is still open, that opportunities would still abound were it not for the heavy-handed interference of the state, and that the possibility of social ascent is open to all regardless of race, color, and for the most part, creed, though, fortunately for the future of the American nuclear family, not regardless of sex. Thus he defiantly flings the charges of the left back in their faces.

To the charge that capitalism entails the rapid depletion of non-renewable resources and engenders ecological chaos, Gilder replies that in fact the problem of resource depletion has been exaggerated and that, in any event, any problems created by the current generation of capitalist enterprises become the new frontier in which the next generation can test their entrepreneurial skills. The problems of today are the challenges of tomorrow, the successful resolution of which both replenishes the spirit of entrepreneurial endeavour and, presumably, creates in turn yet another set of problems for the future (p.256). To Joseph Schumpeter's notion of creative destruction as the outcome of entrepreneurial activity, Gilder has added destructive creation, joining the two in a sort of social-psychological wheel of perpetual motion that continuously replenishes the moral fabric of American capitalism while providing the ecologists' dream of the ultimate non-nuclear solution to the energy crisis.

Sexism at the work place, the more rapid advance of men over women, the sexual hierarchy of authority, and unequal pay for equal work, is the next charge against capitalism on which Gilder sets his intellectual prowess to work. To him the economic manifestations of "sexism" are really the joint products of biology and the social requirements for the preservation of the nuclear family. Men are naturally more aggressive and career-oriented, and the future strength of American capitalism will require tapping these biological urges and harnessing them to the productive machine. Thus "the man's earnings, unlike the woman's, will determine not only his standard of living, but also his possibilities for marriage and children—whether he can be a sexual man. The man's work thus finds its deepest source in love." (p. 87) So much for sexism at the work place.

As to racism and poverty these are largely figments of the overactive imaginations of federal bureaucrats or, to the extent they are real, are due to the misinformed meddling of governments which, in their efforts to aid the "lower class", in fact destroy the initiative of its members and condemn them to the perpetual misery of a non-entrepreneurial role in life. Racism is long gone from American social life; and poverty, being a state of mind more than a social condition, would not exist if there were no federal standards by which to try to measure it nor federal bureaucrats to feed off it. However on one point Gilder is categorical. Poverty is not the same thing as income inequality, for inequality is essential to the functioning of the system. Gilder therefore disparages the "morbid egalitarianism of leveling down rather than summoning up" (p. 92) and the accompanying hatred of wealth and success. This is a tendency particularly pronounced at the United Nations where "voices rise with alternating zeal against the blight of want and against the Americans and Zionists, creators of wealth." (p. 96) As he sees it, in a message directed at once at the American poor and the underdeveloped world, "material progress is ineluctably elitist; it makes the rich richer and increases their numbers, exalting the few extraordinary *men* who can produce wealth over the democratic mass who consume it." (p. 259)

Finally, the ultimate charge against capitalism, and one which commentators prior to Gilder had been most remiss in failing to counter, lies in its supposed moral vacancy, a misconception which Gilder most energetically and imaginatively seeks to refute once and for all. Typically both antagonists and protagonists of capitalism have agreed on its fundamentally amoral character, on its exultation of hedonism and the principle of dog-eat-dog competition. To

Gilder this is patently false. For capitalism starts not with avarice, but with the application to material life of the golden rule!

"Capitalism begins by giving", Gilder claims (p. 21), and finds is evidence in economic anthropology, particularly the potlatch ceremonies of the Indians of Pacific northwest coast of America. In this and similar primitive redistributive systems, gifts are made in the expectation of future returns. Thus the potlach, together with Say's Law of supply creating its own demand, constitute indisputable proof that "capitalism consists of providing first and getting later." As Marx *should* have put it, "redistribute, redistribute. That is Moses and the prophets!" But surely, one is inclined to interject, there is a vast difference between a primitive gift-exchange ceremony and the complex interactions of mature capitalism. Not so, says Gilder, "the gifts of advanced capitalism are called investments"! (p. 24) These are gifts which capitalists make to their society. Granted they are made in the expectation of return, but so too were the gifts made under the potlach ceremony. Even the Bible says the the giver will be given unto. But the actual level of returns to giving is never certain; for ultimately

> Capitalist production entails faith—in one's neighbours, in one's society, and in the compensatory logic of the cosmos. Search and you shall find, give and you will be given unto, supply creates its own demand. It is this cosmology, this sequential logic [sic!] that essentially distinguishes the free from the socialist economy. (p. 24)

Supply-Side Critique of Keynesianism in Practice

Building on the potlach, Say's Law, and the golden rule, Gilder moves on to a demonstration of how Keynesianism has reversed the sequential logic of capitalism, and at what cost. Keynesianism, in its problem analysis and policy prescription, exalts the demand side of the capitalist equation at the expense of the conditions for the growth of productive capacity that supply-siders stress as the key to prosperity and economic advance. Keynes, who evidently had never attended a potlach ceremony, reversed Say's Law and with it the golden rule. To Keynes, demand creates its own supply, thus putting a premium on individual avarice, creating the moral vacancy in capitalism which leftists attack, and implicitly putting a seal of social approval on the quest for a free school-lunch. Keynesianism is also charged with stifling initiative and innovation by focusing on the problem of stabilizing the demand for old products instead of creating the supply conditions for the emergence of new ones. By the same token it prevents the social rejuvenation of the capitalist class through the constant infusion of new talent and the consequent weeding out of dead wood that a fully functioning market economy open to entrepreneurial initiative would permit. The key to the malaise, to the inverted morality, to the stress on taking instead of giving and on demanding instead of supplying, lies in the taxation and social security system of the modern state.

Gilder manages to conjure up a long list of charges against the modern welfare state. In terms of social effects, taxes lead to a loss of initiative and the will to self-improvement as the poor find their material needs taken care of by welfare and the rich divert their incomes into consumption and speculation and away from productive investment. Taxes, too, lead to a decline of public morality and a rise in underground economic activity beyond the range of the tax collector's grasp—drug-peddling, prostitution, theft, babysitting for unreported cash payments, and so forth. Taxes undermine the vitality of the arts, for they take away the surplus income of the formerly rich former patrons and force the arts to become dependencies of the state granting agencies. And most heinous of all the crimes of taxation against American social life, taxes destroy the nuclear family by effectively castrating the American male! For, "unlike the mother's role which is largely shaped by biology, the father's breadwinning duties must be defined and affirmed by culture." (p.122) Hence as taxes geld a large part of his income, forcing his wife into the work place, "the man unable to perform his role as breadwinner is being slowly unmanned." (p. 16)

The adverse social consequences of taxes are reinforced by the social security system they finance. The entire thrust of the welfare system is to take the risk, and the entrepreneurial initiative out of participation in the mainstream of American economic life, and breed precisely the social problems it is supposed to defend against. Hence "arson has for some years been among America's most popular crimes" and, rather than being caused by social tensions in the ghetto, as the white liberal manages to mislead himself and the public into thinking, "most of it is induced by fire insurance." (p. 108) Thieves arraigned in court cite as their defence, not need, but the existence of theft insurance. By the same token one could surmise, though Gilder does not do so explicitly, bank robbieries *caused* by deposit insurance and unemployment caused by unemployment insurance. And one might even be tempted to go further, arguing that disease is caused by medical insurance — though in this instance one would likely have the support of the American medical heretic, Dr. Mendelsohn, who has argued convincingly that universal medical insurance, by increasing the access doctors have to the general population, is dangerous to public health.

As to the macroeconomic effects of the tax and social security system, here three main charges are levied — and "proven" largely by Gilder's standard method of successive iteration and reiteration-cum-thesaurus. The first is that the social security system, apart from its general role in stifling initiative, permits the government to displace the private financial institutions in the intermediation of the flows of savings and investment, causing a decrease in the national (private) savings rate and a consequent capital crisis for industry. (How his contention here that the intermediation process is the heart and soul of the capitalist system squares with his earlier insistence that truly entrepreneurial firms do not borrow from the outside capital market is a matter of some mystery.)

The second major charge is that the rates at which taxes in fact are levied make them actually self-defeating in terms of their revenue objectives. Here Gilder invokes the widely-famed and aptly-named Laffer Curve which resurrects, with the meticulous sense of public relations that only a Californian could muster, a trite old axiom of revenue tariff theory and applies it to the general income tax. The proposition holds that if tax rates get too high they stifle investment, causing output and income to fall, and therefore reducing aggregate tax receipts. Dwelling as they do in a world of ultimate faith, careful specification of secular causation has never numbered among the supply-siders' leading priorities.

The third charge which Gilder lays at the door of the tax and transfer system puts him on more solid ground. It is the contention that taxes—the cost of government services—get diffused throughout the economy and built into the cost of good and services, causing a net upward displacement of the overall inflation rate, rigidifying the structure of relative prices and costs, reducing the overall responsiveness of the economy to changes in scarcity prices, and creating a floor that hampers any subsequent tendency prices might have to fall again when firms become more efficient. This last point, stressing the adverse impact of taxes on the supply-side of the economy in exacerbating inflationary pressures goes to the heart of the on-going public dispute between the supply-siders of the New Right and the monetarists of the Old Right that is currently sowing confusion and consternation in Reaganite ranks.

Supply-Siders Versus Monetarists

Unlike both Keynesians and monetarists (to different degrees), supply-siders do not see inflation as a problem *per se.* Rather it is a symptom of a problem—the underlying malaise of productivity and the stifling of entrepreneurial initiative for which the final responsibility rests with the heavy hand of government. To a good supply-sider, inflation can actually accelerate the rate of capital formation by tilting the income stream in favour of the future, favouring the debtor over the creditor, and providing a propitious climate for exercising entrepreneurial initiative—the entrepreneur, unlike the *rentier* capitalist, has little or no difficulty protecting his future income stream from inflation. Inflation becomes a social problem only in the context of a leveling off of productivity growth, and in that case the reactivation of the growth process from the supply side, not hacking away at the level of demand, should be the government's policy priority. Faced with strong inflationary impulses, monetarists, old and new, demand austerity programs — raising of taxes to cut down government deficits and curtailing the growth of the money supply—to deflate aggregate demand. Supply-siders counter that tax increases are themselves inflationary, from the point of view of initiative and costs, and contend that tax cuts to stimulate output and reduce costs is in the long run the only sound anti-inflationary strategy. Nor do supply-siders accept the prescription on monetary restraint, for its likely consequences are simply to squeeze the private sector, particularly small business, while leaving the government relatively impervious to its effects, thus diverting more resources to the public and away from the private sector. Indeed to Gilder and other supply siders the very notion of a monetary target is largely a chimera—the money supply adapts itself to a price level determined by costs, including taxes, either by changes in velocity or by the evolution of new institutional forms of payment.

Sense and Nonsense in the New Testament

It is clear enough from their critique of monetary policy and their perception of the consequences of the decline of the innovatory capacity of the American economy, that supply-siders, including George Gilder, have put their thumbs on real issues that have long eluded their demand-side foes. Contrary to the self-advertisement American supply-siders are prone to engage in, there does exist a long and impressive intellectual legacy to back up some of their claims. Latin-American structuralists have long argued convincingly that primary attention to supply-side conditions was essential to the development process, and their critique of demand-side austerity measures, aimed against the International Monetary Fund in particular, was at heart the same even if much more intelligently formulated and with careful reference to the international division of labour—as that which American supply-siders level at domestic monetarists. Furthermore the stress on the entrepreneurial process found in Gilder and other supply siders is largely copied from Joseph Schumpeter who, unlike his modern protegé, had enough basic economic sense to understand that the world had changed irreversibly since the days when Horatio Alger and Wyatt Earp extended the American frontier, each in their own mutually reinforcing ways. Indeed the very specification by the supply-siders of Say's Law —as a long-run tendency rather than a short-run identity—is so loose as to be acceptable to any Keynesian in terms of methodology, though not in terms of ideology. For it is there—at the level of ideology—that the supply-siders are truly different. Their ideological quirks are two-fold. One is the constant reiteration of ultimate faith in the free-market mechanism, dismissed by the structuralists, Schumpeterians, and Keynesians alike. The second is the social morality—or rather the "middle class" bigotry that they attempt to legitimize as a form of social science.

Gilder's *Wealth and Poverty* in the final analysis reflects the intellectual and social climate in which it was conceived and born. Discursive, meandering, unashamedly self-contradictory where that is expedient, often dull, but more often unconsciously funny, the book ends up being positively embarrassing to read, and not a little frightening. It is something that would have been laughed out the door of any reputable publishing house in the 1960s and 1970s. Its emergence now—complete with the endorsement of political powerhouses from David Stockman (former Director of the Office of Management and Budget) to William Casey (Chairman of the Reagan Transition Team) to Representative Jack "ax the tax" Kemp—is a chilling sign of the times—of a deteriorating intellectual environment, of a rising Cold War cretinism in the guise of political discussion, and of a reassertion of the Archie Bunker streak in the North American soul.

The alternative explanation is that Gilder has out smarted us all, that in reality what he set out to create is the cleverest social satire since *Catch 22.* That if true would be no small relief.

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