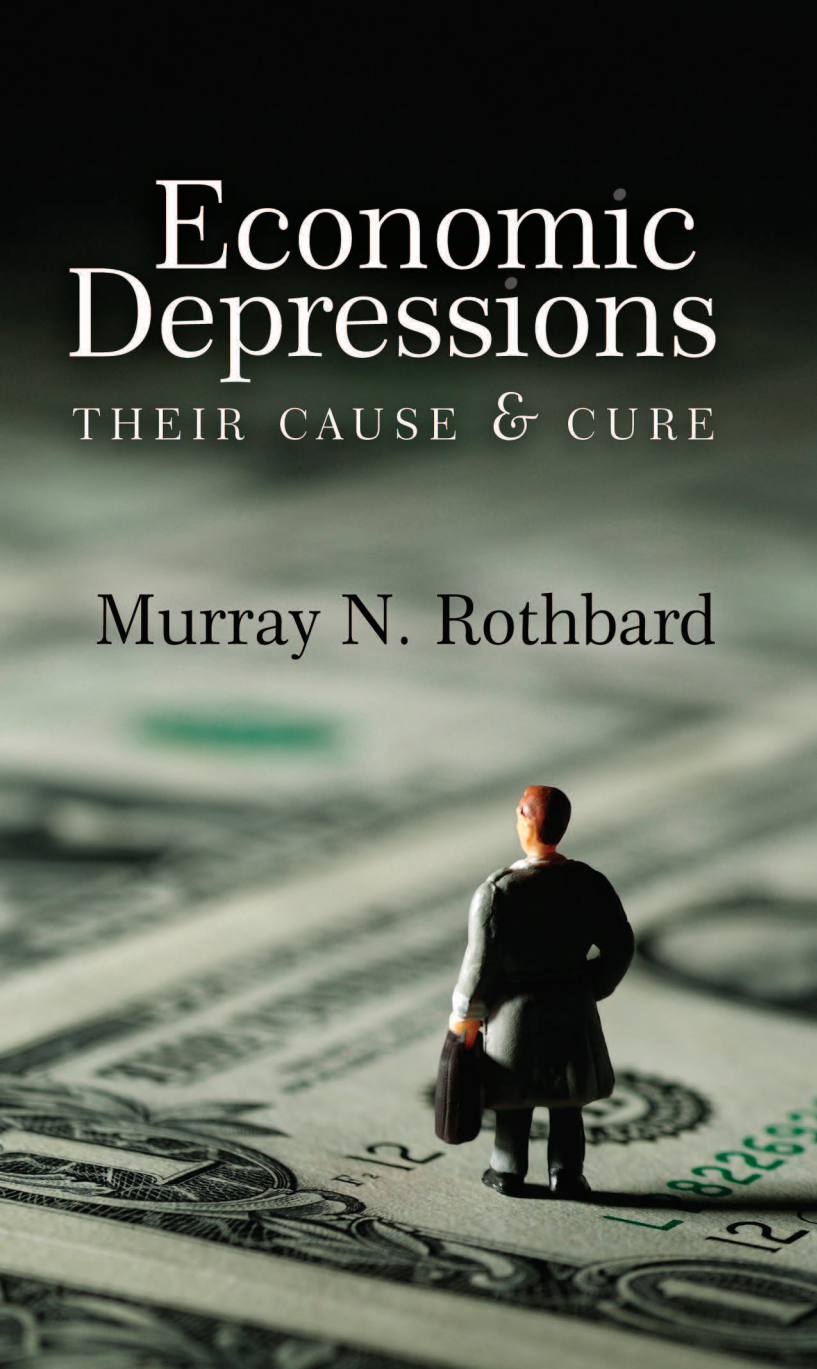
Economic Depressions

THEIR CAUSE & CURE

Murray N. Rothbard



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...banks would never be able to expand credit in concert were it not for the intervention and encouragement of government.

— Murray N. Rothbard

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WE LIVE in a world of euphemism. Undertakers have become "morticians," press agents are now "public relations counsellors" and janitors have all been transformed into "superintendents." In every walk of life, plain facts have been wrapped in cloudy camouflage.

No less has this been true of economics. In the old days, we used to suffer

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nearly periodic economic crises, the sudden onset of which was called a "panic," and the lingering trough period after the panic was called "depression."

The most famous depression in modern times, of course, was the one that began in a typical financial panic in 1929 and lasted until the advent of World War II. After the disaster of 1929, economists and politicians resolved that this must never happen again. The easiest way of succeeding at this resolve was, simply to define "depressions" out of existence. From that point on, America was to suffer no further depressions. For when the next sharp depression came along, in 1937–38, the economists simply refused to use the dread name, and came up with a new, much softer-sounding word: "recession." From that point on, we have been through quite a few recessions, but not a single depression.

But pretty soon the word "recession" also became too harsh for the delicate sensibilities of the American public. It now seems that we had our last recession in 1957–58. For since then, we have only

had “downturns,” or, even better, “slowdowns,” or “sidewise movements.” So be of good cheer; from now on, depressions and even recessions have been outlawed by the semantic fiat of economists; from now on, the worst that can possibly happen to us are “slowdowns.” Such are the wonders of the “New Economics.”

For 30 years, our nation’s economists have adopted the view of the business cycle held by the late British economist, John Maynard Keynes, who created the Keynesian, or the “New,” Economics in his book, *The General Theory of Employment, Interest, and Money*, published in 1936. Beneath their diagrams, mathematics, and inchoate jargon, the attitude of Keynesians toward booms and bust is simplicity, even naivete, itself. If there is inflation, then the cause is supposed to be “excessive spending” on the part of the public; the alleged cure is for the government, the self-appointed stabilizer and regulator of the nation’s economy, to step in and force people to spend less, “sopping up their excess purchasing power”

through increased taxation. If there is a recession, on the other hand, this has been caused by insufficient private spending, and the cure now is for the government to increase its own spending, preferably through deficits, thereby adding to the nation's aggregate spending stream.

The idea that increased government spending or easy money is "good for business" and that budget cuts or harder money is "bad" permeates even the most conservative newspapers and magazines. These journals will also take for granted that it is the sacred task of the federal government to steer the economic system on the narrow road between the abysses of depression on the one hand and inflation on the other, for the free-market economy is supposed to be ever liable to succumb to one of these evils.

All current schools of economists have the same attitude. Note, for example, the viewpoint of Dr. Paul W. McCracken, the incoming chairman of President Nixon's Council of Economic Advisers. In an interview with the *New York Times* shortly

after taking office (January 24, 1969), Dr. McCracken asserted that one of the major economic problems facing the new administration is "how you cool down this inflationary economy without at the same time tripping off unacceptably high levels of unemployment. In other words, if the only thing we want to do is cool off the inflation, it could be done. But our social tolerances on unemployment are narrow." And again: "I think we have to feel our way along here. We don't really have much experience in trying to cool an economy in orderly fashion. We slammed on the brakes in 1957, but, of course, we got substantial slack in the economy."

Note the fundamental attitude of Dr. McCracken toward the economy—remarkable only in that it is shared by almost all economists of the present day. The economy is treated as a potentially workable, but always troublesome and recalcitrant patient, with a continual tendency to hive off into greater inflation or unemployment. The function of the government is to be the wise old manager

and physician, ever watchful, ever tinkering to keep the economic patient in good working order. In any case, here the economic patient is clearly supposed to be the subject, and the government as "physician" the master.

It was not so long ago that this kind of attitude and policy was called "socialism"; but we live in a world of euphemism, and now we call it by far less harsh labels, such as "moderation" or "enlightened free enterprise." We live and learn.

What, then, are the causes of periodic depressions? Must we always remain agnostic about the causes of booms and busts? Is it really true that business cycles are rooted deep within the free-market economy, and that therefore some form of government planning is needed if we wish to keep the economy within some kind of stable bounds? Do booms and then busts just simply happen, or does one phase of the cycle flow logically from the other?

The currently fashionable attitude toward the business cycle stems, actually,

from Karl Marx. Marx saw that, before the Industrial Revolution in approximately the late eighteenth century, there were no regularly recurring booms and depressions. There would be a sudden economic crisis whenever some king made war or confiscated the property of his subject; but there was no sign of the peculiarly modern phenomena of general and fairly regular swings in business fortunes, of expansions and contractions. Since these cycles also appeared on the scene at about the same time as modern industry, Marx concluded that business cycles were an inherent feature of the capitalist market economy. All the various current schools of economic thought, regardless of their other differences and the different causes that they attribute to the cycle, agree on this vital point: That these business cycles originate somewhere deep within the free-market economy. The market economy is to blame. Karl Marx believed that the periodic depressions would get worse and worse, until the masses would be moved to revolt and destroy the system, while the modern economists believe that the

government can successfully stabilize depressions and the cycle. But all parties agree that the fault lies deep within the market economy and that if anything can save the day, it must be some form of massive government intervention.

There are, however, some critical problems in the assumption that the market economy is the culprit. For "general economic theory" teaches us that supply and demand always tend to be in equilibrium in the market and that therefore prices of products as well as of the factors that contribute to production are always tending toward some equilibrium point. Even though changes of data, which are always taking place, prevent equilibrium from ever being reached, there is nothing in the general theory of the market system that would account for regular and recurring boom-and-bust phases of the business cycle. Modern economists "solve" this problem by simply keeping their general price and market theory and their business cycle theory in separate, tightly-sealed compartments,

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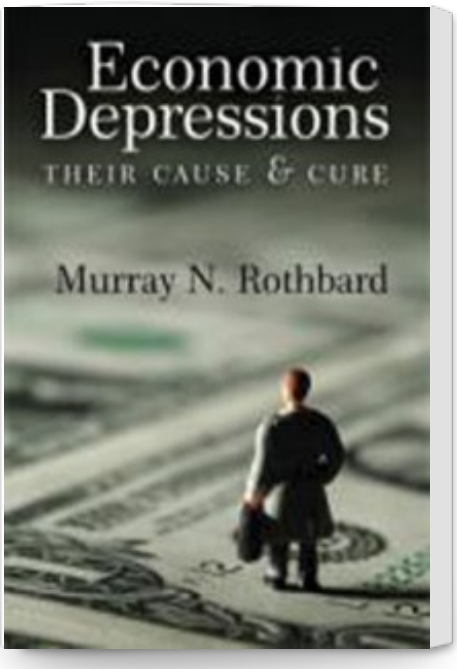

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