A Review Essay and Response:

Paul Craig Roberts' *The Failure of Laissez Faire Capitalism*

Paul Craig Roberts, *The Failure of Laissez Faire Capitalism.* Atlanta: Clarity Press, 2013. Pp. 190. ISBN 13: 978-0-9860362-5-5. $18.95 pb.

Roberts' Account of How Multinational Corporations Have Dismantled the US Economy and Impoverished Its Workers

Walter Gulick

Key words: Paul Craig Roberts, Michael Polanyi, J.M. Keynes, globalization, regulation, offshoring production, economic theory, "self-regulating" markets, printing money, foreign worker visas, Federal Reserve, spontaneous order, wealth inequality, multinational corporations, free trade, ecological economics

ABSTRACT

Roberts' The Failure of Laissez Faire Capitalism *offers a persuasive and serious indictment of US economic policy. Neither political party seems capable of even challenging corporate-influenced policies like the outsourcing and offshoring of jobs, policies which further enrich the very few at the expense of the many.*

Paul Craig Roberts has put into book form the brash, prophetic insights that pepper his regular columns available on line. *The Failure of Laissez Faire Capitalism* is an impassioned critique of most every major decision that the US government has made during the past twenty years. Roberts' critique of economic globalism and free market ideology is bound to no particular ideology and certainly to no political party. Although he was Assistant Secretary of the Treasury in the Reagan administration, current Republicans can take no comfort from Roberts' claims. Neither can Democrats.

The heart of Roberts' critique is presented in Part One, "Problems in Economic Theory." Part Two, "The New Dispossession," recounts in more detail the results of the US (and world) economy gone wrong. The book includes a fairly brief Part Three, "The End of Sovereignty," which is focused on the aspiration of the EU and the European Central Bank to undermine the sovereignty of EU member states so that banks don't suffer losses. The German edition of this book was published in 2012 and includes a twenty-page Preface by Johannes Maruschzik, now translated and included in the American publication. A two page Conclusion and an Appendix disputing claims of a significant recovery from the Great Recession conclude the work.

A political economist, Roberts was among the last graduate students of Michael Polanyi. The University of Virginia Economics Department released Roberts to study with Polanyi at Oxford in 1964-65. As he made evident in his article, "Michael Polanyi: A Man for All Times" (*Tradition and Discovery* 32/3), Roberts was deeply influenced by Polanyi the person as well as Polanyi the thinker. Indeed, he writes that "Michael was the most exciting man I ever encountered" (15). In the late 1960s, Roberts and Polanyi were invited to the University of California to give jointly a course on Polanyi's epistemology, an invitation which Polanyi felt he had to decline.

Polanyi was an advocate of liberalism in the classical sense of that term. Classical liberalism emphaszed the liberty articulated in human rights and economic reliance on suitably structured markets. Polanyi particularly celebrated the liberal spirit of vigorous debate in a cosmopolitan culture that he experienced in his youth in Hungary prior to World War I. However, he viewed classical liberalism as falling into decline both through its own narrow allegiance to a laissez faire version and through the rise of several forms of socialism. Consequently he yearned to recover "the intellectual leadership of the world which the exportation of a doctrinaire liberalism has foolishly lost us" (*SEP* 209). Unfortunately, fifty-eight years after Polanyi wrote those words they could still be applied by Roberts to the world economy today. Roberts' book may be seen as an attempt to begin the process of recovering a liberal economic policy that Polanyi calls for in the following excerpt from "Civitas," an unpublished proposal written in 1944 to found a new quarterly journal devoted to describing and promoting progress toward a good society.

> For the last hundred years liberal economic policy has been conducted without effective guidance from liberal theory. It was in fact made up of a series of disjointed concessions from a theory of laissez faire to the claims of humanitarianism and the obvious demands of the public interest. This unsatisfactory intellectual situation has caused comparatively little trouble so long as the major premises of liberalism were uncontested. To-day it must be remedied without delay if liberalism is to be restored again. The great task of laying down a system of liberal economic policies must be shouldered forthwith (MPP, Box 50, Folder 3).

Polanyi's strong pleas for economic reform were all too often ignored. Roberts, however, can be seen to identify with Polanyi's assertion of the "grave, and in many respects fateful, error of the followers—particularly the popular followers—of economic orthodoxy in adopting a negative attitude with respect to social reform" (*Full Employment and Free Trade*, Cambridge: Cambridge University Press, 1945, p. 145). Not only does Roberts identify with Polanyi's willingness to challenge prevailing opinion, he has developed it into an edgy art form. Smoke and heat emanate from most every page of Roberts' book. He mentions Polanyi on only one page of this book, but it is enough to suggest an influence on the supply-side economics that Roberts promoted during the Reagan years. Roberts claims that in *Full Employment* Polanyi has gone beyond Keynes' strict concern with maintaining appropriate demand.

> Polanyi anticipated Milton Friedman and the American monetarists. Polanyi interpreted Keynes' theory to mean that widespread unemployment meant that there was *a dearth of money.* What the government needed to do was to expand the monetary circulation. It could do this, Polanyi noted, simply by printing money to finance its deficit. . . He said that it was expensive for the government to borrow money, on which it had to pay interest, in order to cover its deficit and that this expense was pointless. Government could more cheaply provide the missing purchasing power by printing the money to cover its budget deficit (38).

Polanyi emphasized regulating the amount of money in an economy to efficiently harmonize the relation between supply and demand and thus keep employment high while minimizing inflation. The supply-side economists like Roberts added insights into how marginal tax rates affect the production of goods. "Supply-side economics says that some fiscal policies shift the aggregate supply curve, not the aggregate demand curve. Specifically, if marginal tax rates are raised, aggregate supply will decline. There will be fewer goods and service supplied at every price" (40).

In any case, Polanyi's advocacy of printing money—a lot of it—is exactly what the Federal Reserve Board is doing currently. By the Fed purchasing Treasury bonds with newly printed money, the federal budget deficit is being financed. To the extent this money enters the world economy, demand for US dollars will weaken and inflation result. Roberts notes that the US standard of living has been protected by international recognition of the dollar as the world reserve currency, protection threatened by prolonged trade deficits and offshoring of jobs. Most members of the European Union cannot print their own money, which has contributed to the economic crises experienced in Greece especially, but also in Spain, Italy, Ireland, and Portugal. Should the dollar be replaced by some other currency as the world reserve, printing additional money will have more negative impacts in the global marketplace, and our economic troubles would be multiplied. As it is, I would observe that the printing of money rather than borrowing funds has driven down interest rates, so that investors looking for a place to earn better returns often turn to securities. Many suspect that Wall Street stocks are overvalued as a result (although Roberts does not raise this particular concern). Has a new bubble been created that, if it bursts, will seriously diminish retirement income and create a new recession or depression?

Polanyi's vision of a thriving economy is centered on establishing regions of spontaneous order properly structured by government regulations that "serve to regulate, guide, correct and supplement the market without ever trying to suppress and replace it" (*SEP* 170). Presumably these regulations would discourage rampant speculation, expose corrupt manipulations, and reform other malfunctions of an unregulated market. Roberts shows convincingly that, in contrast, the "new economy's" order is structured to benefit the few on the backs of the many. And Roberts is decidedly on the side of the many being exploited by the few. The US response to the 2008 economic crisis is instructive regarding the degree to which the rich are protected while the poor are not.

> An audit of the Federal Reserve released in July, 2011 revealed that the Federal Reserve had provided $16 trillion—a sum larger than US GDP or the US public debt—in secret loans to bail out American and foreign banks, while doing nothing to aid the millions of American families being foreclosed out of their homes. Political accountability disappeared as all public assistance was directed to the mega-rich, whose greed had produced the financial crisis (32-33).

In the US currently, those on the right tend to blame the federal government for the current mess, while those on the left tend to blame multinational corporations and the mega-rich. Both are right because politics has evolved to the point that there is little difference between the interests of big business and governmental policy. Regulatory agencies are routinely run by those who were the heads of the corporations to be regulated. A republican form of governance involving checks and balances and founded on people's commitment to public liberty, which Polanyi advocated, is far from what is in play today. Roberts quotes Herman Daly to the effect that economic globalism is the "space into which transnational corporations move to escape regulation by national governments" (70, see also 174).

What is the burden of Roberts' critique? He is particularly critical of mainstream economists, who he says share blame for creating and sustaining a tiny but hugely wealthy class at the expense of the middle and lower economic classes. The reforms Roberts advocates are primarily directed to American economic policies and secondarily to European policies and practices. American business managers might object that in a competitive global economy, the restrictive regulations Roberts proposes would put them at a competitive disadvantage. Indeed, a criticism of Roberts' approach to be set forth shortly is that he pays insufficient attention to the global context of business. Before addressing that issue, however, here are five persuasive claims Roberts advances.

First, mainstream economists have promoted the fallacious notion that markets are self-regulating. Roberts reminds us that what is regulated is not a market, which is a social institution rather than an actor.

> People act, and it is the behavior of people that is regulated. When free market economists describe the ideal as the absence of any regulation of economic behavior, they are asserting that there are no dysfunctional consequences of unregulated economic

> behavior. . . Why is it that economists recognize that robbery, rape, and murder are socially dysfunctional, but fail to see unlimited debt leverage and misrepresentation of financial instruments as socially dysfunctional? (79)

Second, in accord with Polanyi, Roberts advocates sensible policies of regulation designed to promote the common good, not the current situation in which regulatory agencies have been captured by the industries they regulate (58). Even where an appropriate regulatory regime is in place, enforcement is often either absent or too weak to ensure compliance.

Third, the alleged benefits of free trade are challenged. Mainstream economists have lauded free trade on the basis of Ricardo's theory of comparative advantage. But, as Roberts states, the economic conditions of the 19th century, in which the theory made sense, no longer prevail. In our era of instant capital mobility and a demand for short term profits, production tends to flee to areas of low labor cost (48-49) and rewards accrue to those executives who can best slash wages and externalize other costs.

Fourth, as a result of the cost-slashing practice of offshoring jobs, America has been largely de-industrialized and the economic future of its young pauperized. "As the production of most tradable goods and services can be moved offshore, there are no replacement occupations for which to train except in domestic "hands on" services such as barbers, manicurists, and hospital orderlies. No country benefits from trading its professional jobs, such as engineering, for nontradable domestic service jobs" (102). The political dominance of free trade ideology, in which "protectionism" is a dirty word, portends that the current economic prospects for US workers will only get worse in the future. Roberts fiercely deplores the corporate practice of offshoring American jobs, a practice furthered by such free trade agreements as NAFTA.

A fifth flaw in current economic theory and practice, Roberts states, is that "economists have failed to understand that infinite growth in a finite system is impossible" (71). He advocates thinking in terms of what he calls "full-world" economics rather than the standard "empty world" economics that considers natural resources to be virtually unlimited. Man-made capital cannot fully substitute for nature's capital, as the Solow-Stiglitz production function assumes (67). There are ecological limits to economic growth that ought to be included in any economic policy making.

Our society has been unjustly reshaped by these theories and practices. We hear frequently the phrase, backed by statistical evidence, that "the rich are getting richer and the poor poorer." The reality is even starker than the phrase suggests. "The distribution of wealth in the US is so highly concentrated that the 400 richest US families, all of whom are billionaires, have the same net worth as the fifty percent less well-off Americans. When 400 have the same wealth as 150,000,000, clearly things are out of balance" (135).

While for the most part Roberts focuses on the dysfunctional status of the US economy, he does offer some potential remedies. "The U.S. could bring home its offshored production by abolishing the corporate income tax and taxing corporations according to whether value is added to their products at home or abroad. Corporations that produce their products in the U.S. would have a low rate of tax; those that offshore their production would have a high rate of tax" (46). But, I would ask, in a world without effective international regulations, would such a change in taxing policy motivate corporations to move their headquarters to countries that look favorably on offshored production and thereby diminish taxable income in America?

Another of Roberts' proposals is to "break the connection between CEO pay and short-term profit performance" (116). However worthy a goal this may be, it seems unlikely that there is the political will to intrude in such a way into private transactions. Roberts does not provide specifics about how such an adjustment would be worded, enacted, and implemented.

Roberts notes that the repeal of the Glass-Steagall act separating investment from commercial investment banking is what set off the fraudulent transactions culminating in the Great Recession of 2008 (146). The reinstatement of the Glass-Steagall Act would again separate commercial banking, for which FDIC insurance is a reasonable guarantee of economic stability, from investment banking, with regard to which there ought to be no federal support of reckless speculation. TARP funds (Troubled Asset Relief Program) from taxes paid by all of us would then no longer be available to "businesses too big to fail," and risky economic behavior would be curtailed. There seems to be a reasonable chance that a new Glass-Steagall bill can be passed.

Roberts agrees with those who believe the federal budget is bloated. An obvious way to cut the deficit is to trim the military budget. "The U.S. could reduce the budget deficit by hundreds of billions of dollars by ending its pointless and illegal wars, by closing hundreds of overseas military bases, and by cutting an overstuffed military budget" (45, see also 157). In our artificial climate of fear, to challenge the military and its dependent businesses would take courage nowhere evident in the contemporary political scene.

Finally, there needs to be effective enforcement of laws that theoretically prohibit the replacement of US workers by more poorly paid foreign workers. Roberts chronicles various ways corporations get around the requirements for H-1B visas, which states foreign workers may only be hired when there are no qualified Americans that can be found to do the work in question. "Business organizations allege shortages of engineers, scientists and even nurses. Business organizations have successfully used public relations firms and bought-and-paid-for 'economic studies' to convince policymakers that American business cannot function without the subsidy provided by H-1B visas. The evidence is conclusive that the visas do not fill a 'skills gap'" (107).

Roberts cautiously suggests that planning is useful to "reduce the rate of the exhaustion of nature's resources and preserve the U.S. dollar as world reserve currency . . ." (74). But in an environment where government has largely become controlled by corporate interests, can governmental agencies be trusted to plan for the common interest and enforce those plans? Here again, Polanyi's preference for putting in place systems of spontaneous order that serve society as a whole ought to be promoted. Top-down planning is too easily skewed in favor of special interests.

Although Roberts provides a keen, sharp-edged critique of failures in American economic practices, it seems to me that in our age of globalization his broad agenda for reform is incomplete because the international context of doing business is largely peripheral in his account. When multinational corporations are free to situate their businesses in countries where they can negotiate the lowest labor costs, be restricted by the fewest environmental and other regulations, and externalize the most costs, then those countries whose regulations better protect the welfare of their citizens will continue to lose business. But surely, it might be thought, the IMF, the WTO, and the World Bank do not permit corporations to exploit poor nations and peoples. Unfortunately, for the most part these international trade and financial institutions do not set minimal conditions for fair trade and socially beneficial business. Rather the conditions of trade and doing business are established through contracts, often arranged between partners decidedly unequal in power. Organizations like the International Chamber of Commerce exist to resolve disputes between parties to a contract, not to establish fair contracts. Certainly, some laudable attempts to provide stable, fair international business practices exist. For instance, the BASEL regulations advance banking practices designed to prevent fiscal crises. But these regulations are voluntary; they do not have the force of law. In general, minimal conditions needed to support social welfare do not have legal standing in the