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The Origins of Power, Prosperity, and Poverty

BY **DARON ACEMOGLU**

What explains the enormous differences in income per capita that exist across the world today? The question has been posed many times over. The gaps in prosperity that surround us in the modern age are much wider than those that motivated Adam Smith to write *The Wealth of Nations* in 1776, which of course is where the modern discipline of economics began. Whereas back then the gap between the richest and poorest nations was 4- or 5-fold, today it is over 40-fold. Why is it, then, that certain nations are distinguished from others in terms of wealth and poverty, health and sickness, food and famine?

Theories abound. If you turn to the popular media—or even some respectable journals such as *Science* and *Nature*—you will most likely come across articles that argue that geographic factors are what explain these differences. Climate, soil quality, disease, and the environment have all been put forth as the determining elements of prosperity. Yet, when you look at the evidence, these geographic factors don't seem to be all that important. The same countries that are very rich today were once poorer than oth-

ers with the same soil quality, for instance.

An even more popular explanation is the importance of cultural factors. You will hear, for example, that it is the difference between Catholics and Protestants (as Max Weber argued), or perhaps between Christians and Muslims and Judeo-Christians that leads to economic differences. Others have focused on Asian versus non-Asian values, or differing social attitudes toward work. The significance of cultural factors is

a popular explanation for the differences that exist between North America and the Iberian cultures of Latin America, as well.

Popular among academics and journalists is the notion that “enlightened leadership” is what matters—meaning that either leaders or their advisers have the right ideas about what drives prosperity. It's no surprise that this has some appeal to economists, who, of course, are in the business of

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MAO YUSHI (left), one of China's most outspoken and influential activists for individual rights and free markets, was named the 2012 winner of the Milton Friedman Prize for Advancing Liberty. Professor Mao accepted the award from Cato senior fellow **TOM G. PALMER** at the Washington Hilton on May 4. **PAGES 3, 13**

DARON ACEMOGLU is the Killian Professor of Economics at the Massachusetts Institute of Technology. This article is adapted from a book forum held at the Cato Institute on April 4, 2012, for his latest *New York Times* bestseller, *Why Nations Fail*, coauthored with James Robinson.



BY DAVID BOAZ

Editorial Power and Law

At Public Policy Day, our event for Cato Sponsors held after the Milton Friedman Prize for Advancing Liberty Dinner, I thanked our Sponsors for our beautiful expanded building.

But as they always say about a church, a think tank is not a building. Cato is ideas—the ideas of peace, liberty, dignity, tolerance, human rights, property rights, open markets, and limited constitutional government.

And it's the people—the people who have spent the past 35 years building the Cato Institute into what George Will called “the foremost upholder of the idea of liberty in the nation that is the foremost upholder of the idea of liberty.” That didn't happen by accident. Led by Ed Crane, a lot of people have put a lot of effort into developing the books and studies and ideas that have put Cato on the map—and into developing the institutional infrastructure that makes it possible to deliver those ideas.

Now don't get me wrong—the building is an important part of that institutional infrastructure. It's not just 76,000 square feet of a generic office building. It's a building designed for the needs of a think tank, especially with its multiple public event spaces, audio and video studios, and state-of-the-art multimedia capabilities. It's all here to help the people advance the ideas.

The Cato Institute's success is built especially on three factors: commitment to libertarian principle, nonpartisanship, and independence.

Even if they disagree with us, people know we say what we think. No politician or special interest tells us what to say. That's why Ezra Klein of the *Washington Post*, who doesn't agree with us on much, said, “When I read Cato's take on a policy question, I can trust that it is informed by more than partisan convenience. The same can't be said for other think tanks in town.” That's crucial to our success.

Just recently I've noticed several cases where Cato's longstanding efforts are having some impact:

- A shift in legal thinking toward the idea of enumerated powers and judicial enforcement of constitutional limits on government;
- The legal and policy challenge to President Obama's health care overhaul, reflecting our work in both health care policy and constitutional law;
- Latin American leaders finally echoing our 20-year critique of the war on drugs; and
- The explosion in opposition to the Stop Online Piracy Act (SOPA) and other laws that infringed on internet freedom.

It's tough to fight big government in the United States. But for many people around the world, it's a lot tougher, even dangerous, to challenge the state.

The 2012 Milton Friedman Prize for Advancing

Liberty went to Mao Yushi, who has been punished, sent down to hard labor in the countryside, expropriated, nearly starved, and threatened with death for his life-long commitment to improving the lives of the Chinese people. You can trace the history of Chinese communism—the anti-Rightist campaign, the Great Famine, the Red Guards, the Cultural Revolution—through the life of Mao Yushi. But they never broke his spirit.

Lately the newspapers are full of news about another courageous Chinese dissident, a much younger man, Chen Guangcheng. Blind from childhood, Chen was illiterate into his 20s. About the time he finally entered a school for the blind, he traveled to Beijing to appeal against unlawful taxes and organized protests against such taxes. Shades of English and American history from John Hampden and the Boston Tea Party to Vivien Kellems!

Still with no legal education, in 2005 he exposed how local authorities had enforced China's one-child policy through forced abortions and forced sterilization. He filed lawsuits, traveled again to Beijing, and talked to foreign reporters.

That was too much for the authorities. They placed him under house arrest for six months. When he tried to escape, they beat him. Then they tried him on bogus charges and sentenced him to four years in jail. After four years he was again detained in his home—all without any legal authority. They harassed his family and confiscated his six-year-old daughter's toys.

They prevented journalists, members of Congress, and even a movie star from visiting him in his home. When he smuggled out a video about his treatment, he was badly beaten.

Finally, as the world now knows, he escaped. And now he is studying the Declaration of Independence and constitutional law at a great American university.

But think of this: in a country of 1.2 billion people, the all-powerful party-state is so afraid of one blind, barely educated man. Think what that says about the desire for human freedom and the power of the freedom message.

I was asked once by some skeptics what the most important libertarian accomplishment ever was. I said “the abolition of slavery.” OK, they conceded. Name another. I thought more carefully and said “bringing power under the rule of law.”

That was a revolutionary achievement, but it's incomplete. It's what we still fight for. Heroes like Mao Yushi, Chen Guangcheng, and thousands of others fight for it. We fight for it here. Thank you for being part of that historic struggle.

“Is the most important libertarian accomplishment bringing power under the rule of law?”

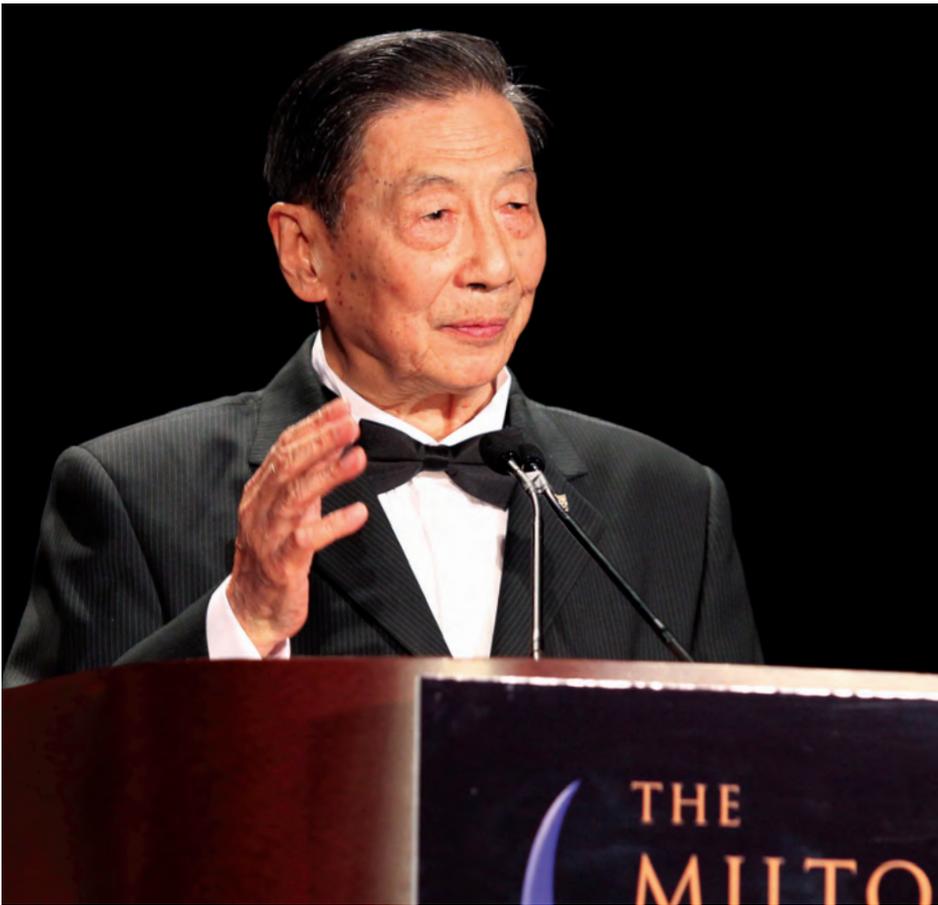


THE MILTON FRIEDMAN PRIZE FOR ADVANCING LIBERTY

China finds itself today at a crossroads. While a growing leftist movement seeks to hinge the country's future on ideologies of the past, an energized freedom campaign appears to be countering that trend. As China braces for its upcoming leadership transition, an unlikely hero has emerged from the nation's move toward liberalization.

On May 4, in recognition of his role as one of the pioneers of the freedom movement in China, Mao Yushi was awarded the 2012 Milton Friedman Prize for Advancing Liberty. Joining more than 1,000 Cato Sponsors and friends at the Washington Hilton's gala ballroom, the 83-year-old economist accepted the honor after traveling from his home in Beijing.

Before the award presentation, Chris Christie, the governor of New Jersey, offered advice to the nation at large by way of his leadership experiences at the state level. "The only thing the American people care more about than today is tomorrow," Governor Christie said, "because tomorrow is about our children and grandchildren, and today is just about us."



Originally trained as a railway engineer, Professor Mao was just 20 years old when the Chinese Revolution brought the Communist Party to power in 1949. After personally witnessing the economic devastation and social chaos that resulted, he forged his own independent movement, patiently promoting market reforms as he fearlessly illuminated the path that China would ultimately move toward.

“The journey on this road to liberty has been long,” Mao said in his acceptance speech (see page 14), delivered with the help of his granddaughter. In offering his gratitude, he acknowledged that he nevertheless stood in the shadow of those before him who sacrificed their lives in defense of liberty. “This award is accepted on behalf of them, with the solemn promise that your torch will be carried by each succeeding generation with the same energy, faith, and devotion you brought to your endeavors.”

Mao has faced a lifetime of severe punishment, exile, and near starvation for his outspoken efforts to advocate individual rights and free markets in China. Taking advantage of his country’s economic transition toward liberalization in 1978, Mao began dedicating himself to educating his fellow citizens on the ideas that animate a liberal society. Over the last two decades, he founded the Unirule Institute of Economics and the Fuping Development Institute—both of which have been instrumental in speaking out against government policies that hinder freedom of choice.





FACING: LEFT: MAO YUSHI RECOUNTED THE MANY YEARS IN WHICH HE ENDURED POLITICAL PERSECUTION IN CHINA. **ABOVE RIGHT: GOV. CHRIS CHRISTIE** CHATS WITH CATO BOARD MEMBER **JEFFREY YASS**. **MIDDLE RIGHT: MAO YUSHI** TAKES THE STAGE TO ACCEPT THE AWARD WITH HIS GRANDDAUGHTER, **MAO SHANGBIN**. **BELOW RIGHT: HARRY WU**, THE MOST PROMINENT CRITIC OF PRISON LABOR IN CHINA, AND **YU JIE**, A DISSIDENT CHINESE WRITER, JOINED THE CELEBRATION. **THIS PAGE: TOP:** CATO INSTITUTE PRESIDENT **EDWARD H. CRANE** WELCOMED MORE THAN 1,000 FRIENDS AND SUPPORTERS TO THE FRIEDMAN PRIZE DINNER. **ABOVE LEFT:** THE EVENT WAS HELD IN THE WASHINGTON HILTON'S SPECTACULAR GALA BALLROOM. **BELOW LEFT:** JUDGE **DANNY BOGGS** JOINED **JULIANA GERAN PILON** AND **ROGER PILON**, CATO'S VICE PRESIDENT FOR LEGAL AFFAIRS. **RIGHT:** IN HIS KEYNOTE ADDRESS, **GOV. CHRIS CHRISTIE** RELATED HIS EXPERIENCES IN NEW JERSEY TO THE IMPORTANCE OF PRINCIPLE IN EFFECTIVE LEADERSHIP. "I'M NOT LOOKING TO BE LOVED," HE SAID. "I GET PLENTY OF LOVE AT HOME—AND WHEN YOU'RE LOOKING FOR LOVE IN THIS JOB, THAT'S WHEN DEFICITS GET RUN UP."

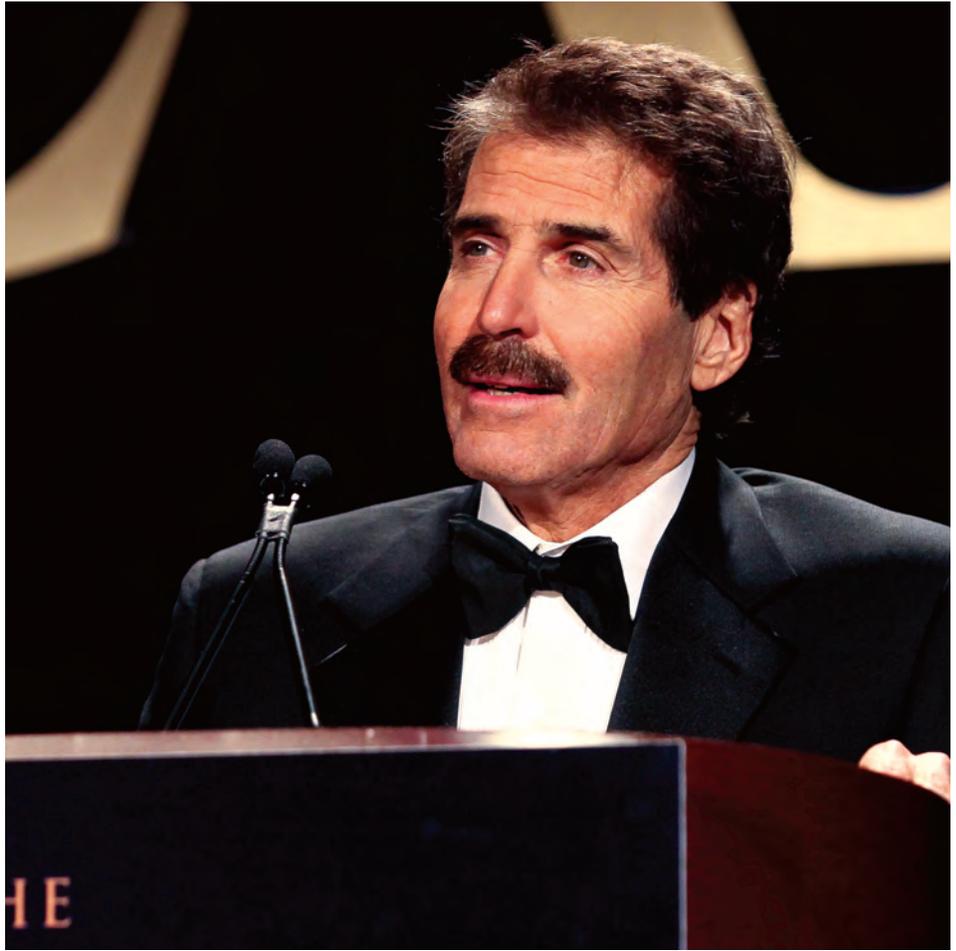




“Tonight I speak for those who cannot be here. Their sacrifices have not been in vain, and I thank the Cato Institute for giving their lives renewed meaning,” Mao said, capping off a celebration that highlighted his achievements as well as the legacy of Nobel laureate Milton Friedman.

The Friedman Prize, named in honor of the great 20th-century champion of liberty, is presented biennially to an individual who has made a significant contribution to advance human freedom. Established in 2002, the award is given out following a long process of deliberation by a distinguished panel of international judges. The honoree receives a \$250,000 cash prize, which is made possible by generous earmarked donations.





FACING: TOP LEFT: CATO SENIOR FELLOW **TOM G. PALMER** PAID TRIBUTE TO MAO YUSHI BEFORE PRESENTING HIM WITH THE FRIEDMAN PRIZE. OTHER ATTENDEES INCLUDED THE *WALL STREET JOURNAL*'S **MARY ANASTASIA O'GRADY**, A MEMBER OF THE INTERNATIONAL SELECTION COMMITTEE FOR THE PRIZE (ABOVE RIGHT); **JAY LAPEYRE**, A CATO CLUB 200 MEMBER (MIDDLE RIGHT); **MATT KIBBE**, PRESIDENT AND CEO OF FREEDOMWORKS (BELOW RIGHT); AND **BOB** AND **RUTH REINGOLD**, LONG-TIME CATO CLUB 200 MEMBERS, WITH **KRISTINA CRANE** OF THE ATLAS FOUNDATION. **THIS PAGE: ABOVE LEFT:** **SALLIE JAMES**, A CATO TRADE POLICY ANALYST, WITH HER FIANCÉ, **PAUL DIMITRI**, AND **DAN IKENSON**, DIRECTOR OF THE HERBERT A. STIEFEL CENTER FOR TRADE POLICY STUDIES, WITH HIS WIFE, **KRISTIN**. **MIDDLE LEFT:** **ROBERT A. LEVY**, CHAIRMAN OF THE CATO INSTITUTE. **BELOW LEFT:** **MAO YUSHI** AND HIS WIFE, **ZHAO YANLING**, EXCHANGED GREETINGS WITH **JAMES A. DORN**, CATO'S VICE PRESIDENT FOR ACADEMIC AFFAIRS, AND HIS WIFE, **CAROL**. **ABOVE:** **JOHN STOSSEL**, HOST OF THE FOX BUSINESS NETWORK SHOW *STOSSEL*, DISCUSSED THE IMPORTANCE OF FIGURES LIKE MAO, WHO EXPOSE THE CORRUPTION OF AUTHORITARIAN REGIMES.



On the Saturday after the Friedman Prize Dinner, the Cato Institute opened the doors of its newly expanded headquarters building on Massachusetts Avenue (above). More than 300 guests turned out for the “Liberating the Future” celebration, held in honor of the many supporters who made our recent capital campaign a success.

The morning was filled with presentations by our senior policy staff—on topics ranging from the blessings of globalization to who holds the blame for high gasoline prices. The evening was capped off by speeches from some of our long-standing supporters, followed by dinner, dancing, and live music in the Ken & Frayda Levy Liberty Garden on the building’s brand new seventh floor (right).





ABOVE LEFT: AT THE “LIBERATING THE FUTURE” CELEBRATION ON SATURDAY NIGHT, **KATHRYN WASHBURN**, WHO WAS MARRIED TO THE LATE WILLIAM A. NISKANEN, TALKED WITH SPONSOR **PETER FLINCH**, A CATO CLUB 200 MEMBER. **ABOVE RIGHT:** CATO BOARD MEMBER **DONALD G. SMITH** WITH **YARON BROOK**, PRESIDENT OF THE AYN RAND INSTITUTE. **MIDDLE:** AT PUBLIC POLICY DAY, THE MORNING AFTER THE FRIEDMAN PRIZE DINNER, MORE THAN 150 FRIENDS AND SUPPORTERS WERE TREATED TO PRESENTATIONS BY THE CATO INSTITUTE’S SENIOR STAFF, INCLUDING SENIOR FELLOWS JERRY TAYLOR, PAT MICHAELS, AND MICHAEL TANNER, AND EXECUTIVE VICE PRESIDENT DAVID BOAZ. **BELOW LEFT (UPPER):** **FRAYDA** AND **KEN LEVY**, WHO FIRST MET THROUGH THEIR PARTICIPATION IN THE CATO SPONSOR PROGRAM, CHATTED WITH **ISAAC MOREHOUSE** OF THE INSTITUTE FOR HUMANE STUDIES. **BELOW LEFT (LOWER):** CATO SENIOR FELLOWS **WILLIAM POOLE** AND **JAGADEESH GOKHALE**. **BELOW RIGHT:** **BOB** AND **RUTH REINGOLD** VISITED THE STUDENT CENTER THEY ENDOWED, A BRAND NEW FACILITY ON THE BUILDING’S FIFTH FLOOR THAT ACCOMMODATES UP TO 40 INTERNS.



Continued from page 1

developing the best micro- and macroeconomic policies—ones believed to be so critical to a nation's ultimate success.

However, once again, these all seem to have relatively little explanatory power. Remember that it was only four decades ago that many scholars were talking about the deleterious effects of Confucian values—the same cultural traits that are now touted as the foundation upon which Chinese growth has been built. And while economic policies that condemn nations to poverty abound, it will soon become clear that those policies are not adopted by mistake. They are adopted by design. It is not in the ignorance of leaders, in other words, that we should look for the causes of poverty. *It is in their incentives.* Let me explain.

INSTITUTIONS: INCLUSIVE VERSUS EXTRACTIVE

Our theory rests upon the nature of institutions—meaning the rules, both formal and informal, that govern our economic and political life. It should not come as any surprise that there are certain sets of economic institutions—property rights, enforcement of contracts, and so on—that create incentives for investment and innovation. Those institutions that create a level playing field through which a nation can best deploy its talents are referred to as “inclusive economic institutions.”

Inclusive economic institutions, however, are the exception rather than the rule. That holds true throughout history as well as around the world today. Instead, many nations today and in the past operate under extractive institutions, which do not create property rights, generate law and order, create secure contract environments, or reward innovation. They certainly do not create a level playing field, and therefore they do not encourage sustained economic growth.

As I have already mentioned, however, these extractive institutions do not develop by mistake. They are designed by the politically powerful to extract resources from the mass of society for the benefit of the few. Such institutions are in turn sustained by extractive political institutions, which con-

“There are certain sets of economic institutions—property rights, enforcement of contracts, and so on—that create incentives for investment and innovation.”

centrate power and opportunity in the hands of an elite. This elite, in essence, designs, maintains, and benefits from these extractive institutions.

So the question is: Why do these extractive institutions emerge and persist? This is where politics enters into the equation. When extractive political institutions concentrate power in the hands of the few, those groups that monopolize political power can maintain these institutions in spite of the fact that they fail to create incentives for economic growth. Let me offer an example.

CASE STUDY: SOUTH AMERICA

There is no better laboratory that demonstrates how extractive institutions emerge and persist than the New World. The Americas provide a brilliant example for understanding how different institutions form, how they become supported within different political frameworks, and how that, in turn, leads to huge economic divergences.

The economic and political institutions in the New World have been largely shaped by their colonization experience starting at the beginning of the 16th century. While the tales of Francisco Pizarro and Hernán Cortés are quite familiar, I'd like to start with Juan Díaz de Solís—a Spaniard who in 1516 initiated the colonization of the southern cone of South America, in what is today Argentina and Uruguay. Under de Solís's leadership, three ships and a crew of 70 men founded the city of Buenos Aires, meaning “good airs.” Argentina and Uruguay have very fertile lands, with a climate that would later become the basis of nearly a century of very

high income per capita because of the productivity of these areas.

The colonization of these areas itself, however, was a total failure—and the reason was that the Spaniards arrived with a given model of colonization. This model was to find gold and silver and, perhaps most importantly, to capture and enslave the Indians so that they could work for them.

Unfortunately, from the colonists' point of view, the native populations of the area, known as the Charrúas and the Querandí, consisted of small bands of mobile hunter-gatherers. Their sparse population density made it difficult for the Spaniards to capture them. They also did not have an established hierarchy, which made it difficult to coerce them into working. Instead, the Indians fought back—capturing de Solís and clubbing him to death before he could make it into the history books as one of the famous conquistadors. For those that remained, there were not enough Indians to act as workhorses, and one by one the Spaniards began to die as starvation set in.

The rest of the crew moved up the perimeter to what is now known as Asunción, Paraguay. There the conquistadors encountered another band of Indians, who on the surface looked similar to the Charrúas and the Querandí. The Guaraní, however, were a little different. They were more densely settled and already sedentary. They had also established a hierarchical society with an elite class of princes and princesses, while the rest of the population worked for the benefit of the elite.

The conquistadors immediately took over this hierarchy, setting themselves up as the elite. Some of them married the princesses. They put the Guaraní to work producing food, and ultimately the remainder of de Solís's original crew led a successful colonization effort that survived for many centuries to come.

The institutions established among the Guaraní were the same types of institutions that were established throughout other parts of Latin America: forced labor institutions with land grants for the elite Spaniards. The Indians were forced to work for whatever wages the elites would pay them. They were under constant coercive pressure—

forced not only to work but also to buy what the elites offered up for sale. It is no surprise that these economic institutions did not promote economic growth. Yet it's also no surprise that the political institutions underpinning this system persisted—establishing and continuously recreating a ruling class of elites that did not encourage economic development in Latin America.

Yet, the question still remains: Could it have been geography, culture, or enlightened leadership—rather than institutional factors—that played a critical role in the distinct fates of the two teams of explorers?

CASE STUDY: NORTH AMERICA

Roughly a thousand miles north, at the beginning of the 17th century, the model of the Virginia Company—made up of the elite captains and aristocrats who were sent to North America—was actually remarkably similar to the model of the conquistadors. The Virginia Company also wanted gold. They also thought that they would be able to capture the Indians and put them to work. But unfortunately for them, the situation they encountered was also quite similar to what the conquistadors witnessed in Argentina and Uruguay.

The joint stock companies found a sparsely populated, very mobile band of Indians who were, once again, unwilling to work in order to provide food for the settlers. The settlers therefore went through a period of starvation. However, while the Spaniards had the option of moving up north, the captains of the Virginia Company did not have this option. No such civilization existed.

They therefore came up with a second strategy. Without the ability to enslave the Indians and put them to work, they decided to import their own lower strata of society, which they brought to the New World under a system of indentured servitude. To give you a sense of this, let me quote directly from the laws of the Jamestown colony, promulgated by the governor Sir Thomas Gates and his deputy Sir Thomas Dale:

No man or woman shall run away from the colony to the Indians upon pain of death. Anyone who robs a gar-

“Inclusive economic institutions are not only more conducive to economic growth than extractive ones. They are also supported by, and support, inclusive political institutions.”

den, public or private or a vineyard or who steals ears of corn shall be punished with death. No member of the colony will sell or give any commodity of this country to a captain, mariner, master, or sailor to transport out of the colony or for his own private use upon pain of death.

Two things become immediately apparent in reading these laws. First, contrary to the image that English colonies sometimes garner, the Jamestown colony that the Virginia Company was chartered to establish was not a happy, consensual place. Pretty much anything the settlers could do would be punished by death. Second, the company encountered real problems that were cause for concern—namely, that it was extraordinarily difficult to prevent the settlers they brought to form the lower strata of society from running away or engaging in outside trade. The Virginia Company therefore fought to enforce this system for a few more years, but in the end they decided that there was no practical way to inject this lower stratum into their society.

Finally, they devised a third strategy—a very radical one in which the only option left was to offer economic incentives to the settlers. This led to what is known as the headright system, which was established in Jamestown in 1618. In essence, each settler was given a legal grant of land, which they were then required to work in exchange for secure property rights to that plot. But there

was still one problem. How could the settlers be sure that they had secure rights to that property, particularly in an environment in which a stolen ear of corn was punishable by death?

The very next year, in order to make these economic incentives credible, the General Assembly offered the settlers political rights as well. This, in effect, allowed them to advance above the lower strata of society, to a position in which they would be making their own decisions through more inclusive political institutions.

LESSONS

These historical examples illustrate several important lessons. The first is that there is clear positive feedback between inclusive economic and political institutions.

Inclusive economic institutions are not only more conducive to economic growth than extractive ones. They are also supported by, and support, inclusive political institutions, which distribute political power widely, while still achieving some amount of political centralization so as to establish law and order, the foundations of secure property rights, and an inclusive market economy.

Second, this example illustrates that none of the alternative theories has much explanatory power. The large disparities in prosperity that exist around us today formed mostly in the 19th and early 20th centuries. But why did they form? The examples we have considered give us several insights.

It wasn't geography that caused the divergence between South and North America. If anything, much of South America had higher agricultural productivity, supporting a greater population density, at the time of colonization. But South America ended up poorer than North America. This reversal cannot be accounted for by the impact of geographic factors. It wasn't some sort of culture either. In fact, it's remarkable how similar the objectives and chosen methods of the Spanish and English colonialists were. Even if their religion and culture were different, they were after the same thing and they had the same way of going about getting it. But the conditions on the ground

meant that the Spanish could achieve their goals and the English could not. And the divergence wasn't related to enlightened leadership. If anything, the Spanish leaders were more successful because they could achieve what they wanted. The Virginia Company, Sir Thomas Dale, and Sir Thomas Gates could not.

Instead, the root cause of the divergence between South and North America is in the different economic and political institutions that developed in these territories. Because the Spanish were successful in setting up extractive institutions to enrich themselves and their king, the long-run economic development of most of their empire was hampered. Because the English failed in setting up similar extractive institutions—and instead inclusive institutions started developing there—the United States would be much better placed to take advantage of new technologies and economic opportunities come the 19th century.

The history of the Americas is illustrative because it shows how the trajectory of institutions and economic development depends on whether elites bent on setting up extractive institutions succeed or fail. But the Americas are not fully representative of the rest of the world. In many other parts of the world, extractive institutions are not so much imposed from the outside, but are created by domestic elites. The crucial part of the story, therefore—which *Why Nations Fail* tries to explain in detail—is the process of institutional change.

“Most societies suffering under extractive economic institutions do so because political power is concentrated in the hands of an elite ruling under extractive political institutions.”

CONCLUSION

A key lesson of the framework we present in *Why Nations Fail* is the importance of politics. Of course, it is economic institutions that determine economic incentives and the resulting allocation of resources, investment, and innovation. But it is politics that shapes how economic institutions work and how they have evolved. Most societies suffering under extractive economic institutions do so because political power is concentrated in the hands of an elite ruling under extractive political institutions.

The recent events in the Middle East and North Africa also highlight the role of politics. The Arab Spring has shaken not only Tunisia, where it started, but Egypt, Libya, Yemen, Bahrain, and Syria, even if

the governments in the latter two countries are still holding onto power. The roots of discontent in these countries are economic and social, but those are in turn shaped by political factors. The general population has been repressed and excluded from political power for generations. The protesters in Tahrir Square in Egypt understood this and this is why they demanded not just handouts or concessions from the existing regime, but fundamental political change.

This all implies a simple but critical conclusion: You can't succeed economically if you don't get your politics right. And that's where the difficulty lies, because there is no formula for getting politics right. This is illustrated, for example, by the challenges lying ahead for the Middle East and North Africa—in particular, Egypt and Tunisia. Do we expect democracy or extremism to triumph in Egypt? Have the events in Tahrir Square changed the nature of politics irrevocably or will a similar economic and political structure reemerge under a different guise? Have they opened the way to a new authoritarian regime under the auspices of the Muslim Brotherhood? Central though these questions are for understanding the economic trajectory of the region, unequivocal answers are not possible. It's only the details of politics and how the contingent path of history will play out that will determine how successful politically and thus economically these nations will be. ■



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The Importance of Liberty: At Home and Abroad

On May 4, 2012, the Cato Institute honored economist Mao Yushi as the recipient of the 2012 Milton Friedman Prize for Advancing Liberty. One of the most outspoken activists for individual rights and free markets in China, Mao has emerged over the last several decades as an instrumental voice against the nation's heavy-handed, authoritarian grip. Before the presentation of the award, attendees heard a keynote address by Chris Christie, the governor of New Jersey. Governor Christie stressed the significance of communicating the ideas of freedom, and how his experience in office holds lessons for the nation at large.

GOV. CHRIS CHRISTIE: It's a pleasure to be here this evening—to leave all that's exciting in New Jersey on a Friday night, come down here to this sleepy little hamlet, and speak before you all.

Back in 2008, I remember Barack Obama talking about the lack of hope around the country. And although he and I always defined the solutions to that problem differently, the environment in which I found myself shortly thereafter was not significantly different.

When I first took office in New Jersey in January 2010, optimism was a hard thing to find. In the eight years before I became governor, our state had raised taxes *115 times*. From 2000 to 2009, New Jersey had—literally—a zero job growth decade. In the four years before I became governor, \$70 billion in wealth had left the state—not diminished wealth, *departed* wealth. Our unemployment rate was over 10 percent, with 115,000 private sector jobs lost during the four years of my predecessor.

New Jersey had the highest tax burden in the country, the worst climate for small business, and a bloated state government that contained the most public workers per square mile in the country—yeah, you can laugh unless you live there. And it only got worse. In my second week in office, my state treasurer told me that, in the subsequent five weeks, we had to find \$2.2 billion in cuts from money that had already been appropri-

ated. We essentially had to impound the money back from certain departments just to meet payroll—all in what was the second wealthiest state per capita in America.

If you need any greater example of what happens to an economy when a government overtaxes, overspends, overborrows, and overregulates, just visit New Jersey in January 2010.

So what did we do? Thanks to New Jersey's unique constitutional structure, which allows spending to be cut by executive order, my staff and I sat in a room over the course of three weeks and went over all 2,400 line items in the state budget that I inherited. The result was finally cutting \$2.2 billion. And the great thing about operating by executive order was that, at first, I didn't have to tell anybody.

But, after delivering the news in my first speech before the joint session, you can imagine the reaction from the legislature. Reporters descended upon the floor as the Democrats began calling me names: Julius Caesar, Napoleon Bonaparte—all of those great leaders of the past that I admire. And I realized something. The way I confronted my first substantial problem in office set the tone for my administration. I made clear from the first day that decades of fiscal irresponsibility were no longer going to be tolerated. As I said on the campaign trail, I was ready to go to Trenton and turn it upside down.

Last year we passed a \$2.3 billion tax cut

for businesses, with nearly 70,000 new private sector jobs created. We've cut spending in every department of our state government, from areas that folks told me were the third rails of politics. Given that I was still upright, I decided to go after public pensions and benefits next. And what happened? For the first time in 10 years, a majority of New Jerseyans recently polled believe the state is back on the right track. On election day in 2009, that number was 19 percent. Today, it's 53 percent.

The American people are ready to hear the truth. They know our government is out of control. And the only thing they care more about than today is tomorrow—because tomorrow is about our children and grandchildren, and today is just about us.

The bottom line is we took action—we did it with solid principles and strong leadership—putting our state's interests ahead of partisan ones. We turned Trenton upside down. And in the difficult times that America is in now, the only way to govern is by treating our citizens as adults—by telling them the truth about the depth of our challenges and the difficulty of the solutions. When we fail to do this, we pay the price as a country many times over. The domestic price is obvious: growth slows, unemployment persists, and we make ourselves even more vulnerable to the unpredictable behavior of rightfully skittish markets.

But there's also a foreign policy price to pay. To begin with, we diminish our ability to influence the thinking and ultimately the behavior of others. Democracy is the best protector of human dignity, liberty, and freedom—and history shows that mature democracies are less likely to resort to force against both their citizens and their neighbors. Yet, all across the world—in the Middle East and Asia and Africa and Latin America—people are debating their own political and economic futures. They're looking for inspiration, and we have a stake in the outcome of

those debates. There's no better way to reinforce the likelihood that others in the world will opt for more open societies and market-based economies than to demonstrate that our own system is working well.

At one time in our history, our greatness was a reflection of our country's innovation, determination, ingenuity, and the strength of our democratic institutions. When there was a crisis in the world, Americans found a way to come together to help our allies and fight our enemies. When there was a crisis at home, we put aside parochialism and put the greater public interest first.

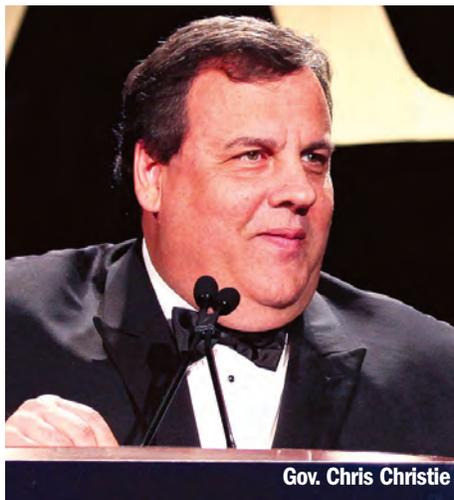
Today, our ability to effect change has been diminished because of our own inability and unwillingness to effectively deal with our problems. Now, I understand full well that succeeding at home and setting an example is not enough. But it's a start. And I realize that what I'm calling for requires a lot of our elected officials and our people. I plead guilty to that. But I also plead guilty to being an optimist, because I believe in what this country and its citizens can accomplish *if they understand what's being asked of them*.

We seem to have forgotten that this is a human business. Day after day, I've spent time sitting with colleagues on both sides of the aisle, convincing them of my intentions and letting them know that I don't believe compromise is a dirty word. There's always a boulevard between compromising your principles and getting everything you want. You should never compromise your principles.

But you also need to understand that you're not always going to get everything you want. The job of a leader is to find your way onto the boulevard between the two without driving into the ditch of compromising what you believe. And trust me, if you can do this in New Jersey, you can do it anywhere. That's where my optimism comes from. See, I'm not looking to be loved. I get plenty of love at home—and when you're looking for love in this job, that's when deficits get run up.

However, if you make people understand that you're willing to say no, but you're also always willing to listen—that you're willing to stand hard on principles, but you're also willing to compromise when those principles won't be violated—then respect will come.

It's about being consistent. It's about leading by example. It's about standing up for the things that we believe in, instead of simply trying to figure out which way the wind's blowing. There's no need for varnish anymore. In fact, I don't think we have the



Gov. Chris Christie

“If you need any greater example of what happens to an economy when a government overtaxes, overspends, overborrows, and overregulates, just visit New Jersey in January 2010.”

luxury to put it on. Liberty and freedom and the human spirit are the most powerful things in the world—and we need to say that directly to the American people. They're ready to hear it.

I want to thank the Cato Institute for setting an example of why liberty and freedom are so important to the future greatness of America. But please never forget that it's not going to come without a fight. We need to fight hard, even harder than we are now because the stakes are too great to do any-

thing less. Only then can we allow the United States to, once again, export hope and liberty and freedom around the world, not just because those values are a part of our past, but because we will be acting to make them a bedrock of our future.

MAO YUSHI: Ladies and gentleman, I bring you all my humble greetings from China. Tonight, we are here together in this “Shining City upon a Hill” to celebrate our common beliefs, our common hopes, and our common commitment to the values that make the Cato Institute so very special. Those Cato values bring us together today, united as common citizens of the world. I like to think of us all as “Cato citizens.”

The values of which I speak, of course, are peace, free markets, limited government, and the preservation of individual liberty. Tonight, we celebrate those timeless values—the common thread that runs through all great civilizations of the world from the beginning of humanity. Regardless of whether your traditions and cultural roots are in Africa, the early settlements along the Yellow River, the Tigris and Euphrates, the Nile, or the valleys and mountain ranges of Meso-America, these universal values are our common heritage. They touch each heart and resonate in the basic moral fiber of our souls.

I am personally honored and humbled to be recognized as the recipient of the Milton Friedman Prize for Advancing Liberty. I cannot express enough my grateful appreciation for this recognition and for Cato's many decades of invaluable guidance on the long road to liberty in China.

Over the last 83 years, I've endured many threats and fearful nights, years of deprivation and political persecution. My family and friends, however, provided the love, the loyalty, the dignity, and the moral compass to continue that journey, regardless of the headwinds. They helped me remember the lessons of our nation's past heroes and heroines, as well as our moral responsibilities to the future generations. They provided the light in the storm so that we could stay the course. I could not be here today without them.

My family and I are honored tonight, but we realize that we are not here just as sons

and daughters of China. We are also here on behalf of three additional constituencies who join us *in absentia*.

First, we stand in the shadows of earlier honorees from Estonia, the United Kingdom, Peru, Venezuela, and Iran. Each represents societies that have traveled on their own Homeric Odyssey, which Cato has appropriately recognized. We honor them individually and we salute their great peoples and cultures.

Secondly, we stand in the foreshadow of Cato honorees yet to emerge. To these future Cato citizens, let them know that we see their courage. We feel their heartbeats, their yearning, and their allegiance to the values of the Cato Institute. In the years to come, let everyone here be our proxy and congratulate them on their journey to a shared better tomorrow.

Thirdly, and most importantly, we receive this honor on behalf of two constituencies in China.

The first is the tens of thousands of grassroots organizations who currently work every day to serve the common citizen of China, who strive to build a better and more humane tomorrow. Countless scholars, workers, peasants, teachers, students, volunteers, and friends struggle against the common enemies of humanity: tyranny, poverty, disease, and war. They are the real honorees of tonight's prize.

The second constituency we represent is the tens of millions of Chinese over the last century who have sacrificed their lives along the road to overthrow feudal dynasties, defeat warlordism, and defend liberty against foreign colonialism and imperialist invasion. They have proven countless times that freedom is more precious than life itself, and their struggle is also revered here tonight.

This award is accepted on behalf of them, with the solemn promise that your torch will be carried by each succeeding generation with the same energy, faith, and devotion you brought to your endeavors. We do this to continue to brighten our country's future and to deliver the inalienable and universal rights of all human beings to our descendants. This glow—when combined with the lamps carried by fellow Cato citizens around the world—will become beacons of light from the “Shining City upon a Hill,” spread-

ing Cato values to the dark corners of the world. In your hands, more than mine, will rest the final success and failure and hopes for liberty of our peoples.

Many have sacrificed for China's people, for her dignity and her liberty. Despite my



“Many have sacrificed for China's people, for her dignity and her liberty. I see their faces. I hear their voices. I feel their souls.”

eight decades—my now weak hearing and failing sight—I still remember the names of those who sacrificed for our country. I see their faces. I hear their voices. I feel their souls. Tonight I speak for those who cannot be here. Their sacrifices have not been in vain, and I thank the Cato Institute for giving their lives renewed meaning.

China is a very old country. She is a noble and wise civilization, with a grand history of fine art, science, medicine, philosophy, exploration, hard work, tolerance, and openness. It is a society based on balance known as the Golden Mean, or the middle way. This theme runs through our great traditions of Daoism, Buddhism, and Confucianism. Our

people have always sought balance between the needs of the collective and the individual—and against extreme government.

China understands the power of economic liberalism. Her people know that free markets and liberty nourish each other, acting together as a force for social progress. Our long history is full of examples of people rejecting the arbitrary power of the state, refusing to subordinate the rights of the individual, and recognizing that unchecked collectivism stifles human creativity and productivity.

Systemic checks and balances against unlimited government power, corruption, and improper privileges—mechanisms which include free markets, the rule of law, an independent judiciary, and the shift to a smaller, more accountable government—need to be built and put in place permanently. These are so important because of China's horrific past. This generation has personally experienced mass repression through the government apparatus, witnessing the more than 50 million Chinese who died directly as a result of the influence of the rule of man over the rule of law.

Both our leaders and our people know what is at stake for China's future. They are all personally invested in ensuring that Cato's values—tailored to China's realities—can help build a strong, prosperous, and harmonious country in the finest traditions of our ancestors.

In modern times, many countries have recalibrated their societies to fundamentally improve them with these balanced values. In the early 1970s, there were about 40 democracies in the world. As the 20th century ended, there were 120 diverse countries with some form of self-government crafted by the people—a largely peaceful trend that continues to this day. China needs to learn from these powerfully instructive experiences.

In order to preserve societal harmony and build China's better tomorrow, the government should further extend liberty, freedom, and free markets—and reestablish the peaceful rise of “good neighbor” policy to preserve regional and world peace. If China's leaders can implement the essential principles common to every successful society, she can fur-

Continued on page 23

Cataloguing the transgressions of law enforcement

The Cato Institute Launches PoliceMisconduct.net

On May 16, 2009, two New Jersey police officers beat 21-year-old James Bayliss during a traffic stop, at one point slamming his head against a tire while his limp body lay handcuffed. Bayliss is mentally disabled. Despite dozens of attempts over the last three years, his family has still not received an explanation—though, after a video of the incident was made public this June, the state police acknowledged for the first time that unreasonable force was used.

In an effort to bring more incidents like this to light, the Cato Institute has launched PoliceMisconduct.net, a project originally created by a private researcher in 2009. The purpose of the website is to bring more attention to the problem of police wrongdoing and to identify policies that will enhance police professionalism and minimize misconduct.

The site's resuscitation comes at a time when hard information on police impropriety is severely lacking. In 2004 the Department of Justice released a statistical report analyzing misconduct trends—yet the report was based on stale data that had trickled in voluntarily from less than 5 percent of the country's 17,000 police departments. That was the last

such analysis generated by the Department of Justice.

To fill this void, our researchers are scanning media reports each day to locate news stories on misconduct, record those reports in a database, and transmit the details through a social media newsfeed on Twitter—providing transparent data that allows for independent verification through public review.

The purpose of the website is to determine the extent to which law enforcement officials exceed the limits of their authority. “We are simply trying to create a ruler with which we can measure police misconduct, so that people can determine for themselves if it’s really a problem,” says Tim Lynch, who oversees Cato’s National Police Misconduct Reporting Project, of which PoliceMisconduct.net is the cornerstone.

Each quarter, the database is reviewed, categorized, and analyzed to produce statistical reports that identify patterns in the types of misconduct that occur and what factors might affect the likelihood of abuse.

These quarterly updates will provide the



raw figures for a yearly aggregate report, which examines some of the more long-term trends that emerge—including localized rankings, agency comparisons, detailed per capita rates, and other statistical information. Over time, PoliceMisconduct.net will offer a wealth of data on what is currently one of the more obscure threats to our civil liberties.

In doing so, the new site dovetails closely with the larger mission of the Institute. “We believe good policy analysis can improve government decisionmaking,” Lynch says. To the extent that PoliceMisconduct.net provides a window into where specific procedures go wrong, we hope to improve lives as well. ■

Making the transition to sound money in the Cato Journal

The Role of Monetary Policy in a Free Society

In the Spring/Summer 2012 issue of the *Cato Journal*, Robert B. Zoellick, president of the World Bank, argues that it would be a mistake to ignore markets in the conduct of monetary policy. In an edited conversation with Sebastian Mallaby, senior fellow at the Council on Foreign Relations, Zoellick discussed how the world could potentially move to a multiple reserve currency system. He suggested that gold should be used, not as a formal anchor, but as “an information tool”—or “a check on the checkers” in the global monetary order.

Rep. Ron Paul (R-TX), chairman of the House Subcommittee on Domestic Monetary Policy, attacks the present discretionary regime, arguing instead for currency competition and ultimately a return to the gold standard. A strong critic of the Federal Reserve’s money monopoly, Paul argues that a false trust in the paper dollar has ushered in the current crisis. This policy, he argues, has been little more than “a grand deception.”

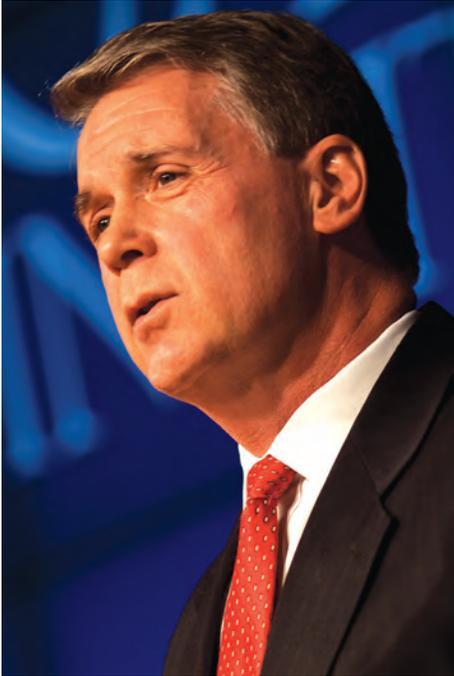
Allan H. Meltzer, a leading historian of Fed policy, makes a strong case for the adoption of monetary rules to replace pure discretion. In criticizing the Fed’s vastly increased powers of late, Meltzer examines in particular the politicized misallocation of credit. Elsewhere, economist Lawrence H. White of George Mason University provides a detailed analysis of how to make the transition to a gold standard.

John Allison, former chairman and CEO of BB&T, holds that the recent financial crisis, ensuing recession, and slow recovery were caused primarily by government policy. Those in the Fed were guilty of what F.A. Hayek called the “fatal conceit,” he explains. “I don’t care how smart you are,” Allison writes, “you cannot coordinate the economic activity of seven billion people on this planet.”

Other contributors to this issue include Jeffrey M. Lacker on “Understanding the Interventionist Impulse of the Modern Central Bank” and Gerald P. O’Driscoll Jr. on moving “Toward a Global Monetary Order.” ■

All of these articles, as well as the three book reviews in this issue of the *Cato Journal*, are available online at www.cato.org, or by subscription.





At a Cato Institute Conference on homegrown terrorism, GLENN CARLE, an author and retired CIA officer, discussed whether the terrorist threat is increasingly a local one.



At a Cato Book Forum, RUCHIR SHARMA (center), head of Emerging Market Equities at Morgan Stanley, presented some of the more surprising trends from his latest economic travelogue, *Breakout Nations: In Pursuit of the Next Economic Miracles*. Sharma was joined by SWAMINATHAN S. ANKLESARIA AIYAR (right), research fellow at Cato’s Center for Global Liberty and Prosperity, and IAN VÁSQUEZ, director of the Center.



Since the recent financial crisis, many pundits have questioned the value of homeownership. At a forum for his latest book, *American Nightmare: How Government Undermines the Dream of Homeownership*, Cato senior fellow RANDAL O’TOOLE (at podium) argued that the idea of owning a home is worth defending. O’Toole was joined by PAUL EMRATH (center) of the National Association of Home Builders and ADRIAN MOORE (right) of the Reason Foundation—as well as the Cato Institute’s MARK CALABRIA, who moderated the event.



At a Cato Institute Conference, “Is Immigration Good for America?” TAMAR JACOBY, president and CEO of ImmigrationWorks USA, discussed the current state-of-play on Capitol Hill and made her case for change in the immigration debate.



The last 100 years have seen dramatic experiments in economic policy, from the Bolshevik Revolution to the World Trade Organization. In his new book, *The Clash of Economic Ideas*, LAWRENCE H. WHITE (left) of George Mason University examines the intellectual roots of today’s debates, tying the development of economic ideas to the key events in economic history. At a Cato Book Forum, White was joined by JAMES A. DORN, vice president for academic affairs at the Institute, and SYLVIA NASAR, author of *A Beautiful Mind* and *Grand Pursuit: The Story of Economic Genius*.



At a memorial service to celebrate the life of William A. Niskanen, longtime chairman of the Cato Institute, guests were treated to a tribute by the Capitol Hill Chorale, to which Niskanen belonged. The service included testimonials from many of Niskanen’s colleagues and friends, including Lew Uhler, Richard E. Wagner, and Mickey D. Levy.



At a policy lunch on succeeding in the media world, TUCKER CARLSON, editor in chief of the *Daily Caller* and a senior fellow at the Cato Institute, addressed a room full of aspiring journalists in the beautiful new George M. Yeager Conference Center. Among the many topics he addressed were health care and the upcoming election. “There are only two people in world history who have signed laws containing an individual mandate. One’s the president, the other’s running against him,” Carlson said. “So somehow, out of three hundred and fifteen million Americans, the Republican Party managed to find the one guy who couldn’t run on Obamacare.”



At a forum for his new book, *The Lost Majority: Why the Future of Government Is up for Grabs—and Who Will Take It*, author SEAN TRENDE (center) of RealClearPolitics joined legendary pollster LANCE TARRANCE, JR. (at podium), and EMILY EKINS, research fellow at the Cato Institute, to discuss the future of American politics.



SEN. RAND PAUL (R-KY) spoke at a recent Cato Book Forum for Ron Paul’s *rEVOLution: The Man and the Movement He Inspired*, along with the author, *Reason* magazine’s Brian Doherty.



At a Cato luncheon in May, pioneering development economist **ARNOLD HARBERGER** (left) shared a word with **RICARDO LÓPEZ MURPHY**, former finance minister of Argentina. López Murphy was in town to discuss the current economic and political landscape in his country.



In her new book, **LINDA KILLIAN** (left) argues that independent and swing voters are “the centrist voters who decide elections and represent more voters than those at the conservative and liberal ends of the spectrum.” At a forum for her new book, *The Swing Vote*, Killian joined **DAVID KIRBY** of FreedomWorks, coauthor of Cato studies on “the libertarian vote,” for an uncommon look at the American electorate.



As military spending starts to decline, naval shipbuilding has been under close scrutiny. Speaking to journalists after a Cato Policy Forum on the future of the surface fleet, **ROBERT WORK**, under secretary of the Navy, addressed questions on the current composition of the naval combatant fleet and its potential impact on future missions.



CHRIS EDWARDS (left), director of tax policy studies at the Cato Institute, and former Florida governor **JEB BUSH** testified at a House Budget Committee hearing on “Removing the Barriers to Free Enterprise and Economic Growth,” chaired by Rep. Paul Ryan.



ALLAN H. MELTZER, professor of political economy at Carnegie Mellon University and a leading authority on Fed policy, discussed his new book, *Why Capitalism?* at a Cato Book Forum in April.

APRIL 4: *The Lost Majority: Why the Future of Government Is Up for Grabs—and Who Will Take It*

APRIL 4: *Why Nations Fail: The Origins of Power, Prosperity, and Poverty*

APRIL 11: Succeeding in the World of Media and Policy, with Tucker Carlson

APRIL 11: Trade Policy Priority One: Averting a U.S.-China Trade War

APRIL 13: Evaluating the Homegrown Terrorist Threat

APRIL 18: Cato Club Naples: The Great Contradiction—Government Schooling for a Free Society

APRIL 19: *Free Market Fairness*

APRIL 20: Citizens v. the Ruling Elite

APRIL 23: “Stand Your Ground” Laws: Self-Defense or License to Kill?

APRIL 24: *Why Capitalism?*

APRIL 25: *The Swing Vote: The Untapped Power of Independents*

Cato Calendar

CONSTITUTION DAY

Washington • Cato Institute
September 18, 2012

Speakers include Paul Clement.

CATO CLUB 200 RETREAT

Asheville, NC • Inn on Biltmore Estate
September 27–30, 2012

Speakers include David Stockman, Charles Murray, and John Allison.

CATO INSTITUTE POLICY PERSPECTIVES 2012

New York • Waldorf-Astoria
October 26, 2012

CATO INSTITUTE POLICY PERSPECTIVES 2012

Chicago • The Drake
November 28, 2012

MONEY, MARKETS, AND GOVERNMENT: THE NEXT 30 YEARS

30th Annual Monetary Policy Conference
Washington • Cato Institute
November 15, 2012

Speakers include Vernon L. Smith, Thomas Hoenig, Charles Plosser, Lawrence H. White, George S. Tavlas, Allan H. Meltzer, and John B. Taylor.

CATO INSTITUTE POLICY PERSPECTIVES 2013

Naples, FL • Waldorf-Astoria
January 30, 2013

25TH ANNUAL BENEFACITOR SUMMIT

Scottsdale, AZ • Four Seasons Resort
February 21–24, 2013

APRIL 26: Is Immigration Good for America?

APRIL 27: Talking Shop: Online News Editors

APRIL 30: Nuclear Weapons Spending in the 2013 Budget

APRIL 30: *Financing Failure: A Century of Bailouts*

MAY 4: 2012 Milton Friedman Prize for Advancing Liberty

MAY 5: Public Policy Day and “Liberating the Future” Celebration

MAY 9: Federal Cyber-Security Regulation: Critical Safety Measure, or Privacy Nightmare?

MAY 11: *The Clash of Economic Ideas*

MAY 14: The American Welfare State: How We Spend Nearly \$1 Trillion a Year Fighting Poverty—and Fail

MAY 15: *The Tea Party: Three Principles*

MAY 15: *Ron Paul’s rEVOLUTION: The*

Man and the Movement He Inspired

MAY 16: *American Nightmare: How Government Undermines the Dream of Homeownership*

MAY 17: The Future of Federal Highway Finance: Diversions, Deficits, or Devolution?

MAY 17: Investment Protectionism and What to Do about It

MAY 18: Gasoline Prices: Who’s to Blame and What to Do?

MAY 21: The Future of the U.S. Navy Surface Fleet

MAY 22: Breakout Nations: In Pursuit of the Next Economic Miracles

MAY 23: Corporate Tax Reform: An International Perspective

MAY 30: What Made the Financial Crisis Systemic?

Audio and video for all Cato events dating back to 1999, and many events before that, can be found on the Cato Institute website at www.cato.org/events. You can also find write-ups of Cato events in Ed Crane’s bimonthly memo for Cato Sponsors.

Should Policymakers Be Encouraging Homeownership?

Since 1997, the erratic behavior of real estate prices has led many to reexamine the nature, size, and role of housing policy in the United States. In “Questioning Homeownership as a Public Policy Goal,” Morris A. Davis of the University of Wisconsin argues that we should rethink whether encouraging homeownership is a desirable objective for policymakers to pursue. Morris begins his study by challenging the effectiveness of housing policy. While federal attempts to reduce the burden of mortgage interest have done little to boost homeownership over the last four decades, “the cost of these policies is astounding,” he writes—calculating that their net present value is on the order of \$2.5 trillion. As such, Morris then turns to the motives behind these interventions: Should homeownership be encouraged as an explicit policy goal? He argues that it should not. “Housing is a risky asset,” he explains, with several peculiar liabilities that come along with it. Given the questionable benefits associated with those

policies that further homeownership, Morris concludes that government institutions designed to promote them are deeply flawed. “We need to unwind the current set of public policies,” he writes—and “rethink whether homeownership is a desirable public policy goal” to begin with.

Making Roads More Responsive

For more than 50 years, the funds to build, operate, and maintain federal and state highways have come primarily from the gasoline tax. But in “Ending Congestion by Refinancing Highways” (Policy Analysis no. 695), Cato senior fellow Randal O’Toole proposes an entirely new system to pay for the country’s network of roads. According to O’Toole, the current scheme is fatally flawed for several reasons. To begin with, gas taxes fail to price congested roads properly—creating well over \$100 billion worth of annual delays. In addition, they fail to cover the costs of all roads—leaving local government dependent on approxi-

mately \$30 billion of general funds. Finally, gas taxes fail to keep up with increasingly fuel-efficient cars. “When combined with inflation,” O’Toole writes, “this means the tax paid by car owners per mile of driving is less than a third of what their grandparents paid in 1956.” The solution, O’Toole suggests, is to switch to an affordable vehicle-mile fee system—one that preserves privacy, eliminates congestion, and adequately funds roads in a revenue-neutral manner. This, ultimately, would “make road providers more responsive to users because the providers would depend on them, rather than politicians, for revenues.”



The Tilt of Public Broadcasting

Since its creation in 1967, public broadcasting in the United States has been in the

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crosshairs of critics. In **“If You Love Something, Set It Free: A Case for Defunding Public Broadcasting”** (Policy Analysis No. 697), Cato legal associate Trevor Burrus assesses the industry with a critical eye, examining the necessity, prudence, and constitutionality of PBS, NPR, and similar media organizations. “Public broadcasting,” Burrus says, “fails all three tests.” His analysis illustrates the role of political influence in public media operations, evidenced in debates such as the removal of Juan Williams from NPR. Public broadcasting has a reputation for being biased, or “tilted,” as Burrus prefers to call it. The “exclusion of groups from coverage seems to be driven more by the group’s ability to create a political fuss sufficient to bend the ears of public broadcasters than by good journalistic standards,” he writes. As such, Burrus argues that the only solution is to defund it. “Public broadcasting not only can survive on its own, it can thrive”—and ultimately be free.

Competing Currencies

The Federal Reserve has a monopoly on currency in the United States. In **“Competition in Currency: The Potential for Private Money”** (Policy Analysis no. 698), West Texas A&M economist Thomas L. Hogan makes a strong case for monetary reform by applying firmly established free-market concepts to the dollar itself. “Privately issued money can benefit consumers in many ways,

particularly in the areas of value stability and product variety,” he says. “Unlike a central bank, competing private banks must attract customers by providing innovative products, restricting the quantity of notes issued, and limiting the riskiness of their investing activities.” Hogan points to Hong Kong, Scotland, and Northern Ireland, where “private banks issue banknotes redeemable for the national currency. Despite the availability of central banknotes in these locales, consumers transact almost exclusively in private currency.” The analysis covers the complexities that the Fed faces, saying it has “neither the incentive nor the information to optimize the size of the money supply.” To make things worse, these “monetary policies intentionally deceive dollar holders in order to influence spending and economic activity.” Lastly, Hogan discusses the challenges American private banks would have in issuing currency, and for some, recommends commodity-backed notes as a potential remedy.

The Poverty of Welfare

On January 8, 1964, President Lyndon B. Johnson delivered a State of the Union address to Congress in which he declared an “unconditional war on poverty in America.” Yet, despite nearly \$15 trillion in total welfare spending since then, the poverty rate is perilously close to where we began more than 40 years ago. As Michael Tanner, director of health and welfare studies at the Cato

Institute, points out in **“The American Welfare State: How We Spend Nearly \$1 Trillion a Year Fighting Poverty—and**



Fail” (Policy Analysis no. 694), the poverty rate is now at 15.1 percent—its highest level in nearly a decade. “When most Americans think of welfare, they think of the cash benefit program known as

Temporary Assistance to Needy Families,” Tanner writes. In reality, however, this represents just one of 126 separate federal government programs designed to fight poverty. In 2011 the federal government spent approximately \$668.2 billion—which represents an increase of more than \$193 billion since Barack Obama became president. Federal welfare spending, in other words, has increased by 41 percent since 2008, “roughly two and a half times greater than any increase over a similar time frame in U.S. history.” Yet, for all of the money thrown at the problem, the United States has made remarkably little progress in reducing poverty. As such, Tanner calls for a new approach. “All of this suggests that the answer to poverty lies not in the expansion of the welfare state, but in building the habits and creating the conditions that lead to prosperity.” ■

Continued from page 15

ther contribute to the world’s peace, prosperity, and harmony.

I remain optimistic that China’s government will hear her people’s desire to make this vision a reality. If one examines our country objectively, they will see that there is great reason to be hopeful given China’s tremendous progress already. Edmund Burke, the great British parliamentarian, once warned that “a state without the means of some change is without the means of its conservation.” China has been changing and progressing—a process which does not require disruptive instant transformation.

Our country has successfully raised more than 300 million people from poverty—a

huge number, even in China. Knowingly or not, accomplishments like this have been achieved by the balanced implementation of Cato values in the context of the Chinese society. China’s successful evolution over her long history has been rooted in the balance between rights and responsibilities—a balance that is in focus now as we approach a transition in leadership at the end of this year.

Those of us in China know that the rights of the individual do not come from the generosity of the state. In fact, we have very limited expectations from government. We ask only that the system lives up to our constitution, abides by our laws, and complies with the international covenants of the world community. The people of China know that

the fruits of society are not the sole prerogative of the powerful and privileged few. As the next generation steps forward to battle against tyranny, poverty, disease, and war itself, I believe that our journey into the future will be long, but successful.

All big rivers come from small streams. Our efforts in China are but one small stream.

Tonight’s constituencies—from the people of China to the other tributaries inspired by the timeless wisdom of the Cato Institute—will join together as a mother river to nourish the human spirit and wash away the hardships of our imperfect world.

Thank you once again for this great honor. ■

CATO POLICY REPORT

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Washington, D.C. 20001

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CATO

“To Be Governed...”

DEMOCRACY IN ACTION

In the midst of the Presidential election, a new national survey from Xavier University's Center for the Study of the American Dream reveals one in three native-born citizens failed the civics portion of the naturalization test. . . .

59% of survey respondents could not name one power of the federal government, 77% could not name one power of the states, and 62% could not name the Governor of their state. . . .

When asked questions about our government and political leaders, the survey results found:

- 85% did not know the meaning of the “the rule of law.”
- 82% could not name “two rights stated in the Declaration of Independence.”
- 75% were not able to correctly answer “What does the judiciary branch do?”
- 71% were unable to identify the Constitution as the “supreme law of the land.”
- 68% did not know how many justices are on the Supreme Court.
- 63% could not name one of their two US Senators.
- 62% could not identify “What happened at the Constitutional Convention?”
- 62% could not answer “the name of the Speaker of the US House.”

—Xavier University, April 27, 2012

BAD APPLE! BAD APPLE!

Apple is taking a bruising in Washington, and insiders say there's a reason: It's the one place in the world where the company hasn't built its brand.

In the first three months of this year, Google and Microsoft spent a little more than \$7 million on lobbying and related federal activities combined. Apple spent \$500,000—even less than it spent the year before.

The company's attitude toward D.C.—described by critics as “don't bother us”—has left it without many inside-the-Beltway friends.

—Politico, May 9, 2012

WASHINGTON'S ONE PERCENT

Long before “the 1 percent” became part of the political lexicon, a growing number of highly educated, dual-income families were driving the [Washington] region's top income levels into the stratosphere.

To be considered part of the 1 percent in this area, it takes a household income far above the national average of \$387,000. The gateway for the region is \$527,000. In the District, the top 1 percent of households bring in at least \$617,000; in Montgomery County, more than \$606,000; and in Fairfax County, \$532,000, according to an analysis of census statistics by The Washington Post and Sentier Research, a firm that specializes in income data. . . .

The percentage of area households with impressive, if not eye-popping, salaries has grown as well. In 1980, just 3 percent of households in the region had incomes that were the equivalent of \$200,000 or more in today's dollars. Now [after an increase in the national debt from \$1 trillion to \$15 trillion] 13 percent do.

—Washington Post, April 22, 2012

ARE WE THE WORLD'S POLICEMAN?

Behind razor wire and bamboo walls topped with security cameras sits one of the newest U.S. military outposts in Africa. U.S. Special Forces soldiers with tattooed forearms and sunglasses emerge daily in pickup trucks that carry weapons, supplies and interpreters—as well as the expectations of a vast region living in fear of a man and his brutal militia.

“The Americans have captured Osama bin Laden and Saddam Hussein,” said Bassiri Moke, a tribal chief. “Surely they can catch Joseph Kony.”

In this far-flung nook of central Africa, the United States has assumed a small but vital role in one of Africa's most vexing military challenges: to capture Kony and dismantle his Lord's Resistance Army.

—Washington Post, April 16, 2012

SO LET'S HAVE THEM OVERSEEN BY THE \$3.6 TRILLION FEDERAL GOVERNMENT

[James] Dimon, chairman and chief executive of J.P. Morgan Chase & Co., is showing that large banks are far too big to manage.

—Francesco Guerrera, Wall Street Journal, May 15, 2012

THE JOY OF TAX

Doug Shulman is America's top taxman, the commissioner of the Internal Revenue Service. Shulman says he loves his job, even though he knows he's not the most popular man in the country.

“The IRS, in many ways, is a misunderstood agency. When people hear the letters, ‘I-R-S,’ sometimes they have a negative connotation,” Shulman says. “But 80 percent of Americans get an average of a \$3,000 refund. So most people actually have a very pleasant experience with us.”

—Morning Edition, National Public Radio, April 16, 2012

IT'S ALSO EASIER IF YOU LIVE IN LONDON

Howard Stern: You like Obama?

Elle MacPherson: Yeah, I'm living in London and I'm socialist. What do you expect?

—Howard Stern Show, March 13, 2012