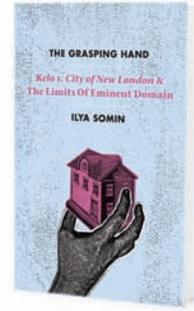




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Cato Policy Report

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How Piketty Misses the Point

BY DEIRDRE N. MCCLOSKEY

Thomas Piketty has written a big book—577 pages of text; 76 pages of notes; 115 charts, tables, and graphs—that has excited the left worldwide. First published in French in 2013, an English edition was issued last year to wide acclaim and a top position on the *New York Times* bestseller list. It has been a long time since a technical treatise on economics has had such a market. An economist can only applaud. And an economic historian can only wax ecstatic.

Piketty’s central theme is the force of interest on inherited wealth causing, he claims, increasing inequality of the income earned from the wealth. In 2014 he declared to the BBC’s Evan Davis that “money tends to reproduce itself,” a complaint about money and its interest rate repeatedly made in the West since Aristotle. As the philosopher said of some men, “the whole idea of their lives is that they ought either to increase their money without limit, or at any rate not to lose it. . . . The most hated sort [of increasing their money]. . . is usury, which makes a gain out of money itself.”

Piketty’s theory is that the yield on capital usually exceeds the growth rate of the economy, and so the share of capital’s returns in national income will steadily increase, simply because interest income is growing faster than the income the whole society is getting. Let us therefore bring in the government to imple-

ment “a progressive global tax on capital”—to tax the rich. It is, he says, our only hope.

Reading the book is a good opportunity to understand the latest of the leftish worries about capitalism, and to test its economic and philosophical strength. Piketty’s worry

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DEIRDRE N. MCCLOSKEY is Distinguished Professor of Economics and of History at the University of Illinois at Chicago and the author of *Bourgeois Equality: How Ideas, Not Capital, Enriched the World* (University of Chicago Press), to be published in January 2016. A longer version of this article appears in the *Erasmus Journal of Philosophy and Economics*.

In May, leading academics and prominent reformers came together to examine the Greek debt crisis at a conference in Athens cosponsored by the Atlas Network, the Cato Institute, and the Friedrich Naumann Foundation for Freedom. **TOM G. PALMER** (left), executive vice president of Atlas and a senior fellow at Cato, welcomed Greek finance minister **YANIS VAROUFAKIS**, who gave a keynote address in which he weighed the government’s options for reform in the face of mounting international concerns. **PAGE 12**



BY DAVID BOAZ

EDITORIAL

Second-Best Solutions

Two issues this summer—gay marriage and trade agreements—highlight the Cato Institute’s efforts to apply libertarian principles to specific policy issues, and the angst that sometimes generates among principled libertarians.

The Cato Institute has urged the Supreme Court for several years now to find that the exclusion of gay couples from legal marriage violates the equal protection clause of the Fourteenth Amendment to the Constitution. At the end of June, it did, in the case of *Obergefell v. Hodges*. Throughout the 20-year debate over gay marriage, some libertarians have insisted that legal marriage should not be extended to include gay people; rather, government should get entirely out of the business of licensing marriage. Let people write contracts, and marry in churches if they choose, but leave government out of it.

That’s an appealing libertarian position. In fact, I wrote one of the first articles proposing it (“Privatize Marriage,” *Slate*, 1997). I said that social conflicts, such as the then-growing conflict over same-sex marriage, can “be depoliticized and somewhat defused if we keep them out of the realm of government.”

But there’s a problem: The country was not and is not ready to privatize marriage. So then should libertarians advocate only a radical libertarian policy solution that won’t be implemented any time soon, leaving some people excluded from a legal institution open to others? Or do they advocate a second-best solution, equality under the law for whatever services government supplies? As Steven Horwitz, author of the forthcoming book *Hayek’s Modern Family: Classical Liberalism and the Evolution of Social Institutions*, puts it:

Suppose we had a Social Security system in which all residents of the US paid FICA but only white ones received the benefits. Would you argue that the libertarian position is to continue to deny people of color access to Social Security benefits on the grounds that giving the benefits to them would “extend federal power”? Would you continue to insist that the only libertarian position is to argue for the elimination of Social Security even though it continues to benefit only whites?

Cato chairman Robert A. Levy has written that “marriage today should be a private arrangement, requiring minimal or no state intervention . . . [but] whenever government imposes obligations or dispenses benefits, it may not deny to any person within its jurisdiction the

equal protection of the laws.”

Cato Unbound editor Jason Kuznicki argues, however, that privatizing marriage would mean “much greater government interference in family life, higher taxes for married couples, invasions of privacy, difficulties related to child custody, and other negative consequences.” So that’s another perspective. And of course my colleagues and I intend to fight for religious liberty, as we have always done, including the liberty of bakers, florists, and others not to participate in weddings or other activities that offend their conscience.

Trade agreements present similar challenges. Scholars at Cato’s Herbert A. Stiefel Center for Trade Policy Studies have generally supported trade agreements such as NAFTA and the new Trans-Pacific Partnership. In the past few months they have advocated giving President Obama “trade promotion authority” (TPA), also known as “fast-track,” to let the administration negotiate trade agreements that Congress can reject or ratify, but not amend.

Some libertarian critics say that 2,000-page agreements such as NAFTA are by definition not free trade: a free-trade agreement would take one page. Unilateral free trade would be even better. They have a point.

But again, it isn’t within Cato’s power to wave a magic wand and make free trade or marriage privatization happen. So our scholars usually opt for trying to move policy in a better direction. Center director Dan Ikenson writes, “Despite their flaws, free trade agreements have helped reduce domestic impediments to trade, expand our economic freedoms, and lock in positive reforms, even if only as the residual byproduct of an ill-premised mercantilist process. Ultimately, free trade agreements have delivered freer trade.” Not free trade, alas. But freer trade.

As I put it in a Facebook debate in June, “Best is best, but better is better than worse.” And that’s the standard that has mostly guided us at Cato for 38 years. We want to push public debate and public policy in a direction consistent with liberty and limited government. Sometimes, as in my book *The Libertarian Mind* and much of the material on *Libertarianism.org*, that entails laying out the case for libertarianism and strictly limited government. And sometimes, as in many of our policy studies, it involves offering politically realistic reform plans or second-best solutions.

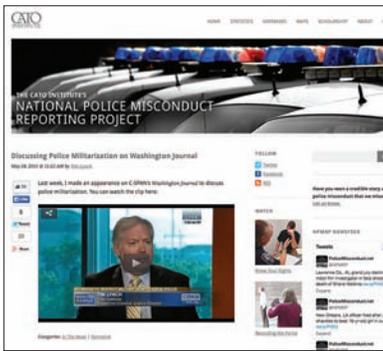
“Best is best, but better is better than worse. And that’s the standard that has mostly guided us at Cato for 38 years.”

Tracking law enforcement abuse

Three Years of 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 in the years following the incident, his family received no explanation—though, after a video was eventually made public, the state police acknowledged for the first time that unreasonable force was used.

More recently, the death of Freddie Gray while in custody in Baltimore has triggered a wide-ranging debate about policing in America. In order to grapple



with the difficult issues surrounding these tragedies, the Cato Institute offers PoliceMisconduct.net—a project originally created by a private researcher in 2009. The purpose of the website, which marked three years under the editorship of Cato’s Tim Lynch in May, has been to bring more attention to the problem of police wrongdoing. Ultimately, the goal is to identify policies that will enhance professionalism and minimize misconduct.

To fill the void in hard data on policy impropriety, the Institute’s researchers scan 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. “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 Lynch, who oversees the Institute’s National Police Misconduct Reporting Project, of which PoliceMisconduct.net is the cornerstone.

“The victims of police misconduct are too often without a voice, and the extent of the problem was unknown because few seemed interested enough to study it,” he added. “We at Cato thought it important to lend some institutional support to this critical area.” Over the past year, the website has been cited by the *Washington Post*, the *Wall Street Journal*, *The Economist*, ABC News, the *Atlantic*, and *Frontline*.

Over time, PoliceMisconduct.net will offer a wealth of data on what is currently one of the most troubling threats to our civil liberties. In doing so, the new site dovetails closely with the mission of the Institute at large. “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.

PLEASE CHECK OUT CATO’S NATIONAL POLICE MISCONDUCT REPORTING PROJECT BY VISITING POLICEMISCONDUCT.NET.

LAYING BARE LEVIATHAN

DownsizingGovernment.org is complete! Created by Chris Edwards, Cato’s director of tax policy studies, the site is designed to help policymakers and the public understand where federal funds are being spent and how to reform each government department. In identifying specific programs to cut, DownsizingGovernment.org describes the failings of federal agencies and explores the systematic reasons why government programs are often obsolete, mismanaged, and dysfunctional. Edwards describes the site with more brevity, calling it “a great aid to help the layman understand where his money goes in Washington.”

By visiting pages dedicated to each agency and department, users can quickly assess the growth of budgets, pinpointing billions of dollars in cuts that can be responsibly made. The site also now includes an updated charting tool, which allows users to plot real outlays for about 500 departments, agencies, and programs dating back to 1970. Nowhere is more information about the alarming size of the federal government more readily accessible. Simply put, government is too big and needs to be cut. DownsizingGovernment.org shows how to do exactly that.

IDEAS WITHOUT BOUNDARIES

Since 2005 *Cato Unbound* has given readers access to a state-of-the-art virtual trading floor in the intellectual marketplace. Every month one of the world’s leading thinkers presents an essay on a topical issue. A panel of distinguished experts responds, each offering his case before challenging and refining the arguments in an ongoing conversation. Readers are then encouraged to join the dialogue, with these contributions pulled together to create an easily accessible media product that is virtually distinct within the digital realm.

The latest issue of *Cato Unbound* looks at civil commitment, a legal process that involuntarily confines individuals for purposes of medical treatment. It is not intended to punish a crime. Rather, it has been most commonly applied to the mentally ill, particularly those who pose a danger to themselves or others. In recent years, however, civil commitment has been extended to many others, including sex offenders, typically after they have already served a prison term. Is civil commitment ever justified? If so, is it being applied fairly in our current legal system? Visit www.cato-unbound.org to find out.



At a Cato Policy Forum in May, EUGENE GHOLZ, associate professor at the University of Texas at Austin, discussed his new study investigating how changing trade flows and energy revenues affect U.S. national security.



With polls routinely showing majority support for legalization of marijuana, the legal cannabis economy is likely to boom. In April (from left) KAT MURTI of the Cato Institute, AMY POINSETT of MJ Freeway, BETTY ALDWORTH of Students for Sensible Drug Policy, and TAYLOR WEST of the National Cannabis Industry Association considered the ways in which this new industry can harness the power of technology.



Despite many predictions to the contrary, the British Conservative Party secured a majority in the House of Commons in May's general election. At a Cato Policy Forum, IAIN MURRAY, vice president at the Competitive Enterprise Institute, asked what this means for the state of freedom in the United Kingdom. "Government spending has been coming down," he said. "However, over the past fifteen years, it has been interfering more and more in the lives of individual businessmen."



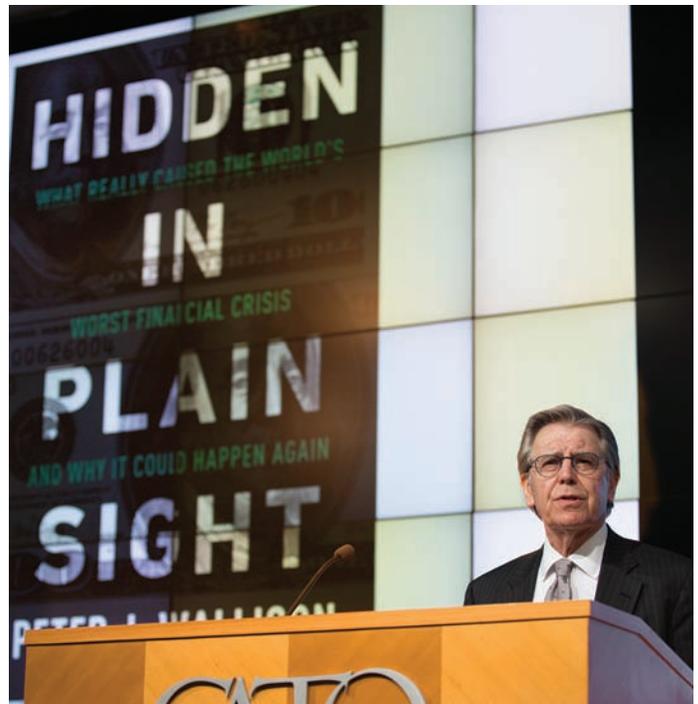
RENE QUASHIE, senior counsel at Epstein, Becker & Green, discussed regulations at both the state and national level that have interfered with the ability of online medical care to cross traditional borders.



The *Newburgh Sting*, a recent documentary from HBO, shows how an undercover FBI informant induced four men to join a plot to blow up a Bronx synagogue and attack a nearby U.S. military base. After segments of the film were featured in the F. A. Hayek Auditorium, Cato senior fellow JOHN MUELLER (left) echoed the words of a federal judge in the case: “The government indisputably ‘manufactured’ the crimes of which the defendants stand convicted.”



From the Great Depression to the financial crisis of 2008, reform attempts have rested on the assumption that the crises were caused by securities market participants misbehaving. In *Wasting a Crisis*, Paul Mahoney, dean of the University of Virginia School of Law, shows that this narrative is formulated by political actors hoping to deflect blame from prior policy errors.



Presenting his new book *Hidden in Plain Sight*, PETER J. WALLISON, the Arthur F. Burns Fellow at the American Enterprise Institute, argued that it was federal mandates, not greed, that drove the demand for subprime lending and ultimately led to the 2008 financial crisis.

Continued from page 1

about the rich getting richer is indeed merely the latest of a long series going back to Thomas Malthus, David Ricardo, and Karl Marx. Since those founding geniuses of classical economics, trade-tested progress has enormously enriched large parts of humanity—which is now seven times larger in population than in 1800—and bids fair in the next 50 years or so to enrich everyone on the planet. And yet the left routinely forgets this most important secular event since the invention of agriculture—the Great Enrichment of the last two centuries—and goes on worrying and worrying in a new version every half generation or so.

All the worries, from Malthus to Piketty, share an underlying pessimism, whether from imperfection in the capital market or from the behavioral inadequacies of the individual consumer or from the Laws of Motion of a Capitalist System. During such a pretty good history from 1800 to the present, the economic pessimists on the left have nonetheless been subject to nightmares of terrible, terrible faults. Admittedly, such pessimism sells. For reasons I have never understood, people like to hear that the world is going to hell, and become huffy and scornful when some idiotic optimist intrudes on their pleasure. Yet pessimism has consistently been a poor guide to the modern economic world.

SUPPLY, DEMAND, AND CREATIVE DESTRUCTION

The technical flaws in Piketty's argument are pervasive. When you dig, you find them. The fundamental problem is that Piketty does not understand how markets work. In keeping with his position as a man of the left, he has a vague and confused idea about how supply responds to higher prices. Startling evidence of Piketty's miseducation occurs as early as page 6.

He begins by seeming to concede to his neoclassical opponents: "To be sure, there exists in principle a quite simple economic mechanism that should restore equilibrium

“For reasons I have never understood, people like to hear that the world is going to hell, and become huffy and scornful when some idiotic optimist intrudes on their pleasure.”

to the process: the mechanism of supply and demand. If the supply of any good is insufficient, and its price is too high, then *demand for that good should decrease, which would lead to a decline in its price.*" The words I italicize clearly mix up movement along a demand curve with movement of the entire curve, an error of first-term college students. The correct analysis is that if the price is "too high" it is not the whole demand curve that "restores equilibrium," but an eventually outward-moving supply curve. The supply curve moves out because entry is induced by the smell of super-normal profits.

Piketty does not acknowledge that each wave of inventors, entrepreneurs, and even routine capitalists find their rewards taken from them by entry. Look at the history of fortunes in department stores. The income from department stores in the late 19th century, in Le Bon Marché, Marshall Field, and Selfridge's, was entrepreneurial. The model was then copied all over the rich world. In the late 20th century the model was challenged by a wave of discounters, and they then in turn by the internet. What happens is that the profit going to the profiteers is more or less quickly undermined by outward-shifting supply. The original accumulation dissipates.

The economist William Nordhaus has calculated that the inventors and entrepreneurs nowadays earn in profit only 2 percent of the social value of their inventions. If you are Sam Walton the 2 percent gives you personally a great deal of money from introducing

bar codes into stocking of supermarket shelves. But 98 percent at the cost of 2 percent is nonetheless a pretty good deal for the rest of us. The gain from macadamized roads or vulcanized rubber, then modern universities, structural concrete, and the airplane, has enriched even the poorest among us.

HUMAN CAPITAL AND INEQUALITY

This brings me to the next technical problem. Piketty's definition of wealth does not include human capital, owned by the workers, which has grown in rich countries to be the main source of income, when it is combined with the immense accumulation since 1800 of capital in knowledge and social habits, owned by everyone with access to them. Once upon a time, Piketty's world without human capital was approximately our world, that of Ricardo and Marx, with workers owning only their hands and backs, and the bosses and landlords owning all the other means of production. But since 1848 the world has been transformed by what sits between the workers' ears.

The only reason in the book to exclude human capital from capital appears to be to force the conclusion Piketty wants to achieve. One of the headings in Chapter 7 declares that "capital [is] always more unequally distributed than labor." No it isn't. If human capital is included—the ordinary factory worker's literacy, the nurse's educated skill, the professional manager's command of complex systems, the economist's understanding of supply responses—the workers themselves, in the correct accounting, own most of the nation's capital—and Piketty's drama falls to the ground.

Finally, as he candidly admits, Piketty's own research suggests that only in the United States, the United Kingdom, and Canada has income inequality increased much, and only recently. In other words, his fears were not confirmed anywhere from 1910 to 1980; nor anywhere in the long run at any time before 1800; nor anywhere in Continental Europe and Japan since World War II; and only recently, a little, in the United States,

the United Kingdom, and Canada. That is a very great puzzle if money tends to reproduce itself as a general law. The truth is that inequality goes up and down in great waves, for which we have evidence from many centuries ago down to the present, which also doesn't figure in such a tale.

Sometimes Piketty describes his machinery as a "potentially explosive process." At other times, he admits that random shocks to a family fortune means that "it is unlikely that inequality of wealth will grow indefinitely . . . rather, the wealth distribution will converge toward a certain equilibrium." On the basis of the *Forbes* lists of the very rich, Piketty notes, for example, "several hundred new fortunes appear in [the \$1 billion to \$10 billion] range somewhere in the world almost every year." Which is it, Professor Piketty? Apocalypse or a steady share of rich people constantly dropping out of riches or coming into them, in evolutionary fashion?

The science writer Matt Ridley has offered a persuasive reason for the slight rise in inequality recently in Britain. "Knock me down with a feather," Ridley writes:

You mean to say that during three decades when the government encouraged asset bubbles in house prices; gave tax breaks to pensions; lightly taxed wealthy non-doms [that is, "non-domiciled," the citizens of other countries such as Russia and Saudi Arabia living in the U.K.]; poured money into farm subsidies; and severely restricted the supply of land for housing, pushing up the premium earned by planning permission for development, the wealthy owners of capital saw their relative wealth increase slightly? Well, I'll be damned. . . . [Seriously, now] a good part of any increase in wealth concentration since 1980 has been driven by government policy, which has systematically redirected earning opportunities to the rich rather than the poor.

“The central problem with the book is an ethical one. Piketty does not reflect on why inequality by itself would be bad.”

In the United States, one can make a similar case that the government, which Piketty expects to solve the alleged problem, is in fact the cause.

IS INEQUALITY BAD?

The central problem with the book, however, is an ethical one. Piketty does not reflect on why inequality by itself would be bad. To be sure, it's irritating that a super rich woman buys a \$40,000 watch. The purchase is ethically objectionable. She should be giving her income in excess of an ample level of 2 cars, say, not 20; 2 houses, not 7; 1 yacht, not 5—to effective charities. Andrew Carnegie enunciated in 1889 the principle that "a man who dies thus rich dies disgraced." Carnegie gave away his entire fortune. (Well, he gave it at death, after enjoying a castle in his native Scotland and a few other baubles.)

But the fact that many rich people act in a disgraceful fashion does not automatically imply that the government should intervene to stop it. People act disgracefully in all sorts of ways. If our rulers were assigned the task in a fallen world of keeping us all wholly ethical, the government would bring all our lives under its fatherly tutelage, a nightmare achieved approximately before 1989 in East Germany and now in North Korea.

Notice that in Piketty's tale the rest of us fall only relatively behind the ravenous capitalists. The focus on relative wealth or income or consumption is one serious problem in the book. Piketty's vision of apocalypse leaves room for the rest of us to do very well indeed—rather non-apocalyptically—as in fact since 1800 we have. What is worrying Piketty is that the rich might possibly get richer, even

though the poor get richer, too. His worry is purely about difference, about a vague feeling of envy raised to a theoretical and ethical proposition.

But our real concern should be with raising up the poor to a condition of dignity, a level at which they can function in a democratic society and lead full lives. It doesn't matter ethically whether the poor have the same number of diamond bracelets and Porsche automobiles as do owners of hedge funds. But it does indeed matter whether they have the same opportunities to vote or to learn to read or to have a roof over their heads.

Adam Smith once described the Scottish idea as "allowing every man to pursue his own interest his own way, upon the liberal plan of equality, liberty and justice." It would be a good thing, of course, if a free and rich society following Smithian liberalism produced a Pikettyan equality. In fact, it largely has, by the only ethically relevant standard of basic human rights and basic comforts. Introducing liberalism in Hong Kong and Norway and France, for instance, has regularly led to an astounding betterment and to a real equality of outcome—with the poor acquiring automobiles and hot-and-cold water at the tap that were denied in earlier times even to the rich, and acquiring political rights and social dignity that were denied in earlier times to everyone except the rich.

The economists Xavier Sala-i-Martin and Maxim Pinkovsky report on the basis of detailed study of the individual distribution of income—as against comparing distributions nation-by-nation—that "world poverty is falling. Between 1970 and 2006, the global poverty rate has been cut by nearly three quarters. The percentage of the world population living on less than \$1 a day (in PPP-adjusted 2000 dollars) went from 26.8% in 1970 to 5.4% in 2006."

In 2013 the economists Donald Boudreaux and Mark Perry noted that "according to the Bureau of Economic Analysis, spending by households on many of modern life's

'basics'—food at home, automobiles, clothing and footwear, household furnishings and equipment, and housing and utilities—fell from 53 percent of disposable income in 1950 to 44 percent in 1970 to 32 percent today.”

The economist Steven Horwitz summarizes the facts on labor hours required to buy a color TV or an automobile, and notes that “these data do not capture . . . the change in quality . . . The 1973 TV was at most 25 inches, with poor resolution, probably no remote control, weak sound, and generally nothing like its 2013 descendant . . . Getting 100,000 miles out of a car in the 1970s was cause for celebration. Not getting 100,000 miles out of a car today is cause to think you bought a lemon.” He observes further that “looking at various data on consumption, from Census Bureau surveys of what the poor have in their homes to the labor time required to purchase a variety of consumer goods, makes clear that poor Americans are living better now than ever before. In fact, poor Americans today live better, by these measures, than did their middle class counterparts in the 1970s.”

The political scientist and public intellectual Robert Reich argues that we must nonetheless be alarmed by inequality, rather than devoting all our energies to raising the absolute condition of the poor. “Widening inequality still hampers upward mobility,” he declares. Reich is mistaken. Horwitz summarizes the results of a study by Julia Isaacs on individual mobility from 1969 to 2005: “82% of children of the bottom 20% in 1969 had [real] incomes in 2000 that were higher than what their parents had in 1969. The median [real] income of those children of the poor of 1969 was double that of their parents.” There is no doubt that the children and grandchildren of the Dust Bowl refugees in California, for example, are much better off than their fathers or grandfathers. John Steinbeck chronicled in *The Grapes of Wrath* their worst and terrible times. A few years later many of the Okies got jobs in the war industries, and many of their children later went to university. Some then went on to

“In the historical lottery the idea of an equalizing liberty and dignity was the winning ticket, and the bourgeoisie held it.”

become university professors who think that the poor are getting poorer.

THE MAIN EVENT: THE GREAT ENRICHMENT

The most fundamental problem in Piketty's book, then, is that he misses the main act. In focusing solely on the distribution of income, he overlooks the most surprising secular event in history: the Great Enrichment of the average individual on the planet by a factor of 10 and in rich countries by a factor of 30 or more. Many humans are now stunningly better off than their ancestors were. This includes a gigantic improvement of the poorest—your ancestors and mine. By dramatic increases in the size of the pie, the poor have been lifted to 90 or 95 percent of equal sustenance and dignity, as against the 10 or 5 percent attainable by redistribution without enlarging the pie.

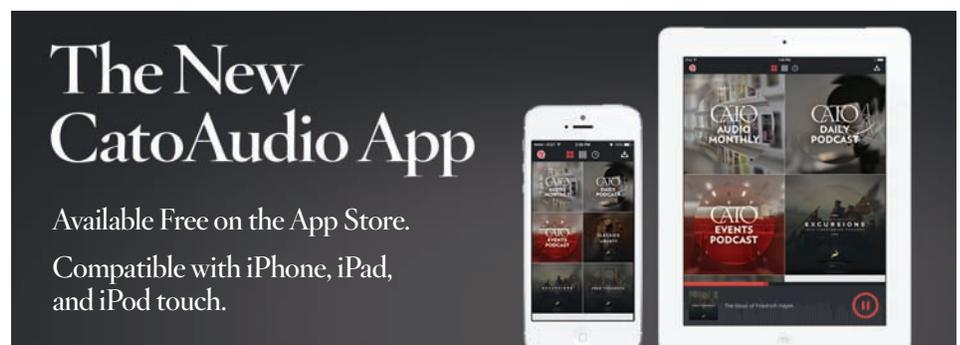
What caused the Great Enrichment? It cannot be explained by the accumulation of capital, as the very name “capitalism” implies. Our riches were not made by piling brick upon brick, bachelor's degree upon bachelor's degree, bank balance upon bank balance, but by piling idea upon idea. The bricks, BAs,

and bank balances were of course necessary. Oxygen is necessary for a fire. But it would be unenlightening to explain the Chicago Fire of 1871 by the presence of oxygen in the earth's atmosphere.

The original and sustaining causes of the modern world were indeed ethical, not material. They were the widening adoption of two new ideas: the liberal economic idea of liberty for ordinary people and the democratic social idea of dignity for them. This, in turn, released human creativity from its ancient trammels. Radically creative destruction piled up ideas, such as the railways creatively destroying walking and the stage coaches, or electricity creatively destroying kerosene lighting and the hand washing of clothes, or universities creatively destroying literary ignorance and low productivity in agriculture. The Great Enrichment requires not accumulation of capital or the exploitation of workers but what I call the Bourgeois Deal. In the historical lottery the idea of an equalizing liberty and dignity was the winning ticket, and the bourgeoisie held it.

That even over the long run there remain some poor people does not mean the system is not working for the poor, so long as their condition is continuing to improve, as it is, and so long as the percentage of the desperately poor is heading toward zero, as it is. That people still sometimes die in hospitals does not mean that medicine is to be replaced by witch doctors, so long as death rates are falling and so long as the death rate would not fall under the care of the witch doctors.

It is a brave book Thomas Piketty has written. But it is mistaken. ■



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Toward a Libertarian Foreign Policy

For decades, libertarians have expressed pointed and principled opposition to U.S. interventionism, offering alternatives that have been largely ignored by policymakers in Washington. The promises of stability and peace from both Democratic and Republican administrations have yet to be fulfilled, and the costs of foreign wars in blood, treasure, and prestige have taken their toll. The American public is both tired and wary of intervention. Has the time finally come for a libertarian foreign policy? At a Capitol Hill Briefing in May, several experts came together to examine this question. Christopher A. Preble, vice president for defense and foreign policy studies at the Cato Institute; Jim Antle, managing editor of the *Daily Caller*; and Justin Logan, director of foreign policy studies at the Cato Institute, considered what a more libertarian foreign policy would mean for American security.

CHRISTOPHER A. PREBLE: An abhorrence of war flows from the classical liberal tradition. Adam Smith taught that “peace, easy taxes and a tolerable administration of justice” were the essential ingredients of good government. War, on the other hand, is the largest and most far-reaching of all statist enterprises. It’s an engine of collectivization that undermines private enterprise, raises taxes, destroys wealth, and subjects all aspects of the economy to regimentation and central planning.

It also subtly alters the citizens’ view of the state. “War substitutes a herd mentality and blind obedience for the normal propensity to question authority and to demand good and proper reasons for government actions,” the late scholar Ronald Hamowy writes in *The Encyclopedia of Libertarianism*. He continues, “War promotes collectivism at the expense of individualism, force at the expense of reason and coarseness at the expense of sensibility. Libertarians regard all of those tendencies with sorrow.”

Nobel Laureate Milton Friedman stated the issue more succinctly. “War is a friend of the state,” he told the *San Francisco Chronicle* about a year before his death. “In time of war, government will take powers and do things that it would not ordinarily do.”

The evidence is irrefutable. Throughout human history, government has grown dur-

ing wartime, rarely surrendering its new powers when the guns fall silent.

Some might claim that a particular threat to freedom from abroad is greater than anything we could do to ourselves in fighting it. But that is a hard case to make. Even the post-9/11 “global war on terror”—a war that hasn’t involved conscription or massive new taxes—has resulted in wholesale violations of basic civil rights and an erosion of the rule of law. From Bush’s torture memos to Obama’s secret kill list, this has all been done in the name of fighting a menace—Islamist terrorism—that has killed fewer American civilians in the last decade than allergic reactions to peanuts. It seems James Madison was right. It was, he wrote, “a universal truth that the loss of liberty at home is to be charged to the provisions against danger, real or pretended, from abroad.”

But surely, some say, the United States is an exceptional nation that serves the cause of global liberty. The United States pursues a “foreign policy that makes the world a better place,” explains Sen. Lindsey Graham, “and sometimes that requires force, a lot of times it requires the threat of force.” By engaging in frequent wars, even when U.S. security isn’t directly threatened, the United States acts as the world’s much-needed policeman. That’s the theory, anyway.

In practice, the record is decidedly mixed. This supposedly liberal order does not work as well as its advocates claim. The world still has its share of conflicts, despite a U.S. global military presence explicitly oriented around stopping wars before they start. The U.S. Navy supposedly keeps the seas open for global commerce, but it’s not obvious who would benefit from closing them—aside from terrorists or pirates who couldn’t if they tried. Advocates of the status quo claim that it would be much worse if the United States adopted a more restrained grand strategy, but they fail to accurately account for the costs of this global posture, and they exaggerate the benefits. And, of course, there is the obvious case of the Iraq War, a disaster that was part and parcel of this misguided strategy of global primacy. It was launched on the promise of delivering freedom to the Iraqi people and then to the entire Middle East. It has had, if anything, the opposite effect.

Libertarians should immediately understand why. We harbor deep and abiding doubts about government’s capacity for effecting particular ends, no matter how well intentioned. These concerns are magnified, not set aside, when the government project involves violence in foreign lands.

In domestic policy, libertarians tend to believe in a minimal state endowed with enumerated powers, dedicated to protecting the security and liberty of its citizens but otherwise inclined to leave them alone. The same principles should apply when we turn our attention abroad. Citizens should be free to buy and sell goods and services, study and travel, and otherwise interact with peoples from other lands and places, unencumbered by the intrusions of government.

But peaceful, non-coercive foreign engagement should not be confused with its violent cousin: war. American libertarians have traditionally opposed wars and warfare,

even those ostensibly focused on achieving liberal ends. And for good reason. All wars involve killing people and destroying property. Most entail massive encroachments on civil liberties, from warrantless surveillance to conscription. They all impede the free movement of goods, capital, and labor essential to economic prosperity. And all wars contribute to the growth of the state.

JIM ANTLE: I want to focus on the politics of what makes it difficult for there to be a libertarian foreign policy. There are a lot of political and structural impediments to the government doing less of anything. And there's a strong bias among the American people that when you face some economic or social problem—from healthcare to education to welfare—the government should do something. When you say the government should do less or limit its response, many are skeptical.

When it comes to foreign crises, you're constantly faced with bad actors on the international stage—from dictators to ayatollahs. The argument that we should restrict intervention or avoid projecting strength often doesn't resonate. What's interesting, however, is that you generally don't get both of these attitudes—government activism at home and abroad—from the same person.

Those most likely to grasp that government is not the solution to every domestic problem are the most likely to be skeptical of that argument when it's presented in foreign policy. And that really means that those advocating a libertarian foreign policy are men and women without a country. In our binary political system, there's no party or constituency that's really speaking for that viewpoint.

You can see the evidence of that in the congressional vote for the Iraq War. Among Republicans, there were only seven who voted against authorization. What's less well remembered is that half the Democrats in the Senate voted to authorize the Iraq War. The list includes Hillary Clinton, Joe Biden,

John Kerry, Chuck Schumer, and Harry Reid. These are not “back-bencher” Democrats. They're some of the most prominent figures, including the supposed Peace Party's most likely next candidate for president of the United States.

That means that the parties really present an echo, not a choice. There's this “me tooism,” even when it comes to Democrats. In some respects, that makes sense because



“There are political and structural impediments to the government doing less of anything.”

they're the party that believes in the government's ability to keep us safe all of the time and in every situation. But some of it is also a relic of politics from the 1980s and 1990s, when a lot of these people came of age at a time when the Democratic Party was seen as weak on foreign policy. A lot of Democrats internalized that critique and regarded it as a political liability. Ultimately, they tried to counter that liability by becoming more hawkish.

The odd thing about that is that it doesn't reflect many of the trends in public opinion,

particularly those of rank-and-file Democrats. But politicians tend to stick with the ideas they adopted during their formative years. So you have a generation of hawkish Democrats leading a party of people who are hesitant to see such an outsized U.S. role in the world, and particularly in the Middle East. Thus a lot of the core assumptions that are being batted around by both parties in discussing the potential nuclear threat from Iran are very similar to the core assumptions that led us into the Iraq War.

So what do we do about this? There was a period when we were seeing real growth in the libertarian wing of the Republican Party, and some chastened conservatives seemed to be moving in that direction. But, again, it's easier to make those arguments when everything is going well. As soon as there's any significant instability in the world, it becomes much harder to make non-interventionist arguments in foreign policy. The Republican Party seems at the moment to be reverting to form.

But I don't think all is necessarily lost. True, the political incentives for even the best-intentioned libertarian-leaning Republicans are bad. They will be punished by the loudest voices on the right if they say anything that deviates from the idea of aggressively projecting strength. At the same time, there's been a lot of success framing a libertarian non-interventionism as President Barack Obama's foreign policy. Now I find it interesting that a president who escalated one war, launched two more without congressional approval, and proposed a fourth is any kind of non-interventionist. But there you have it. Our binary political system makes it difficult to have these debates in a nuanced fashion.

On the positive side, I've always argued that we need to get people who are engaged in economics—those conservatives and libertarians who specialize in fiscal areas—to be a little more vocal on foreign policy. In private, you often hear a lot of conservative

budget experts express their doubts about an ever-expansive military footprint abroad. There of course still needs to be some foreign policy expertise that comes from a less interventionist perspective on the right. But, in the meantime, as we cultivate those voices, there's a vacuum that needs to be filled by people who are philosophically sympathetic to less intervention and yet specialize in other issues. They shouldn't let the wall of separation between budget gurus and defense hawks dictate what the Republican Party's foreign policy is going to be.

JUSTIN LOGAN: I want to start off by asking: What do people want from foreign policy? And I want to first consider whether or not the foreign policy judgments of libertarians, conservatives, and liberals flow from their respective political philosophies.

In a basic sense, what we want from foreign policy is the efficient production of national security. We want to make sure that Americans are safe, that our sovereignty is protected, and that we have the ability to live our lives without coercion from some external threat. Simply put, if someone has a good way of achieving these ends, everyone should support it—libertarians, liberals, conservatives, whomever. Thus, the first-order considerations about foreign policy turn on questions about how dangerous the world is and how to effectively interact with it.

In terms of what libertarian foreign policy scholars believe, on those first-order considerations, most think that the United States is the most secure great power in modern history. We're not in Shangri-La or the Garden of Eden, but we're pretty close. Libertarians also think that if the United States defended fewer countries on their behalf, they would defend themselves to a greater extent than they do now.

In a recent academic article, it's mentioned that the United States has formal treaty commitments to countries comprising 75 percent of the world's gross domestic prod-

uct. That is a striking figure. To what extent has Uncle Sam become Uncle Sucker? The U.S. government is paying for other people's defense, forcibly taking money from taxpayers in order to spend it on other countries.

To be more provocative, I think the greatest threat to U.S. national security in recent decades has been the ideas that have sprung from the minds of the American foreign policy elite—not al Qaeda, not Iran, not China,



“What we want from foreign policy is the efficient production of national security.”

not Russia. Rather, the wreckage that the American foreign policy elite has produced in carnage and in trillions of dollars squandered has been most damaging to Americans' well-being.

But it's on second-order considerations where I think we can draw a straight line from libertarian principles to opposition to ambitious foreign policies. For instance, war makes the government bigger. War is very damaging to civil liberties. War costs lots of money, damages lives, and leads to corruption. But

unless you're a pacifist, those second-order considerations really are subordinate. If we could never do anything to violate civil liberties, or if we could never do anything to get our fellow citizens killed in large numbers, if we could never do anything that spent lots of money on overseas adventures, then we would never have any security commitments. If the cost of protecting civil liberties were an ISIS amphibious landing in Miami, many libertarians would support abrogating civil liberties. So what we're trying to figure out is when a libertarian would support damaging liberty and favor intervention.

But that goes back to those first-order considerations about the nature of the world in which we live, how states relate to one another, and how secure the United States is. A belief in the value of a system of government that embraces individual liberty doesn't necessarily tell you how much to worry about China. All political philosophies need help in thinking about how to craft foreign policy.

To recapitulate, what's libertarian about our foreign policy is a concern for those second-order implications. As to the first-order judgments about how dangerous the world really is, a political theory that prioritizes liberty is only so much help. Only in extreme circumstances—one example being the Iraq War—could we say that a foreign policy is blindingly anti-libertarian.

So what do libertarians (or conservatives or liberals) need to bring to the table in order to think about these first-order considerations? They need theories of international politics and foreign policy. They need an understanding of how states relate to one another, what causes conflicts, and how to judge those threats. With some exceptions, libertarian foreign policy scholars embrace a school of thought called realism. Realism is a pessimistic view of the world. It holds that states jealously compete with one another for power and position. It's skeptical

Continued on page 19

A conference in Athens on the fiscal catastrophe in Greece

Emergency Economic Summit for Greece

Greece has been in the spotlight for more than five years since the country's debt crisis erupted. Throughout that time, both the country's political class and the broader international community have focused largely on the bailout negotiations, Greece's place in the Eurozone, and the "austerity" policies implemented by successive governments. What has become overwhelmingly clear throughout this process is that the Greek economy cannot continue on its present path, going from one crisis to the next.

At a conference held this May in Athens, successful economic reformers and leading academics presented a realistic diagnosis of the Greek government's problems, as well as the policy changes that would return the country to growth and prosperity. Cohosted by the Cato Institute, the Friedrich Naumann Foundation for Freedom, and the Atlas Network and its local partners, the forum provided an opportunity for a frank discussion with the Greek public and Greek policy makers about what has to happen to set the country on the path toward fiscal responsibility.

Various experts at the event each offered their judgement on how to best avoid this cycle of crises in the future. As Omaira Gill of *Vice* magazine wrote, "Greek Finance Minister Yanis Varoufakis made a brief appearance at the Emergency Economic Summit for Greece, organized by the Atlas Network and the Cato Institute, to say the country could not keep lurching from bailout to bailout but must insist on radical change." Varoufakis added, however, that the government cannot be expected to reform itself. He declared that all parties should acknowledge that Greece's debt is unpayable and that postponing a debt restructuring—which is ultimately unavoidable—would



ABOVE: More than 500 guests attended the Emergency Economic Summit for Greece held in Athens in May, a conference cohosted by the Cato Institute and the Atlas Network, among others. BELOW: Keynote speakers included Nobel laureate THOMAS SARGENT (left)—who stressed the necessity of setting the country on a path toward fiscal responsibility—as well as economist NICHOLAS ECONOMIDES (right), Greek finance minister Yanis Varoufakis, and former Bulgarian deputy prime minister Simeon Djankov.

only be counterproductive. "For the last five years we've been going from bailout to bailout, loan to loan, crisis to crisis," he said. "We need to see how we can use public assets through privatization . . . [to] create the investment flows and bring investment in from the private sector."

Thomas Sargent, a Nobel laureate in economics, said that tough choices will need to be made in spite of the immediate pain they inflict. The goal should be to revive international confidence in Greece over the long-term. Sargent compared the problems in Greece to those difficulties within the European Union at large, drawing parallels to the continent's bailouts and debt restructuring measures. In both cases, he said, the countries in question are facing punishing taxes, prolonged joblessness, and stagnant economic growth as a result of the unsustainable commitments of their governments. As Greek newspapers noted, Sar-

gent also responded to Varoufakis's remarks directly. "This is a crisis of insolvency, and the position of his government is that the people on the other side should just understand that they are not going to pay that whole amount," he said. This is unrealistic, Sargent said. Fiscal crises like this, he added, are due to "the macroeconomics of broken promises"—and any solution needs to address that underlying cause.

Other speakers at the conference included Nicholas Economides, professor of economics at the Stern School of Business at New York University, on the structural reforms needed in Greece; Juan José Daboub, former managing director of the World Bank, comparing the Greek situation to the economic crises in Latin America over the years; and Simeon Djankov, former deputy prime minister and finance minister of Bulgaria, discussing the role of municipal corruption and cronyism. ■

Cato at Times Square

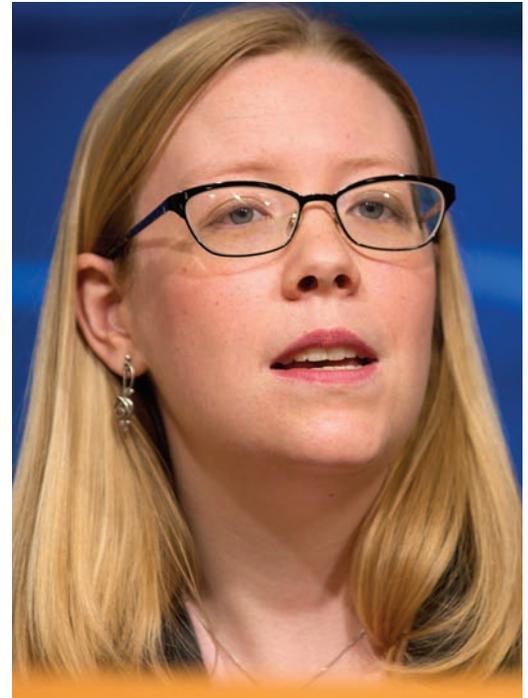


Individual liberty and limited government light up Times Square. All summer long, Cato's commitment to stopping the government from overspending, overregulating, policing the world, and invading our privacy has been shining down to passersby from a jumbo screen at Broadway and West 43rd Street. In conjunction with this, a special section was created on the Cato website for those who visited the site after viewing the advertisement, highlighting Cato scholars' work on the subjects raised, along with links to the wide range of other current, new, and emerging issues

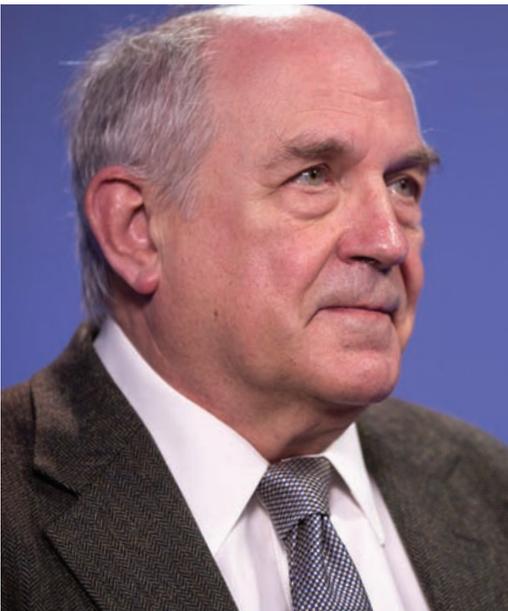
Cato scholars are exploring every day.



The Federal Reserve’s monetary policies have become a topic of bitter debate. At a Cato Policy Forum in April, (from left) former U.S. comptroller general DAVID WALKER, DAVID WESSEL of the Brookings Institution, MARK CALABRIA of the Cato Institute, and JOSH ZUMBRUN of the *Wall Street Journal* debated whether or not performing a program audit on the Fed is good public policy.



EMMA ASHFORD, a visiting fellow at the Institute, argued at a Cato Policy Forum in April that America’s goals in Syria are unclear, pointing to the broad consensus that the current approach—loosely defined as “degrading and destroying” ISIS—is murky at best.



In May, CHARLES MURRAY of the American Enterprise Institute joined the Institute’s director of multimedia for a Cato podcast conversation about his new book, *By the People: Rebuilding Liberty without Permission*.



The death of Freddie Gray in Baltimore has ignited a wide-ranging debate about policing and poverty in American cities. At a Capitol Hill Briefing in May, several Cato scholars considered the lessons from this tragedy, discussing everything from the effectiveness of body cameras in law enforcement to whether the Department of Justice should sue the city of Baltimore for civil rights violations.



At a Capitol Hill Briefing on international strategies that have been proven to restrain public spending, DANIEL J. MITCHELL (left), senior fellow at the Cato Institute, spoke with CLEMENT LEUNG, Hong Kong's commissioner to the United States, about one of the world's most successful spending caps.

APRIL 2: Drinks at your Fingertips: Klink and Regulatory Hurdles to Alcohol Delivery

APRIL 7: Did Affordable Housing Policy Cause the Financial Crisis, and Can It Happen Again?

APRIL 10: Cato Institute Policy Perspectives 2015 (New York)

APRIL 10: Defining the Tax Base: The Real Challenge for Tax Reform

APRIL 13: *The Newburgh Sting* and the FBI's Production of the Domestic Terrorism Threat

APRIL 16: Cato Institute Policy Perspectives 2015 (Dallas, TX)

APRIL 17: Cato Institute Policy Perspectives 2015 (Houston, TX)

APRIL 17: Should GAO Audit the Federal Reserve?

APRIL 23: America and the Middle East Mess

APRIL 27: High Tech: How the Burgeoning Legal Cannabis Industry Is Harnessing Technology

APRIL 30: In Search of a Syria Strategy

APRIL 30: Cato Institute Policy Forum and Luncheon 2015 (St. Louis, MO)

MAY 1: National Security Implications of New Oil and Gas Production Technologies

MAY 4: South Africa: The Next Ten Years

MAY 7: Toward a Libertarian Foreign Policy

MAY 11: The U.S. National ID Law at 10 Years

MAY 12: *Economic Interdependence and War*

MAY 13: Cato Institute Policy Perspectives 2015 (Palo Alto, CA)

MAY 13: *Wasting a Crisis: Why Securities Regulation Fails*

MAY 15: Threats to the U.S. Energy Renaissance

MAY 19: Emergency Economic Summit for Greece (Athens)

MAY 20: The State of Freedom in the UK

MAY 22: Lessons from Baltimore

MAY 26: *The Global Village Myth: Distance, War, and the Limits of Power*

MAY 27: Proven Strategies to Restrain Spending: An International Perspective

MAY 28: Removing Barriers to Online Medical Care

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NOVEMBER 5, 2015

RETHINKING MONETARY POLICY 33RD ANNUAL MONETARY CONFERENCE
WASHINGTON • CATO INSTITUTE
NOVEMBER 12, 2015

Speakers include James Bullard, Jeffrey Lacker, Rep. Bill Huizenga, Claudio Borio, Manuel Sanchez, George S. Tavlvas, George Selgin, and John B. Taylor.

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CATO INSTITUTE POLICY PERSPECTIVES 2016
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LAS VEGAS • FOUR SEASONS HOTEL
FEBRUARY 25–28, 2016

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OCTOBER 13–16, 2016

A new book that revisits the controversy behind *Kelo v. City of New London*

The Grasping Hand

In 2005 the Supreme Court ruled that the city of New London, Connecticut, could condemn 15 residential properties in order to transfer them to a new private owner. Although the Fifth Amendment only permits the taking of private property for “public use,” the court ruled that the transfer of condemned land to private parties for “economic development” is permitted by the Constitution—even if the government cannot prove that the expected development will ever actually happen. The decision in *Kelo v. City of New London* perpetuated the Court’s long-standing failure to enforce constitutional property rights.

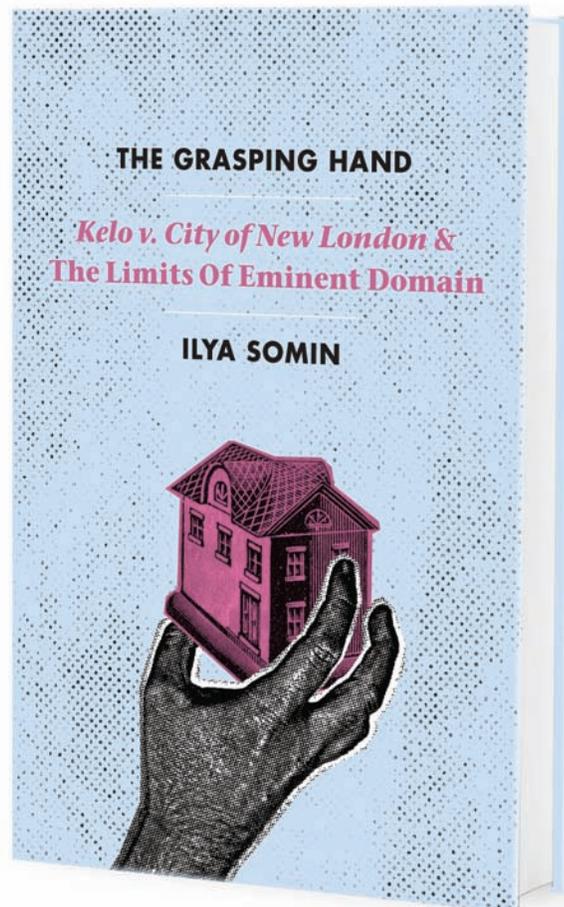
In *The Grasping Hand: Kelo v. City of New London and the Limits of Eminent Domain*, author Ilya Somin offers the first book-length analysis by a legal scholar of one of the most controversial Supreme Court cases in modern times. A law professor at George Mason University and an adjunct scholar at the Cato Institute, Somin presents a detailed study of the infamous decision alongside a broader history of the dispute over public use. He also evaluates the options for reform. Ultimately, Somin concludes, *Kelo* was a tragedy at the end of a long line of grave errors.

“The right to private property is a central part of the American constitutional tradition and of our political culture,” Somin writes. “But for many decades, federal courts—and especially the Supreme Court—have given constitutional property rights far less protection than that routinely granted to other constitutional rights.” Somin argues that the courts have abdicated their responsibility in this regard. “To a large extent, they have left those rights at the mercy of the very government officials that they are supposed to protect us against.”

Economic development and “blight” condemnations are unconstitutional under both originalist and most “living constitu-

tion” theories of legal interpretation. They also victimize the poor and the politically weak for the benefit of powerful interest groups and often destroy more economic value than they create. *Kelo* itself exemplifies these patterns, according to Somin. The residents targeted for condemnation lacked the influence needed to combat the formidable government and corporate interests arrayed against them. Moreover, the city’s poorly conceived development plan ultimately failed: the condemned land lies empty to this day, occupied only by feral cats. The Supreme Court’s unpopular ruling triggered an unprecedented political reaction, with 45 states passing new laws intended to limit the use of eminent domain. But many of the new laws impose few or no genuine constraints on takings. The *Kelo* backlash led to significant progress, but not nearly as much as it may have seemed.

Despite its outcome, the closely divided 5-4 ruling shattered what many believed to be a consensus that virtually any condemnation qualifies as a public use under the Fifth Amendment. It also showed that there is widespread public opposition to eminent domain abuse. Polls showed that over 80 percent of the public disapproved of the Court’s ruling. And in the years following the decision, both the federal government and 45 states passed new laws limiting the use of eminent domain. No other Supreme Court decision has ever led to such a broad legislative reaction. At the same time, however, many of these new state laws turn out to impose few or no genuine constraints on the government’s power to condemn property.



With controversy over takings sure to continue, Somin’s book is an indispensable resource on an alarming trend. “In *The Wealth of Nations*, Adam Smith famously argued that private property and decentralized market transactions generate prosperity as if “by an invisible hand,” he wrote. “The use of eminent domain to promote ‘economic development’ is based on the exact opposite assumption: that resources will often fail to generate as much wealth as they should unless their allocation is controlled by government. Instead of the invisible hand of the market, eminent domain relies on the grasping hand of the state.” ■

VISIT STORE.CATO.ORG/BOOKS, ONLINE RETAILERS, OR BOOKSTORES NATIONWIDE TO GET YOUR COPY OF *THE GRASPING HAND* TODAY.

A new issue of the Cato Journal examines alternatives to central banking

Finding a Path to Free-Market Money

When the Federal Reserve was created in 1913, its powers were strictly limited and the United States was still on the gold standard. Today the Fed has virtually unlimited power and the dollar is a pure fiat money.

The Spring/Summer 2015 issue of the *Cato Journal* examines the case for alternatives to central banking and the reforms needed to move toward free-market money. “A limited constitutional government calls for a rules-based, free-market monetary system,” writes James A. Dorn, Cato’s vice president for monetary studies, “not the topsy-turvy fiat dollar that now exists under central banking.” The distinguished authors in this volume examine the role of gold in a market-based monetary system, the advent of the bitcoin revolution, and the obstacles to fundamental reform, among many other topics.

Axel Leijonhufvud, an emeritus professor of economics at UCLA, begins by noting that, for decades, stability in a market economy has been all but ignored in macroeconomics, while income distribution has been similarly neglected in monetary economics. “The crisis of recent years tells us in no uncertain terms that we have to pay more attention to these two topics,” he writes. “Changes in financial regulation and in the conduct of monetary policy have not only played a very significant role in generating the financial crisis but have also been important in bringing about a large shift in the distribution of income over the last two or three decades.”

James Grant, the founder and editor of *Grant’s Interest Rate Observer*, argues that the need for sound money is both urgent and obvious. “Yet we must pause to consider that there is nothing either obvious or urgent about the idea of sound money to the people who own so much of the other

kind,” he added. “The asset-holding portion of the community has hugely profited by zero-percent funding costs and the levitation of stock, bond, and real estate prices.” Grant went on to offer a modest agenda for achieving a few reasonable reforms in the short term. “I will count us victorious when the name of the chairman of the Federal Reserve Board is just as obscure as that of the head of the Weight and Measures Division of the Department of Commerce,” he concluded.

Other contributors to this issue include George Selgin on “Law, Legislation, and the Gold Standard,” Lawrence H. White on “The Market for Cryptocurrencies,” Bennett T. McCallum on “The Bitcoin Revolution,” Kevin Dowd and Martin Hutchinson on “Bitcoin Will Bite the Dust,” Judy Shelton on “Building an Orderly and Ethical International Monetary System,” and Norbert J. Michel on “A Roadmap to Monetary Policy Reforms.”

As early as 1988, Nobel laureate James M. Buchanan underscored the fundamental problem with the Fed at an international monetary conference in Lugano, Switzerland. “What we have now is a monetary authority that essentially has a monopoly on the issue of fiat money, with no guidelines to amount to anything; an

authority that never would have been legislatively approved, that never would have been constitutionally approved, on any kind of rational calculus.”

Buchanan later added that there is “a moral obligation to think that we can improve things.” That is precisely the spirit of this volume of the *Cato Journal*, as well as the Institute’s newly established Center for Monetary and Financial Alternatives. ■

ALL OF THESE ARTICLES, AS WELL AS THE BOOK REVIEWS IN THIS ISSUE OF THE CATO JOURNAL, ARE AVAILABLE ONLINE AT WWW.CATO.ORG.



Federal Transit Funding Burdens Taxpayers

Federal transportation aid programs often create perverse incentives for states and metropolitan areas. As Randal O’Toole, a Cato senior fellow, and Michelangelo Landgrave of California State University write in “**Rails and Reauthorization: The Inequity of Federal Transit Funding**” (Policy Analysis no. 772), “the worst incentives are created by discretionary funds that encourage state and local governments to adopt wasteful programs in order to get the largest possible share of those funds.” For example, instead of encouraging cities and transit agencies to spend funds efficiently, the New Starts capital grants program encourages them to build the most expensive projects. By building a wildly expensive rail transit system, for example, Salt Lake City has collected \$2.17 in federal funds per

transit rider over the last 22 years. In comparison, by focusing exclusively on buses, Milwaukee has collected only 26 cents per transit rider. Nearly all of this variation is due to the New Starts and other discretionary funds, while formula funds are more equitably distributed. Such expensive projects not only waste federal transportation dollars, they impose huge burdens on local taxpayers. As a result, far from promoting urban growth, regions that build rail transit end up growing slower than ones that don’t. To fix these problems, Congress should convert the New Starts and other discretionary funds to formula funds. To encourage states



and regions to build transportation systems that respond to user needs, Congress should incorporate user fees into the formulas.

NO QUICK FIX IN HIGH-FREQUENCY TRADING

High-frequency trading (HFT) involves the use of computer programs to automatically trade securities in financial markets. This is a problem, critics say, because it creates unfair informational asymmetries between different types of market participants and because it increases the risk of a “flash crash”—a sudden market downturn driven by computer-automated trading. They add that more regulation should be introduced to level the playing field. However, according to Holly A. Bell, an associate professor of business at the University of Alaska Anchorage, this approach neglects the fact that problems

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Steve H. Hanke..... Senior Fellow
John Hasnas..... Senior Fellow
Penn Jilette..... Mencken Research Fellow
David B. Kopel..... Associate Policy Analyst
Deepak Lal..... Senior Fellow
Christopher Layne..... Research Fellow, Foreign Policy Studies
Gerald P. O’Driscoll Jr...... Senior Fellow
P. J. O’Rourke..... Mencken Research Fellow
William Poole..... Senior Fellow
Jim Powell..... Senior Fellow
Richard W. Rahn..... Senior Fellow
Vernon L. Smith..... Senior Fellow
Teller..... Mencken Research Fellow
Cathy Young..... Research Associate

James M. Buchanan (1919–2013)..... Distinguished Senior Fellow
F. A. Hayek (1889–1992)..... Distinguished Senior Fellow
William A. Niskanen (1933–2011)..... Chairman Emeritus

with market fragmentation, price synchronization, information dissemination, and market technology long predate the advent of HFT. In “**Beyond Regulation: A Cooperative Approach to High-Frequency Trading and Financial Market Monitoring**” (Policy Analysis no. 771), she notes that these problems have persisted for at least 40 years—despite repeated good-faith efforts to find regulatory solutions. What’s more, there is evidence to suggest that HFT has led to increased liquidity, lower spreads and transaction costs, more efficient price discovery, and wider participation in financial markets. Instead of further regulation, a cooperative solution should be pursued: firms could confidentially report human/automation interface errors to a neutral third party, which would anonymize, aggregate, and analyze such incidents in order to identify patterns that could help prevent a major market-disrupting event. In fact, as Bell highlights, a successful model for such an approach already exists in the airline industry.

TINKERING WITH THE WELFARE STATE

There is a growing consensus across the political spectrum that our current welfare system is not working as intended. Although federal, state, and local governments spend nearly \$1 trillion annually on at least 126 anti-poverty programs, we are doing little to help the poor become self-sufficient. Among the alternatives that have been gaining traction recently are proposals for some form of a guaranteed national income. Those proposals can take a variety of forms, including a uni-

versal grant, a negative income tax, or a wage supplement. In “**The Pros and Cons of a Guaranteed National Income**” (Policy Analysis no. 773), Michael D. Tanner, senior fellow at the Cato Institute, acknowledges that the case for replacing the current welfare system with a guaranteed national income seems intriguing. “But what sounds good in



theory tends to break down when one looks at implementation,” he writes. The idea appears to involve serious trade-offs among cost, simplicity, and incentive structure, and attempts to solve problems in one area would raise questions in others. Tanner details these trade-offs in full. “As strong as the argument in favor of a guaranteed income may be,” he writes, “there are simply too many unanswered questions to rush forward with any such plan.” Instead the country should pursue incremental steps: consolidate existing welfare programs, move from in-kind to cash benefits, increase transparency, and gather additional data. “This would allow us to reap some of the gains from a universal income without the costs or risks,” Tanner concludes.

REDUCING HARM FROM SYNTHETIC DRUGS

News media accounts abound regarding the proliferation of synthetic drugs that produce physical and psychological effects similar to those of traditional mind-altering sub-

stances such as marijuana, cocaine, and heroin. There is a bewildering variety of new drugs, most of which until recently were not covered by existing laws. As Ted Galen Carpenter argues in “**Designer Drugs: A New, Futile Front in the War on Illegal Drugs**” (Policy Analysis no. 774), the wide array often seems limited only by the creativity of enterprising chemists. “The daunting task of trying to outlaw substances that can sometimes regain legal status with a modest change in chemical makeup has caused consternation among officials in the United States and other countries determined to stamp out drug abuse,” writes Carpenter, a senior fellow at the Cato Institute. Policymakers have scrambled to come up with legal rationales to contain an ever-changing situation. They have experienced limited success—and even then only by using strained, dangerously expansive interpretations of criminal statutes. The multiple problems associated with suppressing the use of designer drugs underscore the inherent futility of the broader War on Drugs. Even as officials devote billions of dollars each year to enforcing laws against marijuana, cocaine, and other drugs, the market for synthetic equivalents or variations has soared. Instead of persisting in the failed strategy, policymakers should examine ways to accommodate legal markets in mind-altering substances while requiring strict production standards to prevent contamination or mislabeling. “Those are beneficial and attainable objectives, unlike the utopian goals of crusades against illegal drugs,” Carpenter concludes. ■

Continued from page 11

about how states use and in many cases abuse power against one another.

There’s also an emphasis on balancing power in realism. If you think about the debate around the separation of powers during the Founding period, it wasn’t so much that the Framers thought that any particular

president or any particular legislature or any particular judiciary was going to be wicked and venal. They thought that concentrated power itself was dangerous, and the only way to ensure that people would be free from the rapacious use of that power was to check it with countervailing powers. This notion permeates the theory of realism.

The political scientist Hans Morgenthau, for instance, approvingly cites John Randolph’s statement that “you may cover whole skins of parchment with limitations, but power alone can limit power.” This is one element of how most libertarian and realist foreign policy scholars think about international politics. ■

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MAOISM COMES TO SANTA MONICA

California's drought is turning neighbor against neighbor, as everyone seems to be on the lookout for water wasters. . . .

In this new age of social media and apps for everything, so called “drought-shaming,” can be much more public, and nastier than what Demian got a taste of.

Just look at Twitter. If you search the social media site for the hashtags #Drought-Shame or #DroughtShaming,” you'll find hundreds, if not thousands of very public reprimands of water wasters, often with pictures, video, and a lot of addresses.

—NATIONAL PUBLIC RADIO, 05/25/2015

OR HE COULD HAVE NOT PROPOSED TRILLION-DOLLAR SPENDING INCREASES

“I think that, in Washington during my brother's time, Republicans spent too much money,” Mr. [Jeb] Bush said Thursday when asked to describe where there was a “big space” between himself and his brother George W. Bush. “I think he could have used the veto power. He didn't have line-item veto power, but he could have brought budget discipline to Washington, D.C.”

—NEW YORK TIMES, 05/21/2015

VENEZUELA REACHES THE FINAL STAGE OF SOCIALISM

Venezuela's product shortages have become so severe that some hotels in that country are asking guests to bring their own toilet paper and soap, a local tourism industry spokesman said on Wednesday. . . .

“It's an extreme situation,” says Xinia Camacho, owner of a 20-room boutique hotel in the foothills of the Sierra Nevada national park. “For over a year we haven't had toilet paper, soap, any kind of milk,

coffee or sugar. So we have to tell our guests to come prepared.”

—FUSION, 04/02/2015

ECONOMICS STINKS

You can't just continue growth for the sake of growth in a world in which we are struggling with climate change and all kinds of environmental problems. All right? You don't necessarily need a choice of 23 under-arm spray deodorants or of 18 different pairs of sneakers when children are hungry in this country.

—BERNIE SANDERS ON CNBC, 05/26/2015

YES, WASHINGTON IS THE CAPITOL IN “THE HUNGER GAMES”

Hermès inaugurated its CityCenterDC boutique with a grand, eccentric flourish befitting a nearly 180-year-old French luxury firm that was born as a harness-maker and grew into the purveyor of \$10,000 Birkin handbags. At a seated dinner in the stately surroundings of the Andrew W. Mellon Auditorium, 120 guests began their meal with a foie gras feuilleté and ended it with a white chocolate “flower pot” filled with raspberries and mousse—a dessert so finely executed it could have been a porcelain figurine.

Though the fine china upon which the pea-crusted lamb loin was artfully arranged came directly from the company's stock, the dinner otherwise did very little to showcase the actual stuff of Hermès. But in the digital millennium, luxury is defined less by products than by *experiences*.

And so the company recently presented an evening of culinary theater choreographed and costumed by Belgian artist Charles Kaisin (who recently dazzled Hong Kong with a 35-foot golden goat constructed from 13,500 origami horses for

Chinese New Year). Two sopranos trilled the “Flower Duet,” and 60 waiters imported from New York—one for every two guests, as if catering to a royal court—marched out in synchronized precision to deliver the meal. They changed costume with each course: silver origami masks, golden welding suits and, finally, white cumulus headdresses lit from within.

—WASHINGTON POST, 05/19/2015

I'LL DO IT FOR \$27 MILLION

The grand Balsams hotel [in New Hampshire] is crumbling, though a Maine developer is planning to rebuild it into a resort with 1,000 jobs if he can secure \$28 million in state aid.

—WALL STREET JOURNAL, 05/12/2015

INSANITY STRIKES REPUBLICAN SPOKESMAN

Rand Paul, I sort of agree with Brian Kilmeade, what he was saying a few minutes ago, that his sort of worldview may not be fitting the world as a lot of people see it right now. He's got to prove, in my opinion, Rand Paul's got to prove that he will nuke a Muslim country if we have to. I'm not saying we should, but I'm saying that we will do that if it takes that to save America.

—DALLAS WOODHOUSE ON FOX NEWS, 04/07/2015

IS UBER SAFE? ITS DRIVERS ARE NOT ONLY CHECKED AND MONITORED, THEY CAN PROTECT YOU FROM RANDOM SHOOTERS

Authorities say no charges will be filed against an Uber driver who shot and wounded a gunman who opened fire on a crowd of people in Logan Square over the weekend.

—CHICAGO TRIBUNE, 04/20/2015