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Amongst the Advantages of Being a Neighbour of the US

Two features from *The New York Times* and carried in the *Toronto Star* (16/08), the first, "More spending, less saving called disturbing trend" by Tracey Tyler reports: "Niagara Falls, Ont. – More stringent banking regulations and a 'basically more humane society' have helped Canada weather the economic storm better than most countries but a complete recovery is 'by no means a sure thing,' says Princeton University economist Paul Krugman.

"Krugman, a 2009 Novel laureate, told lawyers at the Canadian Bar Association's annual meeting here Sunday that while it is 'amazing' Canada was not sucked into the vortex of economic collapse like the US and much of the European Union, certain aspects of its economy are, if not exactly scary, a little disturbing.

"One is that Canadians, he said, spend and borrow, 'a lot like the Americans.'

"The other is that we are saving less.

"The latest figures show that the personal savings rate of Canadians in the first quarter of 2010 was 3% of income. In the US, the savings rate rose to 6.4%.

"It is the first time since the 1970s that Canadians are saving less than their neighbors to the south.

"'Though it has recovered much better than the US, Canada is by no means fully recovered,' Krugman said at the conference keynote.

"Globally, the signs are slightly ominous that much of the world is drifting towards deflation, with employment rates basically flat on both sides of the Atlantic.

"While government and banking officials have forecast a return to full employment within five years, those predictions are based on traditional assumptions about the cycles of economic downturns and recoveries, said Krugman.

"'It is not at all clear when and how this ends.'

"That said, while Canada has gone through what would in ordinary circumstances be considered 'a severe recession,' its financial system has emerged remarkably unscathed given its close proximity to the US and its open economy, said Paul Krugman."

At this point we must take our readers to the second article carried in this issue of *The New York Times,* "The case of the missing Japanese centenarians" by Martin Fackler.

"Tokyo – Japan has long boasted of having more of the world's oldest people – testament, many here say, to a society with a superior diet and a commitment to the elderly.

"That was before the police found the body of a man thought to be one of Japan's oldest, at 111 years, mummified in his bed, dead for more than three decades."

Since the analogy of the alleged achievements of the Japanese the longevity parallels some of the alleged achievements of Canada with respect to its economic statesmanship, we will examine the analogy more carefully.

"His daughter, now 81, hid his death so she could continue collecting his pension, police say.

"Alarmed, local governments started checking on other seniors. So far, there are hundreds of centenarians they haven't been able to locate.

"One woman, supposedly the world's oldest at 125, is among the missing, likely for a long time.

"When officials tried to visit the 125-year-

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In the Long Run We're All Dead

The Kingston Chapter of COMER held its summer meeting at the home of Hugh and Claire Jenney on Amherst Island. Present were George Biro and Lisa, Henry Becker and Andrée, Helen Channen, Kevin Connolly and Martha McDermott, Wilmer Hill, Bill and Nora Parish, Garth and Rilla Rutherford, Keith Wilde and Nicole Schwartz-Morgan, Richard and Dolores Priestman, guests Paul and Joan Hubbard (Island neighbours of Hugh and Claire) and special guest Bill Krehm.

Paul and Joan Hubbard have worked for the World Bank for over 20 years, and although Paul is now retired he still consults for the Bank. Paul was keenly interested in learning more about COMER. He saw me as I was spreading out several issues of *ER* on the wide sill of the dining room window which looked out on the front lawn and asked what the goal of COMER is. I said it was to get the government to use the Bank of Canada to carry public debt, pointing out that in 2008-09 Canadians paid over $62 billion ($170 million a day) in interest on public debt.

Besides that specific goal, he asked if COMER had a broader vision. Yes, I replied, the (financial and physical) resources of the country should benefit more of the people. You mean, he said, that the government is mismanaging the economy? Yes, mismanaging the economy and the way it borrows (from the private sector instead of from its own bank). But, he asked, if the government borrows from the Bank of Canada (the Bank) won't that cause inflation? I asked Paul if he remembers what he paid for a house 20 or 30 years ago. Yes, he said, I remember that well. The difference between that and today's prices is "inflation," I said, and during that time the government did *not* borrow significantly from the Bank. (That is, the "inflation" was caused by something else.)

When Ottawa Used Its Own Bank to Finance Vital Services

I said that from WWII to the early seventies the government borrowed from the Bank regularly – not all of its borrowing, but a significant portion – and inflation never got out of control. But, Paul said, by the *end* of the seventies it did. Yes, and by then the Bank was being used *less* for government financing. In 1980 interest rates were raised very high. That was to kill inflation, Paul said, adding that it hurt at the time, but in the long run it was said to save us from a fate which might have been much worse. (I thought to myself, in the long run we're all dead.) The thousands of people who lost their jobs, their homes and their businesses did not feel saved, I said. Paul looked very thoughtful.

Then I said it was in the mid-1980s that a group of economists and others including John Hotson, Professor of Economics at Waterloo U. and William Krehm got together in Washington, DC, to discuss their concern about what was happening to the financial system and to consider what action might be taken. That was when COMER was organized.

At this point the meeting was called to order by Hugh who welcomed Bill Krehm and Paul and Joan Hubbard. Hugh said it was an honour to have William Krehm, the national head of COMER, at our meeting.

Then he mentioned that I had a little bit of history I wanted to share with the group. I began by saying Bill Krehm was born to Russian and Ukrainian parents in 1914 (1913, Bill interjected). He was a gifted violinist and at age 14 was sent to Chicago to further his violin training. At 15 he went to New York where he delivered hats for a living (and studied Marx, Lenin and Trotsky, Bill added).

After the crash he returned to Toronto where he enrolled at U. of T. to study mathematics. He left after two years and organized a group of Trotsky and Marxist youth. When I turned to Bill for confirmation of some facts Bill took over and gave an interesting half hour biographical outline. He found that as the depression wound down support for Trotsky in Toronto dwindled, so he went to Mexico where Trotsky was still active. When WWII started he tried to return to Canada to enlist, but the US would not let him cross their border. He suspected the RCMP might have had something to do with that. To survive he was a "string man" for the *Time* magazine writing pieces (and paid by the piece) on the coups and revolutions taking place in Central America.

In 1947 *Time* magazine dropped him because he had "ruffled some American feathers" by writing about US involvement in Latin American coups. He returned to Toronto with wife Gladys and son Adam, supporting his family by writing music reviews. In 1955 he formed a property development company, O'Shanter (now run by sons Adam and Jonathon). In the early 80s he retired from O'Shanter, co-founded COMER, began writing about economics, the policy of combating inflation by raising interest rates and the Bank of Canada.

A recurring theme in Bill's presentation was, as he put it, the "suppressed lessons of history." He referred to this as he began to talk about G.G. McGeer, a high-school drop-out who eventually earned a law degree, became Mayor of Vancouver, and a Liberal MP. McGeer was concerned about the private money system and used his position to "act as a bee on Mackenzie King's bottom" to get him to nationalize the Bank of Canada. Bill spoke highly of McGeer's book, *The Conquest of Poverty*, and suggested that it had been suppressed.

Keith did not agree that it had been suppressed and for a few minutes the discussion heated up, but cooled down just as quickly. Of interest to NDP supporters Bill mentioned that along with Gerry McGeer the CCF, forerunner of the NDP, must also have had an influence on King's decision to nationalize the Bank.

After the meeting I showed some CCF documents to Bill which indicated that as early as January 1932 J.S. Woodsworth and those around him started building the foundation for the CCF, culminating in the Regina Manifesto adopted at the CCF Convention in Regina on July 20, 1933. The manifesto included "Socialization of Finance…to make possible the effective control of currency, credit and prices…" Two weeks after the CCF Convention, in a radio address, August 2, 1935, while campaigning to become Prime Minister, King said, "Once a nation parts with control of its currency and credit it matters not who makes that nation's laws. Usury, once in control, will wreck any nation. Until the control of the issue of currency and credit is restored to government and recognized as its most conspicuous and sacred responsibility, all talk of the sovereignty of Parliament and of democracy is idle and futile."

McGeer knew Woodsworth and what he was attempting to do because in March 1932 Woodsworth rose in the House of Commons to propose the establishment in Canada of a "Co-operative Commonwealth." Its preamble spoke of the "large numbers of unemployed" and the "fundamental defects in the existing economic system."

Other similarities between McGeer and those working to establish the CCF included a close connection with organized labour and support of the use of a planned economy to "conquer poverty" (McGeer)or "eliminate exploitation of one class by another" (CCF). Whether or not McGeer drew upon CCF documents he is said to have used his position close to the seat of power to get King to support a policy on "the control of currency and credit" and thus helped to bring about, at least in part, one of the most important goals of the CCF.

Bill spoke at length about the non-inflationary causes of higher prices. He realized many years ago that prices can go up not only because of excess demand over supply (inflation), but also because of increased government investment in physical and human capital (which he called the "social lien"). Many years ago he wrote an essay on this and sent it to over 30 economic journals. *La Revue économique*, France, published it (May, 1970) following which it received excellent reviews in several European publications.

Public investment in human capital (through education, health and social security) had been shown to be the best investment a government could make by the work of Theodore Schultz, an American economist. Bill explained that at the end of WWII the American government had sent hundreds of economists to Germany and Japan to asses how long it would take before these two countries would once again become formidable trading countries. To the American's surprise Germany and Japan recovered far quicker than the economists predicted. Schultz explained that he and the other economists had concentrated on the physical damage, paying little attention to the skilled work force which had come through the war almost intact. From that he concluded that public investment in human capital was/is the best investment a government could make.

Bill also spoke of the concept of "dominant revenue," first described by François Perroux. It held that in every period those with the most money identified the source of their revenue (the "dominant revenue") as an index of the welfare of society as a whole. For example, today if the stock market is doing well it is assumed that society as a whole is doing well even though hundreds of thousands of people remain unemployed.

As Bill wound down his remarks, Paul Hubbard thanked Hugh for having invited him and Joan. He had no idea that discussions of this sort were taking place on Amherst Island and talked briefly about his work with the World Bank. Immediately Norah challenged Paul on the way the bank had treated developing countries. Paul responded graciously admitting that the bank had made some mistakes, but adding that on the whole it had also done much good. Norah continued to question Paul until, out of respect for a guest, a motion to adjourn was made.

Before the meeting broke up I mentioned that COMER was suing the federal government over its misuse or lack of use of the Bank of Canada. I had hoped for more discussion of this, but time had run out.

Richard Priestman

My contacts with Latin American democratic groups living in exile in Mexico city were close and ever spreading. And when a coup against the Washington-imposed dictator of Guatemala was planned, a descendant of the liberator of Guatemala from the Spaniards tipped me off to come down to Guatemala and we awaited in his basement the artillery duels between the various guardhouses in the fortification wall surrounding the capital. Jacobo Arbenz, son of Swiss immigrants, future president of the land, arranged the capture of a key artillery officer who, in tears, a pistol pointed to his head directed fire against his comrades. Soon I left Granados's cellar and picked my way to the central square. There I found single dead soldier. Arbenz's strategy had worked. like a charm.

I was the only foreign journalist on the site for the triumph that initiated Latin America's bid for democracy. *Time* had dropped me as stringer. I had nowhere to send it. So I sent it to *Time*, which bought it, and hired me as staff correspondent. Henry Luce, it seems, was getting bored with the big war, and relished the material that I sent in. And when the Mexicans refused to renew my visa when it expired not long after. ("It wasn't us but the gringos made us do it," explained Senor de la Selva, the high official in the Mexican Foreign Office told me, when I asked what this was all about.) I was picked up as I returned to the *Time* office, held overnight and put on a plane to Guatemala the next morning. When it landed in Tapachula in southern Mexico, I was not even allowed to set foot out of the plane, before it resumed the flight to Guatemala.

At that point *Time* solved my visa problem I was brought to their New York office for a month. I found everybody from the senior editor down to my fellow-writers sympathetic. I was offered to take my choice of postings in Europe or Latin America. My heart was in Latin America and I chose the West Coast republics, based in Lima, Peru. However, American policy, was getting absorbed in undermining Latin America's incipient liberties.

These days when we hear so much about the abuses of the prisoners in Guantanamo, it has slipped from public memory that in the postwar period, the US ran a school teaching Latin military men the art of torture in the Canal Zone.

Within a year I was dropped by *Time*, with a quite generous separation package, and was able to return to Canada with my young family.

W.K.

Sad Fate of the Greatest Lesson of World War II

The reference is to the conclusion by one of the many hundreds of economists sent by Washington to Japan and Germany right after the WWII to study the damage done. From that they were to predict how long it would take those two once-great traders to achieve such roles again. Sixteen years later one of those economists, Ted Schultz of the University of Chicago, published a book in which he explained why he and his colleagues had struck out in their conclusion. And in a stroke of genius, he explained that they had concentrated on physical destruction, and paid scant attention to the fact that the highly talented and trained work force had come out of the conflict basically intact. In 1961 he formulated his conclusion: human capital is the most productive investment a country can make. For a few years Schultz was celebrated, decorated with a Bank of Sweden Nobel price, and then dropped like a hot potato. He and his great conclusion have been completely forgotten.

Several economists and sociologists have explained how this could have happened.

I will choose of these the notion of the "dominant revenue" of the late great French economist, with whom I had an intimate relationship, François Perroux. In his theory of the "dominant revenue," Perroux held that in every society the class or social group in power present their revenue as an adequate index of the well-being of society as a whole. Thus before the industrial revolution in Great Britain it was the high land rents that Britain's landlords could charge the farmers who rented their lands, profitting from the high tariffs. After the introduction of steam power the dominant revenue shifted to the industrialists who promoted low tariffs at home and abroad to exploit to the utmost their introduction of steam power in their factories.

Failing such a change, bloodier means – notably in Mexico – were used to replace one dominant class by its successor.

The great disillusionment about President Obama's regime in the US stems from the fact that his chief advisor in economic matters is a former high official of earlier regimes that brought on the present deepening mess. As a result, there can be no serious change in the "dominant revenue."

That is the advantage of a knowledge of the history of economic theory that has been long banished from the public domain.

With such criteria in place, let us proceed to *The Wall Street Journal* (27/07, "Temp Jobs Gain as Uncertainty Reigns" by Paul Vigna and John Shipman): "Despite rising profits, big businesses remain hesitant to hire permanent employees, a reluctance that is fueling demand and higher profits for the companies providing temporary staffing services.

"Manpower, TrueBlue Inc., and Robert Half International report second-quarter gains in their businesses as employers continue to prefer the flexibility that temporary workers provide while awaiting more tangible signs that the budding recovery won't stall.

"TrueBlue, a Tacoma, Wash., blue-collar temporary staffer that operates Labor Ready, Spartain Staffing and other staffing outfits, last week said profits more than doubled, aided by a 15% rise in revenue and an income tax benefit.

"Chief Executive Steven Cooper said manufacturers are hiring more temps now than during similar points in prior economic recoveries. 'It feels like they're hiring back shifts full of temps,' he said during an investor call. There may be a point when businesses become more comfortable with hiring permanent workers, 'but we don't see those conversions happening yet,' Mr. Cooper said.

"In fact he suggested businesses are quite happy with the flexibility offered by hiring temps, and aren't in a hurry to give that up. 'They don't have to deal with the outplacing on the downside and so as we have gone through a couple of recessions in the 2000s and this [last] one being a big one, lots of lessons learned,' he said.

"So far this year, the private sector has added 593,000 jobs according to the Bureau of Labor Statistics' establishment survey, a little more than a third of them, 218,000 have been temporary jobs.

"Bigger rivals Robert Half and Manpower each posted a doubling of second quarter income; Robert Half, which had a 10% first quarter drop, posted a sales gain of 2% over a year ago.

"'We believe there is greater acceptance by companies of flexible staffing models that include a mix of both full-time and temporary workers,' Robert Half CEO Harold Messmer said last week.

"Manpower's revenue jumped 21%, aided by an acquisition, and built on its 13% first quarter sales gain over a year ago. That first quarter gain ended a string of revenue declines that stretched back to 2008.

"Manpower of Milwaukee, Wis., forecast third-quarter revenue will rise between 20% and 22% over a year ago.

"CO Jeffrey Joerres noted that while the company is seeing some strength in its permanent hiring business, it is off a low pace. The trends in temporary hiring, meanwhile, are accelerating. 'We think this is a secular change,' he said in an interview Monday. Companies remain reluctant to hire permanent staff, given the uncertain economy.

"'The environment is continually improving. It's just methodical and slow,' he said. 'Companies remain unsure of the future, or they are more comfortable with using temporary workers,' he added.

"Still, Robert Half finance chief Keith Waddell noted the company is seeing strength in permanent hires. 'We think people over-cutback and to some extent they're having to reinstate levels of cut backs, and they can do that at a time when supply of labor has never been better,' he said, 'so it's a win-win.'

"Robert Half reported operating income from its permanent staffing services flipped to a profit of \$5.5 million from a \$1.97 million loss a year ago."

W. Krehm

Floating Remembrances Tip Their Hats as Paths Cross

The New York Times Book Review (15/06, "The Two Churchills – The man who led the charge against Hitler had his own disturbing history of conquest, racism and brutality" by Johann Hari) reviewed the book *Churchill's Empire* by Richard Toye with this outburst of admiring revelation: "Winston Churchill is remembered for leading Britain through her finest hour – but what if he also led the country through her most shameful one? What if, in addition to arousing a nation to save the world from the Nazis, he fought for a raw white supremacy and a concentration network of his own? This question burns through Richard Toye's superb, unsettling new history, 'Churchill's Empire' – and is even seeping into the Oval Office under President Obama.

"George W. Bush had left a big, growling bust of Churchill near his desk in the White House, in an attempt to associate himself with Churchill's heroic stand against fascism. It's not hard to guess why Obama followed a very different course: his Kenyan grandfather, Hussein Onyango Obama, was imprisoned without trial for two years and tortured on Churchill's watch, for resisting Churchill's empire.

"Can these clashing Churchills be reconciled? Do we live, at the same time, in the world he helped to save and the world he helped to trash? Toye, one of Britain's smartest young historians, has tried to pick through these questions dispassionately. Churchill was born in 1874 into a Britain that was coloring the map imperial pink, at the cost of washing distant nations blood red. He was told a simple story: the superior white man was conquering the primitive dark-skinned natives, and bringing them the benefits of civilization.

"As soon as he could, Churchill charged off to take his part in 'a lot of jolly little wars against barbarous peoples.' In the Swat valley, now part of Pakistan, he experienced, fleetingly, an instant of doubt. He realized that the local population was fighting back because of 'the presence of British troops in lands the local people considered their own,' just as Britain would if she were invaded. But Churchill soon suppressed this thought, deciding instead that they were merely deranged jihadists, whose violence was explained by a 'strong aboriginal propensity to kill.'

"He gladly took part in raids that laid waste to whole valleys, writing: 'We proceeded systematically, village by village, and we destroyed the houses, filled up the wells, blew down the towers, cut down the shady trees, burned crops, and broke the reservoirs in punitive devastation.' He then raced off to help reconquer the Sudan, where he bragged that he personally shot at least three 'savages.'

"The young Churchill charged through imperial atrocities, defending each in turn. When the first concentration camps were built in South Africa, he said they produced 'the minimum of suffering' possible. At least 115,000 people were swept into them and 14,000 died, but he wrote only of his 'irritation that kaffirs should be allowed to fire on white men.'"

The Racist Churchill

"Later he boasted of his experiences. 'That was before the war degenerated,' he said. 'It was great fun galloping about.'

"After being elected to Parliament in 1900, he demanded a rolling program of more conquests based on his belief that the Aryan stock is bound to triumph. As war secretary and then colonial secretary in the 1920s, he unleashed the notorious Black and Tans on Ireland's Catholics, to burn homes and beat civilians. When the Kurds rebelled against British rule in Iraq, he said, 'I am strongly in favor of using poisoned gas against uncivilized tribes,' It 'would spread a lively terror.' (Strangely, Toye doesn't quote this.)

"Of course, it is easy to dismiss any criticism of these actions as anachronistic. Didn't everybody in Britain think that way then? One of the most striking findings of Toye's researches is that they really didn't, even at that time. Churchill was seen as standing at the most brutal and brutish end of the British imperialist spectrum. This was clearest in his attitude to India. When Gandhi began his campaign of peaceful resistance, Churchill raged that 'he ought to be lain bound hand and foots at the gates of Delhi and then trampled by an enormous elephant with the new Viceroy seated on its back.' He later added: 'I hate Indians. They are a beastly people with a beastly religion.'

"This hatred killed. In 1943, to give just one example, a famine broke out in Bengal, caused, as the Nobel-prize-winning economist Amartyra Sen has proven, by British mismanagement. To the horror of many of his colleagues, Church raged that it was their own fault for 'breeding like rabbits' and refused to offer any aid for months while hundreds of thousands died.

"Hussein Onyango Obama is unusual among Churchill's victims only in one respect: his story has been rescued from the slipstream of history. Churchill believed the highlands, the most fertile land in Kenya, should be the sole preserve of the white settlers, and approved of the clearing out of the local 'kaffirs.' When the Kikuyu rebelled under Churchill's postwar premiership, some 150,000 of them were forced at gunpoint into detention camps, later called Britain's 'gulag' by the historian Caroline Elkins. Obama never truly recovered from the torture he endured.

"This is a real Churchill, and a dark one – but it is not the only Churchill. He also saw the Nazi threat far ahead of the British establishment and his extraordinary leadership may have been the decisive factor in vanquishing Hitlerism from Europe….

"So how can the two Churchills be reconciled? Was his moral opposition to Nazism a charade, masking the fact that he was merely trying to defend the British Empire from a rival? Toye quotes Richard B. Moore, an American civil rights leader, who said it was 'a most rare and fortunate coincidence' that at that moment 'the vital interests of the British Empire' coincided 'with those of the great overwhelming majority of mankind.' But this might be too soft in its praise. If Churchill had been interested only in saving the empire, he could probably have cut a deal with Hitler. No, he had a deeper repugnance to Nazism than that. He may have been a thug, but he knew a greater thug when he saw one – and we may owe our freedom today to this wrinkle in history.

"This is the great, enduring paradox of Churchill's life. In leading the charge against Nazism, he produced some of the richest prose poetry in defence of freedom and democracy ever written.

"It was a check he didn't want Black or Asian people to cash, but as the Ghanaian nationalist Kwame Nkrumah wrote: 'All the fair brave words spoken about freedom that had been broadcast to the four corners of the earth took seed and grew where they had not been intended.' Churchill lived to see democrats use his own hope-songs of freedom against him.

"In the end, the words of the great and glorious Churchill who resisted dictatorships overwhelmed the works of the cruel and cramped Churchill who tried to impose it on the world's people of color. Toye teases out these ambiguities beautifully. The fact that we now live at a time when a free and independent India is an emergent superpower in the process of eclipsing Britain, and a grandson of the Kikuyu 'savages' is the most powerful man in the world, is a repudiation of Churchill at his ugliest – and a sweet, unsought victory of Churchill at his best."

I would like to take up the report on Toye's conclusion on the better side of Churchill. But I will do so from my own experiences how orbits of one's personal life may open up to us an angle of vision of even certain great issues of the world that it might take further decades for scholars to grasp by more conventional routes.

I was a good high school student so in 1929 I was sent to Chicago to study music, and I was able to write my (4th year junior matriculation without having attended school. During my year in Chicago I had come to contact an anti-Stalinist Marxist group, and worked my way through the three volumes of Marx's Capital. But with my head on fire, on my history paper I referred to Winston Churchill as a scoundrel or some such thing. Undoubtedly though it helped me beat Toye's conclusion by some eighty years, it must have contributed to my not getting a university scholarship. I had been living in New York during the crash of 1929, when I lost my job and returned to Toronto Being close to Wall Street when brokers were jumping out of windows, was not pleasant, but highly educational. It impressed me not to take too seriously talk of a balanced market being just around the corner. Even when made by as persuasive a political leader as President Obama, who apparently is not aware of what has been rated the greatest lesson to come out of WWII.

That is that investment in human capital is the most rewarding investment a government can make. Especially when technologies are being improved, population is on the rise, and urbanization is at record levels.

From my first-hand experience of the great 1929, and a knowledge of economic literature in several languages and periods, and what mathematics I had studied, I emphasize the need of looking at the economy from a variety of angles.

When a President of the US can treat as debt what was recognized as the most valuable investment a government can make – i.e., education, health, the environment – we are in first-class trouble. Particularly since this has not been picked up by the world's great universities – obviously because the guilty party would become jobless in this cold jobless world.

Treating recognition of the "best investment a government can make" as debt means that we are sailing blind with all lights out. Mr. Churchill at his worst could just hold his own for ghastly policy.

William Krehm

Alongside an Older Generation that Must Work into Great Grandfatherhood, We Have a Lost Generation Without Work

The same issue of *The Globe and Mail* relays this dispatch from *Agence France-Presse* from Geneva: "Youth unemployment hit a record 81 million youngsters worldwide last year with the economic crisis, potentially breeding a 'lost generation,' the UN's International Labour Organization said Thursday.

"The youth unemployment rate grew twice as fast as that for adults, to affect 13% of those between 15 and 24 years of age in 2009, the UN' agency's report found.

"'This is the highest number of global unemployed youth ever measured by the ILO,' said Sarah Elder, author of *Global Employment Trends*.

"Nearly 73 million youngsters were out of work.

"The report warned that, despite a marginal improvement that's forecast for 2011, the recovery in the jobs market for young men and women is likely to lag behind opportunities for adults.

"'Young people are the drivers of economic development,' ILO Director-General Juan Somavia said. 'Forgoing this potential is an economic waste and can undermine social stability,' he added.

"The authors underlined that their decent education and skills were less likely to open up job opportunities for youth than before, while pay and working conditions for those who found work had suffered, 'leaving permanent scars.'

"'Fears have been expressed regarding a possible crisis legacy of a "lost generation" made up of young people who detach themselves from the labour market altogether,' it said.

"'Developing nations account for 90% of the world's population of young people, who are made more vulnerable to underemployment and poverty in the informal economy,' according to the UN agency.

"About 152 million people – 28% of the world's youth working population – work but never earn enough to break out of the poverty trap.

"Nevertheless, the report estimates that 45% of the increase in youth unemployment, during the two-year period under review hit developed economies, home to 10% of the global youth labour force.

"Central, Eastern and Southern Europe the most, notably Estonia, Latvia, Lithuania, and Spain. In the US, youth unemployment rose by 8 percentage points to 18 percent.

"The agency urged governments to keep up support for youth employment despite cuts in public spending, while Mr. Elder warned of 'dire consequences' for youngsters if stimulus spending was stopped too early."

What is urgently needed to remedy this obscene situation is some accountancy. When you mistake for debt "the best investment a government can make" you are standing on your head, so that the banks can make a killing by selling subprime bond fraud for serious insured investments, and confusing our "best investment" as debt. Currently, the banks bailed out by the government are engaged in peddling split-second stock deals in which internet eavesdropping is a feature, with advance information of the trading orders available for those who will pay a price on trades that have been submitted even before the deals go through.

Surely those who authorize such a trading world, must have skipped Sunday school, jail, and much, much else.

W.K.

Why Can't Our Press Utter the Words "Human Capital" Even When Recounting How Important Such "Spending" Is?

Part of trouble is that in these dire times they are dependent for their own financing on the big banks that have banned mention of what a half-century ago was celebrated as the greatest lesson to have come out of World War II. At its end, Washington had sent hundreds of economists to Japan and Germany to study the damage and predict how long it would take for those two defeated nations to become leading traders again. And in 1961 one of these economists, Theodore Schultz published a book explaining why he and his colleagues had been so wrong; they had concentrated on the physical destruction, and overlooked the importance of the highly educated and human resources that had come out of the struggle virtually intact. Schultz concluded from this the investment in human capital – education, health, and proper care of the environment is the most important investment a government can make.

For a few years Schultz was acclaimed, decorated, and then completely forgotten.

Instead of being treated as a prepaid investment, government investment in human capital is treated as debt, and its price effects as "inflation" to be repressed with wage cuts, the shutting down of schools and with high interest rates.

And yet, though the term "investment in human capital" is shunned like the plague, the same press is replete with the anonymous details of how vital human capital is to society's survival.

The New York Times (17/08) carries an editorial, "Haiti's Schools," from which I quote: "A plan to build a brand new education system in Haiti is one of the most encouraging things to emerge from the rubble of the January 12 earthquake. It is expected to be endorsed at a meeting on Tuesday of the Interim Haiti Recovery Commission, the joint Haiti-international body created to guide the country's rebuilding.… The goal is to provide universal free or nearly free education for kindergarten through the 12th grades in accredited schools, with eventual government financing.

The full transformation is expected to take 20 years.

"The first, five-year phase is expected to cost $500 million, half of which would come from the Inter-American Development Bank, which has helped design the program. The rest is expected to come from other donors. The plan is to build at least 625 new primary schools and triple the number of publicly financed schools. It would also retrain 90% of the country's teaching force – 50,000 people – to teach the new curriculum, and it would train 2,500 new teachers a year, many through a program patterned on Teach for America."

Nobody at *The New York Times* need be told was that Haiti was the first instance of a slave society that not only won its freedom by defeating an army of Napoleon, and that gave shelter to Simon Bolivar, the liberator of half of Spanish America during a temporary set-back of his. It was occupied and re-occupied by the US which retained slavery some sixty years after Haiti put an and end to the institution. As revenge for it having held high the anti-slavery cause it was punished by being prevented from accumulating human capital under the Monroe Doctrine that gave Washington the right to determine what Latin American countries might obtain independence from their European overlords – and, of course, remain effectively at the mercy of the US. In short it was denied the opportunity of accumulating human capital.

The New York Times does not have to learn that from me.

However, let us pass on two pages further in the same issue of the *Times* where it provides a fine example of another aspect of human capital – the art of humans of different faiths learning to live in peace side by side. From "The Muslims in the Middle" by William Dalrymple, I quote: "New Delhi – President Obama's eloquent endorsement on Friday of a planned Islamic cultural center near the World Trade Center, followed by his apparent retreat the next day, was just one of the many paradoxes at the heart of the increasingly impassioned controversy.

"We have seen the Anti-Defamation League, an organization dedicated to ending 'unjust and unfair discrimination,' seek to discriminate against American Muslims. We have seen Newt Gingrich depict the organization behind the center – the Cordoba Initiative, which is dedicated to 'improving West relations' – as a 'deliberately insulting' and triumphalist force attempting to build a monument to Muslim victory near the site of the twin towers.

"The problem with such claims goes far beyond the fate of a mosque in downtown Manhattan. They show a dangerously inadequate understanding of the many divisions, complexities and nuances within the Islamic world – a failure that hugely hampers Western efforts to fight violent extremism and to reconcile Americans with peaceful adherents of the world's second largest religion.

"Many of us are perfectly aware of making distinctions within the Christian world. The fact that someone is a Boston Roman Catholic doesn't mean he's in league with the Irish Republican Army bomb makers, just as not all Orthodox Christians have ties to Serbian war criminals or Southern Baptists to the murderers of abortion doctors.

"Yet many of our leaders have a tendency to see the Islamic world as a single, terrifying monolith…."

The Shining Example of Sufism

"Feisal Abdul Rauf of the Cordoba Initiative is one of America's leading thinkers of Sufism, the mystical form of Islam, which in terms of goals and outlook couldn't be farther from the violent Wahhabism of the jihadists. His videos and sermons preach love, the remembrance of God (or 'zikr') and reconciliation. His slightly New Agey rhetoric makes him sound, for better or worse, like a Muslim Deepak Chopra. But in the eyes of Osama bin Laden, he is an infidel-loving, grave-worshiping apostate; they no doubt regard him as a legitimate target for assassination.

"For such moderate, pluralistic, Sufi imams are the front line against the most violent forms of Islam. In the most radical parts of the Islam world, Sufi leaders risk their lives for their tolerant beliefs, every bit as bravely as American troops on the ground in Baghdad and Kabul do. Sufism is the most pluralistic incarnation of Islam – accessible to the learned and the ignorant, the faithful and nonbelievers – and is thus a uniquely valuable bridge between East and West.

"The great Sufi saints like the 13th-century Persian poet Rumi held that all existence and all religions were one, all manifestations of the same divine reality. What was important was not the empty ritual of the mosque, church, synagogue or temple, but the striving to understand that divinity can best be reached through the gateway of the human heart: that we can all find paradise within us, if we know where to look….

"While the West remains blind to the divisions and distinctions within Islam, the challenge posed by the Sufi vision of the faith is not lost on extremists. This was shown most violently on July 2, when the Pakistani Taliban organized a double-suicide bombing of the Data Darbar, the largest Sufi shrine in Lahore, Pakistan's second largest city. The attack took place on a Thursday night, when the shrine was at its busiest. 42 people were killed and 173 were injured.… This was only the latest in a series of assaults against Pakistan's Sufis.… In May, Peeru's Café in Lahore, a cultural center where I had recently performed with a troupe of Sufi musicians, was bombed in the middle of its annual festival. An important site in a tribal area of the northwest – the tomb of Haji Sahib of Turangzai, a Sufi persecuted under British colonial rule for his social work – has been forcibly turned into Taliban headquarters. Two shrines near Peshawar, the mausoleum of Bahadar Baba and the shrine of Abu Saeed Baba, have been destroyed by rocket fire.

"Symbolically, however, the most devastating Taliban attack occurred last spring at the shrine of the 17th-century poet-saint Rahman Baba, at the foot of the Khyber Pass in northwest Pakistan. For centuries, the complex has been a place for musicians and poets to gather, and Rahman Babam at the foot of the Khyber pass in northwest Pakistan.… Rahman Baba's Sufi verses had long made him the national poet of the Pashtuns living on both sides of he Afghanistan-Pakistan border. 'I am a lover, and I deal in love,' wrote the saint, Sow flowers,/ so your surroundings become a garden/ Don't sow thorns; for they will prick your feet./We are all one body. Whoever tortures another, wounds himself.'

"Then, about a decade ago, a Saudi-financed religious school, or madrasa, was built at the end of the path leading to the shrine. Soon its students took it upon themselves to halt what they see as the un-Islamic practices of Rahman Baba's admirers. When I last visited it in 2003, the shrine-keeper, Tila Mohammed, described how young students were coming regularly to complain that his shrine was a center of idolatry and immorality.

"Then, one morning in early March 2000, a group of Pakistan Taliban arrived at the shrine before dawn and placed dynamite packages around the squinches supporting the shrine's dome. In the ensuing explosion, the mausoleum was destroyed, but at least nobody was killed. The Pakistani Taliban quickly took credit, blaming the shrine's administrators for allowing women to pray and seek healing there.

"The good news is that Sufis, though mild, are also resilient. While the Wahhabis have become dominant in northern Pakistan ever since we chose to finance their fight against the Soviets in Afghanistan, things are different in Sindh Province in Southern Pakistan. Sufis are putting up a strong resistance on behalf of the pluralist, composite culture that emerged in the course of a thousand years of cohabitation between Hinduism and Islam.

"Last year, when I visited a shrine of the saint Lal Shabaz Qalandar in the town of Schwan, I was astonished by the strength

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Advantages *from page 1*

old at her registered address, they discovered the site had been turned into a city park in 1981.

"The authorities have been unable to find more than 281 Japanese who had been listed in official records as 100 years old or older. Facing a public outcry, health minister Akira Nagatsuma said officials would meet with every persons 110 or older to verify that they are still alive. Tokyo officials made the same promise for the 3,000 or so residents listed as 100 and up.

"There are no clear answers about what happened to most of the missing centenarians. Is the country witnessing the results of pension fraud on a large scale, or, as most officials maintain, was most of the problem a result of sloppy record keeping? Or was the whole sordid affair, as the gloomiest commentators claim, a reflection of disintegrating family ties, as an indifferent younger generation lets their elders drift away into security?

"Officials in the Adachi ward of Tokyo, where the corpse was found said they grew suspicious after trying to pay a visit to the man, Sogen Kato. (They were visiting him because the man previously thought to be Tokyo's oldest had died and the wished to congratulate Kato on his new status.)"

The qualifies the whole episode being set to light music, revealing Death, that can wink and sing (nothing Wagnerian, of course, but light, wiggly Broadway).

The delegation that came to congratulate what turned out a mummified corpse said the daughter gave conflicting excuses, saying at first he did not want to meet them, and then that he was elsewhere in Japan giving Buddhist sermons.

That parallels precisely the alleged achievements which Dr. Krugman credits Canada's current statesmen.

For the embarrassing questions that must be asked are: Why does the Canadian government do its financing on the market, when it could so through the Bank of Canada through which it financed its second World War more brilliantly than either the UK that nationalized the Bank of England only after the war, or the US whose Federal reserve is partly owned by the government whereas is stat branches are still controlled by private bankers? Why has Washington buried all memory of the great investigation that it initiated at the end of WWII?

The US government sent hundreds of economists to Germany and Japan to assess the war damage and from it predict how long it would be before these two great trading powers could once again assume such roles. Sixteen years later one of these, Theodore Schultz wrote a book in which he attributed their failure to their having concentrated on physical destruction, while attributing little importance to the fact that the highly educated, gifted, and dedicated human capital was given scant attention. And from that Schultz formulated his great conclusion: investment in human capital, which would have to include due preservation of the environment, and adequate infrastructures for the rapid urbanization proceeding throughout the world.

For a few years Schultz was celebrated and decorated, and then completely forgotten. investment in human capital which is *prepaid investment* is today treated as a debt. Which means that we have no accountancy that can be seriously accepted. But our universities have been so *gleichgeschaltet* that few economists who treasure their posts in this non-functioning economy dare raise their voices in protest.

Our history which holds the answer lies mummified, like those ancient Japanese who live on and on in the statistics of longevity.

William Krehm

and openness of the feelings against those puritan mullahs who criticize as heresy all homage to Sufi saints, 'I feel that it is my duty to protect both the Sufi saints, just as they have protected me,' one woman told me. 'Today in our Pakistan there are so many of these mullahs and Wahhabis who say that to pay respect to the saints in their shrines is heresy. They sit arguing about how long their beards should be, and fail to listen to the message of the prophet.'

"There are many like her; indeed, until recently Sufism was the dominant form of Islam in South Asia. And her point of view shows why the West would do well to view Sufis as natural allies against the extremists. A 2007 study by the RAND Corporation found that Sufis' open intellectual interpretation of Islam makes them ideal 'partners in the effort to combat Islamist extremism.'"

W.K.

The Inequalities of Our Society

In a discussion about the problems in our society one of the first items that must come up would be the fact that the rich are getting richer and the poor are getting poorer.

If we examine working conditions in the countries around the world we find that the above is a vast understatement and correcting the problem becomes many times more urgent. We can more easily realize how much of an understatement if we are a reader of Forbes magazine. In 2004 Forbes magazine announced that the number of billionaires in our society had increased to 587 in '04 from 436 in '03, and their total fortunes amounted to $1.9 trillion. We can safely assume that this number has now increased to something over 1,000 and their fortunes would be anybody's guess.

The next question would probably be, who is responsible for the conditions that promote this? Can it be the governments that we elect? That is not what they tell us they are planning to do. But if this is the "democracy" that we are told about, it would appear that we must hold them responsible. So let's examine our "democracy" a little more carefully.

We have placed our trust in a government led by either of two political parties for more years than we care to think about. If we can ignore all of the verbal diarrhea that comes out of Ottawa and examine only the accomplishments of those two parties, can we find any difference? Could it be that they are the same in everything but name? Could it be that they just talk but don't get the opportunity to make the decisions? If they don't make the decisions then who does?

If we are willing to take the time to examine what is happening behind the scenes out of the range of the eyes of the general public, we will find that there is a sector of our society that are only too willing to instruct the political leaders on how their problems should be solved. The results of this advice are not difficult to see. One of the main objectives of this sector is to homogenize the decisions of the governments of all of the countries on this planet to make the citizens more easily controlled and to make sure that those decisions are beneficial to their own interests. The result is frequently referred to as "World Government" and it is promoted by the wealthiest faction of our society utilizing the power of the giant transnational corporations and the financial institutions. How do they coordinate decisions that are made in different countries around the world? Have you heard of the Bilderberg Society, the Trilateral Commission, the Council of Foreign Relations. These groups meet regularly. Those who attend (by invitation only) are prominent influential members of governments, CEOs of giant corporations, and controllers of great wealth.

Have you heard about organizations like the World Bank, the International Monetary Fund (IMF) and the World Trade Organization (WTO)? Are you familiar with the world laws that these organizations promote, such as: the North American Free Trade Agreement (NAFTA) and the General Agreement on Tariffs and Trade (GAAT)? These agreements tie the hands of government officials. If these officials try to pass laws that are not amenable to this wealthy sector of our society they find themselves confronted by more problems than they ever thought possible. It is said that Amsel Rothschild, the originator of the Rothschild wealth once made the statement, "Give me control of the economics of a country, and I care not who makes her laws."

You may think, "This all seems rather remote to me, I'm not having any trouble." But please look around you. Do you see those little tykes, your grandchildren or great grandchildren. They will not be able to avoid the conditions imposed on them by these transnational corporations. You may think, "What conditions?" Have you heard of the "maquiladoras"? Here are a couple of paragraphs from the book, *When Corporations Rule the World*, by David C. Korten.

"Americans need go no farther than the Mexican border to get an idea of what it now takes to be globally competitive. The maquiladoras are assembly plants in the free-trade zone on the Mexican side of the border with the United States. The zone has become a powerful magnet, attracting many US companies – including General Electric, Ford, General Motors, GTE Sylvania, RCA, Westinghouse, and Honeywell that are seeking low-cost locations in which to produce for the US market. Growth has been explosive, from 620 maquiladora plants employing 119,550 workers in 1980 to 2,200 factories employing more than 500,000 Mexican workers in 1992. Many feature the most modern high-productivity equipment and technology. Although the productivity of Mexican workers who work in modern plants is comparable to that of US workers, average hourly wages in maquiladora factories are just $1.64, compared with an average manufacturing wage of $16.17 in the US.

"To maintain the kind of conditions transnational corporations prefer, the Mexican government has denied workers the right to form independent labor unions and has held wage increases far below productivity increases. In the summer of 1992, more than 14,000 Mexican workers at a Volkswagen plant turned down a contract negotiated by their government-dominated labor union. The company fired them all, and a Mexican court upheld the company's action. In 1987, in the midst of a bitter two-month strike in Mexico, Ford Motor Company tore up its union contract, fired 3,400 workers, and cut wages by 45 percent. When the workers rallied around dissident labor leaders, gunmen hired by the official government-dominated union shot workers at random in the factory."

The people who are responsible for these conditions recognize only one benefit, "profit." They would impose these conditions on their own children if it would increase their profit. Don't you think it is time to join one of the many organizations who are trying to get these people under control?

D.D. Keir

Scholarship Elbowed Out by the Internet?

Man was always very much the product of his technology, but today that relationship is verging on the obscene. *The New York Times* (08/02, "For Students in Internet Age, No Shame in Copy and Paste" by Trip Gabriel) reports: "At Rhode Island College, a freshman copied and pasted from a website's page frequently asked questions about homelessness – and did not think he needed to credit a source in his assignment because the page did not include author information.

"At DePaul University, the tip-off to one student's copying was the purple shade of several paragraphs he lifted from the web. When confronted by a writing tutor his professor had sent him to, he was not defensive – he just wanted to know how to change purple text to black.

"And at the University of Maryland, a student reprimanded for copying from Wikipedia in a paper on the Great Depression said he thought its entries – unsigned and collectively written – did not need to be credited since they counted, essentially, as common knowledge.

"Professors used to deal with plagiarism by admonishing students to give credit to others and to follow the style guide for citations, and pretty much left it at that.

"But these cases – typical ones, according to writing tutors and officials responsible for disciplines at the three schools who described the plagiarism – suggest that many students simply do not grasp that using words they did not write is a serious misdeed."

Technology Shapes Our Morality

"It is a disconnect that is growing in the internet age, as concepts of intellectual property, copyright and originality are under assault in the unbridled exchange of online information, say educators who study plagiarism.

"Digital technology makes copying and pasting easy, of course. But that is the least of it. The Internet may also be redefining how students – who came of age with music-file-sharing, Wikipedia and web-linking – understand the concept of authorship and the singularity of any text or image.

"'Now we have a whole generation of students who've grown up with information that just seems to be hanging out there in cyberspace and doesn't seem to have an author,' said Teresa Fishman, director of the Center for Academic Integrity at Clemson University. 'It's possible to believe this information is just there for anyone to take.'

"Professors who have studied plagiarism do not try to excuse it – many are champions of academic honesty on their campuses – but rather [attempt] to understand why it is so widespread.

"In surveys from 2006 to 2010 by Donald L. McCabe, a co-founder of the Center for Academic Integrity and a business professor at Rutgers University, about 40% of 14,000 undergraduates admitted to copying a few sentences in written assignments.

"Perhaps more significant, the number who believed that copying from the web constitutes 'serious cheating' is declining – to 29% on average in recent surveys from 34% earlier in the decades.

"Sarah Brookover, a senior at the Rutgers campus in Camden, NJ, said many of her classmates blithely cut and paste without attribution.

"'This generation has always existed in a world where media and intellectual property don't have the same gravity,' said Ms. Brookover, who at 31 is older than most undergraduates. 'When you're sitting at your computer, it's the same machine [with which] you've downloaded music, possibly illegally, the same machine you streamed videos for free that showed on HBO last night.'

"Ms. Brookover, who works at the campus library, has pondered the differences between researching in the stacks and online. 'Because you're not walking into a library, you're not physically holding the article, which takes you closer to "this doesn't belong to me,"' she said. Online, 'everything can belong to you really easily.'

"A University of Notre Dame anthropologist, Susan D. Blum, disturbed by the high rates of reported plagiarism, set out to understand how students view authorship and the written world, or 'texts' in Ms. Blum's academic language.

"She conducted her ethnographic research among 234 Notre Dame undergraduates. 'Today's students stand at the crossroads of a new way of conceiving texts and the people who create them and quote them, she wrote last year in the book *My Word! Plagiarism and College Culture*, published by Cornell University Press.

"Ms. Blum argued that student writing exhibits some of the same qualities of pastiche that drive other creative endeavors today – TV shows that constantly reference other shows or rap music, that samples from earlier songs.

"In an interview, she said the idea of an author whose singular effort creates an original work is rooted in Enlightenment ideas of the individual. It is buttressed by the Western concept of intellectual property rights as secured by copyright law. Both concepts are being challenged."

Originality on the Wane

"'Our notion of authorship and originality was born, it flourished, and it may be waning,' Ms. Blum said.

"She contends that undergraduates are less interested in cultivating a unique and authentic identity – than in trying on many different personas, which the web enables with social networking.

"'If you are not so worried about presenting yourself as absolutely unique, then its OK. If you say other people's words, it's OK. If you write passages you couldn't care less about because they accomplish the task, which is turning something in and getting a grade,' Ms. Blum said, voicing student attitudes. 'And it's OK if you put words out there without getting any credit.'

"The notion that there might be a new model young person, who freely borrows from the vortex of information to mash up a new creative work fueled a brief brouhaha earlier this year. Helene Hegemann, a German teenager whose best-selling novel about Berlin club life turned out to include passages lifted from others.

"'Instead of offering an abject apology,' Ms. Hegemann insisted. 'There's no such thing as originality anyway, just authenticity.' A few critics rose to her defense, and the book remained a finalist for a fiction prize (but did not win).

"That theory does not wash with Sarah Wilensky, a senior at Indiana University, who said that relaxing plagiarism standards, does not better creativity, it fosters laziness.

"'You're not coming up with new ideas if you're grabbing and mixing and matching,' said Ms. Hegemann in a column in her student newspaper headlined 'Generation Plagiarism.'

"'It may be increasingly accepted, but there are still plenty of creative people –

authors and artists and scholars – who are doing original work,' Ms. Wilensky said in an interview. 'It's a kind of an insult that that ideal is gone and now we're left only to make collages of the work of previous generations.'

"In the view of Ms. Wilensky, whose writing skills earned her the role of informal editor of other student papers in her freshman dorm, plagiarism has nothing to do with trendy economic theories.

"The main reason it occurs, she said, is because students leave high school unprepared for the rigors of college writing.

"'If you're taught how to closely read sources and synthesize into your own original arguments in middle and high school, you're not going to be tempted to plagiarize in college, and you certainly won't do so unknowingly,' she said.

"At the University of California, Davis, of the 196 plagiarism cases referred to the disciplinary office last year, a majority did not involve students ignorant of the need to credit the writing of others."

Students Would Not Engage

"Many times, said Donald J. Dudley, who oversees the discipline offices on the campus of 32,000, it was students who intentionally copied – knowing it was wrong – who were ' unwilling to engage the writing process.'

"'Writing is difficult, and doing it well takes time and practice,' he said.

"And then there was a case that had nothing to do with a younger generation's evolving view of authorship. A student accused of plagiarism came to Mr. Dudley's office with her parents, and the father admitted that he was the one responsible for the plagiarism. The wife assured Mr. Dudley that it would happen again."

However, the most disturbing consequence, is that our abused and abusive technology is training us to be slaves. To resist this, we must draw on the help of the great questioners from Socrates down. Obviously, that is going to require much toasting in hemlock by the brave.

William Krehm

Like Reading a French Version Shakespeare with the Help of a Chinese Dictionary

Associated Press (*The Globe and Mail* of 13/08, "Freedom 70: Europe's workhorses talk of pushing back retirement" by Verena Roschmann) reports from Berlin: "Germans are famous for being hard workers – but retirement at 70?

"That's the prescriptions of two think tanks, which say years more toil are inevitable due to stubbornly low birth rates and the ballooning costs of the cradle-to-grave welfare system in a country that already has decided to bump up the retirement age from 65 to 67.

"'If we look at the higher life expectancy and the shrinking birth rate in Germany, retirement age 70 will have to be introduced over time,' Michael Huether, chief economist of the conservative think tank IW, told the daily *Rheinische Post*.

"The proposal echoes a similar assessment by the European Commission, which said last month that the 27 member states need to hike their retirement ages to 70 by 2060. The topic is on the agenda everywhere in Europe, but no country is planning to go beyond 68 at this point.

"Klaus Zimmerman of the liberal German Institute for Economic Research (DIW) told the *Handelsblatt* daily that 'raising the life work time is the most humane way to deal with the challenge.'

"Many Germans bristle at the idea of working more years. 'I'm already worn out now – how do they expect us to work several years longer?' asked Norbert Schmittbauer, a 50-year-old construction worker in Berlin. 'My body hurts so much and I start working every day at five in the morning,' Mr. Schmittbauer said. His assessment of the think tank proposal: 'Insane.'

"Many critics agree, adding that there are also too few jobs for the elderly, leaving them no choice but to retire early.

"That trend is also hitting the United States, where more people decided to retire early and file for social security benefits in 2009 – 2.74 million – than any year in history, due to a slumping job market.

"The German group, VdK, which is lobbying for retirees' interests, said Wednesday only about one-fifth of those at age 60 or older currently ever find a job again, and only every second business in Germany even employs anyone older than 50.

"VdK chief Ulrike Mascher said in a statement the idea to push retirement back even further to 70 is 'utopian.' She added that a quarter of German employees aged 55 to 59 need to rely early because they are too sick to work.

"Benjamin Ladiges, a 32-year-old Berlin lawyer, said that while some jobs allow later retirement, professions with physical strains should be exempted, especially physical work. 'It is not an option,' he said.

"The debate is complicated by the fact that Germany's shrinking work force means the nation will face an increasingly acute shortage of skilled labor in some sectors – despite generally strong resistance to higher immigration.

"The suggestion of retirement at 70 has fired up an already fierce debate about an unpopular 2007 law to raise the retirement age from 65 to 67 from 2012 through 2029.

"The Social Democrats, then part of the government coalition backed the law at the time, but took a beating from their constituency for it in the 2009 general election and have since raised questions about sticking with the plan.

"The government has defended the law, arguing the job market for the elderly is improving. But Economy Minister Rainer Bruederle has made it clear there are no plans to go beyond 67.

"Raising the retirement age for full benefits to more than 67 is also being floated in the US, along with a small cut in benefits, a slight increase in payroll taxes, or subjecting more income to taxes.

"House Democratic Leader Steny Hoyer suggested raising the retirement age recently, and John Boehner, Republican leader in the House of Representatives, said it maybe should go to as high as 70.

"Doing nothing would require about a 25 percent cut in benefits for US retirees a couple of decades from now.

"All of Europe is facing the same trend of aging populations. While there are currently four people working for each retiree, projections indicate that by 2000, on the average there will be only two."

All of which shows what confused messes we can stray into once those who view society as just a world-size lemon to squeeze, while doing away with history, and elementary rules of logic.

W.K.

Turn the "Most Profitable Investment Governments Can Make" Into Debt and Everything Stands on Its Head

Elsewhere in this issue, and in any of our issues for a couple of decades or so, we have explained the Work of Theodore Schultz of the University of Chicago, reached the conclusion sixteen years after the end of the war, that "investment in human capital is the most profitable a government can make."

However, that key lesson of World War II was suppressed so that the market might resume the gambling games as of old. However, if you mistake prepaid investments for debt and vice versa you end up without serious accountancy, and just about everything having to do with society standing on its head. And at this point we give the floor to *The Wall Street Journal* (06/17, "Fight Over City Hall – Literally" by Ianthe Jeanne Dugan): "A Financial firm is fighting City Hall – and angling to take over the building itself. Buena Vista, VA, borrowed $9.2 million through a bond offering in 2005 to refinance a municipal golf course. It pledged as collateral, of all things, its City Hall and police station.

"Now, amid financial difficulties, the city says it can't pay its debt, triggering a showdown over these public buildings.

"On the other side of the battle is a big New York insurance company, ACA Financial Guaranty Corp., which is obligated to pay bondholders if the city defaults.

"'They put up City Hall to finance the golf course,' says Bonnie France, a lawyer for ACA. 'It's collateral, so they could lose it. I've worked in public finance for 30 years and never seen this happen.'

"Municipalities across the US are struggling with the huge debts and shrinking revenue. Harrisburg, the capital of Pennsylvania, is flirting with bankruptcy. And when Central Falls, RI, couldn't pay its debt recently, it handed its finances to a receiver.

"'This is a huge mess, but we're not alone,' says lifelong Buena Vista resident Jerry Miller, a 67-year-old retired maintenance mechanic.

"The 18-hole Vista Links golf course, with sweeping views of the Blue Ridge Mountains, was opened in 2004 in an attempt to buoy the city's ailing economy. In a town of just 6,500 people, hundreds of manufacturing jobs have vanished in recent years, the latest blow coming with the departure of Bontex Inc., a maker of materials for footwear and luggage, which recently laid off about 69 workers.

"Officials projected the golf course would pay for itself. Plans called for about 70 acres surrounding the property to be dotted with a hotel, homes, small businesses and restaurants. The city took out a loan, then refinanced it by selling bonds.

"'Unfortunately, soon after the project was finished, the country fell into the worst recession since the Great Depression,' Mayor Mike Clements told residents at a recent public meeting, reading from a prepared statement. Mr. Clements didn't return calls seeking comments.

"The number of rounds played on the course has declined 30%, City Attorney Brian Kearney said in an interview. 'People are not playing golf,' he says.…

"So the city has been making the bond payments out of its own strained coffers. This year, it owes $662,000 in two payments, The city didn't pay the first $423,000 chunk due July 15, Mr. Kearneh says, so it is in default….

"It has put the course up for sale, cut the staff from seven to two, reduced fertilization and watering. It had discussions with elected officials and met with bondholders and ACA to renegotiate. 'No one has been able to give us any solution short of a dramatic tax increase,' the mayor told residents.

"So, when it completed its budget last month, Buena Vista completely left out the monthly bond payments for the golf course. The alternative, the mayor said, was to cut education, public safety, the library or social services….

"ACA, on the hook to pay bondholders, sent teams to Buena Vista to persuade officials to put payments back in the budget. A spokesman for ACA declined to comment.

"The insurer has much to lose. The collateral is worth just a fraction of the debt.

"City Hall is a small two-story building, constructed in the 1960s. Like the newer police station, it is worth just a few hundred thousand dollars, Mr. Kearney guesses.

"But the financial backers, he says, were interested in something more than the value of the buildings. 'They wanted the city to put up essential government buildings, because we would not want to risk losing those,' Mr. Kearney says."

Are You Going to Hold Court in the Street?

"The dust-up is causing confusion. Residents are flocking into City Hall asking, 'Are you going to hold court in the street?' Circuit Court clerk Christopher Coleman says.

"Mr. Kearney is working on a legal argument to prevent that outcome. While the city owns City Hall, he says, a Virginia statute gives control of courthouses to judges. That means the insurer could seize City Hall but, he will argue, not the half of the first floor where the courts are based. Worst case, he says, the city might be able to lease the buildings back from ACA.

"But some residents are perplexed by the math. 'If they can't pay the loan on a golf course,' Mr. Miller asks, 'how do they think they're going to get the money to rent a building big enough for the City Hall, courts and a police department?'

"The bonds were floated through a separate parks entity with no assets. The city agreed to a 'moral obligation bond' that promised to pay if the golf course revenues couldn't. But it was only morally, not legally, obligated, says Mr. Kearney….

"'Failure to appropriate money,' Moody's wrote, 'demonstrates uncertainty about the city's willingness to meet its obligations.'

But all this clearly stems from President Obama having been advised by a prominent former high executive have his country's investment in human capital – revealed as the most important could make – to be treated as an expense.

From there on everything has turned up standing on its head. Loans to bankrupt mega-banks are capital assets, but the prepaid investments in human capital, the environment, are debt. And with the economy so thoroughly turned upside down to stand on its head what can we expect other than an accelerating race to the final misplaced gamble – atomic war?

W.K.

Without Compass the Fed Sails the Tossing Sea

The New York Times (08/11, "10-year Treasury Yields Slide on Fed's Decision to Buy Debt" by Christine Hauser) tells a tale designed to confuse rather than clarify: "Yields on 10-year Treasury securities, a vital benchmark for home mortgages and corporate loans, tumbled to the lowest level in more than a year on Tuesday after the Federal Reserve said it would buy up government debt in an effort to bolster the nation's increasingly fragile economy."

Given the suppression in recent decades of the great reforms developed under FDR, we must explain how neither the public nor governments are equipped to deal with the confused mess that passes for economic policy. That holds even for Canada, where the central bank that had been set up as a privately-owned institution in 1934 was bought out in 1938 by our federal government from its 12,000 private shareholders at a profit. In the US the state Federal Reserve banks have remained in private hands and only the central Fed was acquired by the government.

In dealing with the statutory reserves, Americans have been less sweeping than in Canada. This has to do with the *statutory reserves* that provided the government with an alternative to depending exclusively on interest rates, which are the chopping block in our big banks' financial butcher-houses. Statutory reserves required the banks to leave a proportion of the money of the deposits they take in with the central bank on which they receive no interest. If the economy became over-stimulated, instead of increasing interest rates, the central bank could raise the amount of the statutory reserves that the banks had to deposit with the central bank, lessening the banks' ability to drive up interest rates to exploit the scarcity of capital. Canada did away with the statutory reserves entirely, whereas in the United States they continue to exist, but only during bank business hours.

To illustrate the importance of how confusing this complicated field can become, let me tell of a telephone call I received from someone in a Prairie province who wanted to know how we can make so much of our Bank of Canada not being used by our government for financing its programs, when he reads of the Bank of Canada holding large amounts of government bonds. Isn't that using the Bank of Canada? he asked. No it is not. When the Bank of Canada finances a government program, there will be a small service charge, but no bond is needed, any more than a wife borrows the money from her husband to go shopping. She could very well get her carfare from his earnings for the shopping trip. The bonds of the central government held by the Bank of Canada were undoubtedly acquired from private parties in trouble and bailed out by the government, and as security that firm would have surrendered what assets it had.

Our Government Avoids Borrowing from Its Own Bank

Rather than issuing bonds and paying interest to the central bank that it owns, our government is absorbed in bailing out firms in trouble. During War II for example, citizens, fully employed to support in the war industries, were encouraged to buy government bonds, and put up the bonds so acquired with the central bank as security for the Central Banks' financing. But that was to withdraw excess purchasing power from the civilian work-force, to leave it available to finance the war. Basically, it is dedicated to preserving a social order that since the 1980s has placed power in the hands of large speculative banks by proclaiming a flat price level, enforced by increasing interest whenever prices move up. This is justified by the illiterate procedure of reversing propositions by flapping them over as a pastry cook does pancakes. But that only underlines the havoc wreaked in the illiterate procedures that have shaped government policies for the last three or so decades.

Might I prove the point? Easily. If I put a loaded pistol to my head and push the trigger. I fall dead. But the proposition cannot be turned around and remain valid. If I fall dead, it doesn't mean that I suicided. It could have been heart failure. But such nonsense is taught in the economic faculties of our universities today, and not contradicted because of the near certainty that questioning this bad logic would cost the professor his post.

To make this possible, it has been necessary to suppress the most important lesson to come out of World War II. No sooner were the Armistices signed than Washington sent many hundreds of economists to Japan and Germany to study the destruction to predict how soon Japan and Germany could again become the fabulous traders that they had been.

Some sixteen years later one of these, Theodore Schultz of the University of Chicago, wrote a book in which he explained how wrong they had been in their predictions. This he explained by their having concentrated on the physical destruction but paid little attention to the fact that the highly gifted and motivated work force of the two leading axis countries had come out of the war almost intact. And he concluded that human capital is the most profitable investment governments can make.

The Japanese lost no time proving his conclusion. They made and carried out the decision to convert their economy based on textile exports that had imported the fibers for its exports, leaving only a small potion of the proceeds within the country. Step by step, evading the displeasure in the matter of their occupiers, they shifted to heavy metallic products until finally developing the most successful automobile industry in the world.

In his book Schultz reaches his final conclusion: investment in human capital is the most productive investment a government can make. Not only is it prepaid, but its "expenditure" is further investment. The children of educated parents are easier to educate, those of healthy parents are healthier, and so forth.

For a few years he was celebrated, even decorated for his great conclusion, and then completely forgotten. I would love to be proved wrong, when I note that COMER alone seems to remember the man and his great discovery. And yet what been suppressed is the false solutions that have well-embarked our civilization to its doom.

For if governments, including that of Mr. Obama, insist on considering any investment in human capital as debt instead of the greatest of all possible government investments you have nothing that could be mistaken for accountancy in the dark.

Then there is never enough money. In the resulting nightmare, school budgets are cut and the funding for jails increased. To reverse his ruinous policy, Obama would have to change lead personnel of his regime. Instead he had retained high officials who promoted speculative banking as his key advisers. Universities – with very few exceptions – have purged their economic faculties of this nightmare of scientific method.

It is the mission of COMER to rally the forces to put an end to this nightmare.

William Krehm

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A Hurricane of Double Talk

The Wall Street Journal (8/02, "Goldman Defends Valuations with AIG" by Serena NG and Carrick Mollenkamp) recounts a tale billowing with inconsistencies: "Two years after collateral demands from Goldman Sachs Group Inc. helped spark a cash crunch at American International Group Inc. that led to the giant's near collapse, a mystery remains: How did Goldman come up with the mortgage securities prices it used to extract cash from AIG?

"The Wall Street firm is now trying to convince its critics that it used accurate prices amid a congressional inquiry into the causes of the financial crisis.

"Last week, Goldman submitted documents detailing how it established values in 2007 and 2006 for mortgage securities insured by AIG to the Financial Crisis Inquiry Commission, a bipartisan panel probing the crisis, according to people familiar with the matter.

"In a nine-page memo, Goldman noted that the securities AIG had insured, known as collateralized-debt obligations, or CDOs, rarely traded, so Goldman used prices from trades in other CDOs to 'help inform' valuations on the AIG deals. It also took some cues from valuations of a popular subprime index known as ABX. The memo also contained actual prices of trades Goldman conducted in several CDOs, an effort to show how the firm itself bought and sold securities at prices similar to what it provided to AIG as the basis for collateral calls.

"'We believe our marks were accurate and reflected the value markets were placing on the trans-actions,' Goldman said in the memo provided to the FCIC, titled 'Valuation and Pricing Related to Transactions with AIG.'

"At a hearing in Washington a month ago, the 10-member FCIC panel grilled Goldman executives including Chief Financial Officer David Viniar about the bank's method of valuing CDOs insured by AIG and questioned why Goldman's prices were often much lower that those from other banks in 2007. Phil Angelides, a former California state treasurer who is chairman of the commission, said at the hearing that some of Goldman's prices seemed like 'a stab in the dark' and asked the bank for 'more granular' information on its pricing.

"The debate has centered on how Goldman used the values of securities to demand collateral from AIG, which had sold Goldman credit protection on $20 billion in mortgage debt pools or CDOs. Goldman's collateral calls began in July 2007 and were later followed by similar demands for other banks in 2008 as mortgage debt prices fell. Ultimately, unable to come up with enough cash to meet all its collateral calls and other financial obligations. AIG in September turned to the US government for a bailout that now totals as much as $182.9 billion in taxpayer support.

"Goldman's memo acknowledged that 'a certain degree of judgment was necessary' in valuing the CDOs because they were so thinly traded. Goldman said its prices were based on bids and offers and trades in 'comparable instruments' as well as valuations it used for residential mortgage-backed securities and other assets that made up the CDOs.

"For example, in October 2007, when a financial model used by AIG valued the least risky slice of a mortgage-debt pool called Altius II Funding at full value, or 100 cents on the dollar, Goldman told AIG the same slice was worth 87 cents for every dollar of outstanding debt. In its memo Goldman said that in the same month, it had paid 70 cents on the dollar for a riskier slice of a mortgage deal called Altius I Funding, which was issued in 2005, the same year as the Altius II deal AIG insured, and that had several similar characteristics. The 70-cents price, which reflected a 30% decline from the security's original value, 'clearly demonstrated a significant degree of stress' for CDOs issued in 2005, Goldman's memo said.

"Another bank, Credit Suisse valued the Altius II slice insured by AIG at 85 cents on the dollar around the same time, according to documents released by the FCIC. However, in another AIG-insured CDO called Sherwood Funding, Goldman's value of 60 cents on the dollar was well below a 90-cents-on-the-dollar price from Morgan Stanley, the documents said.

"Goldman's memo acknowledged that 'certain degree of judgment was necessary.'"

W.K.

RENEW TODAY!
(SEE PAGE 2)

Price Stability and the Public Sector

The following essay was translated into French and appeared in the March, 1970, issue of Revue économique *of Paris.*

A spreading skepticism is making itself felt concerning the ability of governments to contain the upward surge of prices. The pharmacopoeia of conventional economic theory has been emptied for the purpose, but its specifics seem only to add to the violence of the symptoms. Higher taxes, punitive interest rates and credit tightening have only imparted new momentum to the price swell. Governments are encountering even greater hardship in placing their bond issues, and find that a new credibility gap has opened up between them and their electorate. Stepped-up interest rates seem only to sharpen the ravening demand for more credit. In the letters-to-the-editor columns of our press more and more irreverent citizens are asking whether higher taxes and interest rates really do serve to keep prices down, no matter what the assurance of authoritative economists on the point.

On such matters, of course, *vox populi* is hardly *vox dei.* Yet it would be rash for economists to ignore a cardinal lesson from a not too remote period of history. There have been turning-points in the economic life of nations, when intelligent laymen where quicker to assess what was taking place than most of the trained experts. This, of course, was notably so in the depression of the Thirties. That was because they were less shielded from reality by blinkers of highly stylized theory. We could conceivably be approaching a like crisis in economic science today. It might therefore be worth the while of economists to try stepping outside the framework of accepted doctrine, and review its best established truths in a spirit of cool reappraisal. I propose undertaking just that in this paper. Should I prove unsuccessful in making my point, my effort may at least help confirm my readers in their more comfortable beliefs.

Let us start with the definition of inflation as taught in our schools:

"Inflation is an upward trend in the general price level…we should reserve the term inflation for a longer, non-reversing trend that is of such duration and intensity that the effects of rising prices are widely felt." After noting that in the past inflation has been associated with every major war, the author goes on to say that "the principal distinction of World War II is that inflation was largely repressed by controls.… The creeping inflation after 1956 could not be attributed to war. Many people came to view inflation as the inevitable price of economic growth, although the rate of growth was well below 3 per cent.… However, it is clearly not true that inflation has always been a concomitant of growth.… From 1820 until the beginning of the Civil War, the trend of prices was moderately downward while the average growth rate of our young economy was high.

"There may new conditions in the economy, such as powerful labour unions, greater concentration of capital, farm price supports, and a managed monetary system which support the belief (that inflation is the inevitable price of economic growth). The case is not clear."[1]

Walker's is a frank statement of a perplexity that is increasingly widespread on the point. Significant in this list of conditions that might be connected with "creeping inflation" is the absence of any reference to the growth of the public sector of our economy. Here, indeed, is the blind spot in the vision of our economic theory today.

For were we to single out the most characteristic institutional trait of the economic scene before us, few would hesitate to choose the portentous expansion of the public sector. In many works J.K. Galbraith, along with many others, has enlarged on the inevitability of this trend with insight and wit. But the facts laid bare by him have as yet found no echo in the theories and techniques of any school.

The bulk of this mounting government expenditure is not self-liquidating. Comparatively few items of state-produced goods and services are paid for by a direct charge upon their immediate consumers. Most government activities not only do not pay their own way, but they are altogether *unpriced.*[2] Their costs are covered by imposts on goods and services originating in the *priced* private sector, or on income of the factors of production associated with the latter.

The taxes collected from the private sector to pay for the upkeep of the public sector can take one of two forms. They may appear as a direct additive to the price of the good or service at the point of its ultimate consumption. Or they may be levied not directly on the ultimate consumer but on the raw materials, or on various stages of the unfinished product, or on the factors of production (income tax, corporation income tax, business taxes, real estate taxes on commercial or industrial structures). Should the tax be of the latter sort, the market conditions will determine whether or not it is passed onto the ultimate price of the final product. But even where such taxation cannot be passed on immediately to the ultimate consumer, it still affects end prices in the medium or long term. For in such cases it bites into the profits of the industry in question, and must eventually lead to the redistribution of investment.

It would be possible to construct a value theory to show the effect of the growth of the public sector on price[3] in the simplest and most direct form. All value theories, of course, contain a large normative element. Of necessity they single out a facet or two of complex social interrelationships to serve as the basis for their orderings. This implies a judgment on what is fundamental and what secondary – and as an inevitable extension of this a bias as to what may be desirable. Thus marginal theory could never have arisen without a bedrock faith in free market processes. And Adam Smith's labour theory of value sprang from an 18th century Scottish burgher's conviction that a "man is a man for a' that."

To allude to this normative element in all value theory is to suggest its limitations. For to single out some aspects of the economic complex, is to supplant others. This process may take one of two forms. An isolated relationship or two may be excised from the living body of reality to serve as the premise for neat mathematical procedures. We might call this the method of *mathematical abstraction.* The danger here is that the ensuing mathematical treatment may be pressed to a degree of refinement in no way warranted by the truncated social data on which its original equations were set up – it thus becomes misleading. Every first-year student of physics is drilled to evaluate the margin of error in his experiments, and is warned against losing sight of the number of significant digits in his results. Economists are not invariably so wise.

Mathematical abstraction is what underlies marginal theory, posited as it is on the fiction of perfect competition. Its insensitivity to aggregate economic problems was the inevitable consequence of its abandonment of an objective unit of value. This omission was long covered by a devout belief in Say's Law that denied the serious possibility of discrepancies between aggregate supply and demand, and thus seemed to strip aggregate problems of all urgency. The elegances of marginal theory thus became a positive detriment when it came to determining not only where the economy was headed for, but in the 1930s where in fact it had already arrived. A similar fiasco may be shaping today from the helplessness of conventional theory to deal with the price gradient created by the growth of the public sector.

The other method is that followed by Adam Smith or Karl Marx in their respective versions of the labour theory of value. We might call it *sociological abstraction.* By this they captured in closely packed form what they deemed the economico-sociological essence of their society. Thus in Marx's labour theory of value – with its surplus-value extension – he condenses notions of production for exchange rather than for direct use, the divorce of labour from the means of production. It was because his theory had encapsulated the social reality of mid-19th century capitalism, Marx was able to achieve real feats of prognosis. On the other hand, due to this same concentration on underlying *qualitative* relationships, Marx's theories, like those of Adam smith, lent themselves but poorly to deal with short-term market phenomena. In this closer domain they were simply not operational. The necessary choice between these two methods of abstraction – each with its severe handicaps – has been the besetting dilemma of economic theory in every period.

John Maynard Keynes had wrestled with just this dilemma: he came to recognize that the abandonment of an objective value theory by marginalist school had blunted its powers for dealing with the problems of aggregate economics. In this *The General Theory*[4] the following significant passage occurs: "I sympathize, therefore, with the pre-classical doctrine that *everything is produced by labour,* aided by…technique, by natural resources which are free or cost a rent according to their scarcity or abundance, and by the results of past labour, embodied in assets, which also command a price according to their scarcity or abundance. It is preferable to regard labour, including of course the personal services of the entrepreneur and his assistants, as the sole factors of production, operating in a given environment of technique, natural resources, capital equipment, and effective demand. This partly explains why we have been able to take the unit of labour as the sole physical unit which we require in our economic system, apart from units of money and time." It is revealing that though Keynes commentary soon became a major industry, his followers with few exceptions have chosen to ignore this pregnant passage.[5]

Indeed, it may well be said that the divorce from reality of an economic theory can often be measured by the degree of refinement of its mathematical elaboration. When a break-through in theory occurs – and one is overdue today – it can be safely predicted that it will come in the form of a powerful but crudely formulated idea, one whose purchase on reality will not have been sacrificed to permit too finely decanted techniques.

The main outlines of such a theory are not hard to foresee. It must be an objective theory of value for we are most concerned today with problems of aggregate economics. It will thus be necessary to return to the great tradition of Smith, Ricardo and Marx, as Keynes, indeed, attempted to. For there is after all nowhere else to seek a basis for an objective notion of value: the one thing that commodities and services, for all their diversity, have in common is that they are the products of human labour. Yet the classical labour theory of value will have to be amended in some vital respects.

Smith and Marx after him held that in order to be productive labour had to be directed to the production of material goods: labour spent on services was deemed unproductive. Faithful to this tradition Communist governments still exclude the output of services from their statistics of the national product. This introduces a gross distortion, since in contemporary society the volume of services had been growing at a faster rate than that of commodities. A value theory suitable to our purpose would then have to embrace both goods and services.

In the eyes of Smith, Ricardo and Marx, the functions of the state were non-productive. This position derived from the liberal bias of the first two: with Marx it was but part of a jaundiced view of the state as an instrument of the exploiters.

Such a position is quite out of the question in our day: the public sector is the more dynamic one in our world. The value of its output in such a theory could, of course, also be assessed in terms of the man-hours of average labour expended in producing it. The matter, however, is complicated by the fact that the greater portion of the output of the public sector is unpriced: directly of indirectly it is paid for by levies on the products and factors of production of the private sector. Yet these public services provide the infrastructure of the entire economy, educate its producers and consumers, and are the means of keeping an ever more complicated society appropriately skewered. Hence we might very well consider these public services provide the infrastructure of the entire economy, educate its producers and consumers, and are the means of keeping an ever more complicated society appropriately skewered. Hence we might very well consider these public services and goods as *intermediate services and goods* indispensable for the production of the private sector. We could thus *define* the value of the aggregate output of the private sector as consisting of two components:

1. The *core value*[6] corresponding to the costs and profits net of all taxation that have entered into the price. In a broad way this will correspond to the quantity of "average, abstract labour" employed in the private sector to produce its output:

2. The *social lien* representing the sum of all taxes that directly or indirectly are levied on the private sector and on its factors of production. In a general way this may be to the amount of "average, abstract labour "expended in the production of the unpriced public sector.[7] We have chosen the name *social lien* because it constitutes a claim of society that must be satisfied before the goods and services of the private sector can enter into circulation.

Such a theory would capture in compact form the essence of our contemporary economic reality. But because it does so, it lends itself to no great precision of mathematical treatment as regards individual goods and services, or specific market situations. Firstly, there would be the traditional shortcoming of labour theories of value – they are qualitative rather than quantitative. Correctly these see in human labour the one common denominator of the output of human industry. But they cannot foretell the proportions in which the different classes of labour will be exchanged. These proportions are parameters established by convention and by the political and social fray, as well as by microeconomics of the market.

Then, too, there is the difficulty of assessing the portion of the cost of the unpriced output of the public sector that is assigned to the individual commodity or service produced by the private sector. In theory this could be dealt with in one of two ways. It could be related to the cost of such state services that have contributed to the production of the particular item in the output of the private sector. Clearly this notion is more readily formulated in theory than applied in practice. Or we might disregard the contribution of the unpriced state services to the particular commodity, and concern ourselves instead with the portion of the cost of the entire unpriced public sector that finds its way into the price of the given commodity. This is determined both by fiscal policy and by microeconomic circumstances that govern the passage of taxation into price.

Such formulations are far more important for abstract qualitative appreciations than as an operational calculus. However, as our attention shifts from individual commodities to the economics of aggregates, many of these difficulties will tend to recede. For our concept would retain a good part of its usefulness even if we were to recognize that such value is not necessarily realized in full at any particular sale. Since the buyer's gain is the seller's loss and vice versa, the overall quantum of value, conceived as an objective entity, remains constant. And such a composite notion of an objective value will help us to some useful insights into the nature of dual economy, insights that we shall be able to retain even when we return – as we propose doing – to more conventional ways of handling the problem.

Gone is the day when the price of a commodity could be related entirely to the cost of its own production ruffled in some minor way by the prevailing market winds. Economists have long operated with the motion of "disposable income," income net of taxes. Our "core value" is a parallel concept relating to price – i.e. price net of all taxation that has found its way into it. Now the fact is that most discussions on price and inflation today are carried on as though "core value" were the whole of price. Except in a few specialized studies on public finance, the "social lien" is usually disregarded. The result is highly misleading.

To remedy this a new notion of stratified price must be worked out. This could be represented on a price scale in Figure 1.

Now since there is a pronounced trend for the public sector to grow in relative importance at the expense of the private sector, it is inevitable that the social lien should loom ever larger in the above price column. While the public sector takes on girth, the private sector that serves as its supporting pedestal becomes slimmer. The whole seems headed for the increasing instability that goes with such a structure.

We can illustrate the matter even better by relating our column of price to the horizontal structure of the economy. The latter is divided into a private and public sector: the public sector in turn consists of a smaller priced public sector and a larger unpriced sector. (See Figure 2.)

We are simplifying the picture by reducing the entire output of the private sector to a single commodity, and representing its price by a vertical column. Onto this is mapped a horizontal range portraying the structure of the economy. The latter is broken into the private sector and the priced and unpriced public sectors. The lowest rungs of the price columns correspond to the core value of the price of the commodity consisting of the usual components of fixed capital consumed, raw materials, wages, salaries, interest, rent and profit. This maps onto the part of the horizontal range representing the private sector which we might also designate "core production." The relatively small priced portion of the public sector maps onto a much smaller portion of the social lien segment of the column, since in part the priced public sector does pay its own way. The unpriced public sector is mapped out onto the greater portion of the vertical social lien segment.

The mapping of the social structure onto commodity prices is not arbitrary. There is a sound causal basis for the correlation. And any policy that advocates compressing the readings on the price scale, without enquiring after the implications of this on the horizontal scale, cannot be helpful.

The transfer of the cost of the public sector to the prices of private production does not, of course, occur as a single mark-up. Instead the burden of taxation is injected at every point in the stream of production. It swells overhead, raw material costs: it bulges wages to make up for tax and social insurance deductions. At every stage it is worked upon by the subtle multipliers set not only by proportions and potences of technology, but by the mountains of paper work thrown up in our society at each stirring of the clerical mice.

When we come to study the factors making up the price of an individual commodity, we find ourselves analyzing not the cost of just one product, but of an emergent way of life. Let me illustrate by singling out one item, say the price of penicillin. In our economy the price of such an antibiotic must cover not only the cost of production of the sample sold, but part of the cost of the research that led to its development, of the cost of training and educating the personnel needed for such research, a quantum towards the cost of educating the children saved from a precocious death through the use of the drug, another towards the cost of maintaining the aged and ailing whose lives have been prolonged through its use, and towards foreign aid to the underdeveloped countries where its introduction has accentuated the pressure of population on food. A profile of our evolving institutions is imbedded in the price of every commodity sold today.

The circuitry of our mixed economy still awaits sorting out: what is required is an adaptation to taxation and its contribution to price of the techniques introduced by Wassily Leotief in his Input-Output Economics. Certainly the present attempts to operate in an increasingly hybrid economy with the categories and probes of a private capital-

Figure 1

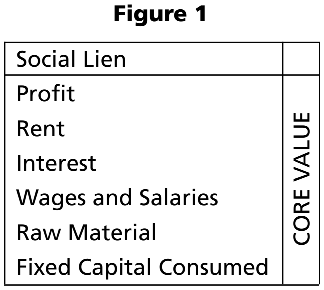
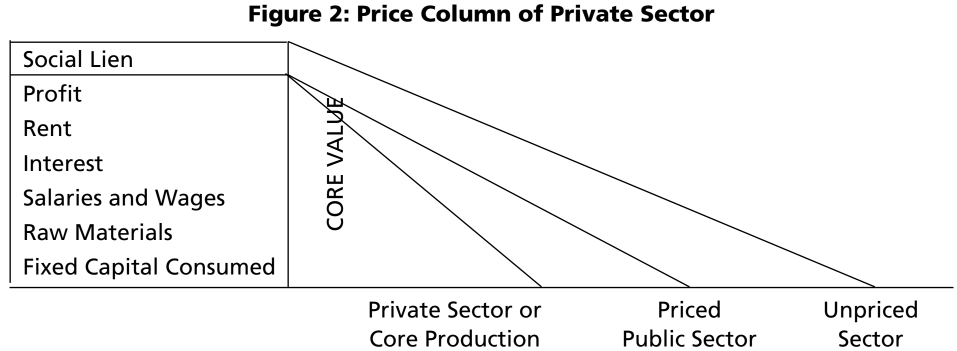


Figure 2: Price Column of Private Sector



ism are bound to lead to grave error. For in such a setting, prices no longer signify what they used to. And to work on the assumption that they do is to invite all manner of inclement awakenings.

Thus the efficacy of Keynes's anti-cyclical techniques depends in large part on the diagnosis of an inflationary trend at its very onset. This is hardly possible if we ignore the role of the social lien and mistake the lengthening shadow cast on prices by the public sector for the autonomous movement of prices themselves. To interpret a rise in prices – the sum of core value *and* the social lien – as necessarily an indication of inflation is a serious flaw in reasoning. It can trigger anti-cyclical measures that may be unwarranted and harmful. The indications, indeed, are that this has happened repeatedly in the United States since the Second World War. To avoid such misreadings it is necessary to develop techniques for distinguishing between the respective parts of core value and social lien in any given price rise. Otherwise misinterpretation of what our prices are signaling will continue to feed mischief into the policy-making of the Western world.

Earlier I remarked that it would be possible to devise a value theory that would present the relation of the public sector to the price level in the simplest possible terms. At this point, however, it would undoubtedly be the better part of valour not to attempt this. For nowhere does mandarism sit more solidly enthroned than in the realm of value theory. Venturing a fresh approach to the problems of our economy is in itself no small task: to complicate it further by challenging the sacred cows of pure theory would be foolhardy indeed. Let us therefore retrace our steps and restate our case in more conventional terms.

Let us for the purpose seek to track the shift of taxation into price. For this we must formulate a *Tax Shift Function* that will give the proportion of taxes paid by the factors of production that is carried into the price of the final product. Clearly there will be two variants of such a function. The first, and for our goal by far the more important, will be the Aggregate Shift Function (ASF). This may be defined as the function determining the proportion of the total taxes collected by the state that is carried into the total prices of the private (and of the small priced public) sector. Another and far more complicated function would give us the distribution of such shifted taxes amongst the various prices of individual goods and services. This we might call the *Micro-Shift Function* (MSF). There will, of course, be a relationship between the two that can be expressed as follows:

$$\text{ASF} \times \text{Gross National Product} = \sum \text{MSF}_i \times Q_i$$

where Q equals the quantity in dollars of the commodity or service I, and MSF_i *the micro-shift function applicable to the given product.*

However, in what follows we shall be exclusively concerned with the ASF.

The ASF is a spreading tent that can offer shelter to the most contrasted views on the actual importance of the tax shift phenomenon. In conjunction with the special value theory designed for our dual economy that we sketched above, the ASF would become a constant equal to unity. Dealing in terms of actual price, we shall see that it is quite possible for the ASF to exceed unity, that is for the impact of tax on price to exceed the total amount of taxes collected, to be subject to a *Tax Shift Multiplier.* On the other hand the most diehard conservative who continues to believe that tax increases lower prices rather than accrete onto them, may be comforted by the belief that the ASF approximates to zero, or even takes on negative values. Though rarely formulated openly, this unlikely notion is implicit much of the time in the reasoning of economists.

The Aggregate Shift Function has several independent variables.

1. *Structural Quotient* (π). This is the proportion of the unpriced sector to the entire economy. Between the years 1929 and 1966 this quotient in the United States rose form about 8% to 24%. A still more revealing proportion, thought in a form less handy for our further purposes, would be the ratio of the unpriced sectors to the priced. Between 1929 and 1966 this ratio – closely related to our Structural Quotient – rose from about 9.0% to 30.2%. The priced sector (private and public) is, of course, the ultimate source of all government revenue. As this tax base shrinks in relation to the volume of taxation exacted from it, we move closer to a limiting situation that could be termed a "tax-saturated economy." In this the proportion of the unpriced to the priced sector has grown so large, that the state must exploit its tax-base with searching thoroughness. Once imposed taxes are less and less likely ever to be rescinded, or even seriously trimmed. Sufficient revenue can no longer be raised from a few isolated areas of the economy, while others remain sheltered. On learning of a new tax, taxpayers no longer ask for whom the bell tolls: taxes imposed on any group are likely to be felt by the entire population via the tax shift onto price. For by the time such a state is reached, taxes will have eaten into vital margins of revenue, and the factors of production will have taken up a stance of riposte to further tax increases. Not only will they react to taxes by upping their own prices: they may even anticipate such tax increases. The aggregate Shift Function may thus even develop a negative time lag. The most obvious instance of this is the labour contract with escalation clauses running several years ahead.

2. *Fiscal Index* (λ). The structural quotient is important because it lays bare an element of institutional change that determines the specific weight of the tax burden to the economy. But in the Shift Function the structural quotient appears only as co-factor of another variable – the proportion of public expenditure that is actually covered by current taxation. We might call this co-factor the *fiscal index,* and it is another important variable of the ASF. Their product is equivalent to the amount of current taxation over the Gross National Product. (See Figure 3.)

It is this relation of tax burden to tax base that operates as a unit to influence the shift function. But this ratio is compounded of two co-factors, each of which have a highly independent career. We have seen that the structural quotient reflects institutional changes – the proportion of the unpriced sector to the entire economy. For its part the fiscal index is largely shaped by official policy. Into it will enter the effects of anti-cyclical budgetting. It will also mirror the fact that governments rarely make a point of financing their capital investments over periods that correspond to their depreciation spans. The Statistical Abstract of the United States (1968) gives revenue for all levels of Government for 1966 as 225.6 billion dollars and expenditures as $224.8 billion, despite the fact that $40 billion of such expenditures are classified as "capital outlay."

3. *Price Gradient.* The value of the Shift

Figure 3

$$\pi\,\lambda = \frac{\text{Net Expenditure of Public Sector}}{\text{GNP}} \times \frac{\text{Current Taxation}}{\text{Net Expenditure of Public Sector}} = \frac{\text{Current Taxation}}{\text{GNP}}$$

function will also be affected by the previous record of price change. When prices have already been upwardly mobile, further price increases are likely to encounter relatively easy resistance – unless the microeconomic weather veers abruptly. But where prices have long been stable there is static friction to overcome before shifting can occur. It requires circumstances of some force to pry prices out of their grooves. Such circumstances may be provided by the imposition of a tax which may upset the established price structure and enable producers not only to recoup the tax but even certain increases in cost that they had hitherto absorbed out of their profits. In a suitable microeconomic setting, we may thus have the shift function take on a value less than unity. To a large extent the psychology of the buying public and of the factors of production are influenced by the contour of prices in the recent past. To express this contour we need at least the first and second derivatives of price to time – dP/dT and d"P/dT". These there fore make up further independent variables of our Aggregate Shift Function.

We thus have the equation:

ASF = ∅ ((π λ), dP/dT.d"P/dT")

where π *= Structural Quotient,* λ *= Fiscal Index, P = Price Index, T = Time*

In our Western world, the output of the public sector almost entirely takes the form of services. What goods are needed for its operation, the state usually purchases from private industry. In effect the unpriced public sector draws upon the private sector for the intermediate goods and services essential to its own production. As a result not only do higher taxes feed into price, but the prices so increased trickle back to swell government expenditures and thus taxation. We must therefore reckon not only with a shift function setting the proportion of tax increases that accrete onto price, but with a *counter-shift function* that carries a portion of such price increments back into taxation.

We should not lose sight of the fact that the shift function as we have formulated it deals with the *proportion* of the aggregate quantum of taxation that is carried into the *aggregate quantum* of prices. Likewise the counter-shift function sets the *proportion* of the *aggregate* amount of such tax-induced price increases that are carried back into the tax bill. Since the unpriced public sector in the United States comprises something around 25% of the entire economy, the counter-shift function would be relatively minor, though by no means negligible. Assuming an average tax incidence on the goods and services purchased by the state, no more than 25% of the absolute amounts of price increases due to taxes is likely to be carried back into taxation.

Once having recognized the existence both of a tax shift function and a tax counter-shift function, it is easy to see that in conjunction the two will have an effect not unlike that of the multiplier and accelerator in determining the impact on aggregate demand of new investment. We will have a rapidly converging series in which new taxes provoke price rises, and these price increases bring on further taxes. We may illustrate the point by tracing the effect of a unit of increased taxation, with an aggregate shift function equal to .6 and an aggregate counter-shift function equal to .2. (See Table 1.)

Thus the final value of the shift function cum multiplier is .68.

The mere existence of a significant shift function is bound to play ducks and drakes with a good deal of conventional economic wisdom. Thus when price indices rise, it has long been established procedure to afflict the private sector with higher taxes and credit restraints in an attempt to force prices back into a stable pattern. But stable prices even if they could be realized in the face of rising taxation and a sizable shift function, could actually be a sign of deflation. The mind boggles at the mass of scholarship that would have to be reworked if it can indeed be demonstrated that the tax shift function does indeed take on substantial values.

Before sampling statistical evidence on the point, let us there fore turn to an authoritative work on public finance, Richard A. Musgrave's *The Theory of Public Finance*, New York, 1959, to see what specialized opinion in this field would lead us to expect.

Table 1

Tax Increase (Quantum)	Resulting Price Increase (Quantum)	Tax Increase due to Counter-Shift
1.0	.6	.12
.12	.072	.0144
.0144	.0086	
	.68	

Of the phenomenon of "shifting" in general Musgrave (p. 231) has this to say: "Perhaps a more useful concept of shifting may be secured by measuring the difference between actual change in distribution (or effective incidence) and the incidence of legislative intent. Shifting thus defined is an index of frustration, as it measures the failure of tax policy to achieve its distributional objective."

"Distributional" in the above refers to one of the three functions assigned to the budget by Musgrave – that of altering the distribution of income amongst the various sectors of the population. From our point of view "shifting" chalks up an even greater "frustration" in connection with the budget's stabilization function – the use of taxes to stabilize prices and the economy through the siphoning off of excess demand.

Let us review Musgrave's remarks on "shifting" as it applies to specific classes of taxes.

Corporation Income Tax

To rule out corporation profit tax shifting into price, academic reasoning draws upon a very formal train of argument that is summed up by Musgrave (p. 277) as follows: "In order to maximize profits, the individual firm determines price and output to equate marginal revenue and marginal cost. A tax on profits does not change the position of the marginal revenue and cost schedule: hence, it does not change the position of optimum price and output.… The marginal firm incurs no profits of any kind. Superior firms, whose cost of production is lower than that of marginal firms, do obtain efficiency earnings, but these are in the nature of differential rents, and hence, costs to the firms. Even if the efficiency earnings were taxed as profits, no change in supply would result. Being differential rents such earnings are determined by, and are not determinants of, cost or prices at the margin."

Other economists, however, have long questioned the validity of these too facile proofs (p. 278): "D.W. Robertson and others have suggested that the profits tax may be shifted because it does not allow for such (normal profits).[8] This group has argued that the Marshallian concept of normal price, defined as the price required to keep output unchanged, allows for normal profits, including a return to capital as well as to management. These returns, it is claimed, are no rents. They are not determined by price but are cost payments to factors, the supply of which is more or less elastic.

"Consider first the normal return to capital.… If necessary returns, such as rewards for waiting, the surrender of liquidity, or risk, are reduced by the tax, the supply of capital and risk-taking will be curtailed.… Such adjustments may come about in the long run and must be distinguished from the proposition that profits are reduced in the short run.

"in the short run, the plant is given, and there is no normal return to fixed capital. A return to capital must be paid only with regard to working capital. Thus the tax affects cost in the short run, if no allowance is made for a normal return to working capital. Such is the case when short-run capital is in equity form, since imputed interest may not be deducted. Depending on the industry in question and on the financial structure of the firm, the imputed return to working capital may be a factor of some importance.

"Another possible component of normal profits is wages or management. Since the demanders and suppliers of such services are frequently the same people, we deal with a highly administered price. Returns to management, though wages by nature, are not easily distinguished from profits…a tax thereon may be absorbed by other cost or profit components."

It is hardly necessary to enlarge on the latter passage. As a result of the increasing impact of taxes on profits and higher-bracket salaries, management has long since evolved advanced techniques for using expense accounts, pensions, and stock options to place a portion of profits beyond the long reach of the tax collector.

The crucial point, however, is made by Musgrave as follows (p. 281): "The proposition that a tax on the seller is more likely to be shifted in a seller's market than in a buyer's market is usually interpreted in terms of various elasticities of supply and demand.… However, the argument may be restated in terms of restraint in price policy. Suppose that price is set so as to secure a limited profit net of tax. An increase in the rate of the profit tax in the boom will be passed on in full, since there exists an ample margin of unused profits."

Under the administered price system it is the practice of large corporations to set aside substantial internal savings not only to meet contingencies but to ensure the smooth course of development and the financial independence of their firms. Should corporation profit taxes encroach upon such reserves, there would be no dearth of reasoning to justify price boosts to safeguard such savings.

After examining the problem of the tax shift in a setting of powerful labour unions bargaining with no less powerful corporations, Musgrave reaches this conclusion (p. 285): "The preceding considerations go far in qualifying the conventional conclusion that the corporation tax cannot lead to price adjustments in the short run.… On balance the theoretical argument lends more support to the moderate conclusions that short short-run adjustments in price (1) play a significant role, and (2) that a part of the tax is passed on, than it lends to the extreme position that no such adjustments occur."

Musgrave adds in a footnote: "Thinking along these lines I have assumed in other connections that approximately one third of the tax is shifted. This, to be sure, is rather arbitrary, but less extreme than the usual hypothesis that the entire tax falls on profits."

It was in 1948 that Musgrave made this estimate. With our economy becoming far more tax-saturated since then, a considerably higher estimate would seem warranted today.

In 1966 the corporation income tax in the United States amounted to $32.1 billion of a total tax revenue for all levels of government of $160.8 billion – approximately 20% of the whole.

Sales Tax

The case of sales and excise taxes – whether levied *ad valorem* or per physical unit – hardly calls for extensive comment. These taxes are *intended* to be tacked onto price. Whether in practice the producer can manage this depends, of course, upon the elasticities of the market. With this qualification we can safely reckon with a 100% shift onto price for sales and excise taxes.

In 1966 in the United States taxes on sales and gross receipts accounted for more than 21% of the tax revenues of all levels of government.

Personal Income Tax

Musgrave ventures no estimate of the shift phenomenon as it relates to personal income taxes. However, in our society the attention of the consumer is systematically directed towards his disposable income – the revenue left him after taxes that he is free to spend as he wishes. For it is primarily as spenders that the members of our culture are most elaborately conditioned to realize themselves. The impact of advertising plots their frustrations. No matter how vital, the services provided by the public sector have none of the seductive sheen that advertising often lends to the most worthless of commercial baubles. This goes far towards associating psychological satisfaction with disposable income, and thus has an important bearing on the shift function as it relates to personal income tax.

Thus it has long been trade union practice to think and bargain in terms of take-home pay. In their negotiations unions even try anticipating the future inroads of tax and social insurance deductions by winning a schedule of increases spreading over several years. And since tax and price increases cannot be foretold with accuracy, the only safeguard against guessing low is guessing high. A conservative estimate of the shift function for personal income tax onto price o would be 50% within one year of any tax increase being introduced. In the United States during 1966 individual income tax accounted for more than 37% of taxes collected by all levels of government.

From the foregoing consideration of the main tax categories, we can safely say that in our dual economy the aggregate shift function takes on very substantial values – of a magnitude somewhere between 50% and 100%.

William Krehm

To be continued in the next issue.

End Notes

1. Walker, Franklin V. (1965). *Growth, Employment and the Price Level.* Prentice-Hall.

2. The Statistical Abstract of the United States (1968) gives the following break-down of revenue for all levels of government in 1966: Taxes $160.8 billion: Insurance Trust Revenue $30.6 billion: Charges and miscellaneous general revenue $27.6 billion: Liquor store revenue $1.6 billion: Utility revenue $5.1 billion. We may take the tax and insurance trust revenue amounting together to $191.7 billion as the revenue for the unpriced public sector, and the other items totaling $34.3 billion as the income of the priced public sector.

3. For the sake of simplicity we are assuming for the longer term the identity of value and price.

4. Keynes, J.M. (1936). *The General Theory of Employment, Interest, and Money,* p. 223. New York.

5. A notable exception is the penetrating essay of Shigeto Tsuro that appeared almost two decades later: Keynes vs. Marx: the Methodology of Aggregates, in *Post-Keynesian Economics,* edited by K. Kurihara, London, 1955.

6. For simplicity's sake we completely disregard the distinction between value and price, except insofar as price is the monetary expression of value – a procedure followed by Marx provisionally in the first volume of *Capital.*

7. To avoid complication we are, of course, ignoring any deficit run up by the *priced* public sector.

8. That is, profits that are really elements of cost rather than genuine profits.