



## Episode 1,051: Want to Be Poorer? Defy These Economic Laws

Guest: Hunter Lewis

**WOODS:** You sure do pump out a lot of stuff on economics. Very good. So the first half of this volume is *Economics in Three Lessons* with a tip of the hat to Henry Hazlitt. Obviously, that's meant to be a bit provocative for those of us who were raised on Henry Hazlitt's book. Why three lessons?

**LEWIS:** Well, it's more than a tip of the hat. It's absolutely following in Henry Hazlitt's footsteps. The first lesson in my book is a recapitulation of his book, *Economics in One Lesson*. But then I just added two more sections, one about prices and one about crony capitalism, because I think it's so important that in addition to getting that core message of Hazlitt's about sustainability and how you've got to think through the long term and not just for one group but all groups and so on, that in addition one realizes how critical prices are to the function of the economy and how destructive crony capitalism is.

**WOODS:** All right, let's not assume, as I might be tempted to, that everybody's already read Henry Hazlitt. Not everybody has. So what actually is the primary message of his book? Apart from all the policies that he talks about the merits or demerits of, what's the core principle he's trying to convey?

**LEWIS:** Well, I think the core principle is simply that we have to think about the long run, not just the short run. We have to think about the effect of policies on all groups, not just one group. And it's interesting, the word sustainability was really not so current in his day, just as crony capitalism wasn't either. It was invented later. And yet he really produced this sustainability concept, which is largely ignored by Keynesians, who tout it in the environmental area continually. So the same people who are talking about sustainability in the environment ignore it in economics.

**WOODS:** I found that interesting, your use of the use term sustainability in this book, because sustainability of course as we know is typically used in ways that are meant to disparage the views that you and I hold, that if you want sustainability, then you need all kinds of top-down controls. So how do you think about that concept?

**LEWIS:** Well, absolutely. First of all, sustainability is a very, very old idea. I mean, Epicurus really expressed it beautifully, that we have to think about the long-term consequences of everything we do. And the idea that somehow we'll achieve that better with more government control is of course completely fallacious, because what government normally gives us is unintended consequences. It's people acting on their

own behalf, working in a market environment, competing and cooperating. They're much less likely to create unintended consequences than some government official sitting in Washington deciding for everybody.

**WOODS:** Let's go over to lesson number two and talk about the price system, which you've written about before. I actually think in my own experience, learning about the way the price system worked was actually the first step toward making me a libertarian, because when I realized what just the free-flow of prices made possible in an uncoordinated way in the sense that there's no dictator in charge made me extrapolate from that to think, wow, if prices can bring about all these miracles and they're not imposed by anybody, they're just created by the spontaneous interactions of individuals, then maybe just the spontaneous interactions of individuals are sufficient for society. So that to me was a central, central insight.

So if you were to talk to, let's say, a typical young person who supports Bernie Sanders who's never thought about the price system before, never thought about how amazing it is that we can coordinate all the things that we coordinate without coercion, how would you give a *precis* about this to them?

**LEWIS:** Well, I think it's helpful to think of it as a free price system. Everybody talks about a free market system, but I think that confuses people. If we simply say we're trying to have free prices so that people can cooperate and compete together without interference, that is I think more communicable to people. I think they understand it better. They get it. *Oh, yes, we don't really want price controls. We do want the freedom in the economy to set prices and for people to do that on their own.* So it's very important to understand this concept.

And meanwhile, I think also young people, when they begin to understand that the tragedy of the middle class being destroyed today and the poor doing so badly and doing worse and worse, really, and the source of the problem is government price controlling in one way or another — price manipulating, price controlling, price fixing. And people just don't understand how all this works. They don't see it. I mean, take the medical system, for example. Almost nobody knows that medical prices, which are invisible to the public in general, are mostly set by a committee of the American Medical Association, which then gives those prices to the Medicare system, which is run by private insurance companies. Those private insurance companies then apply those prices to their own system. And so those prices really go throughout the economy and in effect we have controlled and manipulated medical prices, and that in turn leads to higher and higher prices, of course. But people just don't see this. It's invisible to them.

**WOODS:** You have a section in that part of your book called "Who Are the Bosses in a Free Price System?" And again, I think this would run completely counter to what even just the average person with no axe to grind thinks.

**LEWIS:** That's right. I remember I was at a dinner once, and the professor to my right and the professor to my left and of course they were both Keynesians, or really more socialists, certainly progressives. And they were saying capitalism is the system that favors the bosses, and socialism is the system that favors the workers. And I said, what about the consumers? Where do they fit in to your picture? Because actually,

capitalism or a free price system is run by the consumers, and the consumers includes all workers and others as well.

**WOODS:** There is a quotation later in the book that you take from Howard Zinn talking about profits, because of course we can calculate profits and losses thanks to having a price system. That helps us to navigate all the many, many billions of possibilities in terms of things we could produce and how we could produce them and what inputs and methods and locations and all that. Profits are made possible, the calculation of profits are made possible by the price system. And Zinn says that profits have distorted our economy completely because it just leads people to make whatever things tend to maximize profits. I think he said something like that. I mean, I just — my breath is taken away by what a stupid remark that is, and I'm curious about your answer to that.

**LEWIS:** Well, profits are an absolutely key thing to the free price system, because they provide the incentive for people to kind of drive costs down and therefore prices down. Why is it that we can produce certain things that are not so government controlled, like computers and electronics and so on, more and more cheaply? It's because there is the incentive to earn a profit by finding ways to do it more cheaply and to make a better product at the same time. So profits are absolutely essential, and the signals the profits send are again sent by the consumers. The consumers are the bosses, and they're telling producers what they want, when they want it. And so the whole system would collapse without the profits. It's just part of the pricing.

**WOODS:** I've heard people say, I don't want to have an economy based on profits. And I don't remember who it was that put it this way, but a kind of snarky response is: would you rather have an economy based on losses? Which I realize is actually not that snarky, because if you don't have an economy based on profits, that is exactly what you have, by definition. You have an economy based on losses. You actually have a section in here called "The Essential Role of Loss and Bankruptcy," which I'd like you to comment on, because that again helps us to show how the price system makes sure that what's being produced is what people want and it's in the right quantities and it's being as produced as inexpensively as possible so as to be least wasteful of our resources. So what is the essential role of loss?

**LEWIS:** Well, I think it's more accurate really to call the profit system the loss and bankruptcy system, because I actually think that sort of the stick there is more powerful than the carrot in terms of modifying human behavior and getting the results you want. I mean, most new businesses fail, and even very profitable businesses, eventually their profits diminish, decline, and disappear. So actually, profits are only earned when there is a problem to be solved, and entrepreneurs go out and solve that problem and they have an opportunity by doing so to earn a very high profit. But it doesn't last very long, and eventually other people come in and compete and do the same thing and the profit disappears.

**WOODS:** I want to talk about the third plank of your three lessons, which is crony capitalism. We know that this exists, but I think a lot of people think it's a minor factor. Maybe — I can't remember — it was the Obama administration and green energy, but this seemed to be such a small-scale thing that it was hardly worth

worrying about. So how would you counter that? Why is crony capitalism actually more serious than people think? I think they're not defining it broadly enough, is my opinion.

**LEWIS:** Well, first of all, most of it is largely invisible like the price manipulations that are so closely connected to it. For example, you mentioned the Obama green energy program, but you might remember there was that fiscal cliff bill, in which Obama finally succeeded in raising taxes on the rich, so to speak. And that sounded fine to me, but on the other hand, in that same bill he had giveaways to his corporate donors, which in aggregate were larger than any additional taxes he was going to get from the rich. So that bill did not increase revenue of the government, even in theory. It was just full of these giveaways to his corporate donors.

And of course, the green energy program is yet another example where, if you analyze who got those green energy grants and loans and so on, more than two-thirds of them were people who were major donors to the Obama administration. And it's not just the Obama administration, of course. It was the Bush administration; it's the Trump administration. I mean, this goes on and on.

But the whole thing works as a system because the government gives these price manipulations to special interests, and the special interests in turn give the government campaign contributions and other support, and it's all designed to help the special interests or help the government. It's not designed to help consumers, the economy, the voters.

**WOODS:** All right, now I want to get to probably not all 100 economic laws but some of the more fun and juicy ones, which we'll do after we thank our sponsor.

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All right, you've got 100 economic laws in here. Now, you put this together. It's really two books in one. Is there a reason you did it that way?

**LEWIS:** Yes, the first half, which is a book itself, the *Economics in Three Lessons*, was really designed to be an introduction to economics for young people. This whole book is really intended for young people. And then the second part, the *100 Economic Laws*, is intended, although very short, to be much more comprehensive. So the first part is rather easygoing and the second part takes a little more work.

**WOODS:** Well, I actually really like the second part because I think it's really helpful summaries of a lot of important insights. Now, when we look at your 100 laws, we note that the initial however many of them are actually focused primarily on economic method and making sure that our economic method is right, because if the method is wrong, then the conclusions we're drawing are precarious at best. So what would be some fundamental pieces of advice you would give when it comes to studying economics correctly?

**LEWIS:** Well, the most important advice I would give would be to avoid economic courses in colleges. And again, one of my motivations in doing this was to provide an alternative perspective for young people. Economics is one of the most popular

majors, because young people go to college and they think, well, I won't necessarily be a business major but I don't want to be a history major that'll be hard to get a job from, so therefore I'll take economics. That sounds practical and at the same time intellectually challenging.

So so many young people sign up for these courses, and then of course, as you know, much of what's taught is irrelevant. It's Alfred Marshall supply and demand curves that don't have any reality, or much of it, if not irrelevant, is simply wrong. For example, in every economics textbook you have today, you see this idea that new money is created and goes into the economy, it comes in evenly, it affects all prices if it does everywhere. And that was refuted by David Hume in the 18th century, and yet today it's in the economic textbooks.

**WOODS:** Your section on laws pertaining to the division of labor will be familiar to a lot of listeners of the show and students of Austrian economics and really frankly students of any good economics at all. And so I actually don't want to dwell on them, though I just want to convey to the audience that you will find laws pertaining to voluntary exchange, private ownership, diminishing returns, comparative advantage. These sorts of things that we're familiar with definitely have their place in here.

What I want to focus on is the emphasis on other points that we might know but might not classify as a law. So I want to go on ahead to the laws of prices, even though we've already been talking about price, just because there are so many insights in here. Yeah, let's see. Like for example, the one on demand. And you say if we want to increase prices — for example, wages — the most effective way to do so is not to mandate it but to increase demand. What do you mean by that?

**LEWIS:** Well, absolutely. I mean, there are so many fallacies. Take price controls as another example of this, where people think that in order to get prices down, you simply mandate that prices will go down, whereas in fact what you need to do is increase supply. And a good example of this is in the medical system again today. Right now, government laws and regulations prevent nurses from doing most of the things they could do, even though they're almost as well trained as doctors themselves, and yet they're not allowed to do it. There are four-year trained naturopathic doctors. They're not allowed to do all the things they could do. So the supply — chiropractors are not allowed to do all the things they could do. So the supply of medical services could be greatly increased if the government would allow it. And why doesn't the government allow it? Because again, they are working together with the American Medical Association to prevent that competition for medical doctors or MDs. So again, if you want lower prices, you need more supply.

**WOODS:** The laws of profits is a section that I'm particularly interested in. The very first one you give is if you want lower prices for ordinary people, do not try to abolish profits. The existence of profits tends to bring prices down. So what's the mechanism exactly by which profits tend to bring about lower prices?

**LEWIS:** Well, actually, what usually happens is that if there's a problem, some entrepreneur sees a profit opportunity to solve the problem. And then as they solve the problem, they're making a lot of money, and so competition comes in. Other people want to do the same thing. And as they do, supply increases, increases, and so

on, and prices fall. And of course, the other reason that prices fall is that, as you solve the problem, you've become more efficient and more productive, and that enables prices to fall as well.

**WOODS:** Another one of these is, "If you want ordinary people to control the economic system, then profits are essential for that purpose as well." Now, we've already gotten to that a bit in the sense that, if you want to earn profits, you darn well better produce what people want. And so in a way, those people are, if not literally in charge, well, their opinions are very, very much at the forefront of what producers are interested in obeying. And of course this runs counter to the idea that profits somehow again put big business in charge, but big business has to cater to you if it's going to succeed.

Now, the corollary to that, though, from their point of view might be: but big business can manipulate our desires. It can make us want the latest widget or the latest gadget, and therefore we are still very much in thrall to them. But I think the response to that is, if it were really that easy to just manipulate our desires, there'd be no need to do market research on products. Who knows how many billions of dollars are spent on that? You wouldn't need to do any research. Just produce the product anyway and bamboozle everybody into buying it. So I think that criticism fails completely. Is that the way you see it?

**LEWIS:** Yes, and in addition, if it were so easy to manipulate the consumer and to bamboozle him or her, then why do all these big businesses go to the government and try to get protection from competition? Why are they so involved in trying to get special deals from the government for protection?

**WOODS:** Yeah, they shouldn't need it, first of all. Yeah, it shouldn't be necessary. All they have to do is run a commercial and we're going to go out like zombies and buy whatever it is. Now I'm interested in this one: patience —

**LEWIS:** I just want to —

**WOODS:** Oh, yeah, go ahead.

**LEWIS:** I just want to add that the whole purpose of the crony capitalist system is to evade the discipline of the consumer, is to evade consumer control.

**WOODS:** Yeah, and the state is all too happy to oblige. Now, you have a principle here. You say, "Patience" — and in parentheses — "If you are unwilling to think very long term, even beyond your lifespan, you will not be able to realize the full fruits of the profit system." That's a very tantalizing principle. Can you elaborate on it?

**LEWIS:** Yes, and of course it's closely related to the incredible power of compound interest. One of the most fundamental things that students in economics who are starting out ought to be taught is how incredibly powerful that is. You earn 10% a year — let's say you grow 10% a year. All right, well, it takes you seven years to double your sales. And if you begin with a small base, that doesn't add up to much. But then if you do it again and again and again, pretty soon you get to phenomenal numbers. This is

why in another book of mine I pointed out that if you had just started with \$10 a few thousand years ago and compounded at a relatively modest rate like 3%, let's say, you would have 10 times larger a global GDP today, which shows that we've had almost no growth for most of human history. So once this principle of compounding was discovered and practiced beginning in the 18th century, then that's enabled the economy to grow and people to escape poverty and so on.

**WOODS:** I want to move ahead to the laws of economic quality and inequality, which is a topic that I think is being discussed a lot more today than it was in Hazlitt's day. And in particular here — in fact, I really actually would like to spend a little time with this. You start off, the very first one of these is, "If our goal is economic equality, we must recognize that not all forms of economic equality are logically compatible." Ah, so there's a problem at the very heart of the idea. So what problem are you trying to identify here?

**LEWIS:** Well, we all pretty much agree that equality of opportunity is a good idea. We want everybody to start the race at the same point and so on. And that's not easy, because obviously if you have wealthy parents you get an advantage and so on. But it's not realized that equality of opportunity and equality of outcome are logically incompatible. You can't have both at the same time. So obviously if you mandate that everybody has the same result, then I don't have an opportunity to do anything different or be outstanding or accomplish anything.

**WOODS:** Then you talk about the problem of envy, and you say, "If our goal is a better economic outcome, envy will make it harder to achieve." Now, is that because if we're envious, we're going to — envy yields very bad economic policies that will undermine capital accumulation, which undermines prosperity? Or do you have something else in mind?

**LEWIS:** No, that's sort of the basic idea. I mean, again, we need entrepreneurs to solve economic problems, and if we're envious of their success, we're simply going to prevent them from succeeding in doing so.

**WOODS:** Now, what do you mean when you talk about the inequality of data? You say, "If we try to illuminate these matters with data, it takes a great deal of careful thought to ensure that it is not irrelevant or even misleading. With information as with production or investment, the most critical issue is quality not just quantity." So what problems are you identifying there in particular?

**LEWIS:** Well, I mean, for example, the government data on inequality is almost useless. It's not logical. It's badly put together. It's not accurate. Just to give you one example, the government does not include the refundable tax credits in the poverty calculations. I mean, that's just one example among many, many, many. Now, today the government's own statistics say that since 1980 through 2014, the top 1% of earners have increased their earnings by 200% while the bottom 50% have actually had a decline. So even the government data, which is very bad, shows that it's not working for most people.

**WOODS:** There are so many of things and I could pick any of them, but let's go on down, all the way down, even below — you've got sections on economic calculation, on

government, on money. How about interest rates, given that most people hear interest rates and they just think, *Boring* – which is a shame, because interest rates in some ways are, if not the whole thing, a pretty darn important ingredient in a smoothly functioning economy. So what can you tell us there?

**LEWIS:** Well, the two most important prices in the economy are the prices of money and interest rates, which is the price of credit. Those are just incredibly important prices. They affect everything. And the role of the Federal Reserve and other central banks is incredibly important within the crony capitalist system. The Fed in the U.S. is in effect financing the entire crony capitalist system. And I just saw Janet Yellen just recently testified and she said what a success their program had been since the crash. And her own staff have published articles saying that they estimated that everything the Fed did after the crash added one fourth of 1% per year to the growth rate for the four years following, and yet she's testifying to Congress and saying this is a great success. And of course, I don't even believe the one fourth of 1%. I think it actually held back the recovery.

**WOODS:** Let me ask you a question about your own background, if I may. You founded or your cofounded Cambridge Associates?

**LEWIS:** Yes.

**WOODS:** Okay. And that's a global investment firm. In what way did the kind of insights that you have in this book come to bear on your activities there? Like in other words, were you observing some of this craziness and economic absurdity from your perch there, or are these entirely separate parts of your life?

**LEWIS:** Well, they're certainly not separate at all. Cambridge Associates is an investment firm, and I founded it with another partner in the mid 1970s, and so I've seen a lot of ups and downs in the markets. I've seen a lot of the Federal Reserve over that time. I've closely observed it. But I must say that the period since about 1996 has been fundamentally different. Ronald Reagan appointed Alan Greenspan as chairman of the Fed, and I think that was probably his worst single decision that he made. And the Greenspan Fed started the current period of boom and busts, and then of course Bernanke made it far, far worse, and then Yellen has carried it on. So I think we're in a completely different period. Since '96, it's just been bubble and bust, bubble and bust. And of course I believe we're in another one.

**WOODS:** All right, let's say something quickly about the banking system, because you say as law number 86, the way banking is currently set up guarantees its instability. Now, is that because – well, actually, I'll let you answer the question. Why is that the case?

**LEWIS:** Well, the way it's the case right now of course is that, if everybody decided to go to the bank and demand their money back, the bank is supposed to provide it. They're legally obligated to do so. But they can't do it. And of course that's a function of fractional reserve banking, which was a great mistake and we almost avoided it. There were court cases back in the 19th century both in England and in the U.S. that were very close things, but we got fractional reserve banking as a result. Any bank is kind of technically bankrupt any day in the sense that any bank could fail if everybody



demanded their money back immediately. So that's one of the most fundamental problems in the economy, although it's not the only one.

**WOODS:** But we have deposit insurance, and given that we're not likely to have a whole bunch of banks collapsing at once, can't the Fed just come in and resolve this and everybody's fine?

**LEWIS:** Well, deposit insurance makes people feel better, but what would actually happen if we had a repetition of 1932 when all the banks were failing and closing and the government had to make it good? Well, the government can only do that by printing a lot more money, and so a lot more money would flow into the economy, and then the value of the money that you got back from the bank wouldn't be worth as much. So it's kind of a fool's security.

**WOODS:** What would be your preferred system? What would banking look like under the Hunter Lewis regime?

**LEWIS:** Well, I'd get rid of the fractional reserve banking. I wouldn't allow that. And I think that's the most important thing, but then in addition, ideally the government wouldn't be in control of money. Money would just be like any other product. There would be private providers of that product. The good ones would survive; the bad ones would not. And I think that would just transform the whole economic system, and we'd have much more stability.

**WOODS:** So what is preventing that kind of a reform? I mean, okay, vested interests. I'd like to know what are the vested interests in the current system? And secondly, scare tactics, right, because the system that you're advocating probably caused the Great Depression or something.

**LEWIS:** Well, first of all, the present system enables the government to keep spending well beyond its means, so the government has the great incentive to keep it going. And special interests have a great incentive to work with the government. Corporations, for example, have greatly benefited in their bottom lines from the deficit spending over the last ten years when it's been especially extremely bad. Most of that deficit spending has just flowed into corporate profits. So all the big players have an incentive to keep the present system going so long as it doesn't completely collapse.

**WOODS:** All right, well, again, of course we have 100 of these laws, so I want to urge people, especially as you say younger folks, to just check out the book, because you're going to get in a short space digestible an awful lot of economic insight packed into this. And then at your leisure, you can read a whole lot of other books that elaborate on all these individual points. Now, is there any particular theme, though, that we didn't hit on that you feel like is a major piece of the puzzle and you would be hopping mad after this call if we didn't get to it?

**LEWIS:** Not at all.

**WOODS:** Oh, that's good. That's a compliment to me, then [laughing]. I'll take that, okay. All right, well, the book once again is *Economics in Three Lessons and 100 Economics Laws: Two Works in One Volume*. We're going to link to it at [TomWoods.com/1051](http://TomWoods.com/1051). And go check that out. Hunter Lewis, thanks so much.

**LEWIS:** Thank you.