



**EPSTEIN:** I'm glad that you said yes to allowing me to discuss a little coda, as I put it, a little epilogue in my mother's story.

**WOODS:** Yes, so we're going to do that. We're definitely going to do that. [laughing] I'm laughing because immediately before we started recording, we were talking about how to manage our time because you have so much to say, you made a remark about a Gene Epstein Month instead of a Gene Epstein Week.

**EPSTEIN:** I mean that in all seriousness, Tom. There could be a lot of fans out there who think it would be a good idea.

**WOODS:** Yeah, I mean, maybe 2020 is the Year of Epstein [laughing]. Who knows?

**EPSTEIN:** Well, I signed up for the week, Tom, and I'm a man of my word.

**WOODS:** Yeah, that's right; that's right. All right, so let's finish up the story with your mother; then we're talking about your intellectual hobbyhorses.

**EPSTEIN:** Sure, sure. Well, this is especially for Bob Murphy, our friend Bob. Bob just admires me, so envies me so, because I had a mom who was followed around by the FBI. And I forgot to mention that in our previous interviews between you and me, Tom. My mom had an FBI file, which about 15 years ago, I finally got around to requisitioning it by invoking the Freedom of Information Act, and indeed, it seemed as though a lot of former communists had FBI files. I had an Uncle Abe who did have a job as a scientific consultant. Maybe that was the reason. I just wonder why my mom had an FBI file, especially why they kept following her around even years after she left the party. And of course, Bob Murphy maybe could do a deep dive into the file and answer the question: was it really worth taxpayers' money to finance an FBI continual probe into my mother's activities? That's a separate question.

But more to the point for me is that the file was rather boring, with part of me, I pitied the FBI agents who were given this assignment; with the other part of me, I realized, what the heck, it was probably a sinecure because it was really just, you know, she went out to buy a bottle of milk and this is what they're recording about her suspicious activities.

But the only really interesting part of the file was a constant memo update on an open question, which was: should we approach this woman — they called her Mrs. Keanan. She was then married to a socialist named Keanan — should we ask her to be a double agent, to infiltrate and become an informer? That was the question, as indeed, frequently I guess they did approach people who were ripe prospects for this. And they kept writing the same thing about why they decided against it, and they decided against it because, "she was a deeply immoral woman." A deeply immoral woman.

And I, having been a scholar on my mother's papers, knew where that phrase came from. It came from the final judgment of the courts as to why they were not giving my mother custody of the kids. The passage read, paraphrased approximately, in the judge's ruling: while it is normal to give a woman the right to the children, even when she has been convicted of adultery, this is a deeply immoral woman. That was their conclusion: a deeply immoral women. And of course, I, knowing the background of that phrase in the court's judgment, knew what they really meant. This is a woman who was a member of the Communist Party and slept with black guys. That was why she was a deeply immoral woman.

So I just want that filed, that pointed little moment about the government's judgment about my mother. Don't you hate the state? I don't think my mother really was deeply immoral. She was a complex, somewhat confused woman. She made a few mistakes, but I have to disagree with the FBI's judgment. That's all I wanted to say about that, Tom.

**WOODS:** Wow. Okay, well, now everything else we say is not going to be nearly as juicy as that.

**EPSTEIN:** [laughing] All downhill from here, Tom.

**WOODS:** All right, all right — go ahead —

**EPSTEIN:** No, go ahead. My intellectual hobbyhorses.

**WOODS:** Yeah, I'm just going to pick them in whatever order, okay —

**EPSTEIN:** Yeah, sure.

**WOODS:** And I don't even necessarily — all I have is the list. I don't necessarily know what all they amount to. Like for example, I know and like Alex Tabarrok, but I don't know what the hobbyhorse related to entrepreneurship and startups is.

**EPSTEIN:** No, I know and like Alex, as well. And it's only this: that Alex did research on the ebb and flow of entrepreneurship in the US economy, and his research was strictly based upon the number of startups, the ebb and flow of startup businesses. And so my only hobbyhorse there is that Alex was committing the cardinal error of associating entrepreneurship solely with startups, not realizing that companies on all levels must exercise entrepreneurship, and then very possibly, and I think even arguably, there has been a real wave of entrepreneurship from very established companies. There was a scholar named Amar Bhidé, who is kind of a free market fellow traveler, who did a good analysis of the different kinds of entrepreneurship you expect from deep-pocketed companies versus startups. But again, I took Alex to task a little bit for that. I believe it was a moment of myopia. I do think that what is expected of CEOs — and their assistants and their minions/ I do think, of course, entrepreneurship is often a group effort — is to be entrepreneurial about the company, to take entrepreneurial initiatives. So that's all.

And indeed, actually, a little background to this is that you may have noticed on Facebook, as you were involved on the Tom Woods Elite Facebook, Peter Klein put me in my place when I said maybe Israel Kirzner, who has been associated with entrepreneurship, had more to say than Peter was giving him credit for. Peter said no, I'm wrong. But I will say that when Kirzner said that entrepreneurship is taking place on the level of the executives who run a corporation, that that's sort of like his classic idea of the entrepreneur who is not necessarily a capitalist, because they're just paid a high salary and they're given incentives in terms of stock options. But I think it's important to understand that the entrepreneurial function is very important for CEOs and the people who work for them, report directly to them. And that's just my only hang-up there, and I think it's an important point to emphasize, especially when someone as enlightened as Alex Tabarrok can make that mistake.

**WOODS:** All right, I want to move on to the next one. Again, "next one," not in any order.

**EPSTEIN:** Okay.

**WOODS:** Not that the people listening know what the order is. I'm looking at your list.

**EPSTEIN:** Sure.

**WOODS:** The one about — I like how you call it "Epstein's law," maybe "Epstein's tendency"? Boy, that's a sad, pale thing compared to a law. But anyway:

"Productivity gains in a particular industry and sector mainly benefit those outside that sector. Gains are mainly not captured within that sector."

Yeah, that reminds me of the analysis of George Reisman, who agrees with you.

**EPSTEIN:** Yeah.

**WOODS:** Because he would say, he gives the example of butlers. Now, look, there really aren't that many technological advances that are going to affect butlers, because all the labor-saving devices that — well, forget labor-saving devices. I mean, basically, a butler brings things to you on a tray. Well, now that tray's been invented, there really aren't going to be any big productivity advances. But does that mean that the wages of the butler will never go up?

**EPSTEIN:** Yeah.

**WOODS:** No, because what will happen is there will be productivity increases elsewhere in the economy. Those productivity increases will increase the demand for labor and wages in those sectors, and that competition will tend to pull the butler out of butlerdom if you don't keep his wage high enough competitive with that to keep him in the butler spot. But meanwhile, productivity has not increased in the world of butlerdom. So is that your analysis, or do you have a different way of looking at that?

**EPSTEIN:** Well, one way of putting it — and I know and like and admire George, and I always say that about 70% of his book, *Capitalism*, that massive tome, is truly wonderful stuff. And by the way, I kept asking Joe Salerno to give me a clear idea of where the other 30% went really wrong in George's book, and Joe just let slip that he believed Israel Kirzner had done a review of George's book, and lo and behold — and I told Joe afterwards — I discovered this very lengthy, very appreciative review by Israel Kirzner, in which Kirzner did indeed very clearly take George to task. I mention that only because I think it's of some interest.

But interesting that George chose butlers. As you probably know, the favorite example is barbers, people who cut at least men's hair. But indeed, that's all valid. I guess the only way I would want to put it in the other direction, though, Tom, and just say briefly, the two main productivity stories of the last, say, 150 years, certainly the last 100 years is certainly, just for starters, the productivity revolution on the farm. But what did that do? Did that really enrich farmworkers? No, basically it decimated the ranks of the farmworkers, and they went into other industries. So food prices collapsed. Food prices basically collapsed, because there was such an abundance of food coming out of an ever-shrinking labor force. But it didn't benefit that sector specifically at all. Of course, it's another matter that rich farmers are supported by the government, but the family farm basically folded —

**WOODS:** Right, okay, but isn't that a matter of, in that case it's that, let's say productivity on the farm increased by 50 times. The issue there was nobody wants 50 times the food.

**EPSTEIN:** That's right.

**WOODS:** But suppose there's an industry where there's an explosion of productivity, and we do want 50 times the output. Then can you deal with that case?

**EPSTEIN:** Okay, I want to get to — I just want to say that, certainly, that's the main story of our time. And then of course the second main story of our time, Tom, where there's actually an exception, would be manufacturing. Obviously, the productivity revolution in the factory brought a very similar outcome, although, of course, now we deal with, if there was an explosion of productivity in the auto sector specifically, then indeed, we can deal with 50 times more cars. That's basically what did happen. So that presumably speaks to your request for a good example in that regard.

But the point, then, is that it doesn't really benefit the people in that industry, because, unions aside, the auto industry of course is distorted by having been politicized for so many decades and having been unionized with politicized unions. But if we just abstract away from that for the moment, then what will happen is that, if there's a massive increase in a demand for this product, it may well be that the productivity gains are going to bring even more jobs into the industry, as you might want to indicate. But of course, what will happen

then is that more labor will stream into that industry. So there's no particular reason — and then, of course, as more labor streams into that industry, then that puts a dampener on the potential increase in wages in that industry. So there's no particular reason to say that the productivity revolution in the auto sector specifically, and certainly in the manufacturing sector specifically, brings unusual gains to that particular industry. That's my only point.

And you might recall, Tom, I remember you on the Contra Cruise when you were talking about your dad — we won't get into that — and the forklift, and you basically said that was just a sort of offhand story, which you never meant quite seriously. But for example, I do find most recently that people can name a few names, they're basically talking about the assumption that where the productivity — like the productivity gains from computers. So therefore, we're going to pay people in computers a whole lot of money, because that's where the productivity gains are, well, the only reason, the only *potential* reason why people in computers are getting paid a whole lot and still paid a whole lot, even though there's a huge expansion in demand for them and a lot of them are streaming into the industry, is that you have to have probably unusually high IQ to be a computer programmer. So that's a special case. I try to remind them that that's a special case. It's not generally true of productivity gains in most industries, so that, as you indicate, Tom, even where the productivity gain sparks a huge increase in demand for the product, so there's even an increase in the number of jobs available, what will happen normally in a free market is that workers will stream into the industry and the thing will level out.

So my point is only that — I guess Epstein's tendency is really all it is, that it tends — actually, it's almost a law. Almost any productivity gain will tend to be diffused throughout the economy. That's my only point.

**WOODS:** Yeah.

**EPSTEIN:** Hopefully you were persuaded.

**WOODS:** Yeah. Yeah, no, I am, I am.

**EPSTEIN:** And it's a frequent error people make, to believe that the productivity gain is just specific to that industry, not realizing about the flow of labor, not realizing about the huge expansion in the number of goods that can result, that very often decimates employment in the very industry where the productivity gains occur. That's all.

**WOODS:** Well, I wasn't actually trying to contradict you, by the way. I just wanted you to give examples of productivity gains where labor leaves the industry and productivity gains where labor is attracted to the industry, that the same phenomenon exists in both cases.

**EPSTEIN:** You were trying to help me out, Tom, and you did. Hopefully, we got the point across then. Thank you very much.

**WOODS:** Okay, yes.

**EPSTEIN:** Yeah.

**WOODS:** All right, so now, I don't know what this one could be about.

**EPSTEIN:** Yeah, what is it?

**WOODS:** Private institutions righting global wrongs.

**EPSTEIN:** Oh, okay, well, this is where it comes from, Tom. And it's really just a sort of humble and tentative question I'd put out to people. Let me put it in terms of a little story. I have a friend named Michael strong. He might have been on your show.

**WOODS:** Yes.

**EPSTEIN:** He's a very great guy, libertarian. And we have talked about the fact that we libertarians have got to say, look, when government gets involved in righting global rules, our government in particular, it will almost inevitably do more harm than good. So that if you

want to argue that, look, right now we are very upset about what's happening in Hong Kong, about what the Chinese government is doing to the demonstrators in Hong Kong is symbolic of the free market, of course originated with Milton Friedman who made it symbolic, and so it's very upsetting to observe, to be on the sidelines and see what's going on. Should we then empower the Trump government, or should we've empowered the Hillary Clinton government if she had won, to make war or to intervene on the behalf of Hong Kong? Well, look, our answer is that if you start giving our government some kind of blank check to get involved, then they'll often ignore real genocide like in Rwanda, and they'll usually make a mess of things. It's not going to work.

So then where are we left? Well, we're left is with a kind of a hollow feeling. And that's when my friend Michael Strong, who's a more aggressive visionary than I, said, well, look, I too, could imagine Oxfam or some kind of major nonprofit or even profit-making company responsible to its shareholders, responsible its donors, and they will say we do employ mercenaries. We do intervene. We invest. When Soros, by the way, George Soros was apparently pouring money, I know into several Eastern European countries, to combat the communists, that was fine.

So I'm only talking about that alternative vision, the alternative vision of free market initiatives to right certain wrongs in the world. Obviously it's an unsatisfactory approach, but government is only going to make matters worse. So that's the idea that I wanted to throw out, because I find and perhaps you find that there's a hollow feeling we all have when we're going to say, well, no, the US government's going to make a mess of things, but wouldn't you want to do something about what's happening to those in Hong Kong? Wouldn't you want to do something about the slaughter in Rwanda? That's my only hobbyhorse, and I wanted to throw that question out. And if there are visionaries listening to me, I would love to hear you talk about how that might work

**WOODS:** Okay, so now people have an assignment. This is something that needs to be worked on and explained, for sure. Let's try and do one that looks a little dry, and then we'll get to the two juicy ones that remain. So I think this one may touch on something that we covered on an earlier episode: labor share of output and depreciation. What's that about?

**EPSTEIN:** Well, it's interesting that I know that our friend Bob Murphy was able to correct Thomas Piketty because he forgot depreciation. But this dry one is fairly simple. If you look on the website of the Bureau of Labor Statistics, they will show that labor share of output or labor share of income, GDP – they call it output generally in the Bureau of Labor Statistics – has been precipitously declining, and it's only recently turned up a little bit. But if you draw a trend line, labor's percentage share of output, it's a nominal figure against a nominal figure of a measure of output. You will find that from 1947, where they have quarterly numbers beginning, to the present, labor share of output has been in a long-term decline, a fairly steep decline, according to those numbers, since the year 2000.

But then when you actually read their own discussion of the subject, they mention depreciation, but then they don't pursue it. So now, what's depreciation all about? Depreciation is otherwise called capital consumption, capital consumption allowances. And there's no way for an economy to progress unless an allowance is made for the consumption of capital. Speaking more abstractly, there's such a thing as gross domestic product and net domestic product. The standard textbooks will tell you that net domestic product is actually the more accurate measure, because the difference between net and gross is depreciation, capital consumption, the consumption of capital. In any economy from a Robinson Crusoe economy to a communal economy to a national global economy, unless you're making allowances for capital depreciation and replenishing your capital, then eventually we're all going to starve, because capital does depreciate.

So now, again, abstractly, if you were to put a line on the graph, gross domestic product, and then underneath it, net domestic product, and then take net domestic product as a

percentage of gross domestic product, you will find that in the 1950s and '60s, NDP, network domestic product, was about 94% of gross domestic product, and it's now about 84%. There's been a huge bite that depreciation has been taking out of gross output, and that's because investment, nonresidential fixed investment — I'm only talking about the standard numbers issued by the Bureau of Economic Analysis. The standard numbers are that businesses are investing more and more in software and equipment and less and less proportionately in structures. Structures depreciate very slowly; equipment and software depreciate very quickly.

So that if you then take net output, output after depreciation — because only after depreciation can you then allocate to profits, can you allocate to wages. Only after you do that, only after you've netted it out for depreciation will you then find what is labor's share, what is profit's share? And once you do that, once you make that obvious correction that any mainstream economist should be aware of, then you find that it's completely bogus that labor's share has been declining. And this is something that mainstream economists completely misgauge, because the Bureau of Labor Statistics will not stop issuing this number.

But there is an economist at the BEA who's written a paper on this, and I just finished an article in which I elaborate, because again, now at least I have the authority of a BEA economist who's saying that they're making an obvious mistake. They're not netting out depreciation. Obviously, as we know about trends, if gross and net were pretty much in line with each other, it wouldn't change the long-term trend. But as I've said, gross and net are not in line with each other. Net has really been not increasing at the rate that gross has been increasing. Depreciation is taking an increasing share out of it. And so that correction has to be made. And again, it's a mistake that I could name some names of people, and even somebody, an economist you recently interviewed who made that mistake, as well. So that's my only dry point about what's really going on with labor's share.

**WOODS:** All right, now, two more. We're going to try and go through them quickly.

**EPSTEIN:** Yeah.

**WOODS:** The first one: "Market failure versus institutional failure, public choice theory and bust." Yeah, what's this all about? I mean, I think I know.

**EPSTEIN:** Well, yeah, I think you know, too, but of course, it has broad ramifications. And it's only that I think that we ought to insist that, ubiquitously in the realm of economics, there is constant institutional failure. Institutions fail us all the time; it's just that market institutions fail us a lot better than any other institution you might imagine. But the point about saying that, and I mentioned Bastiat, because Bastiat actually fully anticipated what is called public choice theory.

And I thank Bob Murphy for explaining to you and explaining to all of us where that term comes from, public choice versus private choice versus private choice. There's private choice, and then public choice refers to government, and that if we then bring in government as the solution, the usual non sequitur is to say, well, this market has failed us; ergo, we've got to bring in government to solve the problem.

Then the public choice theorists say, as did Bastiat in his most elegant way, translated from the French: if people are dumb or if people are inept or if people act unjustly or foolishly, then by what logic can we assume that once they start running government, they're going to act less unjustly or less foolishly? So clearly, government is no solution to market failure unless we can somehow prove that government is going to do it a lot better than markets can. And once we point out that these are the same flawed people, and then we point out that they are flawed people who are operating without price signals, without a rudder, they are likely to muck it up.

But this gets into broad ramifications. Why, for example, in every debate I've had on capitalism versus socialism, I've insisted that socialism be at the top of the marquee? I've insisted that we compare socialism with capitalism, because capitalism is indeed filled with market failure. It's never going to go away, because human beings fail us all the time. So unless we compare capitalism's failures with socialism's failures, we're never going to get anywhere.

And so most recently, Intelligence Squared had a debate in which the resolution read, "Capitalism is a blessing." That was it. It was all about capitalism being a blessing or being a curse. The socialists who debated that on the other side, who happened to be the two socialists I myself debated Bhaskar Sunkara and Richard — why am I forgetting his last name?

**WOODS:** Wolff.

**EPSTEIN:** Richard Wolff. They had a field day just vaguely referring to how socialism can do better, capitalism is terrible, look at all its failures, and socialism can do better. But they were never required to get into the nitty-gritty of how socialism would do better. And then just the other day, I discovered there's yet another debate that's being posted with the same thing, that capitalism is messing up, and that was it. Capitalism is a big mess, and that was going to be the debate. And once again, you don't put socialism up there in terms of the alternative. How is socialism going to do it better? But that's never asked. You just put capitalism in the dock.

And now I want to impress you by quoting from memory one of Schumpeter's best lines, Joseph Schumpeter, the quasi-Austrian guy who really did come from Austria. "Capitalism stands its trial before judges who have the sentence of death in their pockets. They're going to pass it whatever defense they hear. The only successful defense can possibly produce is a change in the indictment." Of course, that's when you put capitalism on trial. But when you have a civil trial, where socialism is also on trial versus capitalism, then you have a fair fight.

And that's a fair fight that I have to claim I won both times according to Oxford-style rules, the first time against Bhaskar Sunkara, the second time against Richard Wolff. But once again, I'm finding that this is a lesson that is yet to be learned, and all of these debates are set up as though only capitalism will be judged and discussed, and the other side is there to dump on capitalism but never put on the defensive about what kind of system they want.

**WOODS:** All right, Gene, we're just about at the half-hour mark, so what I'm going to do is we're going to call this a day.

**EPSTEIN:** Oh my God, I want to discuss — okay, okay.

**WOODS:** I know, we'll still get to that last one, because what we'll do is tomorrow we'll talk books.

**EPSTEIN:** Okay.

**WOODS:** Then we'll do Gene's wisdom, and then maybe if we have some time, I want to get to this last one of your hobbyhorses. But for now —

**EPSTEIN:** Oh my God.

**WOODS:** I know, Gene, that's why we need the month. I'm telling you, that was not a joke. So the hump day of Gene Epstein Week is now complete, and thanks for listening, everybody. We'll see you tomorrow.