



Episode 413: Salon Says Rich Are Parasites; We Dissent

Guest: Peter Klein

WOODS: As long as *Salon* exists, I will never run out of episode topics.

KLEIN: (laughing) Well said.

WOODS: I just told people about this piece that we're going to be talking about today and the book that it's excerpted from, so we won't dwell on that, but I want to start off with -- I guess, the basic point of the piece -- or one of the basic points -- is that it's really wrong to say that the rich are job creators. And he concedes, yes, yes, yes, we know; it's true what the Tea Party people say -- because, by the way, that's the universe for him: him and Tea Party people. That's it. There's no you; there's no me. So all right, I'll go along with that. He says, the Tea Party people say that, "When was the last time you got a job from a poor person?" He says, all right, I'll admit to you: No one ever gets jobs from poor people. But that doesn't mean that the rich are magically, automatically job creators, because after all, if that were true, given all the wealth that has been transferred to the rich over the years, or the inequality that we've seen, we should be drowning in jobs.

KLEIN: Right.

WOODS: Now, see, that -- I almost feel guilty kicking that over to you, because there's too much to answer --

KLEIN: No, no, you're right. And you know, I read the article a couple of times, and it's hard to know where to begin, because there are so many basic and obvious mistakes. There are some more subtle mistakes, as well. The author's whole worldview is fundamentally slanted. The author just misunderstands the very most basic things about how a market works.

But Tom, before taking potshots at the writer, I will point out something that I thought was a little bit encouraging for us, in that, aside from this sort of standard *Salon*-style screed about the evils of the 1 percent and so forth, there was a little bit of discussion here about enterprise and entrepreneurs, and the author even concedes a few points. He says, well yes, of course, there are people like Steve Jobs, who actually do create value for society, but they're the exceptions to the rule. And yes, entrepreneurs do perform some useful functions; yes, you do need creativity and the initiative -- but,

but, but, but. Anyway, the fact that even these concessions were made in a *Salon* article, I find kind of encouraging. You know, there might be a few readers who don't do what *Salon* hopes they'll do and gloss over those points and go straight to ranting about the evil 1 percent, but some people might actually be intrigued about that and say, "Well, wait a minute. That is true; I do think Steve Jobs created something that I like." Of course, *Salon* readers love Apple products. Progressives love iPhones and iPads and anything that comes from Apple, and they might think, "Well, wait a minute. Isn't the guy who created all of these gadgets and actually has added a lot of value to my life -- isn't that an evil 1 percenter?" So we'll do our usual thing and point out all the fallacies here, but I mean, the fact that they conceded even a few little points that they wouldn't have conceded before, I take as sort of a small victory for us.

WOODS: Well, I'll take any -- sure, I'll take that, too. But now bringing us down to Earth, let's go through the fallacies here. Bring us back to crummy reality. But you're right; it is good to point that out, because maybe in the past we wouldn't have gotten those concessions. Maybe we should start with the point about, "Not all investment is going to yield you more jobs." But okay -- what that boils down to is, we're not fundamentally looking to create jobs per se. So why don't you develop that.

KLEIN: I mean, this author combines the typical *Salon* aggressive left-egalitarianism with a very, very crude Keynesian framework. You know, I used to refer to this as sophomoric Keynesianism, but now I think that's an insult to college sophomores. It's grade-school Keynesianism, that, it's not capitalists, it's not entrepreneurs that create jobs; it's aggregate demand -- as if aggregate demand were this sort of mysterious, depersonalized, self-contained force that automatically creates jobs. And as you point out, of course, job creation is not the goal. Job creation is a means to a goal of more well-being, economic prosperity, social freedom, and so forth. But the author makes the point that a wealthy person, per se, or the fact that someone has wealth, does not automatically translate into some sort of economic growth or economic innovation. And of course, that's true, but the question is, so what? I mean, aggregate demand, by itself, doesn't create wealth or create prosperity either. The way wealth is created in a market system is through the interaction of these different aspects of society, different agents in society. I think of -- take aggregate demand: Suppose that there is a huge demand within society for the Tom Woods Show -- which, of course, there is.

WOODS: Of course. Yeah, that's easy for my listeners to understand. Right, good example.

KLEIN: All the wishing and desiring for Tom Woods radio interviews does not automatically make these interviews come into existence. It takes Tom Woods, right? And Tom's supporters and technical people and Tom's guests and so forth, who have to translate that consumer demand into actual interviews and products. So, yes of course, it's true to say that Tom Woods sitting by himself in the basement with no audience -- with no one interested in the products that Tom Woods wishes to offer to the market -- that doesn't create a lot of consumer value, if consumers don't value the things that Tom Woods is offering. But consumer valuation by itself -- wishes, dreams,

hopes -- don't bring forth goods and services either, unless you have entrepreneurs, investors, capitalists, workers, all kinds of agents to actually bring these things to the market. So society is a complex interaction among consumers and producers, capitalists, entrepreneurs, laborers, and so forth. This sort of naive, childish notion of us against them -- you know, capitalists versus consumers, capitalists versus workers -- again, is just sort of a child's way of looking at the world. And I think that's sort of the basic fallacy -- that's the basic worldview -- that this author has. And that's what leads this author into so many blind alleys.

WOODS: One of his points is a fairly common one: That the rich are going to spend a smaller percentage of their income, or when they do spend it, it will be on some frivolous goods; whereas the average guy is going to spend a big proportion of his income on consumption. And that's what makes the economy go round. Whereas the rich are not making the economy go round, because they're stashing their money somewhere and just sitting on it, and so this is, in fact, another reason why the rich don't create jobs. By not spending, they're not creating jobs; whereas the average Joe is doing more to create jobs by going to the mall and blowing his paycheck. What's the basic -- because I think there are people who feel like, "I go to the mall; I buy some things; I'm helping the economy." Why are they wrong to think that?

KLEIN: Of course they're helping the merchant from whom they purchased. Of course people spending their money in the ordinary course of life, that's part of exchange; that's part of what makes the economy go. But the basic fallacy of this position is, if you take Bill Gates, for example. The way that Bill Gates generates economic value for society is not how much he spends on automobiles, not how much he spends on his house or on furs or diamond jewelry for his wife or whatever; it's through the creation of Microsoft. And the profit that Microsoft earns from offering goods and services on the market -- new goods, new services, generating consumer value -- the vast majority of that profit is, of course, reinvested in Microsoft. It's not the little tiny piece that Bill Gates takes for himself. Yeah, sure, I mean, CEOs, entrepreneurs -- there are a lot of successful business people who earn a pretty nice income, but that income is a tiny, tiny, tiny fraction of the value and wealth that is created by their enterprising activities. The vast majority of that goes back into the business, and creates more Windows or iPhones or whatever it is people wish to consume. It's a total red herring to point out that Bill Gates spends a smaller percentage of his income on food than how much I spend of my income on food. That has almost no effect -- a teeny, trivial effect -- on economic well-being. It's innovation and investment that is done by companies, not by individuals, but by the Microsoft Corporation, which retains most of its earnings. That's what creates value, not consumer spending by rich or poor.

WOODS: I want to jump here to what the author -- I guess it's Andrew Sayer -- calls a "contradiction in capitalism" that he believes he has found, along with Marx, by the way -- this does not give him pause, interestingly enough. And that is that, on the one hand, the individual capitalist wants to keep wages low -- which is the same reason he would want to keep the price of any input low, just to save himself some money. But on the other hand, he would like other capitalists to be paying high wages, so that those people could take their high wage payments and spend them on the goods of

that capitalist. And so what we have here is a conflict between capitalists and capitalists. The capitalist, looking at the whole system, would like to see high wages, because then that money will be spent on his goods, but looking at his own situation, he wants low wages, and so the result is, since nobody looks at the big picture, everybody just pays the low wages, and then the workers don't have money to buy any goods.

KLEIN: All right, so again, it's a kind of fundamental mis-framing of the problem. It's a misunderstanding of how capitalism works, about how prices and wages are determined. But first of all, as we've already said, aggregate demand is not the driver of economic well-being. So it's not that Bill Gates is thinking, "Gosh, how can I get consumers in the economy to have more disposable income to spend on my stuff?" Because then they might say, "Let's just get the government to print more money. Won't that lead to general prosperity?" The second point is that, look, Tom, if I go out to eat at McDonald's, you could say, "Well, Peter Klein wants the prices of McDonald's hamburgers to be low, but the owner, the local franchisee at the McDonald's in my town wants the prices to be high, so there's this fundamental conflict between these two agents." Look, the price of McDonald's hamburgers is not set by myself; it's not set by the owner of the McDonald's franchise. It's set by the market. It's set by supply and demand. Likewise, wages and salaries in a market economy are set by supply and demand. It's not the decision of the employer -- the capitalist in Marx and this author's terminology -- doesn't unilaterally set wages, so the idea that, "Well, I'm going to keep the wages of my workers low, and I want my competitor to sort of, for whatever reason, decide to pay his workers more" -- I mean, no entrepreneur decides ultimately what wages or salaries his workers will get. It's determined by market forces. Yeah, I can choose to offer whatever wage package I want. If I offer wages that are below the prevailing market wage, I'm not going to be able to hire anybody. If I pay wages that are much higher than the market wage, then my competitors are going to earn higher profits than I am; I'll be forced to lower my wages and my costs or to go out of business. In other words, this whole idea that capitalists are unilaterally setting wages and other prices to benefit themselves, and hoping that other capitalists will do other things that will benefit them -- that's just not how wages and prices are set in a market system. So it's sort of an irrelevant point.

WOODS: I want to shift to the list of reasons that we need to think of entrepreneurship differently, given that you are an expert on entrepreneurship. We're thinking about entrepreneurs as being "enterprising people," the author says. And he says, "So, an enterprising person does not have to be a capitalist, although, certainly having a lot of money helps to fund business." He says, "However, significant innovation takes considerable time and resources, so particularly where businesses are under pressure to deliver shareholder value in the short term, this may stifle entrepreneurial behavior. The spectacle of major firms spending more on buying back their own shares, so as to push their price up, than they spend on research and development makes a nonsense of the idea that they are enterprising in the sense of innovative and risk-taking." Your thoughts?

KLEIN: Yes, so of course this is completely insane. The author has no understanding of what risk-taking or innovation means. Risk-taking in an economy means investing productive assets in conditions of uncertainty that decision-makers are trying to figure out where to invest resources, whether to expand production, to contract production, to change the technology of production, to invest in R&D, to set up new plants, to replace labor with capital, and so forth. These are all decisions that entrepreneurs and capitalists are making, without knowing for sure what the end result will be. So any business decision that's made under uncertainty is entrepreneurial in this sense. This author seems to think that, from a third party's perspective -- you know, some journalist -- he can say that, "Well, a company that invests X dollars in developing a new technology is more entrepreneurial than some other company that only invests Y dollars, some smaller amount in developing a new technology." Well, what's the right amount to invest? That's an entrepreneurial decision, not the decision of some hack journalist.

This notion that companies buying back their own stock is not entrepreneurial, of course, fundamentally misunderstands the notion of entrepreneurship. This author, again, has a childish, naive vision of maybe something he saw on television or in a movie about -- maybe he saw the movie *The Social Network* or he read the biography of Steve Jobs or saw one of the Steve Jobs movies, and he has this vision in his mind of young, 20-something engineers sitting at a computer desk, programming and experimenting. I mean, yeah, that can be entrepreneurial if it's done by decision-makers who are risking their own capital in an attempt to do better and satisfy consumers. It could also be a complete waste of funds if it's government expenditure. It could be part of the tech bubble, that these could be decisions that are viewed ex post as mistakes. Entrepreneurship means letting market participants decide what to invest, how much to invest, what technologies to develop, how to deploy resources, and so forth -- not to do things that look glamorous or sexy or exciting to third parties. So of course, what shareholders do is entrepreneurial. Of course, what capitalists do is entrepreneurial, whether it means doing R&D, or whether it means closing a plant. These are all entrepreneurial decisions.

WOODS: Let's raise a related point, then. He says, "Enterprise needs patient money, for major innovations can take over a decade to turn into successful products. Market competition may help to drive innovation, but competition for quick gains is more likely to be a brake, especially on major innovation. Obsession with liquidity -- with being able to sell off any fixed assets like machinery, buildings or research divisions the minute they fail to yield gains -- stifles innovation in production." Is that true?

KLEIN: Yes, this is an interesting argument that has been made a lot in the last couple of years, especially by people who, of course -- you can see the hidden subtext here, which the author actually later makes explicit: that it should be the state, you need the government, as a more patient investor to take the long-term perspective. There are so many different ways to think about this, Tom. First of all, do we really think that government actors, whose time horizon extends to the next election, are going to be more patient and more future-oriented than private investors, who have their own

assets at risk? I think that question kind of answers itself. And the other question, the other way to think about this, is that it goes back to, what is the right level of patience? What is the right time horizon? You could imagine a society in which all of us decide that we're all going to radically cut back our consumption, and we want all of the resources that now go in, for example, to producing iPhones all to be set aside to develop some radical new technology that will come to fruition in 50 years, and we'll go back to landline telephones, or we'll go back to carrier pigeons and smoke signals. I mean we could do that, right? And maybe we would get something 50 years hence that we're not going to get, because we spend a fair amount of resources now on creating consumer goods that people currently wish to consume, like iPhones. Would that be a wiser scenario? Is that a better use of resources, in my hypothetical, than the one that we have now? Who's to say? It's certainly not for you or me to say that society as a whole should have this kind of time horizon or that kind of time horizon, so why would it be a good thing if government actors or some other actors decided, contrary to what consumers want -- which is goods and services today, plus the prospect of a certain amount of new goods and services in the future -- we should override that with something else, some Platonic ideal of a long-term future that the state or some journalist or whatever impose on society. Why is that a superior use of resources? What's wrong with companies trying to meet short-term objectives, in addition to meeting long-term objectives? It's not for you or me or for a *Salon* writer to say what these decision makers should do. It's up to them in competition with each other to satisfy consumers in various kinds of collaborations, partnerships, and so forth, to figure out. That's the job of the market: to figure out, not only how much should be invested in iPhones and how much should be invested in food today, but also to decide what's the right amount of investment in current production versus investment in R&D and other kinds of programs to bring about new future products. The market has to decide that. There's no way for us to say that one allocation is better or worse.

WOODS: And of course, another way to think about it would be to look at the way the state really has provided for the future, and to see how good it is at future-oriented behavior. Look at the pension programs in so many of the states. That was all the result of extremely short-term thinking: "We want to get the votes of these interest groups, and we can't raise taxes now, because there'll be a revolt, so we make promises in the indefinite future which are now going to be impossible to keep." And you can find example after example of that. Why would you think these people are particularly suited to think about the future?

KLEIN: Right, and especially if you look at innovation and technology. We constantly hear about Al Gore and the Internet and all these different anecdotes of some technology, some product -- GPS or whatever -- that was a spin-off of some government program. Yeah, but that's completely cherry picking. The U.S. government has spent hundreds of billions -- probably trillions of dollars, basically poured down rat holes -- to develop potential technologies that never went anywhere, never created any value for consumers -- were simply dead ends. And so we know empirically that the government is far, far inferior to the private sector, not only in planning for the future in terms of things like pension funds, but actually in developing technologies

that are more entrepreneurial or more innovative. The government is the last actor on society you would ever trust to have a longer term perspective than private actors.

WOODS: Let me read you this point -- like most critics like this, this person, this Mr. Sayer is very, very much opposed to the idea of the great entrepreneur who comes up with an idea and then risks his capital to pursue it. He says, yeah, yeah, yeah, that happens once in a great while. "But," he says, "the romance of the entrepreneur is like the romance of the individual scientific genius; it is rarely simply individuals who do innovative things on their own, but more often groups or networks, and all are indebted to the accumulated knowledge and infrastructure that they inherit from their society. Wittingly or unwittingly, celebrations of 'entrepreneurs' in the media serve to render invisible the workers on whom they depend."

Now, let me just say one thing here: of course, we all rely on the accumulated knowledge of the past. We all rely on the accumulated capital stock of the past. I suppose I could dig up dead people and throw money at them for that, but I don't see that I could put a dollar amount on that.

But being less facetious here, I want to carry on with a later point he makes, because it's related to this. He says, "We might agree that the likes of Jobs and Dyson deserve more than ordinary workers, though we'd probably differ on just how much more they should get. But let's not kid ourselves; these innovative capitalists do not ask their workforces or the general public: 'How much do you think I deserve for my contribution?' Such employers get what they get because they can."

Now, I point that out to you, because, when I listen to Austrian economists talking, they suggest that people get what they get because of their particular niche in the division of labor, and they get what accrues to them for their contribution within the division of labor. But he's saying that, come on, now; in reality, they get what they get because they're in a position of power, and they write themselves the checks. So the two things that I want you to answer would be, number one, is it relevant to say that this innovator also relies on accumulated knowledge; he relies on the assistance of people? And then secondly, in apportioning the rewards for the great innovation, doesn't he just get what he gets because he's in a position to get it?

KLEIN: On the first point, I actually agree with the author here. I think it's true that we tend to over-romanticize particular individuals -- Jobs, Gates, whatever -- as sort of coming *sui generis*, creating these great technologies out of nowhere. No, they're embedded into a system, a network, a market -- they're embedded within the market. And of course they depend on the talents of many individuals: engineers, manufacturing experts, workers, as well as investors, as well as technologists, consumers -- of course. But that's completely irrelevant to the issues at hand, of how much these people should be paid, whether capitalism is a better system than whatever kind of Marxist system *Salon* prefers. It has absolutely nothing to do with the issues at hand.

On the second point is, I suspect that the writer is taking what he has learned from politics, and importing into the world of the market, which the writer obviously doesn't understand. Yeah, I mean, it's true in politics: Barack Obama gets what he gets, because he has power. The king gets what he gets, because he has power. In politics, there's no market forces. There are no checks and balances that have any meaning whatsoever. It's a brute contest of power. It's a contest of will in the political arena, and it's a zero-sum game. There are winners and losers. Of course, in a free market system, nobody determines his own compensation. Steve Jobs no more determines his own compensation than a McDonald's worker determines his own compensation. As we said before, these things are determined by the market, by entrepreneurs, by capitalists, by investors, and so forth. Steve Jobs, of course he was compensated in salary, and he was paid by Apple as much as Apple believed he should be paid to keep him from quitting and going and doing something else, but most of Steve Jobs' wealth came from equities, from owning Apple stock. And most of the highest-paid CEOs, the majority of their wealth comes from equity ownership, not from salary. And so, of course, it goes without saying, the reason that shares of Apple stock are worth so much is that lots of people in the marketplace would like to own shares of Apple -- because they want those dividends, and they want those capital gains. So it's like a category mistake. I don't even know how to respond to the claim that Steve Jobs was highly paid because he got what he could get, he chose to pay himself this money. Again, it makes as much sense as saying that Mozart was a famous composer because he just decided to give himself the fame and reputation of being a great composer. It just doesn't make any sense.

WOODS: Finally, Peter, let's see what you have to say about, "Capitalism was much more successful when it had top rates of tax of 80% and over, restrictions on capital movements and the top 0.01% controlled a much smaller share of wealth than now."

KLEIN: Yeah, so of course, as we've already discussed, the author doesn't have any sort of argument whatsoever for why capitalism would perform better under those circumstances. What I find interesting, Tom, is that capitalism performed as well as it did under those kinds of restrictions, which I think illustrates our point, that the vast majority of wealth creation does not come from extremely wealthy people spending money on yachts, or whatever. So even when you impose really high marginal tax rates on entrepreneurs, on investors, on capitalists, that is harmful. It diminishes their incentives; it takes money away from productive people; it gives it to the government for people to waste on all kinds of unproductive activities. But it doesn't actually completely crush the system, because so many great entrepreneurs, great capitalists are ultimately motivated by things other than money. They have passion; they have desire. Even when they're crippled and hobbled by this sort of looting, parasitic state, they still want to try to create wealth, and they do a remarkably good job of doing it. So thank goodness that we don't continue to hobble and cripple them as much as we do. But even when we have such bad and inefficient policies, these capitalists and entrepreneurs are still doing a wonderful job.

WOODS: Peter, do you have anything, on a popular level, a book that you can recommend, that would give people a better overview of what entrepreneurship is

really about -- I mean, entrepreneurship in a colloquial sense, not necessarily a Misesian sense -- but that would give them a more accurate look than, say, this particular author might?

KLEIN: Yeah, sure. A lot of the classics of the Austrian tradition, including things like Hazlitt's *Economics in One Lesson*, which is not explicitly about entrepreneurship, and, of course, was published in the 1940s. If you have a very basic understanding of how a capitalist system like this works, then I think that really helps in addressing the kind of claims that are made in this *Salon* article. Mises' book, *The Anti-Capitalistic Mentality*, is very good. There are a number of other books by Hazlitt that are specifically about business people and entrepreneurs. I have several pieces in *The Free Market* newsletter or pieces on Mises.org that deal with entrepreneurship on a very basic level, and we could put some links on your webpage. There are popular writers, -- like Steve Mariotti, who is a great entrepreneurship educator; he has a number of pieces on his website. He did an interview with me that was published on, of all places, *Huffington Post*; we talked about the role of the entrepreneur in society. And I think just having a better understanding of the capitalist system, more generally, will really help people to understand the role played by the entrepreneur.

WOODS: Well, I will put up the links that you shoot over to me; I'll put them up on the show notes page. This is Episode 413, so it will be TomWoods.com/413. Peter, I appreciate your willingness to do this. Probably this will be the last article at *Salon* filled with errors, though, so I don't know when the next time you and I will talk will be, but --

KLEIN: (laughing) I know the *Salon* editorial staff is listening closely, and will go back and issue a retraction soon.

WOODS: (laughing) Oh, no doubt, they'll issue a retraction. But even if they don't, I've sometimes thought of things like *Salon* as being make-work projects for people like you and me. It gives us something to do. Okay, thanks again, Peter.

KLEIN: Okay, thanks, Tom.