

EXTRACT FROM "A POSITIVE PROGRAM FOR LAISSEZ-FAIRE"

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The major responsibility for the severity of industrial fluctuations, however, falls directly upon the state. Tolerable functioning of a free-enterprise system presupposes effective performance of a fundamental function of government, namely, regulation of the circulating medium (money). We should characterize as insane a governmental policy of alternately expanding rapidly and contracting precipitously the quantity of paper currency in circulation - as a malevolent dictator easily could do, first issuing currency to cover fiscal deficits, and then retiring currency from surplus revenues. Yet that is essentially the kind of monetary policy which actually obtains, by virtue of usurpation by private institutions (deposit banks) of the basic state function of providing the medium of circulation (and of private "cash" reserves). It is no exaggeration to say that the major proximate factor in the present crisis is commercial banking. This is not to say that private bankers are to blame for our plight; they have only played the game (and not so unfairly, on the whole) under the preposterous rules laid down by governments - rules which mean evasion or repudiation by governments of one of their crucial responsibilities. Everywhere one hears assertions of the failure of competitive controls, of the chaos of unplanned economy, when the chaos arises from reliance by the state upon competitive controls in a field (currency) where they cannot possibly work. Laissez faire, to repeat, implies a division of tasks between competitive and political controls; and the failure of the system, if it has failed, is properly to be regarded as a result of failure of the state, especially with respect to money, to do its part.

We have reached a situation where private-bank credit represents all but a small fraction of our total effective circulating medium. This gives us an economy in which significant disturbances of equilibrium set in motion forces which operate grossly to aggravate, rather than to correct, the initial maladjustments. When for any reason business earnings become abnormally favorable, bank credit expands, driving sensitive product prices farther out of line with sticky, insensitive costs; earnings become more favorable; credit expands farther and more rapidly; and so on and on, until costs finally do catch up, or until some speculative flurry happens to reverse the initial maladjustment. When earnings prospects are unpromising, credit contracts and earnings become still smaller and more unpromising. In an economy where costs (especially wages, freight rates, and monopoly prices in basic industries) are extremely inflexible downward, the deflation might continue indefinitely (until everyone was unemployed) if governments did not intervene (inflate) to save the banks or to mitigate human suffering.

Thus, the state has forced the free-enterprise system, almost from the beginning, to live with a monetary system as bad as could well be devised. If, as seems possible, both capitalism and democracy are soon to be swept away forever by a resurgence of mercantilism (by the efforts of persons who know not whither they lead), then to commercial banking will belong the uncertain glory of having precipitated the transition to a new era. Such is likely to be the case, even if our institutions survive this time the attentions of their misguided, if well-meaning, guardians. Capitalism seems to retain remarkable vitality; but it can hardly survive the political rigors of another depression; and banking, with the

able assistance of monopoly, seems certain to give us both bigger and better depressions hereafter - unless the state does re-assume and discharge with some wisdom its responsibility for controlling the circulating medium.

(2d paragraph page 14 to end of page 16).
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