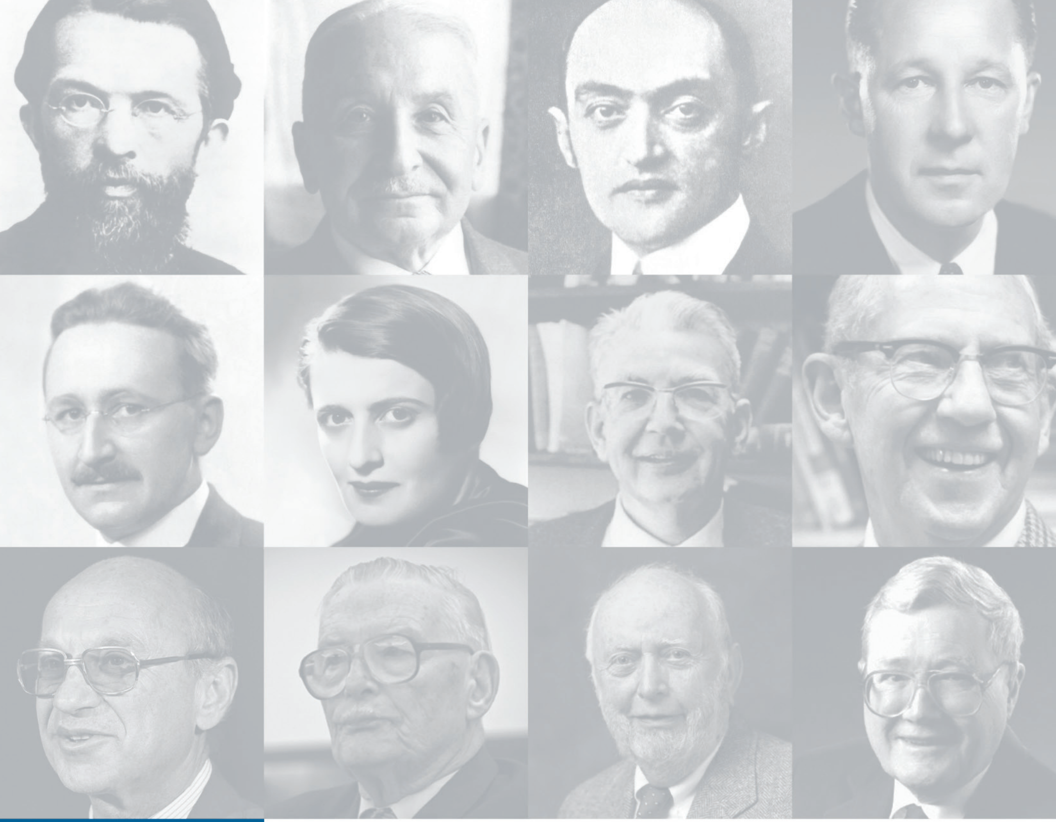

18 Essential
Classical Liberal Thinkers

MEI
Ideas for a More Prosperous Society

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Classical Liberal Thinkers

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Preface

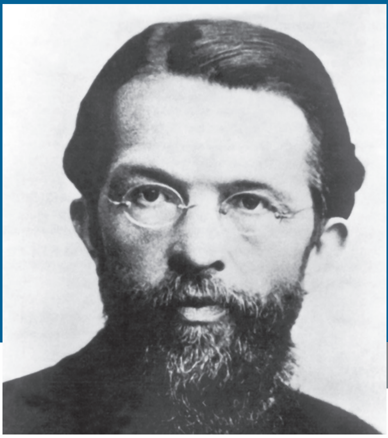
Classical liberalism, which advocates civil liberties, the rule of law, and economic freedom, originated with such thinkers as John Locke (1632–1704), Adam Smith (1723–1790), Jean-Baptiste Say (1767–1832), and David Ricardo (1772 – 1823). It is generally understood to encompass free trade, the protection of private property, and limited government intervention in the economy, along with freedom of religion, freedom of expression, and freedom of the press.

Of course, back in the 18th and 19th centuries, this was just called "liberalism." In the past hundred years or so, however, while self-described liberals have continued to defend civil and social liberties, they have largely abandoned economic freedom in favour of interventionism. Those who have continued to defend economic freedom are now identified as *classical* liberals.

Not that classical liberalism is stuck in the past—far from it. While inspired by the same kinds of basic insights and ideas as Locke, Smith, Say, and Ricardo, many more recent thinkers have made major contributions to this broad body of knowledge. Indeed, several classical liberal schools of thought have emerged, including the Austrian School of Economics, the Chicago School of Economics, and Public Choice Theory, to name three of the most prominent.

This booklet contains short write-ups on the lives and ideas of eighteen classical liberal thinkers from the past century and a half. They were written by MEI President Michel Kelly-Gagnon and MEI Vice President of Operations Jasmin Guénette, with the collaboration of various MEI staffers, over the past few years. They were made available free of charge on the MEI's website, where all of our research on economics and public policy can also be found. They are collected here in slightly modified form, arranged chronologically by date of birth.

Together, these short biographical essays tell the story of the evolution of classical liberal thought as the benefits of freedom have spread, though haltingly and unevenly, around the world. And they point the way forward to a future of greater and more widespread wealth and well-being for all.



Carl **MENGER**

Founder of the Austrian School of Economics

(1840–1921)

Carl Menger was not only the founder of the Austrian School of Economics; he also became one of the pioneers of modern economics with the 1871 publication of his classic work, *Principles of Economics*. Like his disciples after him, Carl Menger, born in 1840 in the Austrian Empire, was both a man of thought and a man of action. He began his career as a journalist, and was subsequently a ministry staffer, an academic, a tutor to the imperial crown prince, and an economic advisor to the Austrian government. Among his numerous contributions to economic thought, three stand out.

The first marked the history of economics thanks to a notable coincidence: In the early 1870s, three intellectuals who didn't know each other, living in three different European countries, made a simultaneous discovery concerning the notion of value. Along with Menger, Léon Walras of Switzerland and William Stanley Jevons of England realized that the value of a good does not depend on the quantity of work devoted to its production, as classical economists from Smith to Marx had maintained, but on the utility consumers place on obtaining one additional unit of the good. It is this additional quantity "at the margin" that counts, which is why this discovery was described as the "marginal revolution."

Value Is Subjective

Among the three discoverers, Carl Menger is the one who placed the most emphasis on the subjective nature of the theory of value, which explains numerous economic phenomena that confront us every day. Starting from the logic of diminishing marginal utility (the more of a good I consume, the less utility I get from the next unit consumed), we can thus explain why water in a desert will be expensive, whereas next to an abundant source, it will be cheap. Scarcity, in other words, helps explain value.

To take a contemporary example, why can the price of an Uber trip suddenly become higher in the space of a few minutes when nothing has changed about the cost of producing the service? Simply because in certain contexts, for example when it rains, there are suddenly more consumers who are ready to pay extra for this mode of transportation because they place greater value on an additional trip. This pushes up the price, which attracts available drivers ready to profit from this demand. The market thus tends to provide more consumer satisfaction when prices are flexible and better reflect the value of goods.

Menger's second original contribution is a methodological one. He disagreed with the German Historical School which taught that economics could only be understood through the study of historical facts. In contrast, the Austrian believed that it is possible to use logic to deduce general laws that can help us understand complex economic phenomena. Theory provides us with tools to help us better analyze facts and organize them in a coherent manner in order to deduce more general laws.

Methodological Individualism

In order to understand society and economics, one has to start with individual actions by considering that everyone tries to maximize his or her interests and satisfy his or her needs. Menger therefore posited the foundations of methodological individualism, which is not the *homo economicus* caricature to which economics is too often reduced. According to Menger and the Austrian economists, individuals are not omniscient and do not know everything about the future. We often make mistakes, and are constantly revising our expectations.

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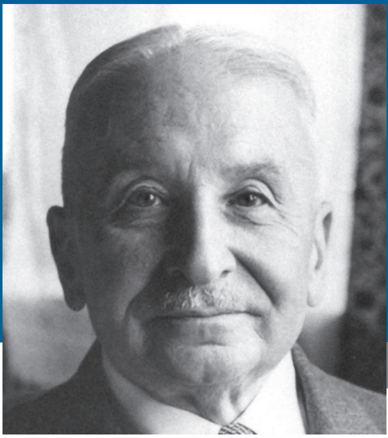
Menger was also a philosopher who thought about the nature of the institutions that govern our daily lives. How do institutions like language, money, and morality arise? In contrast to his adversaries from the German Historical School, Menger thought that these owe nothing to governments or to centralized political power, but are explained instead by the spontaneous emergence of conventions progressively accepted within communities. For example, in the case of money, certain individuals discovered that barter was not practical for exchanging goods that do not share the same characteristics. They realized that certain goods that were more tradable than others could serve as intermediate goods in exchanges. This convention was progressively accepted and eventually used universally without the intervention of any centralized organization.

The Nobel laureate economist Friedrich Hayek pursued this line of thinking with his theory of spontaneous order: Institutions and rules of law arise through trial and error. They are the fruit of human action, but not of centralized human planning.

Carl Menger's disciples in Vienna, Eugen Böhm-Bawerk and Friedrich Wieser, continued to formalize and develop his approach. Several more generations of Austrian economists have since been trained, the most famous being Hayek and Ludwig von Mises. The "Austrian" school today is blossoming around the world. Thanks to Menger, it proposes an original vision of economics and society, and it still has much to offer.



Ludwig **VON MISES**

Prices Will Guide Economic Activity, If We Let Them

(1881–1973)

Ludwig von Mises was one of the intellectual leaders of the Austrian School of Economics. The influence that Mises had on the promotion of classical liberal ideas during the 20th century is impressive.

Born into a well-to-do family in a province of the Austro-Hungarian Empire that is now part of Ukraine, Mises demonstrated his intelligence at a very young age: He mastered French, German, and Polish, and was reading Latin by the time he was 12 years old.

When he began his university studies, Mises believed in socialist ideas. But his views on the world and the economy evolved quickly once he learned of the writings of Carl Menger and Friedrich von Wieser, the founding fathers of the Austrian School of Economics.

In his first book, *The Theory of Money and Credit*, published in German in 1912, Mises developed his explanation of economic fluctuations. From then on, his reputation continued to grow based on the high quality of his work.

His career was very eventful. After founding his own research institute in Vienna, he had to flee the country in the 1930s with the rise of Nazism. He escaped first to Switzerland, and then to the United States,

specifically New York. Five years after his arrival, he began teaching at New York University as a visiting professor and remained there until his retirement in 1969. He died in 1973 at the advanced age of 92.

Economic Coordination

Among the important contributions Mises made to economic theory, his notion of economic coordination through prices and his theory of economic fluctuations deserve special mention.

Given that resources are limited but our needs are unlimited, we have to find the best ways of producing what we need. How to proceed? To answer this question, consider a concrete example: the construction of railways. It is possible to build railways of gold, at least in theory. Of course, gold has many other uses: jewelry, computer parts, and so on. So how do we know if we should prefer gold to steel in the construction of railways?

According to Mises, only prices can inform us of the relative values of resources and their optimal uses for the good of society. This is why legislators must ensure that price information is not “contaminated” by inappropriate regulations that would cause them to rise or fall for reasons not based on voluntary exchanges between individuals.

Mises did not analyze the economy through the traditional lenses of supply and demand. He postulated that markets are generally stable, but are subject to recessions, and even depressions, when there is an artificial expansion of credit by central banks. According to him, this creates inflationary pressure and encourages individuals and companies to make bad decisions. It is the manipulation of prices by government that disrupts normal economic activities.

Only prices can inform us of the relative values of resources and their optimal uses for the good of society. This is why legislators must ensure that price information is not "contaminated" by inappropriate regulations.

The work of Mises influenced that of several others, such as Friedrich von Hayek (Nobel 1974), Robert Lucas (Nobel 1995), and Leonid Hurwicz (Nobel 2007). His influence goes far beyond the Austrian School of Economics.

Since the Nobel Memorial Prize in Economics was only introduced toward the end of his life, Mises never received one. However, the famous MIT economist Paul Samuelson, himself a Nobel laureate, wrote that if the prize had been awarded earlier, Mises would certainly have won it. This is an important recognition, since Samuelson's ideas were diametrically opposed to those of Mises.

Be it through his writings in political philosophy or in economics, the influence that Ludwig von Mises has had on our society is considerable. He succeeded in consolidating the foundations of one of the most important schools of thought in economics, and his work is now more alive and relevant than ever.

VON MISES

Joseph **SCHUMPETER**

Entrepreneurship in the Service of Innovation

(1883–1950)

Contrary to many economists who spend most of their lives at university, Joseph Alois Schumpeter had an adventurous life, including a variety of professional activities carried out on several continents. Born in 1883, the Austrian was ambitious. He claimed to have set as goals to become the best economist in the world, the best horseman in Austria, and the greatest lover in Vienna—and to have achieved two out of the three!

Over the course of his life, he worked as a lawyer, a finance minister, a banker, a teacher, and a writer. These multiple experiences, as well as his interest in sociology and politics, made him an uncommon thinker who left behind a considerable body of work, including *Capitalism, Socialism, and Democracy* and the posthumous *History of Economic Analysis*.

While Schumpeter studied in Vienna under the auspices of some of the most brilliant economists of their generation like Wieser and Böhm-Bawerk, he is considered more of an unclassifiable economist than a representative of the Austrian School. He does not share with that school the idea that socialism is unworkable, and he accords a larger place to history in the explanation of economic mechanisms.

He is nevertheless an essential thinker whose work remains relevant, mainly for two ideas that revolutionized economics.

First, there is the role of innovation and entrepreneurs in explaining economic development. Schumpeter distinguishes the entrepreneur both from the rentier whose income is due to speculation alone and from the heir whose fortune is due to parentage. The entrepreneur, in contrast, discovers new ideas, swims against the current, breaks the routine, and innovates by finding new ways of producing.

For Schumpeter, who was also a sociologist, the lure of profit is not the only thing that motivates entrepreneurs. They are first and foremost animated by an adventurous spirit and seek out the sensation of conquest and discovery. The innovations they create change the lives of thousands of people. Their profit is legitimate, as it serves to reward the risks they take. It is entrepreneurs who are the motor of growth in a competitive economy, not government policies.

Second, Schumpeter left his mark on the history of economic thought with his theory of business cycles dominated by the phenomenon of innovation. The process of economic growth is punctuated by episodes of routine and moments of rupture marked by the generalized destruction of businesses in certain sectors. These are then replaced by new economic actors who organize new production techniques.

Creative Destruction

Indeed, big inventions like the steam engine and electricity were accompanied by clusters of innovations that turned the whole economy on its head. Often denounced, these moments of upheaval are actually good things. For one thing, innovation spreads and benefits society as a whole. For another, economic activity is actually displaced. The job destruction and decreased activity in one sector are offset by job creation and increased activity in a new, innovative sector. This is the well-known theory of "creative destruction" that made this Austrian professor famous.

Big inventions like the steam engine and electricity were accompanied by clusters of innovations that turned the whole economy on its head. Often denounced, these moments of upheaval are actually good things.

This theory was useful in its day for understanding the changes that accompanied the Industrial Revolution. It is just as useful today for understanding the transformations accompanying the digital revolution that is taking place before our eyes. Entrepreneurs have, over the past decades, succeeded in transforming a scientific discovery in the field of computing into a cluster of innovations that improve our lives on a daily basis.

These changes lead some to say that robots and computers are taking our jobs. But recent studies prove Schumpeter right: Innovations in the fields of computing, robotics, and communications merely transfer jobs from certain sectors to others and are beneficial to the entire population overall.

Finally, Schumpeter's work is also striking in its analysis of society and politics. Pessimistic by nature, he predicted the inevitable disappearance of capitalism and its replacement by socialism due to the growing hostility of entire segments of the population to this system. Among these he included intellectuals, who had become masters in the art of contesting the system that allowed them to express themselves freely and to enjoy a certain level of comfort.

Fortunately, the professor's pessimistic predictions did not come true, and socialism collapsed at the end of the 20th century. But his sociological analysis of the paradoxical resentment of certain groups toward the market economy remains relevant. One need only think of the anti-globalization crowd planning the next revolution using smartphones, tablets, and other products of the very economic system they denounce.

Leonard E. **READ**

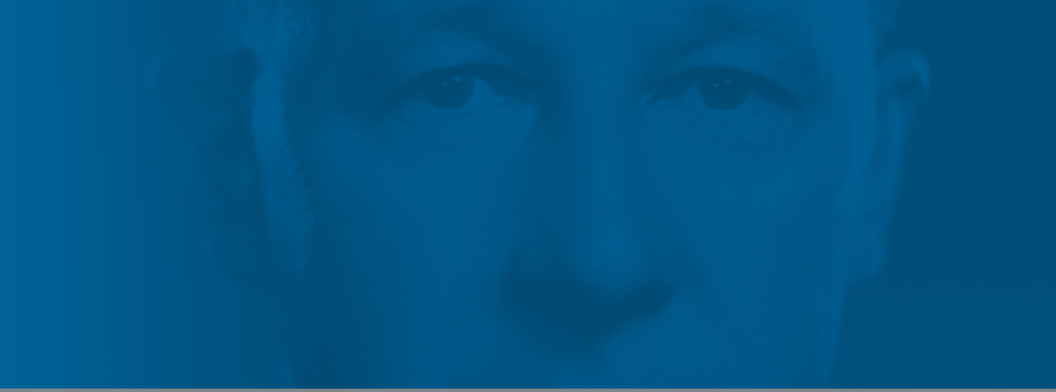
I, Educator

(1898–1983)

Leonard Edward Read was a passionate advocate of freedom in the United States. For nearly 40 years, he was President of the Foundation for Economic Education (FEE), an organization that he founded devoted to the promotion and defence of classical liberal ideas.

After a brief stint in the armed forces during the First World War and an entrepreneurial episode that didn't work out, Read settled in California, where he worked for the Burlingame Chamber of Commerce. In 1933, during a meeting with industrialist Bill Mullendore, Read discovered classical liberal ideas and the harmful effects of government intervention.

Executive Vice President of Southern California Edison, Mullendore was part of a group of California businessmen who were very critical of the New Deal. As representative of the regional Chamber of Commerce, Read met with Mullendore to try to convince him to support President Roosevelt's reform program. Mullendore eloquently explained to Read why the New Deal was fundamentally unfair, and why it opened the door wide open to what we now call rent-seeking.



It is at this point that Read understood the importance of freedom for people's well-being and realized the danger of government intervention. His meeting with Bill Mullendore had such an effect on him that he took it upon himself to read the works of liberal thinkers like Bastiat, Hayek, and Rand, which completely changed the way he thought about economics and society.

The Pencil That Changed Everything

Leonard Read eventually left the Chamber of Commerce, and in 1946 created the Foundation for Economic Education, the first modern-day classical liberal think tank in the United States.

FEE is generally credited with the renaissance of classical liberal ideas in America. The think tank still exists to this day. Leonard E. Read, for his part, wrote 29 books and some one hundred articles in which he defended and promoted the free market and entrepreneurship. One work in particular had a huge impact on the classical liberal literature, and remains relevant today: *I, Pencil*.

This booklet, published in 1958, relates in a few pages the production process for an object that seems boringly simple. From the softwood lumber harvested in a California forest to the graphite mine in Sri Lanka, passing by the dozen products needed to produce the eraser, the production of a simple pencil requires the efforts of several thousand people located in regions that are often far-removed from one another.

We forget, but the sawmill that processes the wood itself uses several complex machines that are the result of the pooling of thousands of factors of production. The sawmill must also be supplied with energy and water, while its employees must be fed, clothed, and transported.

From the softwood lumber harvested in a California forest to the graphite mine in Sri Lanka, passing by the dozen products needed to produce the eraser, the production of a simple pencil requires the efforts of several thousand people.

What can at first seem simple actually requires the contribution of innumerable factors at every stage of production.

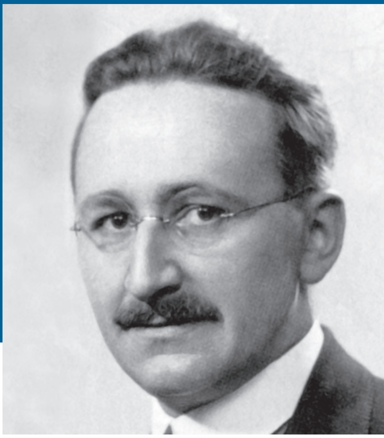
What is fascinating in Read's demonstration is that among the people involved in the production of the pencil, no one knows what he or she is helping to produce in the end. It's not important. They all do it because they determine that exchanging their activity for remuneration is beneficial for them. Moreover, and as incredible as it may seem to some, there is no one who plans or directs this pooling of resources: The invisible hand takes care of it.

More Relevant Than Ever

I, Pencil has rarely been as relevant as it is today, when numerous voices around the world are calling for increased protectionism. Leonard Read's example demonstrates that even the production of the simplest object is the fruit of international cooperation that trade barriers could prevent or make more difficult.

According to Read, governments cannot hope to manage their countries' economies such that everything that individuals want will be produced locally. First of all, no one to this day can claim to know what every single person needs at every moment. Also, given that the factors of production are not spread out evenly around the planet, we need to trade freely in order to fulfill our needs.

Today, the Foundation for Economic Education still devotes itself to teaching as many people as possible about the benefits of a free society. Leonard E. Read believed firmly in this mission, having himself been convinced in the space of a single conversation. This discussion with Bill Mullendore changed his life, and thanks to the ongoing work of FEE, that of countless others.



Friedrich
HAYEK

Avoiding the Road to Serfdom

(1899–1992)

The 20th century was one of the most violent in the history of humanity In addition to the millions of deaths caused by international conflicts, anti-liberal ideologies manifested themselves throughout the world for long periods: communism in the USSR, China, Eastern Europe, and elsewhere; Nazism in Germany; fascism in Italy and Spain. In Western societies, this rise of anti-liberalism led to the questioning of the benefits of the market economy and the rise of socialism and the interventionist state.

Economist Friedrich A. Hayek was born on May 8, 1899 and died on March 23, 1992. He spent his entire career defending liberalism and opposing these collectivist ideologies.

As a young economist in Austria, Hayek distinguished himself through his work on business cycles. He tried to explain why economies have "ups and downs." During these years, he also developed the idea that the market economy was an essential component of a free society.

Having emigrated to Britain, Hayek experienced the Second World War as a traumatic period. Terrified by the rise of fascism and socialism, he popularized his political thought in the book that made him famous: *The Road to Serfdom*.

Creeping Authoritarianism

His argument was simple: Nazism, fascism, communism, and socialism share the same basic assumption according to which the state is above the individual. According to Hayek, this assumption adopted by many individuals lead to the atrocities that occurred at the time, even if these individuals had good intentions. He argued that the interventionist tendencies of Western governments, far from preserving democracy and freedom, would lead instead to the very authoritarianism that they were trying to avoid.

Published in 1944, this book enjoyed great success around the world, and became a bestseller in the United States. However, it represents only a small part of Hayek's work, which, in economics as well as in philosophy and political science, lays the foundations for a free and prosperous society.

One of the pillars of Hayek's thought is his explanation of the role of prices in a free economy. Hayek established his reasoning in his most cited scientific article, "The Use of Knowledge in Society," which is considered one of the twenty most influential articles in economics. Prices help to allocate scarce resources, informing us of alternative uses that can be made of them. And this price system cannot be planned. Prices emerge from the bottom up, and not the other way around.

Indeed, every person in society possesses a tiny fraction of the total knowledge that allows the economy to function. It is at the individual level that economic calculation happens. An economic agent such as an entrepreneur or a consumer is guided in his or her choices by the relative prices of different goods and services.

The Organization of Scarce Resources

Prices therefore contain valuable information, and in order to play their role of coordinating the decisions of economic actors, a decentralized system is needed—namely, a free market. Every time an individual discovers new information, he or she influences prices and gives rise to a new way of organizing scarce resources in order to maximize the well-being of all. Since it is impossible to impose prices from the top, any attempt at planning leads to inefficiencies, shortages, surpluses, deficiencies, and failures. The more a central planner plans, the more these failures multiply, and the more the authoritarian grip must be tightened.

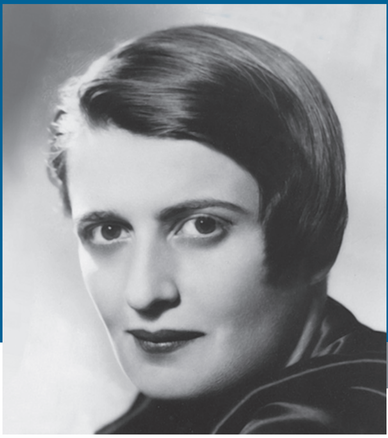
> *Hayek argued that the interventionist tendencies of Western governments, far from preserving democracy and freedom, would lead instead to the very authoritarianism that they were trying to avoid.*

Following upon his idea that information is dispersed, Hayek subsequently developed the idea of spontaneous order. He observed that the economy, without any dominant authority, succeeds in being orderly. The invention of the automobile did not come about because of a central plan in Washington, just as the invention of dental floss did not come about due to a bureaucratic plan in some distant capital.

Evoking Adam Smith's invisible hand, Hayek argued that individuals create this order by pursuing their own interests. In this way, markets serve not only to coordinate large-scale actions, but also to bring people of different religions, cultures, countries, etc., closer through trade.

His work in economics earned Hayek the Nobel Memorial Prize in Economics in 1974. In his last book, *The Fatal Conceit*, he returned once again to the role of prices, human action, and spontaneous order from an evolutionary perspective to explain why socialism and state planning threaten the free and complex societies in which we live today.

It is safe to say that Hayek's ideas will continue to exert enormous influence for many decades to come.



Ayn
RAND

Defending Capitalism on Moral Grounds

(1905–1982)

Few thinkers of the classical liberal tradition elicit the kind of strong reactions that Ayn Rand does. Love her or hate her, the Russian-born American novelist polarizes like nobody else.

Born in St. Petersburg in 1905, Ayn Rand—or Alisa Rosenbaum as she was then called—lived through the Russian Revolution, after which her father's pharmacy was confiscated and her family, like many others, went through hard times. She managed to obtain permission to leave Russia to visit relatives in the United States in 1926, and she never returned.

Her personal experience of life under the repressive communist regime informed her first novel, *We the Living*, published in 1936 when many intellectuals were singing the praises of the "noble Soviet experiment." It would not be the last time Rand dared to challenge the received wisdom of the day.

Yet in addition to actually bucking the intellectual trend, Rand also courted misrepresentation with titles like *The Virtue of Selfishness*, a later collection of essays. How can selfishness possibly be a virtue?

Clearly, this was designed to shock and get people's attention. Rand was not a booster of petty, garden-variety, short-sighted selfishness. Rather, she promoted rational or enlightened self-interest. Your life is your own, and you have a right to live it as you see fit. You have a right to pursue your own happiness, as long as you do so peacefully.

Enlightened Self-Interest

This notion of self-interest being a virtue and your life belonging to you is very appealing, especially to the young who tend to yearn for freedom—and especially when illustrated in exciting novels like *The Fountainhead* and *Atlas Shrugged*, which feature compelling characters striving to pursue their values and lead fulfilling lives.

It is in *Atlas Shrugged*, and in her later non-fiction writing, that Rand made explicit her conviction that the moral principle of rational self-interest has clear political and economic implications. Specifically, if my life is my own, and your life is your own, then human society should be organized through a system of limited government whose primary responsibility is to protect people and their property.

Rand understood and appreciated the practical arguments put forth by classical economists like Adam Smith. She realized that the invisible hand of the market leads people to pursue their peaceful interests in such a way as to be of benefit to others. Trade, it is undeniable, has widespread benefits, and economic freedom can and should be defended on these practical grounds.

If my life is my own, and your life is your own, then human society should be organized through a system of limited government whose primary responsibility is to protect people and their property.

But Rand further believed that in addition to being beneficial, capitalism is moral, and that a more fundamental defence of economic freedom has to be made on moral grounds. In short, if your life belongs to you, then no one has the right to initiate force against you, which means that all human interactions must be voluntary.

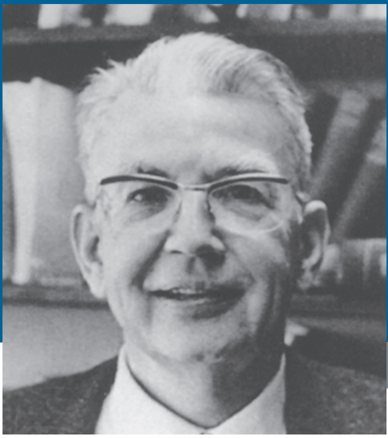
This in turn means that when we do interact with others, especially with people we do not know well, we must do so as traders. We must treat each other not as masters or slaves, but as independent equals, dealing with each other "by means of a free, voluntary, unforced, uncoerced exchange—an exchange which benefits both parties by their own independent judgment."

In a free market, she pointed out, wealth can only be achieved by a kind of "democratic" process, where consumers of goods and services "vote" with their dollars. And when people vote with their dollars, they only vote on matters that they are qualified to judge: their own preferences, interests, and needs. As she wrote, in a free market, "[n]o one has the power to decide for others or to substitute his judgment for theirs; no one has the power to appoint himself 'the voice of the public' and to leave the public voiceless and disfranchised."

Rand was regularly accused of being "pro-business." But while it is certainly true that she unabashedly celebrated the productive businesspeople who contribute so much to society, it is also the case that many of the villains in *Atlas Shrugged* are businesspeople. Unlike the novel's heroic entrepreneurs, though, these crony capitalists get rich by currying favours from crooked politicians, and influencing regulations to their benefit and to the detriment of their competitors at home and abroad.

If she were alive today, Rand would rail against the tariffs and quotas that continue to limit free trade in the name of protectionism for favoured industries, and against the subsidies and other privileges accorded to special interests that have the ear of government.

In a truly free market, government would be powerless to dole out such unearned spoils, and the only way to get rich would be by serving your fellow man and woman. There would be, to use Rand's terminology, a separation of state and economics, and both the boardroom and the legislature would be the better for it.



Ronald
COASE

What Are Firms For?

(1910–2013)

Ronald Coase is an economist whose name is not known by very many people. And yet, despite the fact that he published few scientific articles compared to his colleagues, he is probably the economist who has had the greatest influence on the profession. Why was he so influential? Because he was the first to have provided a satisfactory answer to the question of how companies work.

Generally, economists treated companies like black boxes into which resources were put, and out of which products emerged. Little was understood about why a company would decide to adopt one production method rather than another. For example, why use the services of an accounting firm rather than hire one's own accountant?

For many years, while he was a student at the London School of Economics, Coase polished his response. During the 1930s, he worked on this topic for a long time before publishing, in his 1937 article *The Nature of the Firm*, his answer: It is because of transaction costs.

The Cost of Doing Business

Transaction costs represent the costs incurred for each type of exchange, meaning the costs entailed by the negotiation of contracts

and the terms related to the supervision of the said contracts. A firm may therefore prefer to hire its own accountant instead of spending time and resources soliciting bids, looking for the best possible price, and evaluating the quality of the work done every day. If it decides to do this, it is because of transaction costs.

Moreover, transaction costs affect not just the structure of companies, but also their size. If it is too expensive for a firm to negotiate and supervise a contract with another firm for the provision of certain services, then it is preferable to produce this service within the firm. However, the flipside of such a decision is that time and resources must be spent doing something for which one does not necessarily have an expertise.

For example, a painter who is self-employed and does his own accounting must reallocate time and resources toward the activity of keeping the books. While he does this, he is not painting—the task in which he is specialized and at which he excels. As a result, this entrepreneur produces less and we say that the size of his firm is smaller than it might be.

While all of this may seem obvious today, it was a revolutionary conclusion at the time. Businesses choose how to produce based on transaction costs. So what influences transaction costs?

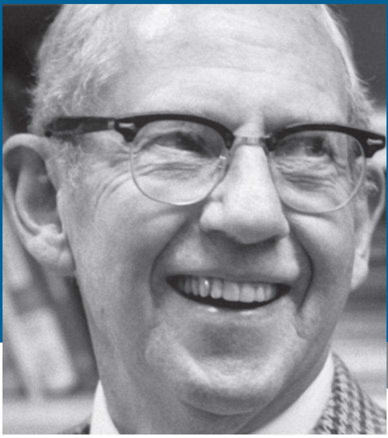
When he won the Nobel Prize in 1991, Coase declared that it is a nation's laws and institutions that determine these costs. More precisely, he spoke of the importance of well-defined property rights. If property is uncertain or the government can punish a firm by helping its main rival, transaction costs go up. A government that taxes a certain activity increases transaction costs related to this activity and encourages people to change their behaviour and/or to reduce the size of their businesses.

A painter who is self-employed and does his own accounting must reallocate time and resources toward the activity of keeping the books. While he does this, he is not painting.

Coase's work led to a revolution among economists. Douglass North, another winner of the Nobel Prize in Economics, explained that it is institutions that determine the wealth of a nation. The concept on which North based his work is that of transaction costs. Indeed, North and Coase fuelled each other intellectually over the course of their long careers. The two of them developed a rhetoric prioritizing a legal environment that minimizes transaction costs as much as possible by establishing stable property rights, low taxes, and the absence of regulations restricting trade.

Coase contributed to the science of economics on several fronts, but if we have to choose one, the concept of transaction costs is the most important. This concept can seem quite dry to some, but it is the most important pillar in understanding the importance of a free society and a non-interventionist government for economic development.


COASE



George STIGLER

When Regulation Does No Good

(1911–1991)

In the middle of the last century, Keynesianism was the dominant school of economic thought. Following the Great Depression of the 1930s, governments increased the scope of their interventions in the market, guided by the mistaken belief that the crisis had been caused by deficiencies in the capitalist system.

Starting in the 1960s, the emergence of the Chicago School helped refute a large portion of the intellectual foundations upon which government interventions were based. For example, it was demonstrated that the Great Depression was actually caused by a failure of monetary policy, and not by the market. George Stigler was among the members of the economics department of the University of Chicago. This economist, who won the Nobel Prize in 1982, made substantial contributions to his field which are felt in multiple ways throughout society today.

Stigler—not to be confused with Joseph Stiglitz, whose vision is diametrically opposed—obtained his PhD in economics from the University of Chicago in 1938. His career as an economist was interrupted temporarily by World War II, during which he joined the statistical research group of Columbia University, thus participating in the war effort. He worked then with Milton Friedman, with whom

he had studied while completing his PhD. After short stays at Brown and Columbia Universities, he returned to the University of Chicago, where he spent the bulk of his career, and also where he developed his most interesting theories.

The Father of Two Theories

Stigler is recognized as being among the first to have drawn the attention of economists to regulation. In the 1960s, he began to study its effects from an empirical standpoint, and in 1962, he published *What Can Regulators Regulate? The Case of Electricity.*

His research aimed to study the effect of regulation on the price of electricity. Stigler arrived at the conclusion that there was none. Nonetheless, he had just launched a new trend: the empirical study of regulation. A few years later, the consensus in economics was that a great many regulations are ineffective and harmful. The movement started by Stigler thus laid the intellectual groundwork for the deregulation of the 1980s. Indeed, this work contributed to his winning the Nobel Prize.

His research led him to develop the theory of regulatory capture. According to Stigler, government intervention often benefits special interests at the expense of society in general. This is due to the fact that the regulatory authorities are pressured and influenced by the industries they regulate, since those industries have a strong interest in tipping the scales in their favour. The public, for its part, has little or no interest in exerting much effort to influence the authorities.

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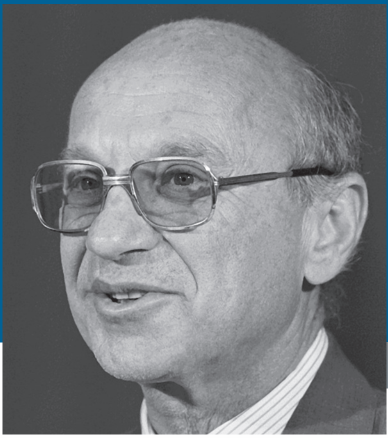
Yet this is not his biggest achievement, at least according to him. In his autobiography, Stigler says that his most important contribution is his emphasis on the role of information in the economy. This may appear to be a strange topic for a field that generally deals with dollars, but Stigler provided a convincing demonstration. He showed that the search for information involves a growing marginal cost and a diminishing marginal benefit. There is a certain point beyond which the search for information is no longer worth it, a phenomenon that explains price disparities. This theory is widely used today in the analysis of unemployment.

In addition to his breakthroughs on information and regulation, Stigler studied the history of economic thought. He also wrote one of the first modern microeconomics textbooks, *The Theory of Price*, and was a founding member of the Mont Pelerin Society, a group of intellectuals who aim to promote freedom around the world, and served as its President.

STIGLER

George Stigler was a remarkable economist for several reasons. Before his work, policies were judged by their intentions: It was taken for granted that their effects followed from those intentions. Thanks to him, we now judge a policy by its effects. Moreover, he was an intellectual who combined abstract theory with empirical rigour. Known for his tendency to use statistical data to support his ideas, for his humour, and for his captivating writing style, and admired for his contributions, Stigler undoubtedly deserves a spot among the great intellectuals of the 20th century.



Milton
FRIEDMAN

A Classical Liberal and a Class Act

(1912–2006)

Milton Friedman had an enormous influence not only on economics, but also on public policies. Describing himself as a liberal in the classical sense of the term and not in the sense of being liberal with other people's money, Friedman spent his entire life leading an intellectual campaign that put individual freedom at the forefront. He won the Nobel Prize in economics in 1976.

Born to two European immigrants in Brooklyn in 1912, Friedman had a modest upbringing. A precocious, hardworking child, he benefited from scholarships that allowed him to complete his university studies.

His experience at the University of Chicago had a significant impact on him. Friedman returned there to spend nearly 30 years teaching and developing a school of economic thought: the Chicago School of Economics. His efforts played a decisive role in discrediting the ideas of John Maynard Keynes that favoured government intervention in the economy. Friedman was at the head of a group of professors who transformed the study of economics, including Gary Becker, George Stigler, and Robert Lucas Jr. Each would go on to win a Nobel Prize.

After World War II, Friedman joined other intellectuals like Karl Popper and F.A. Hayek to found the Mont Pelerin Society. This group still meets annually, and has as its purpose the promotion of classical liberal ideas.

In the Spotlight

Friedman's public engagement reached wide visibility when he defended the capitalist system during an interview on the popular *Phil Donohue Show*. He pointed out how absurd it is to believe that the individuals who make up governments are some sort of altruistic angels who work solely for the good of society, rather than for their own interests. This is just as relevant today as it was in 1979, as evidenced by the over 2 million views the exchange has amassed on YouTube.

Friedman pursued other televised projects. The PBS network notably launched a 10-episode series entitled *Free to Choose*, dealing with subjects like the free market, consumer protection, and inequality. In 1980, he collaborated with his wife, Rose Director, to produce a book of the same name, adding to the list of books that Friedman published to reach the general public.

One of the chapters of this book looks at the matter of public schools. Accepting that education is a legitimate government function, Friedman nonetheless condemned the inequality created by the system in place, since if you live in a wealthy neighbourhood, the school will be of much higher quality than if you live in a poor neighbourhood. He proposed a system of school vouchers, whereby parents would receive from the government a sum of money for each child, which could be used to pay the tuition of any school, public or private. This would increase the competition between schools, and motivate them to improve the quality of their programs in order to attract students. Many programs of this type have since been put in place in the United States, and the results are encouraging.

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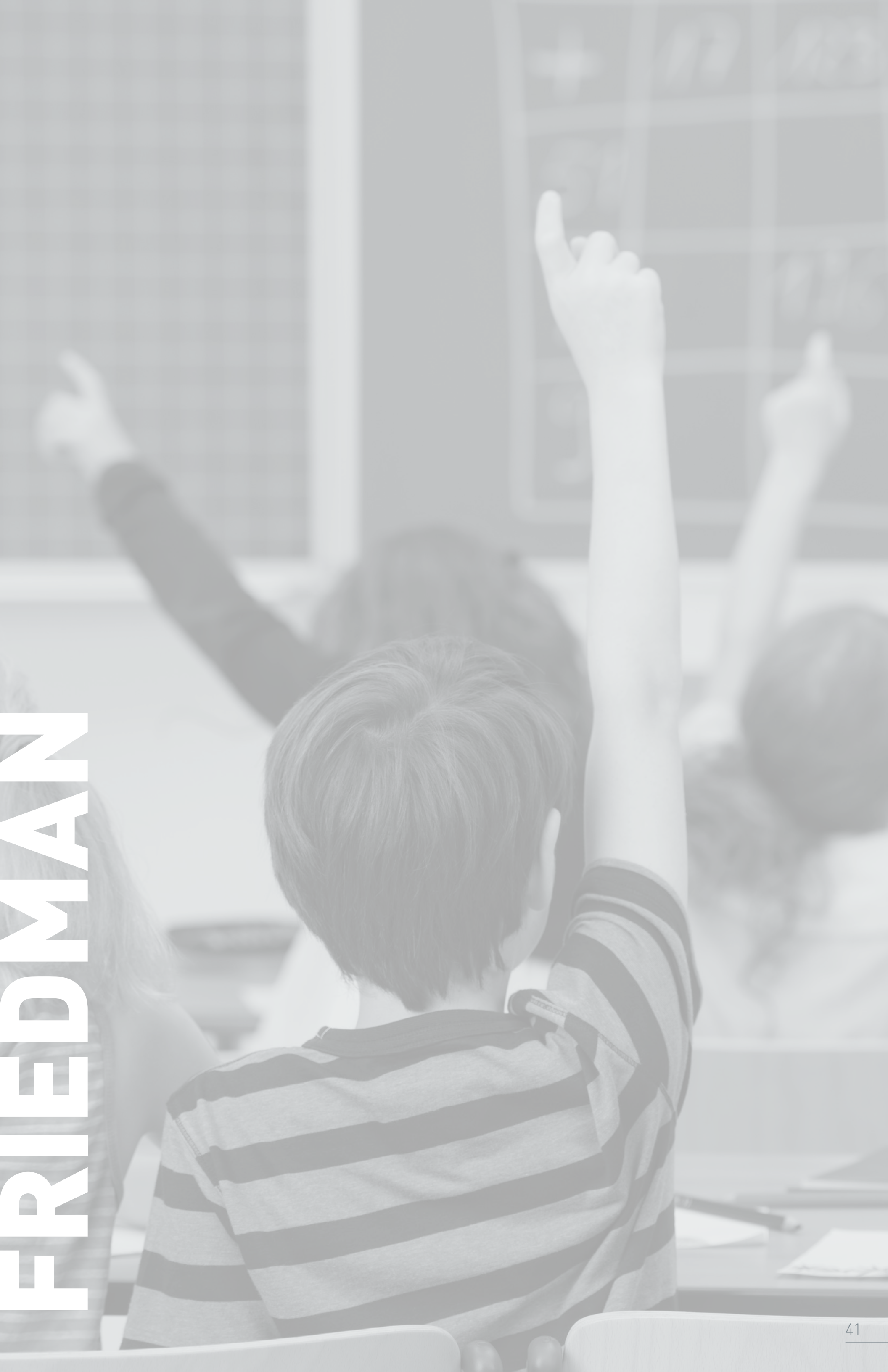
Friedman always maintained that his biggest accomplishment in the public arena was to have played an important role in the abolition of military conscription. Toward the end of the 1960s, during the Vietnam War, the debate was raging in the United States. General Westmoreland said that he did not want to command an army of mercenaries, to which Friedman responded, "Would you rather command an army of slaves?" Conscription was to him an insult to the liberty and dignity of the individual.

With the rise of protectionist and statist sentiment in Europe and the United States, when liberal ideas are increasingly being called into question, Milton Friedman's legacy needs to be kept alive.



FRIEDMAN

James M. **BUCHANAN**

Politics without Romance

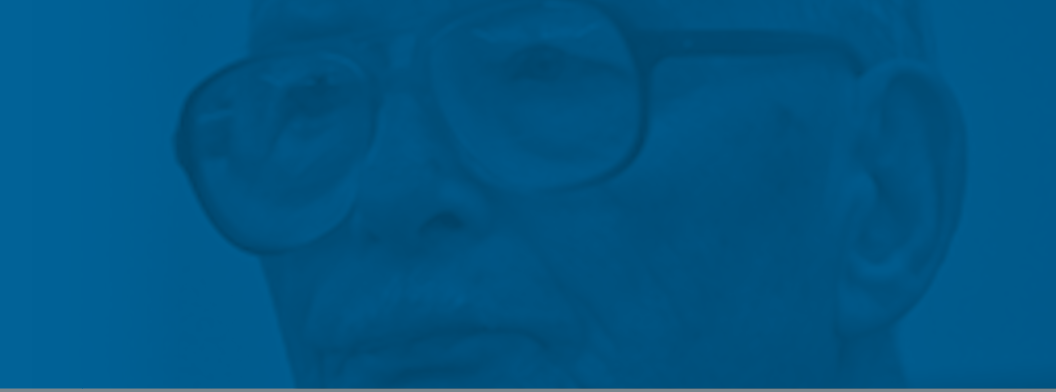
(1919–2013)

Of economists who have won the Nobel Prize, James M. Buchanan is probably among the most singular. Born on October 3, 1919, he rejected the idea that economists should be technocrats guiding government action.

After the Great Depression and World War II, Western societies were dominated by intellectual currents favouring a very substantial role for government in the economy. These schools of thought saw the role of the politician and the bureaucrat as engineers of the economy and of society (others would say technocrats—a term that was indeed coined during this period). In the same way as they had planned the economy during times of war, they would be able to plan the economy in peacetime. These schools of thought also portrayed these public actors as infallible, insensitive to external pressures, and with no individual preferences of their own, as opposed to fallible human beings whose individual decisions could lead to social chaos and crises.

Buchanan, along with his colleague Gordon Tullock, decided to challenge these ideas.

For them, politicians and bureaucrats are also fallible human beings who are motivated by their interests and preferences. They can therefore use the government for their own personal ends.



Based on this intuition, Buchanan published a series of studies that founded a new school of thought called the Public Choice School—which is to say, the study of the mechanisms of government decisions based on economic science. At the time, namely the 1960s, this was a veritable revolution in the world of ideas. The goal was scientific: recognizing that if markets can fail, so too can governments.

This reasoning was indeed revolutionary. Previously, if a market failure was identified, the automatic conclusion was that government action was needed to solve the problem, and that this intervention would necessarily be appropriate. Buchanan's thinking amounts to saying that the solution can actually be worse than the problem.

Buchanan's logic goes further than a simple *a posteriori* criticism of government action. He examined how certain societal problems could actually be caused by government action. In his magnum opus *The Calculus of Consent*, he pointed out the harmful effects of policies that favour one group at the expense of the rest.

The Dispersed Costs of Government Failure

Interest groups (like farmers' lobbies or municipal workers' unions) can achieve substantial gains by trying to influence the political authorities and get them to adopt laws that favour them.

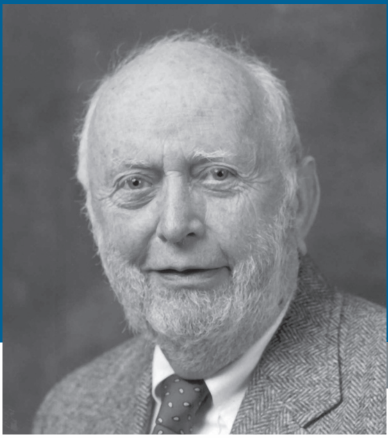
What needs to be understood—and this is an essential point of Buchanan's—is that the costs of the measures that lobby groups favour are paid by all taxpayers. As a result, the cost per person is low and dispersed among the population in general, whereas the benefits for favoured groups are high and concentrated.

Previously, if a market failure was identified, the automatic conclusion was that government action was needed to solve the problem, and that this intervention would necessarily be appropriate.

Supply management in Canada is an example of this phenomenon. For farmers, who are not very numerous, the benefits of this system amount to several millions of dollars in rents and privileges. For the very large number of consumers, the annual cost of this measure represents a little over $400 a year. This cost is certainly not high enough to get consumers to protest in the streets. However, from the point of view of the farmers, losing millions in privileges is important enough to block traffic and bring one's tractor to Parliament Hill.

Buchanan's contributions are many, and go far beyond those discussed here. His analyses were convincing enough to earn him the Nobel Prize in economics in 1986.

In analyzing our public policies in Quebec and across Canada, we should never forget these important teachings. In the end, the political process is managed not by disembodied paragons of virtue, but by normal human beings, which is to say that they are not devoid of interests, that they have individual preferences, and that they respond to the incentives in their environment.



Douglass **NORTH**

Explaining the Great Divergence

(1920–2015)

Douglass North wanted to answer the most fundamental question in economics: How is it that certain countries become rich, while in others, the material conditions of life do not improve?

Up until the Industrial Revolution, the material well-being of humanity had changed little. Life expectancy, income per capita, and quality of life had barely improved for centuries. Periods of progress were long and modest, and were generally followed by catastrophic collapse and slow, difficult recovery. Despite differences between certain regions of the world (India and China were long richer than Europe), poverty was more or less the norm everywhere.

Then, in the 17th century, the Netherlands began to distinguish itself as the first society where a much more widespread prosperity became evident among the population. Great Britain subsequently experienced its Industrial Revolution starting at the end of the 18th century. And in the century that followed, France, Italy, Germany, the Scandinavian countries, Canada, Australia, Japan, the United States, and a few other countries experienced growth that allowed hundreds of millions of people to escape from the abject poverty in which they found themselves. But why only these countries? Why did other societies, in Asia and Africa for example, have to wait until fairly recently to join these pioneers of economic growth?

Over the course of his career, the great majority of which was spent at the University of Washington, Douglass North encouraged his students to measure this “great divergence.” Many of them became historians and developed statistical series in order to measure the economies of the past. Using these data, it is possible to understand several of the reasons for the great divergence.

Here is where Douglass North made his biggest contribution. His answer can be summed up in one word: institutions.

Institutions Matter

According to North, we face constraints every day that prevent us from maximizing our well-being. In order to minimize the problems caused by these constraints, we design institutions.

Consider the case of international trade. Before the era of telecommunications, it was difficult to quickly communicate crucial information about profitable exchanges. For example, a London retailer had no simple way to confirm the honesty of a Turkish merchant (and vice versa). By developing institutions that allow them to resolve these problems, merchants can more easily engage in mutually beneficial exchanges.

There are numerous examples of this kind of institution: codes of conduct within networks of merchants who share a common religion, initiation rites to identify those who are not ready to commit themselves fully, or even private codes of law. These institutions can also take the form of laws and regulations put in place by governments. Simply put, the point of an institution is to create "rules of the game" that punish cheaters, thus allowing exchanges to take place.

If institutions guarantee the protection of private property, protect individuals from arbitrary violence, and allow prices to convey information, they will ensure considerable economic growth.

North developed this theory in a dozen books, and concluded that those societies that enrich themselves are the ones that develop institutions to allow markets to function. If institutions guarantee the protection of private property, protect individuals from arbitrary violence, and allow prices to convey the necessary information about the best uses of available resources, they will ensure considerable economic growth. If they do not manage to create this stable environment, development will not happen.

North also explained in detail how certain societies can persist in the maintenance of inefficient institutions. This happens, for instance, when an institution produces substantial concentrated gains among a small minority that has an interest in pushing for it to be maintained, whereas the costs are widely dispersed so that almost no one has an interest in opposing this institution.

When he died, North was still trying to refine certain aspects of his thought, but the essence of his theory is already widely accepted within the profession. This influence can be seen in the great popularity of the book *Why Nations Fail*, which explains the role of institutions for a general audience. Its author, Daron Acemoglu, is within the same tradition as North when it comes to theoretical approach. Clearly, Douglass North left an indelible mark on the economics profession.

Gordon
TULLOCK

Using Economics to Explain Politics

(1922–2014)

Gordon Tullock may not have won the Nobel Prize, but for someone who took just one economics course during his university training, his surprising contribution to the field places him among the ranks of the great economists. Indeed, the renowned professor devoted the majority of his career to the advancement of economics, more specifically the application of economic theory to non-market areas in order to explain certain human behaviours.

Tullock obtained a Juris Doctor degree from the University of Chicago in 1947, and then briefly practised law before joining the US Foreign Service. After a first posting in China, he studied the language and the culture at Yale and Cornell before being sent to Hong Kong and Korea. Tullock left the Foreign Service in 1956 to devote himself to his real passions: research and teaching.

He first taught in the department of international studies at the University of South Carolina, where he published a first edition of *The Politics of Bureaucracy*. It is his early work on the significant communicational problems within large centralized bureaucracies that led Tullock to collaborate with James M. Buchanan. The two shared an interest in using economic theory to explain political and social phenomena.

Public Sector Angels?

In 1962, the two professors together published *The Calculus of Consent: Logical Foundations of Constitutional Democracy*, the seminal work of a new school of thought: the Public Choice School. In this book, Tullock and Buchanan applied economic analysis to decision-making by agents in the public sector in order to demonstrate that they are not angels devoid of personal interests. At the time, government was seen as a benevolent entity that acted solely in the interest of the public good. The two collaborators rejected this conception of the state, declaring that the foundations of human behaviour do not change when one ascends to a position of political power. Buchanan received the Nobel Prize in economics in 1986 for his contribution to the Public Choice School, an honour not extended to Tullock.

Public choice theory, which seeks to apply economic theory to non-market fields and phenomena, is the basis of Tullock's work. Indeed, the author and professor made a sizable contribution to political economy in general. He is moreover the author of the first work on the theory of rent-seeking. His article "The Welfare Costs of Tariffs, Monopolies, and Theft" (1967) introduces what is now known as the "Tullock Rectangle." Taking up Arnold Harberger's idea of the deadweight social loss entailed by the presence of a monopoly in a sector, Tullock showed that the monopolistic company also wastes resources in order to obtain legal and regulatory protections, expenditures that entail no productivity gains.

Related to his work on rent-seeking, Gordon Tullock noticed an important paradox. He described it as the relatively low cost of lobbying activities compared to its astronomical gains. According to him, the fact that politicians need funding for their partisan activities and their re-election opens the door for their funders to ask for a return on their investment in the form of measures that favour their businesses.

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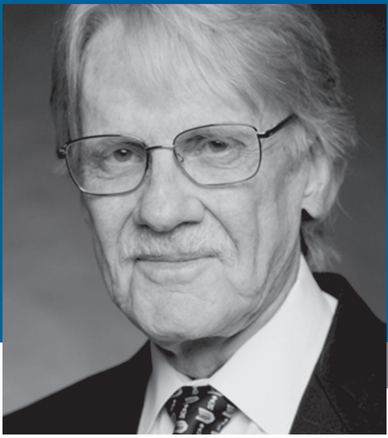
Voters Behaving Badly

Besides political economy, Tullock was also interested in electoral behaviour. Indeed, he explained that individuals' motivations to vote could not be purely rational. According to him, people know that the chances that their vote will have any impact whatsoever on the result of an election are infinitesimally small. For this reason, he posited that their motivations must be more moral than rational, and that individuals do not automatically become informed or interested simply because they choose to vote.

Finally, Tullock made an important contribution to the redefinition of the study of law, then mainly consisting of the perspective of moral philosophy, as a field that could be studied with the help of economic theory. His book *The Logic of the Law* remains an indispensable reference to this day.

The theories put forward by Gordon Tullock can still help us understand and explain observable phenomena today. This is the case, among other things, of rent-seeking in certain sectors of the Canadian economy, like the agricultural sector, where supply management protects producers of milk, eggs, and poultry.

In the end, it is difficult to characterize the scientific legacy left by this professor of law and economics. A prolific, self-taught author, he wrote more than 150 articles and published or co-published nearly 40 books during a university career spanning over 50 years. He may not have won the Nobel Prize like his close collaborator James Buchanan, but his contribution is no less impressive.



Vernon **SMITH**

Proving Adam Smith

(1927–)

For a long time, laboratory experiments were excluded from the economic toolkit, economists preferring natural observation and theoretical and statistical research.

All of that changed thanks to Nobel Prize winner Vernon L. Smith. Born in Kansas in 1927, he grew up during the Great Depression. An electrical engineer, he developed a passion for economics while completing his bachelor's degree. After a master's at the University of Kansas, he obtained his PhD from Harvard in 1955. He began teaching at Purdue University the same year.

Smith taught microeconomics, but realized that he had difficulty conveying its basic concepts. How could he explain to students the way a market can arrive at equilibrium without the intervention of a central authority? Smith decided to organize an experiment to show students the workings of the market mechanism.

His first experiment was relatively simple. He started by modelling on paper the supply and demand situation and found what, in theory, the equilibrium price and quantity should be. He then divided his class into buyers and sellers.

Sellers received cards showing a production cost. They had an interest in selling their goods at the highest possible price, since they would pocket the difference between the price and the cost of production. Buyers, for their part, received a resale price. They had an interest in buying goods at the lowest possible price. The interests of buyers and sellers thus conflicted. What happened when the two groups tried to engage in trade? The price at which the students concluded their transactions turned out to be the same in the experiment as in the professor's calculations, namely the equilibrium price.

This was a moment of revelation for the economist. For one thing, he had just conducted one of the first controlled experiments in a field where the consensus was that experiments were not possible. (The first economic experiment is attributed to Edward Chamberlin, a few years before.) For another, he had just demonstrated Adam Smith's invisible hand in an experimental environment. This theory, developed 200 years earlier, states that an individual pursuing his own personal interest under a system of voluntary exchange ends up serving the common good. This was illustrated in the experiment by the fact that buyers and sellers trying to obtain the lowest and the highest price respectively came to discover an equilibrium price, which optimizes the use of resources. In sum, Smith proved Smith.

Vernon Smith continued his experiments by varying his procedures. In 1962, he published *An Experimental Study of Competitive Market Behavior*, which detailed his experiments and his method. Experimental economics thus began to take form as a branch of economics. Smith pursued his research, and in 2002 he received the Nobel Prize in economics "for having established laboratory experiments as a tool in empirical economic analysis, especially in the study of alternative market mechanisms."

An Impressive Heritage

Experimental economics today is applied to the analysis of the effects of regulation on behaviour, the study of auctions, the development of market solutions for the provision of public goods, and the study of asset bubbles, among other things. Moreover, experimental economics played a big role in the development of behavioural economics. This branch blends psychology and economics to study human behaviour in economic situations.

Adam Smith's invisible hand states that an individual pursuing his own personal interest under a system of voluntary exchange ends up serving the common good.

The introduction of the experimental method in economics is without a doubt this thinker's most important accomplishment, but it's far from the only one. Smith also developed a combinatorial auction system, which improved the efficiency of the process of selling airport landing and takeoff rights. He was involved in Australia's electricity privatization process as a consultant. He worked on more than 200 academic research projects, dealing with experimental economics, but also with finance and natural resources. For his accomplishments, he was named Distinguished Fellow of the American Economic Association in 1992, a very prestigious title.

Vernon Smith is still involved in the world of academics. Thanks to him, economics today has an additional empirical tool in its arsenal, as well as a deeper understanding of the link between human behaviour and the market mechanism.

Israel
KIRZNER

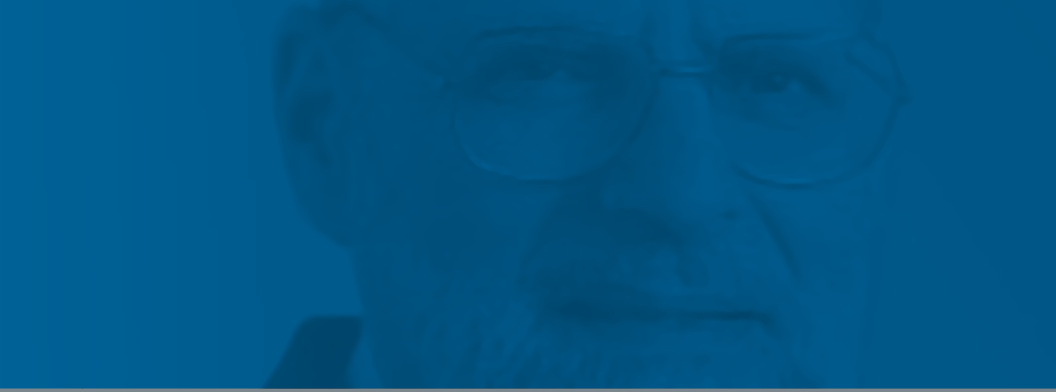
The Vigilance of Entrepreneurs

(1930–)

Israel Kirzner is the most prestigious living Austrian school economist. Born in 1930, he is the direct descendent of a line of economists belonging to the school founded by Carl Menger in 1871.

His life has been marked by a clear passion for trying to understand how markets work. He was born in London, the son of a rabbi, and was himself ordained a rabbi. He studied in South Africa before immigrating to the United States, where he has spent most of his career. He studied economics under the direction of one of the main Austrian thinkers, Ludwig von Mises, who supervised his doctoral thesis. Kirzner had the originality and the courage to enrich his analysis with contributions from the other social sciences in the face of the growing mathematization of economics.

He transmitted his passion through teaching: He taught and supervised doctoral theses for more than thirty years at New York University, where he remains Professor Emeritus. He is a mentor to most of the members of the young guard of economists contributing to the dissemination of Austrian ideas today like Peter Boettke and Mario Rizzo.



His work extended that of, among others, Friedrich Hayek, who saw the market not as a machine that would automatically adjust itself, but rather as a discovery process. Whereas followers of orthodox economics (the so-called neoclassical school) believe that supply and demand adjust themselves mechanically, Austrians reject this analysis, for it does not take into account the passage of time and the fact that market actors possess imperfect information. The market tends toward equilibrium between supply and demand, but is never in perfect equilibrium. It is these imperfections that constitute profit opportunities waiting to be discovered.

On the Lookout

Israel Kirzner thus introduced a central actor at the heart of economic analysis, astonishingly neglected by the rest of the field: the entrepreneur. Where Joseph Schumpeter drew attention to the entrepreneur's role as innovator, Kirzner saw the entrepreneur as the key player in market adjustments. Entrepreneurs are vigilant, always on the lookout for profit opportunities and finding new ways to provide goods and services using untapped resources. They are not rational robots and they do not always have all the information they need. Often, they take risks and have to anticipate future needs. Indeed, Kirzner's book *Competition and Entrepreneurship*, published in 1973, is an indispensable academic reference for understanding the role of the entrepreneur in a market economy.

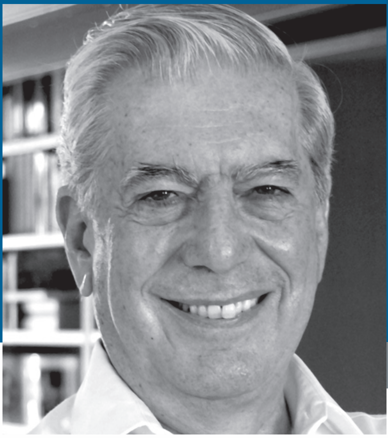
If, as a producer, I propose a product that no one wants, I go out of business. Conversely, if I introduce a new good that benefits everyone on a daily basis, there's a good chance that I will make money.

The market is an ongoing process of trial and error within which producers try to discover, on the one hand, the various preferences of consumers, and on the other hand, the best ways of combining resources to supply consumer demand at the lowest cost. It facilitates the circulation of information about individual preferences and the scarcity of resources.

The market economy thus allows us to distinguish those actions that benefit the greatest number from those that do not. There is a selection mechanism involved. If, as a producer, I propose a product that no one wants, I go out of business. Conversely, if I introduce a new good that benefits everyone on a daily basis, there's a good chance that I will make money. The market is the best system for increasing the well-being of all thanks to its incentive structures that orient market actors toward productive behaviours.

Israel Kirzner's analyses of the market and of the role of the entrepreneur have provided a moral justification for the market economy and its two essential components: profit and entrepreneurs. Profit plays a social role by encouraging entrepreneurs to produce things people want. They have a moral right to collect the fruits of their labour because of the benefits they provide for society as a whole.

The intellectual contribution of Israel Kirzner is not limited to his own research. He also taught generations of students about the Austrian school tradition. He did so through various channels: his lectures (some of which can be viewed online), his biography of Ludwig von Mises, and his articles explaining the originality of this school. His ideas are more relevant than ever today, among other things in explaining the development of the many new information technologies that are not the work of bureaucrats, but of entrepreneurs having taken risks in order to find new ways of meeting our communication needs.



Mario
VARGAS LLOSA

Most of Latin America Has Adopted Democracy. Will Cuba?

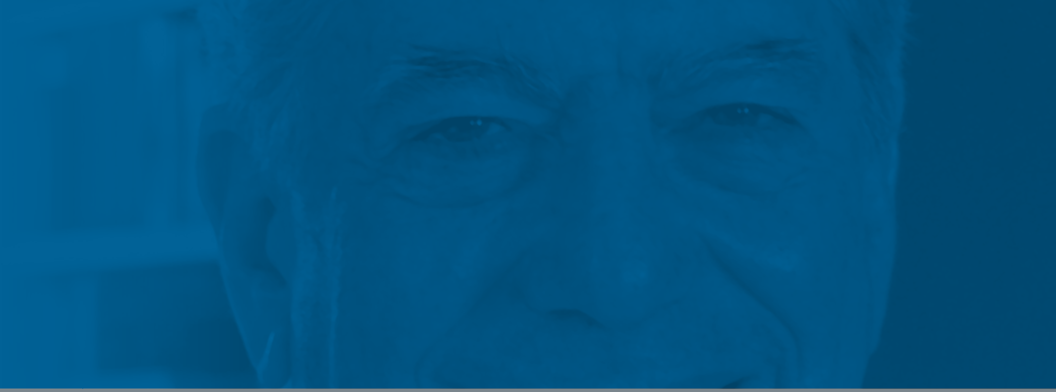
(1936–)

Mario Vargas Llosa is one of the greatest writers of our time, whose collection of novels earned him the 2010 Nobel Prize in Literature.

He's also someone with the curiosity and the intellectual courage to change his mind when faced with evidence that contradicts his beliefs, as detailed in a trilingual booklet entitled *My Intellectual Journey: From Marxism to Liberalism* that was published by the MEI in 2014.

That booklet is based on a very moving and fascinating talk Mr. Vargas Llosa gave in Montreal the year before at an MEI gala event, in which he explained how he came to be an admirer at one time of Fidel Castro's Cuban experiment, as were many Latin American and other intellectuals of his generation. Understandably, though, his enthusiasm began to wane somewhat when he learned of the concentration camps to which were sent a mix of dissidents, common criminals, and homosexuals.

Indeed, he met Castro in the 1960s along with a group of a dozen other writers in order to protest these unjust incarcerations. He was very impressed by the man, describing him as a force of nature on



account of his ability to speak, with such dynamism and contagious enthusiasm, practically uninterrupted for twelve solid hours, barely pausing to take a breath or to let anyone else have a turn. He was impressed, but not convinced.

He also visited the Soviet Union in 1966, which disillusioned him further with Marxism. What he discovered was a country where the distance between the powerful political elite and the powerless majority was even greater than in Latin America, and where a person needed a visa just to travel to another city.

Embracing Freedom

In addition to seeing the failures of Cuba and the U.S.S.R. firsthand, he was also influenced by the works of numerous thinkers and philosophers. Raymond Aron's *The Opium of the Intellectuals* was particularly important in helping him understand the seductive appeal of Marxism for writers, artists, and intellectuals, as were Isaiah Berlin's biography of Marx and Karl Popper's *The Open Society and Its Enemies*, and works by other towering figures of the 20th century such as André Gide and George Orwell. These authors also introduced him to a different vision, one of tolerance, democracy, and the importance of freedom, including economic freedom, for achieving any kind of progress.

But some intellectuals, including some here in Canada and Quebec, have refused to face the facts, and so have not undergone this kind of intellectual journey. Instead, they continue to sing the praises of a Caribbean island prison from which thousands of people still attempt to flee by homemade raft every year, a perilous journey that an estimated one in four do not survive. To be a fan of the Cuban experiment when it started in the early 1960s is one thing, but how blinded by ideology do you have to be to remain a Castro booster over 50 years later?

An admirer at one time of Fidel Castro's Cuban experiment, his enthusiasm began to wane somewhat when he learned of the concentration camps to which were sent a mix of dissidents, common criminals, and homosexuals.

Thankfully, by and large, the countries of Latin America have outgrown the brutal and corrupt military governments that were still the norm a few decades ago, which is why it is now possible, according to Mr. Vargas Llosa, to be optimistic about the future of this part of the world. Though still very far from the ideal, countries like Chile, Columbia, Peru, Brazil, and Mexico have adopted political democracy and market economics, and are moving forward because of it. With any luck, Cuba's dictatorship will also soon crumble, and at long last allow its people to live in freedom.

VARGAS LLOSA

Deirdre McCLOSKEY

Explaining the Great Enrichment

(1942–)

Whether delving into her impressive academic career or the personal battle she led to assert her dignity, Deirdre McCloskey's story is a fascinating one. Her intellectual body of work is impressive, and her fight to stand up for her rights is inspiring.

McCloskey was born Donald McCloskey in 1942. The young man studied economics at Harvard, where he obtained his bachelor's degree and then his PhD in 1970. Very quickly, he emerged as a brilliant economist. His doctoral thesis was published in the *American Economic Review*, a prestigious journal.

In the 1980s, McCloskey turned to a little-studied topic in economics, namely rhetoric. In 1985, he published *The Rhetoric of Economics*, which achieved rapid success. This work was the first in a series of books on economic writing and argumentation. McCloskey's works are widely used today as guides for the writing of economic texts, theses, and studies, as well as for the construction of arguments.

After rhetoric, McCloskey turned to the causes of growth. This time, the economist looked at non-material factors. The main school of thought in economics at the time strongly emphasized material factors: capital, productivity, and technology. Bucking the dominant

trend, he launched the idea of the importance of values, of ideas, and of virtues in economic development: the importance of the non-material in explaining the material.

These ideas would get fleshed out later in *The Bourgeois Era* trilogy, published in 2006, 2010, and 2016. Critically acclaimed, the trio of books explains how the renewal of bourgeois values in the 17th and 18th centuries, much more than economic or material factors, encouraged innovation, entrepreneurship, and wealth creation. The expansion of the bourgeoisie that accompanied capitalism enabled the spread of these values.

A Personal Transformation

In 1994, Donald decided to become Deirdre. The three-year journey was not without its difficulties. Her sister, thinking that Deirdre would regret her choice, fought constantly to cancel her cosmetic surgeries. Deirdre also had to meet with numerous psychiatrists who treated her as if she were suffering from a mental illness. The economist spent tens of thousands of dollars in medical fees, as the surgeries were not covered by insurance.

Deirdre had to travel to the Netherlands to follow a gender reassignment program including surgery, hormones, and therapy. This was fitting in a way, given that the economist identifies tolerance as one of the bourgeois virtues that helped the Netherlands start becoming a wealthy country several centuries ago. Her book, *Crossing: A Memoir*, published in 1999, tells her story.

It is this same tolerance, which to varying degrees characterizes all Western liberal societies today, that has allowed Deirdre to get back to her work and her normal life. Liberalism in the classical sense means free markets and free enterprise economically speaking, but also individual freedom and tolerance regarding the choices of each individual socially speaking. Despite the obstacles, soon after her transition, the economist felt accepted and recognized as a woman by her academic entourage and by the media. When Donald announced his decision to become a woman to the university's dean, the dean said he was actually relieved, having thought that he was going to announce that he had become a socialist!

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It would be impossible to discuss all of McCloskey's intellectual exploits. She has published more than 400 articles and 17 books. She has done research on economic history, the misuse of statistics, the philosophy of the social sciences, and the application of econometrics to history, among many others. Her CV is over 18,000 words long. She has received six honorary doctorates.

She has taught economics, English, communication, and history. McCloskey describes herself as a libertarian. Her work on the impact of culture on growth is considered her magnum opus (among many other works).

Deirdre McCloskey remains active in the university world. She teaches several different subjects at the University of Illinois at Chicago. A proud defender of the free market, and of the rights of gays, lesbians, and transgender people, the academic is in high demand for interviews and conferences—with good reason, since her intellectual and personal journey make her a unique, exceptional woman.

Lawrence H.
WHITE

Currency Competition for a Prosperous Economy

(1954–)

Every day, we use money and engage in transactions, without necessarily asking ourselves how the monetary system works. The notion that it depends on government is rarely called into question in modern society. Yet certain serious economists think that this governmental control is very harmful to the economy, and that it would be preferable if the currency were managed privately.

This is notably what Nobel Prize-winning economist Friedrich Hayek defended in a small book devoted to the issue (*The Denationalization of Money*, 1976). But the credit for having made this idea respectable goes to economist Lawrence H. White, who has shown through historical examples how free banking could exist, without government interference. His articles on banking and monetary history have been published in the most prestigious journals and have challenged the very foundations of central banking.

The basic idea White developed is that central banks, which depend on government, introduce imbalances into the market for bank loans, and this creates harmful economic distortions; they create instability for economic actors, and irresponsibility among bankers, since the value of a given currency ultimately depends on the central bank. Conversely, in a free banking system, there would

be competition between banks, in which the most responsible (those that manage their clients' money with care) would see their currency be more widely used.

Indeed, as in other sectors, competition ensures that companies offering good services (in this case, a stable currency) drive out the bad. In a competitive system, banks have every reason to reinforce confidence and properly manage their clients' money, or they will lose them as clients. The currencies offered by banks would be convertible into precious metals (like gold, whose price varies little). According to Lawrence White, the economy would be more stable with such a system.

The History of Free Banking

In one of his books, he recounts that during a certain period (1716-1844), in Scotland, banks operated freely and completely independently. Scotland enjoyed a remarkable economic situation, and very stable currency, during this period. This was not the case in the United Kingdom, where banks were highly dependent on the Bank of England and its policies, and where there were more bank failures and greater monetary instability. Lawrence White also made an important contribution to the history of economic thought by showing that, until the 19th century, there was a school of thought in England that defended the free banking system.

The economic and financial crisis of 2008 gave renewed relevance to White's theses. According to him, the Great Recession is related to the various currency manipulations of central banks, which contributed to the irresponsibility of banks. The imprudence and errors of some were encouraged by a policy of easy credit that fuelled an excess of non-viable investments in certain sectors. Among other things, White assessed the performance of the American central bank (i.e., the Federal Reserve), since its creation, and observed that there had been more monetary and macroeconomic instability during its existence than in the decades preceding it.

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The Fed notably failed to achieve one of its primary purposes: price stability. Indeed, the purchasing power of the dollar has fallen since the 1970s (when dollar convertibility to gold ended) due to inflation, and the evolution of prices has been unpredictable. Recessions are now longer and deeper. They have not reduced the frequency of banking crises—quite the contrary. For this reason, Austrian school economists like Lawrence White think that the 2008 crisis offered an opportunity to propose alternative solutions to the current banking system that would probably have achieved better economic results.

White thinks that we could return to a free banking system in order to avoid new crises in the future. He also recently took an interest in cryptocurrencies like Bitcoin, which he considers to be a kind of private currency providing an alternative to the public currency monopoly. This is very timely given that in certain countries like Venezuela, a growing number of people are turning to cryptocurrencies, which are seen as more reliable than the money printed by their government.

Peter **BOETTKE**

The Modern Face of the Austrian School of Economics

(1960–)

There are many schools of thought in economics—so many, in fact, that it can get a little confusing: Keynesianism, monetarism, supply-side economics, public choice theory, the Austrian school, and others confront each other in an intellectual struggle. These debates have created a misperception of economics as a field that never reaches consensus, even though most economists agree on a great many things, such as the benefits of free trade.

One of these great schools of thought is the Austrian school, which dates back to 1871. It was founded by Carl Menger, and then developed and popularized by great economists like Ludwig von Mises and Friedrich Hayek, each the subject of an earlier chapter in this booklet.

This school has helped advance our understanding of economics thanks to their development of several important concepts, such as the subjectivity of value and marginal analysis, which are now integrated into modern economic theory. The proponents of the Austrian school were also the first to have anticipated the inevitable failure of centralized planning in the Soviet Union.

However, the Austrian school has been quite marginalized over the past few decades, insofar as it diverges from the main or popular currents of thought in academic circles. One reason is its rejection of the mathematical models which are such a prominent part of contemporary economics. Austrian thinkers see the economy not as a machine, but as a complex system. From their perspective, the study of economics is more akin to philosophy or psychology than to physics or engineering.

Does this make the lessons of the Austrian school less relevant? Do its theories still have a place in the academic world? The example of Peter Boettke leaves little doubt that they do.

Austrian and Multidisciplinary

Professor of Economics and Philosophy at the well-known George Mason University, Peter Boettke mixes Austrian economics with other schools of thought, such as public choice theory and institutional economics.

He is known as someone who loves to share his passion for economics, and he does so in a number of ways: supervising theses and dissertations, inspiring the next generation, giving lectures and interviews, and writing books. He describes his most popular book, *Living Economics: Yesterday, Today and Tomorrow*, as a work designed to show the beauty of economic study and to inspire those who are interested in the subject.

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Boettke is also the author of some 250 studies, including a recent Research Paper he co-authored for the MEI entitled *How to Foster Entrepreneurship in Canada: The Teachings of the Austrian School of Economics.* At the beginning of his career, he worked extensively on the Soviet economy and its collapse. His work now covers a range of fields: political economy, methodology, past thinkers, the role of institutions in economic development, and so on. He is also actively involved with the Mercatus Center, a think tank based at George Mason where he serves as Director of the F.A. Hayek Program for Advanced Study in Philosophy, Politics, and Economics. Finally, he is a past president of the Mont Pelerin Society, a prestigious international association of pro-freedom intellectuals.

Boettke works in a very special environment for an economist. Recognized as having a unique approach, the Economics Department at George Mason University has been home to two recipients of the Nobel Memorial Prize in Economics: James M. Buchanan, one of the founders of public choice theory, and Vernon L. Smith, a pioneer in experimental economics. It is therefore a place where public choice theory, experimental economics, and the Austrian tradition merge. The result is a rather particular view of the economy that is not found anywhere else. It is this way of thinking, outside of the established framework, that the department is famous for.

While central banks around the world are trying to emerge from a decade of unconventional monetary policies, it is quite possible that Austrian theories on currency and economic cycles could enjoy renewed popularity. Uncertain economic conditions raise questions, and the answers are sometimes found in the ideas of thinkers from past centuries. Those developed by Menger, Mises, and Hayek, and now carried forward by Peter Boettke and several others, will certainly demonstrate once again how relevant they are.

Ideas for a More Prosperous Society