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BANKNOTES

NELSON NASH MONTHLY NEWSLETTER

IBC and Constant Compounding

by Robert P. Murphy

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A common method of showing the public the power of Nelson Nash's Infinite Banking Concept® (IBC) is to stress its feature of "constant compounding." In contrast to many other asset classes, dividend-paying Whole Life insurance always increases in value. Indeed, some proponents of IBC enthusiastically declare: "There's nothing else like it!"

In this article I will explain what Nash's fans have in mind. As we will see, there really is something special about IBC; it allows households and business owners to enjoy "constant compounding" in a very safe and convenient way, which *cannot* be matched by other (standard) assets. However, as with most claims, there are some caveats involved (particularly the interest accruing on outstanding policy loans), and I want to make sure the readers of the *LMR* understand all of the nuances on this powerful topic.

IBC AND POLICY LOANS: THE BASICS

In order to focus on the specific issue of constant compounding, I am going to assume in this article that the reader has a basic familiarity with IBC as a cashflow process, and how it uses a dividend-paying WholeLife insurance policy as the platform for implementing it. For those readers who need this foundation in a quick way, I refer you to the podcast series that Carlos and I produce, in particular episodes 17, 18, and 19.¹ For those willing to put in more time, there is no substitute for reading Nelson Nash's classic book, *Becoming Your Own Banker*.

For our purposes in this article, let me review the essential mechanism: A dividend paying Whole Life insurance policy comes with built-in, contractual guarantees on the growth of the "cash surrender value." This is the amount that the life insurance company will give the policyholder if he or she decides to collapse ("surrender") the policy and stop making premium payments. Of course, this dollar amount is lower than what the *death benefit* would have been, if the insured party had died, but with large policies the cash surrender value can grow quite large. Intuitively, it is how much the life insurance company is willing to pay the policyholder to "walk away"

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from the contract, letting the insurance company off the hook from having to pay the looming death benefit (which gets closer every passing day, since the insured person will eventually die or reach the age—such as 121 years old—at which the contract matures).

Now rather than surrender the policy outright, a policyholder who needs money has another contractually guaranteed option: He or she can take out a *policy loan*, up to (almost) the cash surrender value. It's important to understand exactly what is happening here: The policy loan is a loan *made on the side*, from the life insurance company to the policyholder. It does not directly involve the life insurance policy itself; the customer isn't "taking money out of the policy." Rather, the life insurance company is simply directing some of its outgoing cashflows—which it otherwise might use to buy corporate bonds or other assets—into loans to its own customers.

These policy loans are actually *the safest investment possible* from the life insurance company's point of view, because the company itself is guaranteeing the underlying *collateral* on the policy loans: namely, the cash surrender value of the policies in question. Even if the borrower (i.e. the customer who is requesting the policy loan) never pays a penny on the outstanding policy loan, the life insurance company has no worries. The outstanding policy loan rolls over at compound interest (according to the interest rate on the policy loan, which is itself determined by a contractually-fixed formula), and it eventually gets "paid back" either when the insured dies or reaches the maturity age and the contract ends.

A CAR EXAMPLE

For example, suppose a fan of Nelson Nash has begun implementing IBC in his personal life, and is making large premium payments into a properly designed Whole Life policy. When it's time for this man to buy a new car, he doesn't need to rely on financing from the dealership or an outside lender. Instead, the man takes out a policy loan for (say) \$25,000, and pays the full purchase price to the car

dealer to buy the car outright on the spot.

Now even though the man wrote one big check himself from the perspective of the car dealership, in reality the man obtained the financing for his purchase by borrowing *against* the cash surrender value in his well-funded IBC policy. In order to play "honest banker" with himself, the man starts making (at least) the same monthly "car payments" to the life insurance company, as if he had borrowed from a traditional lender and had to make car payments at a standard interest rate.

However, even though the man intends on mirroring the same cashflows doing it the IBC way, in reality he is much more secure and can sleep soundly at night. If he suddenly loses his job, he has the option of *not* making his "monthly car payments" to the life insurance company. His outstanding policy loan of \$25,000 *won't* get knocked out, and instead it will keep growing at interest.

Yet to repeat, the life insurance company has no problem with this scenario. It *won't* send repo agents to seize the car. Remember, legally speaking the man *bought the car outright from the dealership*. The car is *not* the collateral on the policy loan; his life insurance policy's cash value is.

Suppose the man never makes a payment, and the policy loan grows to (say) \$40,000, many years later. Further suppose the man dies of a heart attack, and at this point the death benefit on his policy is \$500,000. In this case, his named beneficiary (let's say it's his widow) only gets a check for \$460,000. This is because the life insurance company first "pays itself back" for the full value of the outstanding policy loan, before sending what it owes to the beneficiary.

I hope this simple example illustrates the advantages of financing major purchases with IBC (rather than traditional lenders), but also clarifies why the life insurance companies agree to this arrangement which at first seems too good to be true to some members of the public.

PAYING CASH VERSUS CONSTANT COMPOUNDING

The fans of IBC will often bring up the special

feature of “constant compounding” when contrasting the virtues of their approach with the strategy of “paying cash” for big purchases. In this section, I’ll explain what the fans of IBC have in mind with this discussion.

Imagine a woman who follows a very conservative approach to money. She has been taught to avoid debt, and to only buy things “that she can afford.” Consequently, if this woman wants to buy a \$25,000 new car every few years, she sets up a sinking fund using certificates of deposit (CDs) issued from her local bank. (Alternatively we could imagine her putting money into a bank savings account, a money market mutual fund, etc.)

What happens is that the woman first figures out what (after-tax) interest rate she is likely to earn on her very conservative investment in bank CDs. Then, using an amortization calculator, she figures out how much money she needs to put into the sinking fund every month, so that when it’s time to buy a new car, her growing stash of CDs has a total market value of \$25,000 (less whatever trade-in value she’ll get for her used car at that point).

This is a very conservative approach, pushed by the likes of “get out of debt” gurus such as Dave Ramsey. Compared to the typical American who “lives beyond his means” by running up credit card and other types of debt in order to fuel consumption, our hypothetical woman is behaving very responsibly.

However, the fan of IBC might point out to the woman that her strategy involves draining out her wealth fund every time she buys a new car. In other words, the value of her “car fund” grows over time, but whenever it hits \$25,000, she redeems her bank CDs and hands over the \$25,000 to the car dealer. At that point, the woman has no financial assets due to this enterprise, and she must start over from \$0. In particular, the woman certainly can’t earn interest income on her previous contributions into the “car fund,” because that money is now gone forever—it was handed over to the car dealer.

In contrast, suppose the woman avoided bank CDs

as her financial vehicle, and instead built up a well-funded dividend-paying Whole Life insurance policy. So long as she kept making the premium payments, this policy would continue to grow over time, with an ever-higher cash surrender value *and* death benefit (if designed according to IBC principles). When it was time for her to buy a new car, the woman would not “take money out of the policy”—the way she might cash in CDs or write a check drawn on a bank savings account—but instead she would take out a policy loan against the cash surrender value in her policy. The life insurance policy would not “fall in value” because of this move; it would keep chugging along on its own,² with the outstanding policy loan merely representing a lien against this asset.

AN ANALOGY WITH HOME EQUITY LOANS

In order to comprehend what’s happening, it might help to use an analogy with home equity loans. Suppose our hypothetical woman never heard about cash-value life insurance, and she had been building up her bank CDs in the fashion that her very conservative parents had taught her.

At the same time, she also owns a paid off house. (Remember, she avoids debt as a rule.) In Year 1, the house had a market value of \$100,000. In Year 2 it rose to \$105,000. In Year 3 it was \$110,250, and so on. Every year, the house tended to rise about 5 percent in market value.

Now it was time for the woman to buy her new car, for \$25,000. She originally planned on cashing in all of her bank CDs, depleting her sinking fund down to \$0. But her friend points out that she could alternatively take out a home equity loan against the value of her house. In this case, she could still buy the car outright—there would be no lien against the automobile—with the equity in her house serving as the collateral. With this approach, the woman could retain her stash of bank CDs, which would continue to appreciate at the interest rate the bank offered.

Furthermore, *the house itself* would also continue to appreciate in market value, so long as real estate kept rising. In other words, the market value of

the woman's house would not be "dragged down" because she decided to borrow against it, in order to finance the new car purchase. It is crystal clear that the market value of her home is a completely separate concept from the outstanding value of the home equity loan she takes out from the commercial bank.

In this context, the woman's friend might point out to her, "If you cash out your bank CDs, you will stop earning interest on them. But if you finance your new car purchase by borrowing against the equity in your house, then you continue to earn the CD interest *and* you still reap any appreciation in real estate on your house."

I hope that this analogy with a home equity loan sheds light on what is happening if the woman instead turns to a well-funded Whole Life policy. By obtaining the \$25,000 from a policy loan, she doesn't need to "draw down" any of her other assets, and even her life insurance policy continues to chug along (subject to the technical caveat about "direct recognition" discussed in endnote 2). *This* is what fans of IBC have in mind when they warn people that "paying cash" for car purchases and other major expenses means that they will lose out on the ability to continue earning interest on their savings.

Before leaving this section, let me address one loose end: If I can use an example of a home equity loan to illustrate the broad principle, why then do IBC fans insist that "there's nothing else like this" in the financial world? Why not, for example, just tell people to use home equity financing rather than building up a Whole Life insurance policy?

The crucial difference is that *the real estate market could collapse*. This is why a commercial bank will *not* grant home equity lines on the same terms that a life insurance company will use for a policy loan. In particular, if you apply to a bank for a home equity loan, it is a laborious process, where the bank will check your credit score and your income, it will ask what you are doing with the loan, and it will insist on a timely repayment schedule. The life insurance company does none of this. They simply check what

your unencumbered cash surrender value is, in order to determine how much of a policy loan you can borrow.

The check can literally be in the mail the next business day, and—to repeat—the life insurance company doesn't care what payback schedule you adopt, *if any*.

In light of these considerations, we can understand the enthusiasm of the fans of IBC, and why they insist that there is no other financing mechanism available that can match the process developed by Nelson Nash.

DON'T FORGET ABOUT POLICY LOAN INTEREST!

Before closing this article, it is important for me to address the issue of policy loan interest. It would be very misleading to tell the public about the virtues of constant compounding *without* keeping track of the corresponding liability due to the policy loan.

The best way for me to illustrate the problem is to contrast Sally, who is going to "pay cash" for a car using a sinking fund, with Jim, who is going to take out a policy loan from a life insurance policy. In this example, we will see the familiar point that IBC fans make about "lost opportunity cost" when paying cash, but we will also see how the policy loan growth offsets the apparent gain of the IBC approach.

In order to minimize the number of moving parts, I am going to assume that Sally earns 5% on her sinking fund, while Jim enjoys an internal rate of return (counting dividends etc.) on his cash surrender value of 5%, *and* that the life insurance policy loan interest rate is 5%. In reality, these numbers may all be different, of course, but my example should help financial professionals and the public to refine their understanding of what factors are actually driving particular wealth outcomes from different strategies.

There's a lot going on in Table 1, so let's first concentrate just on Sally. By assumption, she has a sinking fund (composed of bank CDs, for example) that earns an internal rate of return of 5%. She wants to buy a new car for \$25,000 at the end of Year 5. In

Table 1. "Paying Cash" for a Car versus Policy Loan

	Sally Pays Cash		Jim Uses Policy Loans			
	Annual Contribution (BOY)	Sinking Fund Value (EOY)	Annual Contribution (BOY)	Gross Cash Surrender Value (EOY)	Policy Loan Balance (EOY)	Net CSV (EOY)
Year 1	\$4,309	\$4,524	\$4,309	\$4,524	\$0	\$4,524
Year 2	\$4,309	\$9,275	\$4,309	\$9,275	\$0	\$9,275
Year 3	\$4,309	\$14,263	\$4,309	\$14,263	\$0	\$14,263
Year 4	\$4,309	\$19,501	\$4,309	\$19,501	\$0	\$19,501
Year 5 (Buy 1st Car)	\$4,309	\$25,000	\$4,309	\$25,000	\$25,000	\$0
Year 6	\$4,309	\$4,524	\$4,309	\$30,775	\$26,250	\$4,525
Year 7	\$4,309	\$9,275	\$4,309	\$36,838	\$27,563	\$9,276
Year 8	\$4,309	\$14,263	\$4,309	\$43,204	\$28,941	\$14,264
Year 9	\$4,309	\$19,501	\$4,309	\$49,889	\$30,388	\$19,501
Year 10 (Buy 2nd Car)	\$4,309	\$25,000	\$4,309	\$56,908	\$56,907	\$1

NOTE: In Table 1, all rates of return and loan interest rates are 5%. (BOY=Beginning of Year, EOY=End of Year, CSV=Cash Surrender Value.)

order to achieve this goal, Sally puts \$4,309 at the start of each year into her sinking fund. By the end of Year 5, her sinking fund has grown to a value of \$25,000. She cashes in her CDs and pays cash for her new car.

She repeats the whole process starting in Year 6. Because she had cashed out her fund the prior year, notice that the sinking fund is only worth \$4,524 at the end of Year 6—the same as at the end of Year 1. There is no “memory” in her sinking fund of her earlier contributions; she starts the cycle anew with each car purchase.

Now look at Jim’s figures. We assume that he makes the same out-of-pocket contributions as premium payments into a Whole Life insurance policy. To keep things apples to apples, we are unrealistically assuming that there is no overhead and that all of the payments immediately become available as Cash Surrender Value (CSV). We further assume that with dividend reinvestment etc., the CSV of this policy grows with an internal rate of return of 5%.

For the first five years, the two approaches are identical. That is, the market value of Sally’s sinking fund and the CSV of Jim’s life insurance policy are

the same. However, things diverge at the end of Year 5, when they make their first car purchase.

At this time, Sally wipes out her portfolio of bank CDs, in order to buy the \$25,000 car. She has no debt, but she also has no financial assets. She has a brand new car, but financially she is back to \$0 and has to start rebuilding from scratch.

In contrast, Jim’s *gross* Cash Surrender Value is not affected by the fact that he takes out a policy loan of \$25,000. He keeps making his premium payments, and his policy keeps chugging along, growing at an internal rate of return of 5%. By the end of Year 10, Jim’s life insurance policy has grown to a gross cash value of \$56,908, whereas Sally’s bank CDs have only recovered to their previous high of \$25,000—and they are just about to get knocked back down to \$0 when she buys her second brand new car.

I believe this contrast—between the value of Sally’s sinking fund and the gross Cash Surrender Value in Jim’s life insurance policy—is what the typical IBC proponent has in mind when he teaches people the importance of “keeping your money working for you” and how paying cash “ignores opportunity cost.” This is all true as far as it goes.

However, we must also take into account a very important fact: *If Jim is devoting the same out-of-pocket cashflow as Sally into his life insurance premiums, then he has no extra cashflow to pay down his policy loan.* After all, the *reason* Jim has the luxury of “keeping his money in his life insurance policy” when he buys the new car, is that Jim gets the \$25,000—at the end of Year 5 and then again at the end of Year 10—by borrowing from the life insurance company.

Once we account for this extra cashflow and the liability it brings, we see that Jim's net Cash Surrender Value—which is the gross CSV minus the outstanding policy loan balance—leaves him in basically the same position as Sally. Yes, it is certainly true that Jim enjoys constant compounding on his cash values that “stay in the policy,” but these are offset by the *constant compounding on the policy loan balance*. In this example, I made all of the rates of return identical, so that the two forces perfectly offset each other. But even if the various interest rates are different (which they will be in the real world), the concept is still crucial. It would be an incomplete account of what is happening, to mention *only* the gross cash value and ignore the offsetting policy loan balance.

FINANCING THROUGH IBC IS A GOOD IDEA

I want to stress that I am a huge proponent of Nelson Nash's IBC, especially in our volatile economic environment. The principles Nelson teaches in his book are valid, and his numerical examples were based on real-world illustrations generated by home office software with interest rates that held when he wrote his book.

The simplistic example I discussed in Table 1 above was *not* intended to show the reader that “it's all a wash.” On the contrary, I think it makes *much more* sense to finance large purchases using the IBC approach, rather than (say) building up a sinking fund through bank CDs, commercial savings accounts, money market funds, or other popular and “safe” assets. (For example, the combination of safety and after-tax yield afforded by a life insurance

policy compares quite favorably to these other possibilities, *and* you get the kicker of a large death benefit.)

Furthermore, I think the fans of IBC are correct to stress to the public the virtue of “constant compounding” that is afforded by a dividend-paying Whole Life insurance policy. (For example, the “historical average rate of return” that is touted for the stock market can often mask years when losses occurred, giving a very misleading picture of what would really happen to your money in such investments. In contrast, you don't need to worry about your cash value going down during a “bad year” with life insurance.)

So rather than pooh-poohing the advantages of IBC, the purpose of my example in Table 1 was simply to make sure the public is presented with the full picture. I definitely agree that in practice, someone who uses a sinking fund approach and adopts an “always pay cash” mentality will not end up as wealthy as someone who adopts the IBC approach.

Yet as the figures in Table 1 reveal, the *reason* for the superior wealth accumulation under IBC isn't *merely* the fact that “you lose the opportunity to earn interest on your savings” when you pay cash. By itself, that consideration is counterbalanced by your need to take out a loan (growing exponentially) when you keep your money at work in a policy. There are *other* reasons that IBC is superior to paying cash, including the very real psychological tendency for people to “find more money” to pay down an outstanding policy loan. Another motivation is their willingness to divert large flows of cash into an IBC-structured policy when they see how large the death benefit jumps, even if it is partially offset by a growing policy loan balance.

CONCLUSION

All things considered, Nelson Nash's Infinite Banking Concept (IBC) is an ingenious process of managing cashflows using a dividend-paying Whole Life insurance policy via policy loans. It is a very robust strategy that is superior to more traditional methods of finance, including the conservative

approach of “paying cash” and avoiding all debt.

In the world of IBC, it is standard to teach newcomers the importance of opportunity cost, and to show that IBC allows your money to enjoy constant compounding. These principles are all correct, and the lessons are important. However, as I've shown in this article, evangelists for IBC should be clear to include the offsetting liability of a policy loan balance in their more elaborate discussions. This will provide the public with a full and accurate picture, so that they will hopefully see the superiority of IBC and embrace it in their own households and businesses.

References

1. Episodes 17, 18, and 19 of the Lara-Murphy Show are available at: <https://lara-murphy.com/podcast/page/3/>.
2. Strictly speaking, certain life insurance companies follow the practice of “direct recognition,” in which case the size of the dividends generated by the policy (and hence its “internal rate of return”) could be reduced by outstanding policy loans. However, that is a technical issue regarding how fast the policy grows, and even here, it is not correct to think that the policy loan “comes out” of the life insurance policy.

Peter Bos and the Road to Freedom

06/04/2018 David Gordon

[*The Road to Freedom and the Demise of Nation States*. By Peter B. Bos. Free Trade Press, 2015. Xxv + 620 pages.]

This remarkable book reflects the author's enthusiasm for liberty and his vast intellectual curiosity. I propose to discuss only a few of the book's central insights, but only reading the book will adequately convey Peter Bos's intellectual range.

Like Mises, Bos emphasizes that the free market economy, by taking full advantage of the division of labor, greatly increases prosperity. “In those countries where the exchange of goods and services has been relatively unhampered, capitalism, through investment and the division of labor and skills, has

produced a standard of living unimagined even a few decades ago.” (p.162)

Socialists and other critics of the free market are not content with this abundance. Even if capitalism is, as Mises often said, a system of “mass production for the masses,” is it not unfair that some people earn vastly more than others? Laments about unequal shares of wealth abound.

Bos expertly parries this attack on capitalism. Wages depend on labor's marginal productivity, and this rises as the accumulation of capital increases. With better tools and equipment, labor becomes more valuable to the capitalist and gets paid more. “In capitalist countries, the increase of capital accumulation is exponential and outruns the increase in population. To the extent that this happens, the marginal productivity of labor increases exponentially as against the marginal productivity of the material factors of production, which makes ever-higher wages possible.”(p.163)

Classical liberalism recognized the superior productivity of capitalism, as well as its manifest benefits to liberty, but it suffered from a fatal flaw. Although the classical liberals favored the free market, they made an exception for protection, justice, and defense. Here the state was necessary. “The greatest fallacy of the classical liberals was their assumption that a constitutionally limited state government was necessary and ceding to it a monopoly of coercion over all purported state functions. In ceding to the state these traditional services, the classical liberals never considered that these purported services of the state were no different from other consumer services and thus could and should be provided by proprietary organizations, subject to competitive market forces and incentives in the free market.” (p.184)

A skeptic might say to Bos, “it is easy to postulate that free-market institutions can replace the state, but how do you know this is possible?” Bos has carefully worked out a response. Protection and defense would be carried out by insurance companies. These companies would have strong

incentives to offer protective services efficiently. "In a voluntary market economy, the success of an insurance company will be directly linked to the welfare of its clients, because it will be profitable to enhance that welfare." (p.272)

Many libertarian readers will be familiar with this idea, but Bos tells us something new about it. He claims that he originated the idea. After a presentation on constitutional government in the fall of 1961, "I privately disclosed my insurance concept of natural government to the presenter, Alvin Lowi. . . The concept thereafter became a major part of the Andrew Galambos FEI [Free Enterprise Institute] courses. Regrettably, Galambos never publicly acknowledged or credited my contributions." (p.253)

Again, a critic might respond, "This is an interesting idea, but it is no more than a pipe dream. We will never get rid of the state." Here Bos defies convention. He argues that the state will soon collapse and further that the proprietary communities he favors have an excellent chance of arriving on the scene.

In predicting the demise of the state, Bos has been influenced by Joseph Schumpeter's prescient article, "The Fiscal State," to which he draws our attention. "In a short essay reflecting the experience of World War I, he predicted a new era in state government finance and government policy. He pointed out that before the war there were no absolute governments. By that he meant that nation states before World War I could raise no more than perhaps 5 percent of a country's national income through taxes or borrowing. However, during World War I, every belligerent nation state raised far larger sums year after year. . . Schumpeter predicted that this precedent would create a different economy in which inflationary pressures would become endemic, which in turn would undermine the political system."(p.220)

Bos finds in this dim prognostication grounds for optimism. "Since the state is an inherently unstable and illegitimate organization based on unworkable and immoral premises, its demise is

inevitable."(p.247) This gives us the opportunity to establish a free society.

As should by now be apparent, Bos has firm views on how such a society would be organized. His proposal about insurance companies functioning as protection agencies has already been canvassed, but he also has views about the monetary system and what he calls "proprietary communities."

He supports "individual sovereign money issuance." (pp.286 ff.) Those interested in the details of this proposal must consult the book, but at one point he differs from Mises and Rothbard. He writes, "However, a commodity can never act as money, for the purpose of money is to obviate the necessity of a physical transfer of value from the buyer to the seller. . . The shortcoming of metal-based money is that it still represents a commodity barter system, albeit one based on precious metals." (p.295) Bos has been much influenced in his ideas about private money issuance by the libertarian writer E.C. Riegel. I confess that I should have liked to have seen here a greater engagement with the arguments of the Austrian economists.

Bos, following Spencer Heath, favors proprietary communities. In this system, a private company owns a community's land and "leases separate parts of the land under specified conditions or covenants to selected tenants." (p.389). Bos argues forcefully that such communities could handle in a peaceful and profitable way all the problems so woefully mismanaged by the states of the contemporary world.

Bos offers us a vision of a better world, and readers of *The Road to Freedom and the Demise of Nation States* will be instructed and challenged by what he has to say.

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Liberty as a Life Philosophy

Much more than an idea, liberty is a guiding principle for our lives and interactions in the world.

by Lawrence W. Reed

Editor's Note: This essay is drawn from the *new, second edition* of Lawrence Reed's book, *Are We Good Enough for Liberty?*

Author's Note: In a previous essay, I challenged my readers to ask themselves, "Are we good enough for liberty?" In the following piece, I will ask a second question that is the other side of the same precious coin: do we believe in liberty enough to be good? In other words, will you treat the ideas of liberty as mere fodder for political posturing and internet debates? Or do you love liberty enough to embrace it as a life philosophy? The future of freedom hinges on the answer to that question, so please read on!

FEE's eminent founder, Leonard E. Read, often opined that it was the duty of every lover of liberty to introduce it to others "as a life philosophy." It's a phrase we at FEE still use today, and every day. We're able to preach it with conviction because we practice it with passion.

What does it mean to regard liberty as "a life philosophy"? First, allow me to offer a few words about what it doesn't mean.

If liberty is your life philosophy, you're not its fair-weather friend. You stick with it in good times and bad because its fundamental virtues are independent of what others think of it. Its truth rests on its inherent merit, not on shifting perceptions. Its immediate prospects for success may fluctuate, but your commitment to it shouldn't.

You don't apply a life philosophy to certain aspects of your life and not others, as did the soybean farmer who once told me with a straight face, "Larry, I'm for free markets and no subsidies for everything but soybeans."

Furthermore, if your speech, tactics, or behavior conflict with liberty's high standards—if you're

turning people off to it instead of winning them over—then you're defeating one of the main purposes of possessing it as a life philosophy in the first place. It ought to be something so lofty and universal that you're proud to live it and delighted when others choose to do so too.

A life philosophy is neither superficial nor fleeting. You don't embrace it because it's convenient or fashionable or even profitable. It's deeper, more holistic and lasting than that. It ought to be rooted in ideas and conduct that are right, relevant, and uplifting. It should cause you to be remembered someday as a man or woman whose consistency and example gave the world a model worth emulating.

If you were to choose today the epitaph that will appear on your headstone after you're gone, which one from these two lists would you pick? Or perhaps the better question is, which one most accurately describes you?

List A:

"He said it but rarely meant it."

"No one ever knew what she stood for."

"Left the world as if he was never in it."

"Couldn't see further than herself."

"Subtracted more than he added."

"Honest and upright, except when others were watching."

List B:

"He made bedrock principles soar."

"What you saw was what she was, no pretense or prevarication."

"Devoted to all the right things, in word and deed."

"Loved life and liberty, and others loved him for it."

"She set standards to which every decent person aspires."

"The Golden Rule was his life in three words."

No good and self-respecting person would want to pick from List A, though the world is full of people

who would have to if they were completely honest about it. What a dreadful shame to die never having lived a life that amounted to anything more!

You can certainly commit your life to many things—to God, to truth, to family, to the future, etc. They are not necessarily mutually exclusive. I just want to make the case here, building on the previous essay and the title of this book, *Are We Good Enough for Liberty?*, that liberty is right up there close to whatever the best thing is. That's because, by definition, it makes it possible for you to fully commit to any or all of the other good things, and enjoy the benefits thereof without arbitrary hindrance.

A life philosophy is made up of two components: *The first is how you see yourself. The second is how you see (or interact with) others in society.* Though these two components are distinct on the surface, they should actually be seamless and integrated, one with the other. If they weren't, then your so-called life philosophy would be contradictory and schizophrenic—as if you had two lives and two philosophies. It would be like a thief arguing that theft is a good thing if he's stealing from you but bad if you're stealing from him. Intellectual integrity demands a logical consistency, not selective and self-serving application. Let's look more closely at those components *from a liberty standpoint.*

How You See Yourself

If I were a socialist or a communist, I'd probably see myself as someone else's victim, or maybe as an insignificant piece of something more important—a mob, a group, a class, or whatever. I would likely subordinate myself to the collective will, as determined by some powerful, influential person with a megaphone. I would seek political power over others, as I convince myself of my own good intentions. I'd spend most of my time trying to reform the world and relatively little time attempting to improve myself.

But I'm a lover of liberty—a *libertarian*, if you will—so I see myself as one-of-a-kind. I'm not exactly like anybody else who has ever lived, and

neither are you. To be fully human—to be fully me—I need things like choice and responsibility. I needed a mommy at age 5, but certainly not at 25 or 65.

Maybe on any given day I'm a victim of somebody, but I'm in charge of how I react to that. If I let it paralyze me, I'm simply solidifying and reinforcing my victimhood.

To be called “a common man” is no compliment because it's not commonness that makes me who I am, but my uncommonness. I relish the best, the heroic, the man or woman who carves himself out of the rock of commonality.

No matter how many times other people may tell me how or what I should think, I will think for myself. If that means coming to conclusions no one else agrees with, so be it. I'm especially eager to stand apart from the crowd when the crowd is wrong.

I'm not so full of myself that I think I know enough or am sufficiently fit to manipulate others like pieces on a chessboard. I want to learn and grow, from now until I breathe my last.

I happen to be a Christian, incidentally, so I believe God made me for a purpose. With His help, I will carry it out to the best of my ability. It may not be your purpose, but you didn't make me and you can't live my life for me—not peacefully, anyway. I will leave you alone if you leave me alone, and we'll celebrate our differences in peace and commerce.

All this is empowering—extraordinarily so! I can employ my uniqueness to make a difference in the world! I might even be able to change it profoundly, perhaps as much as those who led the fight to end the age-old institution of slavery! I'm not just another drone in the ant hill, after all!

I can be a superb parent, a fantastic teacher, a remarkable influencer, a great friend. I can invent, produce, and innovate. I can be a risk-taking entrepreneur, adding value to society. I can do things others won't or can't and in so doing, I might stimulate and embolden them, too. The sky is the limit, and I respectfully decline to live down to

somebody else's low expectations for me.

Take charge of your life and even if it's hard to be optimistic for society as a whole, you can still be optimistic for yourself and those you love and affect.

This is how I think each lover of liberty should see himself. It's certainly how I see me. And guess what? I would like nothing better than for you to believe the same about yourself. Freedom is what I want for me, and it's precisely what I want for you (unless by your actions you forfeit the right).

I embrace the Golden Rule. I do my level best to treat others the way I would want them to treat me, which leads me to the second component of liberty as a life philosophy.

How You See Others

If I didn't believe in liberty, I might trust nobody but myself. I might see you as an obstacle to be ruled or overcome rather than as a partner I can associate with for mutual benefit. Taken to an extreme that really isn't all that infrequent, historically, my hostility to your liberty could devolve into tyranny—whereby you'll do as I tell you because I think your purpose in life is to serve mine.

But I'm a lover of liberty—a *libertarian*, if you will—so it would be an affront to my principles to do to you what I would never countenance you doing to me.

I have enough respect for you that when we differ, my first resort will be to employ persuasion. Compulsion is always my last resort, if I use it at all. In any event, I will never initiate force. I will use it only in retaliation once you've proven yourself a threat by either using it against me or credibly threatening to do so.

I believe it is a measure of my character that I deal with you from the loftiest of standards—with honesty, intellectual humility, patience, responsibility, mutual respect, courage, and self-discipline. Until you prove otherwise by your behavior, you are as entitled to those things from me as I am from you. I believe so strongly in those virtues of character, in fact, that I'm not going to let

anybody's lack of them be an excuse to let mine slip.

As a lover of liberty, I respect your right to think otherwise and do otherwise. I respect your right to be different, to be more successful than me, to be better than me at anything and everything, for that matter, and to gain the rewards that others offer you in return. I will not resent you, envy you, drag you down, or try to forcibly make you what you're not. And I will not hire politicians to do these things to you under the mistaken assumption that doing so absolves me of some or all of the guilt.

I will never succumb to that most intoxicating of evil motives—power over others. I'm better than that, and you should be too.

To Leonard Read, the means had to be just as good as the ends. If you want to influence others on behalf of liberty, he argued, you've first got to be committed to self-improvement and then adopt a tolerant, inviting, and hospitable stance toward others, whenever possible. He wrote,

Calling Joe Doakes a fool or stupid harms him little if at all. The damage is to me in that I gain his enmity. He will no longer hear me, whatever wisdom I have to offer. This is to sink one's own ship. But this is not the half of it!...

In a word, the contemptuous subordination of another person—the entertainment of such a thought, even when silent—spells self-destruction.

The better world begins with that man who attends to his inner freedom. Would you have your counsel more widely sought? Emulate that man. To find the way, ask yourself this question: With whom would I rather dine tonight, that man or an angry, know-it-all person?

Embracing liberty as a life philosophy requires that you get your own affairs in order, be a burden to no one, seek nothing from others through the political process except that they leave you alone, and be a model in everything you do so that others will be inspired by your example.

Take charge of your life, accept all your responsibilities at home and elsewhere without

hesitation. Get your mental attitude in shape: Have a healthy sense of humor, a good feel for both your strengths and weaknesses, a bubbly optimism and exuberance about making a difference in the world.

Be a good citizen who respects the lives and property of others. You can't expect to be free if you support making others less so. Make your life a nonstop learning journey—read and become as informed about freedom in all its aspects as you can possibly be.

How we make our case is almost as important as the case itself. Rarely is it appropriate to come across in a hostile, confrontational, or condescending manner. It's never fitting to be arrogant, shrill, or self-righteous. We should convey our ideas in the most judicious, inviting, helpful, and persuasive fashion possible. We should be magnets for every open minded person willing to learn. We can have all the facts and passion in the world but if we lack people skills, we'll just be talking to ourselves.

As indispensable as liberty is to the progress of humanity, its future is never assured. Indeed, on most fronts, it has been in retreat for years—its light flickering against the winds of ignorance, irresponsibility, short-term gratification, and power-lust. That's why it's all the more important that those of us who believe in liberty become more effective spokespersons.

Toward that end, I offer here the well-worn "top ten" list. These rules of thumb do not appear in any particular order. So I leave it to you, Dear Reader, to decide which ones are more important. I am convinced that liberty as a life philosophy offers so much that makes life fulfilling that we owe it to ourselves to be effective exemplars and spokespersons for it.

1. *Get motivated.* Liberty is more than a happy circumstance. It's a moral imperative, worthy of every ounce of passion that good people can muster. It's not just about getting keyed up in an election year or responding to some issue of the day. It's always the difference between choice and coercion, between living your life or others living it for you

(and at your expense). If liberty is lost, it may never be restored in your time or in that of your children and grandchildren. For solving problems, avoiding conflict, and bringing people together, there's no worse course than politics and force, and no better path than liberty for peaceful exchange and cooperation to flourish.

2. *Learn.* More precisely, never stop learning! To be an effective persuader, there's no good substitute for commanding the facts and the foundations. Know our ideas backwards and forwards. You can never read or listen to too much economics, history, or philosophy to be the best persuader in your neighborhood. Let the other side talk in bumper stickers. Come armed with substance as opposed to slogans.

3. *Be optimistic.* It's tiring and disheartening to hear the defeatists talk like this: "It's over. The Republic is lost. There's no turning back. Our goose is cooked. I'm leaving the country." What's the point of such talk? It certainly can't be to inspire. Pessimism is a self-fulfilling prophecy. Pessimists only disarm themselves and dispirit others; there's nothing to be won by it. If you truly believe all is lost, the best thing to do is defer to the possibility that you may be wrong and let the optimists lead the way. (That means leaving pessimism at the door.)

4. *Use humor.* Even serious business needs moments of levity. Seasoning your case with humor can make it more appealing, more human. If you can't smile when you're making the case for liberty—if you can't evoke a smile or a chuckle from the person you're talking to—then you're on the way to losing the battle. Humor breaks the ice.

5. *Raise questions.* You don't have to lecture every potential convert. Learn to deploy the Socratic method, especially when you're conversing with a rigid statist ideologue. Most of the time, such people hold the views they do not because they're well acquainted with libertarian thought and have rejected it, but because they just don't know our side. A skilled line of questioning can often prompt a person to think about their premises in ways they never

have before.

6. *Show you care.* It's been said that people don't care what you know if they don't know that you care. Focus on real people when you argue for liberty. Laws and policies inimical to liberty produce so much more than bad numbers; they crush the dreams of real people who want to improve their lives and the lives of those they love. Cite examples of people and what happened to them when government got in the way of their progress. That said, don't dwell on the negative. Be just as generous in citing examples of what specific people have accomplished when they've been given the freedom to try.

7. *Seize the moral high ground.* Liberty is the one socioeconomic arrangement that demands high standards of moral character. It cannot survive if people are widely dishonest, impatient, arrogant, irresponsible, short-term focused, and disrespectful of the lives, rights, and property of others. This truth speaks volumes about the moral superiority of liberty over all other "systems." Humanity is composed of unique individuals; it is not an amorphous, collective lump to be pushed around by elitists who fancy themselves our masters and planners. Any arrangement that purées our distinct lives in a collectivist blender is a moral offense. Use this argument to strike at the very heart of any opponent's case.

8. *Develop an appealing persona.* A lover of liberty who knows all the facts and theories can still be repulsive and ineffective if he's condescending, vengeful, coarse or crude, self-righteous, or often in "attack" mode. This is why Dale Carnegie's classic, *How To Win Friends And Influence People*, should be on every libertarian's "must-read" list. So should be Olivia Cabane's excellent volume, *The Charisma Myth*. Do you want to change the world or just beat your breast? Talk to others or talk to yourself? And slow down on the negativity! Some of us only talk about bad news. These are the folks who see nothing good happening anywhere. This attitude comes across as if they're telling you, "Stop having fun. The only good news is that there isn't any. If you

think there is good news, we'll tell you why it isn't." This attitude wears badly and rarely wins converts. Heroes and heroic stories are all around us; don't ignore them by dwelling on the scoundrels and the disappointments.

9. *Don't demand total and immediate acceptance.* Have you ever run into a libertarian who lets you know that unless you fully confess all your intellectual sins and repent on the spot, you're a pariah? The history of progress in ideas provides few examples of wrong-on-everything transforming into right-on-everything in a momentary leap. We must be patient, inviting, and understanding. Know when the cracks are appearing in an opponent's wall and give him room to tear it down himself. Remember that all of us hold views today that we didn't accept in our past. None of us came out of the womb with a copy of Hayek's *The Road to Serfdom* in our hands.

10. *Make allies, not enemies.* A handful of cloistered, ineffective—but noisy—libertarians fancy themselves arbiters of the faith. They behave as though the greater enemy is not those who embrace no libertarian precepts at all, but rather those who embrace many, but not all, libertarian precepts. So when they find a fellow libertarian who once held different views, or departs from orthodoxy on an issue or two, they start to vilify him. It makes them feel good, but works against the larger cause. If we say we want to make the world a better, more liberty-loving place, we can't make it painful for anyone to move in the right direction.

So, are we in fact *good enough for liberty*? That question is best answered not in a collective fashion, but in a profoundly personal way—one man or woman at a time.

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Why Unschoolers Grow Up to Be Entrepreneurs

by Kerry McDonald

Almost by definition, entrepreneurs are creative thinkers and experimental doers. They reject the status quo and devise new approaches and better inventions. They are risk-takers and dreamers, valuing ingenuity over convention. They get things done.

It shouldn't be surprising to learn that many unschoolers become entrepreneurs. Able to grow up free from a coercive classroom or traditional school-at-home environment, unschoolers nurture interests and passions that may sprout into full-fledged careers. Their creativity and curiosity remain intact, uncorrupted by a mass education system intent on order and conformity. Their energy and exuberance, while a liability in school, are supported with unschooling, fostering the stamina necessary to successfully bring a business idea to market. Like entrepreneurship, unschooling challenges what is for what could be.

The numbers are startling. In a survey of grown unschoolers, Boston College professor Peter Gray, along with his colleague Gina Riley, discovered that more than half of the grown unschoolers they interviewed were presently working as entrepreneurs. Many of the respondents indicated that their careers were directly linked to childhood interests that they followed into adulthood. Interestingly, the correlation between unschooling and entrepreneurship was the highest for the always-unschooled group, as compared to intermittent unschoolers.

Unschoolers Make Amazing Entrepreneurs
Anecdotally, the link between unschooling and entrepreneurship is fascinating. Karen Leong is a 19-year-old custom cake designer with her own flourishing small business. Unschoolled throughout her childhood, she learned about cake design from watching YouTube videos when she was 11. That triggered a sprouting interest, and she pursued

additional, months-long courses in cake design and pastry work. Today, her business is expanding and she credits unschooling for playing a large role in her current entrepreneurial pursuits. In a recent interview for New Straits Times, she says about her upbringing: "My parents were very involved in my unschooling. It's essential that parents are very proactive in their child's unschooling journey, maintain open communications and have a strong relationship with their child."

Another grown unschooled entrepreneur is New Jersey contractor, Zachary Dettmore. In a recent interview with the Lyndhurst Daily Voice, Dettmore describes how growing up unschooled enabled him to pursue his interests, including his passion for building and construction that emerged when he was around eight-years-old. According to the article: "I was always interested in building and how things worked," he said, "so my reading as a child was geared towards non-fiction topics that interested me. I wasn't pigeonholed into a one-size-fits-all education methodology." At 13, he took a timber-framing course and became increasingly committed to a career as a contractor. Now 29, Dettmore runs a successful custom contracting business with a couple of employees.

Entrepreneurship Is at the Heart of Unschooling
Successful entrepreneurs are self-starters, driven by their own passions and goals to create something new and different that has value to others. As self-directed learners, unschoolers are given the freedom early on to discover these passions and commit to these individual goals. They are allowed the time and space to explore, to tinker. Whether with their family, or while attending a self-directed learning center or unschooling school, unschooled children are surrounded by supportive adults eager to help connect their budding interests with the larger resources of their community, like classes and mentors. This process of pursuing individual passions while being supported by caring adults creates the ideal conditions for aspiring entrepreneurs to imagine new possibilities and leap into unknown enterprises.

As the American entrepreneur and author, Jim Rohn, once said: "Formal education will make you a living; self-education will make you a fortune." While all of us can benefit from his advice, unschoolers have a great head start.

Kerry McDonald (@kerry_edu) has a B.A. in Economics from Bowdoin and an M.Ed. in education policy from Harvard. She lives in Cambridge, Mass. with her husband and four never-been-schooled children. Kerry is the author of the forthcoming book, *Unschooling: Raising Curious, Well-Educated Children Outside the Conventional Classroom* (Chicago Review Press). Follow her writing at Whole Family Learning.

This article was originally published on FEE.org. Read the original article.

Comment by R. Nelson — I had the pleasure of meeting Kerry McDonald at FEEcon in Atlanta on June 7 & 8. It was a real joy to talk with her at length about her work on the subject of un-schooling children. We have been posting articles of hers in past issues of BankNotes because of my deep conviction of the need of what this remarkable lady has brought to the education world. Her competence and passion for getting people to recognize that children have been indoctrinated instead of educated gives me hope for the future.

Nations Don't Gain or Lose from Trade, Individual Traders Do

A "trade imbalance" between countries matters about as much as a "trade imbalance" between tall people and short people.

by Robert Higgs

Let us define the set of all human beings whose height is greater than 170 cm and less than 180 cm. Call this set A. Now let us collect data on all the dealings between members of set A and members of set B, which consists of all human beings whose height is less than or greater than those in set A. What economic significance can we ascribe to the aggregate of monetary flows between members of

set A and members of set B? Correct answer: none.

This aggregation of persons who trade with persons in the complementary set has no economic meaning; the sets are arbitrary so far as economic understanding is concerned. People—individuals, firms and other organizations, and governments—trade in order to improve their economic condition. Whether they trade with shorter or taller people or with people within a certain height range or outside this range has nothing to do with economics or human well-being. To draw up a balance of inter-set payments for set A and set B, or any given subset of B, would serve no purpose. It would be a nonsensical exercise.

Yet Another Nonsensical Exercise

Now let us define the set of all human beings who reside within the boundaries of a certain nation-state, say, the United States of America. Call these people the elements of set P. Now collect data on all the dealings between members of set P and members of set Q, which consists of all human beings who reside outside the USA. What economic significance can we ascribe to the aggregate of monetary flows between members of set P and members of set Q? Correct answer: none.

This aggregation of persons who trade with persons in the complementary set has no economic meaning; the sets are arbitrary so far as economic understanding is concerned. People—individuals, firms and other organizations, and governments—trade in order to improve their economic condition. Whether they trade with people inside or outside the USA has nothing to do with economics or human well-being. To draw up a balance of inter-set payments for set P and set Q, or any given subset of Q (e.g., residents of China or Mexico) would serve no intellectual purpose. It would be a nonsensical exercise.

Yet, exactly such a nation-based "balance of international payments" accounting system has been constructed and "analyzed" for a very long time. In centuries past, when kings needed to accumulate gold and silver to pay mercenaries to fight their

wars, they had a reason to accumulate such data and to promote policies (such as customs duties on imported goods) that would discourage imports, thereby keeping gold and silver from flowing out of the country in payment for the imports.

This sort of “political arithmetic” eventually grew into the modern system of international balance of payments accounts (indeed, the entire system of national income and product accounts, as well). The old monarchical logic for the collection of such data has long since evaporated, however. Modern governments have other ways to organize and finance their wars.

This Medieval Thinking Only Harms Consumers

Meanwhile, other interested parties discovered that they might use certain conditions, such as a so-called deficit in the balance of trade (the value of national imports of goods and services exceeds the value of national exports of goods and services) as rhetorical fodder to feed their politicking for the government to place greater tariffs (import taxes) on goods and services imported into the home country that compete for domestic sales with the goods offered for sale by domestic sellers.

This gambit is nothing but a means of suppressing competition, an activity in which sellers unfortunately commonly engage, employing the government's force in their quest if they can enlist it. This so-called protectionism obviously hurts domestic consumers by depriving them of access to better terms of trade otherwise available from foreign sellers.

Recall, however, what was already said: every trade, whether with members of one's own set or members of another, complementary set, is undertaken in the expectation of gain. The idea that, even though every transaction was voluntarily entered into for mutual gain, there is something wrong if the aggregate value of exports from one's set falls short of the imports is, to speak frankly, preposterous. One cannot add up a number of gainful exchanges, whether they be purchases or sales, and conclude that in the aggregate a baleful situation has been created.

To give this impression is nothing but a trick, a diabolical scheme, by which some sellers in effect hope to pick the pockets of domestic consumers.

The root of this evil is the aggregation that is employed in such balance of payments accounting systems. Nations as such don't gain or lose from trade; only individual traders do. If the trades into which these people voluntarily enter entice them by the prospect of mutual gain, it simply cannot be the case that the sum total of their transactions amounts to a bad deal.

Reprinted from the Independent Institute.

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He is a member of the FEE Faculty Network.

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Comment by R. Nelson Nash — Higgs is one of my favorite writers. Here he points out the absurdity of an idea that consumes so much time in the “news” media and writings of Keynesian “economists.” It is just one of the tools that they use to produce fear in the minds of the general public—and then propose a government program to “do something about it.”

How to Captivate an Audience One Person at a Time

As with most things, to really have an impact, you need to create exceptional value for someone.

by James Walpole

How can a speaker captivate the attention of an audience?

Psychologist Jordan Peterson might suggest that this is the wrong question. He writes in *12 Rules for Life* (a recent read of mine) that:

There is also no "audience." There are *individuals*, who need to be included in the conversation.

A well-practiced and competent public speaker addresses a single, identifiable person...

If Peterson is right, you have to focus in on the smallest unit of your audience—the individual—to hold the attention of a group of individuals (the audience). Good speakers do this.

Great speakers and performers go one step further in applying this individual focus, beyond the best practice of simply speaking to an individual. They bring disproportionate value to one audience member out of a crowd of many.

A Practical Example

Today I saw that one-step-further principle played out when T.K. Coleman (Praxis) and Abbey Lovett (Lyceum Communications and fellow Praxis grad) gave a talk about powerful communication at the Foundation for Economic Education's FEEcon conference. TK brought the word on the importance of patient, non-entitled communication (you shouldn't expect other people to understand you if you don't try to be understood), and Abbey (on fairly short notice) gave a rundown of the power of the thesis statement to clarify takeaways for audiences.

The moment when the talk went from good to great came in the Q&A. A man asked about how to overcome a fear of public speaking. Instead of just giving advice, TK called the guy up to the mic and gave him a minute to confront his fear and speak to the audience.

Things could have gone terribly wrong. But our brave audience member did a great job, speaking eloquently for a bit about the fear of public speaking. It turns out he had nothing to be afraid of. We all cheered as he went up to the stage, and we all cheered when he came back down. It was epic, and it was one of the most memorable moments for me from Friday's FEEcon breakout sessions.

TK brought disproportionate value to this one member of the audience. Conventional thinking might say this is not a good idea for a public speaker—it takes attention away from the rest of the audience, and it denies us some time we might have

used to ask more questions. But in reality, we all enjoyed the talk so much more because of what TK did for that one audience member.

TK transformed the experience of a talk for all of us by focusing in on transforming the experience of a single individual. The guy he called on stage experienced a moment of transformation and profound personal development and courage. And the benefit wasn't just for him. Everyone in the audience shared in that moment and shared in his victory. There's no way we could all have gotten up to that podium in the time available, but somehow, by just touching one person, the speaker touched all of us.

This experience clarifies for me why certain performances and speeches are especially loved. Consider music: there are lots of extremely popular YouTube videos of bands inviting a single fan up on stage to dance or even play music. We go nuts for those moments, and we remember those concerts. Whether or not we are the ones being called on stage, we share in the same transformative moment when a speaker or performer chooses to bring disproportionate value to just one of us.

Reprinted from the author's blog.

James Walpole is a writer, startup marketer, intellectual explorer, and perpetual apprentice. He writes regularly at jameswalpole.com.

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The Myth that Central Banks Assure Economic Stability

When it comes to economic booms and busts, not to mention currency instability, there is no greater perpetrator than government-controlled central banking.

by Richard M. Ebeling

The world has been plagued with periodic bouts of the economic rollercoaster of booms and busts, especially during the last one hundred years. The

main culprits responsible for these destabilizing and disruptive episodes have been governments and their central banks. They have monopolized the control of their respective nation's monetary and banking systems and mismanaged them. There is really nowhere else to point other than in their direction.

Yet, to listen to some prominent and respected writers on these matters, government has been the stabilizer and free markets have been the disturber of economic order. A recent instance of this line of reasoning is a short article by Robert Skidelsky on "Why Reinvent the Monetary Wheel?" Dr. Skidelsky is the noted author of a three-volume biography of John Maynard Keynes and a leading voice on public policy issues in Great Britain.

Skidelsky: Central Banking Equals Stable Prices and Markets

Skidelsky argues against those who wish to denationalize and privatize money and the monetary system. That is, he criticizes those who want to take control of money and monetary affairs out of the hands of the government, and, instead, put them back into the competitive, private market. He opposes those who wish to separate money from the State.

Skidelsky sees the proponents of Bitcoin and other cryptocurrencies as "quacks and cranks." He says that behind any privatization of the monetary system reflected in these potential forms of electronic money may be seen "the more sordid motives" of "Friedrich Hayek's dream of a free market in money."

The famous Austrian economist had published a monograph in 1976 on the *Denationalization of Money*, in which Hayek insisted that governments have been the primary cause of currency debasements and paper money inflations through the centuries up to our own times. And this could not be brought to an end without getting government out of the money-controlling and money-creating business.

In Skidelsky's view, any such institutional change would be a disaster. As far as he is concerned,

human societies have discovered no better way to keep the value of money roughly constant than

by relying on central banks to exercise control of its issue and to act directly or indirectly on the volume of credit created by the commercial banking system.

Robert Skidelsky is a highly regarded scholar and is knowledgeable about many of the important political and economic ideas and events of the 20th century, about which he has often written. But one cannot help wondering if his views of central banks and the governments behind them over the last one hundred years don't concern life on some other planet because they do not reflect the reality of monetary systems and government management of them on Planet Earth.

The Pre-World War I Gold Standard

The 20th century began with all the major nations of the world having monetary systems based on a gold standard. Gold was money, the medium of exchange through which goods and services were bought and sold, and by which the savings of some were transferred to the hands of interested and credit-worthy borrowers for investment purposes through the intermediation of banks and other similar financial institutions.

There were money-substitutes in the form of banknotes and checking accounts to ease the inconveniences and transaction costs of using metal coins and bullion in many everyday exchanges. But they were recognized and viewed as claims to the "real money," that is, specie money.

Yes, this was, in general, a central banking-managed gold standard. And the gold standard "rules of the game" were not always followed, the essential general principle of which being that banknotes and deposit accounts should only increase for the banking system as a whole when there were net increases in the quantity of gold deposited in bank accounts, for which new banknotes would be issued as additional claims to that greater quantity of gold-money. And vice versa, if there was a net outflow of gold from the banking system due to banknotes being returned to the issuers for gold redemption, then the net amount of those banknotes in circulation

was to be reduced.

Though this core “rule” of the gold standard was not always rigidly followed by national central banks, the consequence of which was occasional financial crises and “panics,” the system worked amazingly smoothly, in general and on the whole, in providing a relatively stable monetary environment to foster domestic and international trade, commerce, and global investment. When the monetary system did periodically suffer disruptions, the mismanaging hand of the government and their central banks could usually be seen as the primary, or certainly a leading, cause of it.

Monetary Madness During and After World War I

This came to an end with the coming of the First World War in 1914. All the belligerent nations in Europe went off the gold standard, with banknotes and other bank accounts no longer legally redeemable in gold. Governments used various direct and indirect methods to have their central banks finance growing amounts of loans in the form of created quantities of paper money to cover the costs of their respective war expenditures. To use British economist Edwin Cannan's somewhat colorful mode of expression concerning the currency situation of his own country, Great Britain was soon suffering from a “diarrhea” of paper money to feed the cost of the British war machine.

This culminated in the catastrophic hyperinflations that gripped many countries on the European continent in the years immediately following the end of the First World War in 1918. The worst of such instances were experienced in countries like Germany and Austria. Especially in Germany, the paper money had become virtually worthless by the time the hyperinflation was ended in November 1923 by shutting down the money printing presses and introducing a new currency promised to be linked to gold.

However, the new postwar monetary systems that one country after another attempted to introduce were not like the gold standard that has existed before the war. Nominally, currencies were linked

to gold at new official redemption rates of so many banknotes in exchange for a unit of gold. But gold coins rarely circulated in daily transactions, as had often been the case before 1914. Gold was redeemable only in larger quantities of bullion (gold bars), and few countries kept significant quantities of gold on deposit in their own central bank vaults any more. (See my articles, “War, Big Government, and Lost Freedom,” and “Lessons from the Great Austrian Inflation”.)

The Federal Reserve and the Coming of the Great Depression

The short-lived return to seeming economic “normalcy” with growth and stability in the mid and late 1920s, however, came to an end with the American stock market crash of October 1929, which began to snowball into the Great Depression in 1930 and 1931. But why had this happened? In the United States, a major cause was the Federal Reserve's attempt to “stabilize” the general price level at a time of economic growth and productivity gains that otherwise would have likely brought about a slowly falling general price level, what has sometimes been called a “good deflation.” That is, rising standards of living through a falling cost of living, which need not be detrimental to the profitability of many firms since their ability to sell at lower prices is due to their ability to produce more at lower costs of production.

The Federal Reserve's “activist” monetary policy to counteract this “good” deflationary process in the name of price level stabilization required an increase in the supply of money and credit in the banking system that pushed interest rates below market-determined levels and therefore brought about an imbalance and distortion between savings and investment in the American economy. When the Federal Reserve cut back on monetary expansion in 1928 and early 1929, the stage was set for a collapse of the unsustainable investment house of cards created by investment patterns being out of sync with the real savings in the economy to sustain them.

What might have been a relatively short, “normal”

recession and recovery process was disrupted first by the fiscal and regulatory policies of the Herbert Hoover Administration (including a trade-killing increase in US tariffs that soon brought about retaliation by other countries). The recession was magnified to a degree never seen before in American history with the coming of Franklin Roosevelt's presidency and the New Deal in 1933: the imposition of a fascist-type system of economic planning in industry and agricultural; increases in taxes far exceeded by massive growths in government spending through budget deficits for "public works" and related federal projects; the abandonment of what nominally still remained of the gold standard followed by foreign exchange instability and paper money expansion.

Matching this were wage and price rigidities due to trade union resistance to money wage adjustments in a post-boom environment and goods prices frozen due to the regulations of the fascist-modeled National Recovery Administration (NRA). There was also a downward spiral in international trade resulting from the revival of global protectionism, and there was a monetary contraction exacerbated by a fractional reserve system built into the workings of the Federal Reserve that set off a multiplicative decrease in money and credit inside and outside the banking system as bank loans went bad and depositors "panicked," leading to bank runs. All this brought about the tragedy of the Great Depression, which dragged on through most of the 1930s.

How the disruptive inflations during and immediately after the First World War, or the misguided monetary policies of the 1920s which led to the Great Depression can be laid at the feet of the "free market," as Skidelsky asserts, is beyond me.

Post-World War II Monetary and Government Mismanagements

But perhaps he means the more "enlightened" central banking policies of the leading nations of the world in the post-World War II period. The immediate years after 1945 saw "dollar shortages" due to government manipulation of foreign exchange rates,

experiments in the nationalization of industries, forms of "soft" planning, periodic currency crises, and often-misguided fiscal policies. Does Dr. Skidelsky not remember how, in the 1960s, Great Britain was considered the "sick man" of Europe due to government fiscal, monetary, and regulatory policies or the Lira crises in an Italy that seemed to have a new government every other week? Is all this to be put at the doorstep of the free market?

What about the era of "stagflation" in the 1970s, with its seeming anomaly of both rising prices and increasing unemployment that so confused the Keynesian establishment of the time? In America, this had been set off by the Federal Reserve's accommodation starting in the 1960s to create the money to finance the "guns and butter" of the Vietnam War and LBJ's "Great Society" programs. Was it not the wise and trustworthy hands of the Federal Reserve Board of Governors whose monetary policies created in the late 1970s and early 1980s one of the worst price inflations experienced in American history, with nominal interest rates in the double-digit range? Another "win," clearly, for the steady monetary central planning of the Federal Reserve!

What about the high-tech bubble of the late 1990s that went bust, or the recent financial and housing crash of 2008-2009? What had caused them? Alan Greenspan—the central banking "maestro"—set the stage for these with his "anti-deflation" policies at a time when prices were not falling but which created unsustainable savings-investment imbalances not much different than the disastrous monetary policy followed by the Federal Reserve in the 1920s.

Under the additional guiding hand of Ben Bernanke at the Federal Reserve, interest rates between 2003 and 2008, in real terms, were zero or negative, and government housing agencies subsidized tens of billions of dollars in home loans to uncredit-worthy borrowers made possible through monetary expansion and artificially low-cost lending backed with government guaranteed mortgage assurances. Was this all the fault of the free market? No. The fingerprints of the Federal Reserve and the

agencies of the Federal government are all over this “economic crime.”

Government's Hand Off the Monetary Printing Press

Yet, according to Robert Skidelsky, it is the free market that cannot be trusted to integrate and coordinate the monetary system. How much worse of a track record could a private, competitive banking system create compared to the monetary disasters of the last one hundred years under the control of central banks?

It is not a matter of whether or not Bitcoin or other forms of cryptocurrencies end up being the market-chosen money or monies of the future. What the fundamental issue is: monetary central planning—with its embarrassingly awful one hundred year track record with paper monies—or getting government's hand off the handle of the monetary printing press.

Governments cannot be trusted with this power and authority, whether it is done directly by them or through their appointed central banks. Back in 1986, Milton Friedman delivered the presidential address at the Western Economic Association. He declared that after decades of advocating a “monetary rule,” that is, a steady or automatic two or three percent annual increase in the supply of money in place of a more discretionary Keynesian approach, he had concluded that it was all spitting into the wind. Public Choice theory—the application of economic reasoning to analyze the workings of the political process—had persuaded him that the short-run self-interests of politicians, bureaucrats, and special interest groups would always supersede the goal of long-run monetary stability, with the accompanying pressures on those in charge of even presumably independent central banks.

In this article and others written by him around the same time, Friedman never went as far as calling for the abolition of the Federal Reserve or a return to a gold standard. But he did say that, in retrospect, looking over the monetary history of the 20th century, it would have been better to never have had a Federal Reserve or to have gone off the gold

standard. The traditional criticisms of the costs of a gold standard, he said—mining, minting, storing the gold away, when the resources that went into all this could have been more productively used in other ways—paled into almost insignificance compared to the costs that paper money inflations and resulting recessions and depressions.

Skidelsky's Straw Man and Evasions

Robert Skidelsky creates a straw man when he tries to put fear into people about unregulated cryptocurrencies threatening the monetary and price stability of the world. He cannot even get his argument completely straight. On the one hand, he says that Bitcoin has an eventual built-in limit on how much of it might be mined, and he warns that a Bitcoin money, then, would reach a maximum that would not have the “elasticity” to meet growing monetary needs of the future. And in the next breath, he warns that a Bitcoin-like currency might not have a built-in check against inflation. Well, which is it: the danger of Bitcoin price deflation or Bitcoin price inflation?

There has emerged during the last three decades an extensive and detailed literature about the possibilities and potentials of a private, competitive free banking system. The economists who have devoted themselves to serious analysis and exposition of such as a free banking system—people such as Lawrence H. White, George Selgin, and Kevin Dowd, to merely name three of the more prominent ones—have demonstrated that a market-based commodity money and a fully market-based banking system would successfully operate with greater coordinating ability and with far less likelihood of any of the monetary and price instability experienced under central banking over the last one hundred years.

It is unfortunate that a scholar usually as careful and thorough as Robert Skidelsky has chosen to downplay the historical reality of the failure of central banking, and not grapple with the serious and real literature on the private, competitive free banking alternative.

(See my eBook, *Monetary Central Planning and the State*, for an exposition and analysis of the inherent weaknesses in central banking and the nature and workings of an alternative private, competitive banking system.)

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Nelson's Favorite Quotes

"We must, therefore, emphasize that 'we' are not the government; the government is not 'us.' The government does not in any accurate sense 'represent' the majority of the people."

"The great non sequitur committed by defenders of the State...is to leap from the necessity of society to the necessity of the State."

"All of the services commonly thought to require the State...can be and have been supplied far more efficiently and certainly more morally by private persons. The State is in no sense required by the nature of man; quite the contrary."

— Murray Rothbard

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- [Chris Bay - Lawrence, Kansas](#)
- [Mark Benson - Festus, Missouri](#)
- [Scott Chapman - Sandersville, Georgia](#)
- [Mike Everett - Lawrence, Kansas](#)
- [Anthony Faso - Las Vegas, Nevada](#)
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