

FEBRUARY 2019

# BANKNOTES

NELSON NASH MONTHLY NEWSLETTER

## Ryan [Griggs] Speaks at Nelson Nash Institute Think Tank 2019

I will present on the topic *Why Nelson is an Heir to Menger—Reviving Austrian Capital Theory* from the main stage on Wednesday, February 6, 2019. Slides for the presentation are available to view below, and I'll release the full video and audio recording once it is made available to me.

### The Context

I'm extremely thankful to the Board of Directors of the Nelson Nash Institute—David Stearns, L. Carlos Lara, Bob Murphy, and Nelson Nash—for inviting me to speak at the annual conference of Authorized IBC Practitioners and their invited guests. This is a two-day conference where the hundreds of Authorized IBC Practitioners (and their people) are invited to meet and share best practices in the business of Infinite Banking from the agent's perspective. To be asked to share my views with the NNI membership is a career highlight for me.

### The Subject

I argue in my talk that Nelson Nash should be considered an intellectual heir to the founder of the Austrian School of Economics, Carl Menger. The specific thread that ties these two men together is the subject of *capital*. Unfortunately, the idea of capital is fuzzy. Ask 100 people what it is, you'll get 150 answers.

The problem of conceptual imprecision is compounded by the fact that capital theory in general is already fairly abstract, and can be straight-up confusing. However, I believe that a sound understanding of capital will not only show that Nelson Nash and his *Infinite Banking Concept* are *Mengerian* to the core, but that a good idea of capital may in fact be the key to an Austrian Theory of Finance. An *Austrian Finance* to mirror *Austrian Economics*, if you will.

Here's the rub though. I *do not* think that the current view of capital among most Austrian Economists is sufficient. It isn't that it's totally *wrong*, but the emphasis is certainly misplaced.

This is what happened. In 1871 Carl Menger launched the Austrian School of Economics with the publication of his book *Principles of Economics*. Capital was not the subject of that book. In fact, what counts for Austrian

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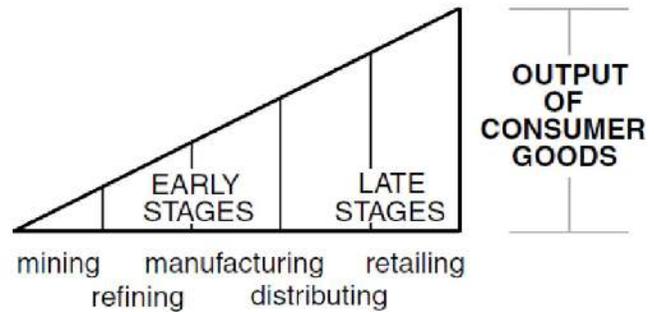
# BANKNOTES - Nelson Nash's Monthly Newsletter - February 2019

Capital Theory today is based on a few lines in what was originally a *footnote* in the book (it's a German footnote, i.e. a very long footnote, and so appears in an appendix in the current publication). In those few lines, Carl Menger calls capital the "quantity of economic goods" employed in production over time.

Those few lines grew up and became modern Austrian Capital Theory. Austrian Economists like Roger Garrison will argue that capital in Austrian Capital Theory is the *temporal structure of production*. *Temporal* refers to time. Production occurs over time. Some production occurs *further away* from the act of consumption. Other production occurs closer in time to consumption. You can group these various production activities, sequentially, according to their proximity in time to consumption.

You can depict this structure in either rectangular or triangular form. In both cases, you see the various stages (or orders) of production arranged (through time) relative to consumption.

You can find this on page 369 of Rothbard's *Man, Economy, and State*.



This is a rendition of the "Hayekian Triangle," a structure of production diagram created by Professor Roger Garrison.

Regardless of the particular choice of shape, capital in this formulation is two things:

1. Heterogeneous (of unlike kind), and
2. Physical

The capital is the stuff. It's the mines, the refineries, the manufacturing plants, the distribution networks, and so on. Obviously, these physical things are of *unlike kind*, meaning they can't be directly compared, or grouped together, with other forms of so-called capital. You can see this if you ask, "how do we measure capital?" Under the *heterogeneous, physical* conception of capital, you can't. The reason is the difference in the *unit of measurement* across the various orders of production. For example, a farm might be measured in acres, a delivery truck in tons, and electricity in kilowatts. Kilowatts of electricity and acres of farmland cannot be aggregated, summed up, or otherwise directly *reconciled*.

The heterogeneous, physical notion of capital does come from Carl Menger, founder of the Austrian School. However, the particular source is one of those lengthy German footnotes in his 1871 book *Principles of Economics*, and that's basically it. The point is that modern Austrian Capital Theory—where capital is heterogeneous and physical—originates in a relatively tiny passage from Menger's book, a book in which the subject

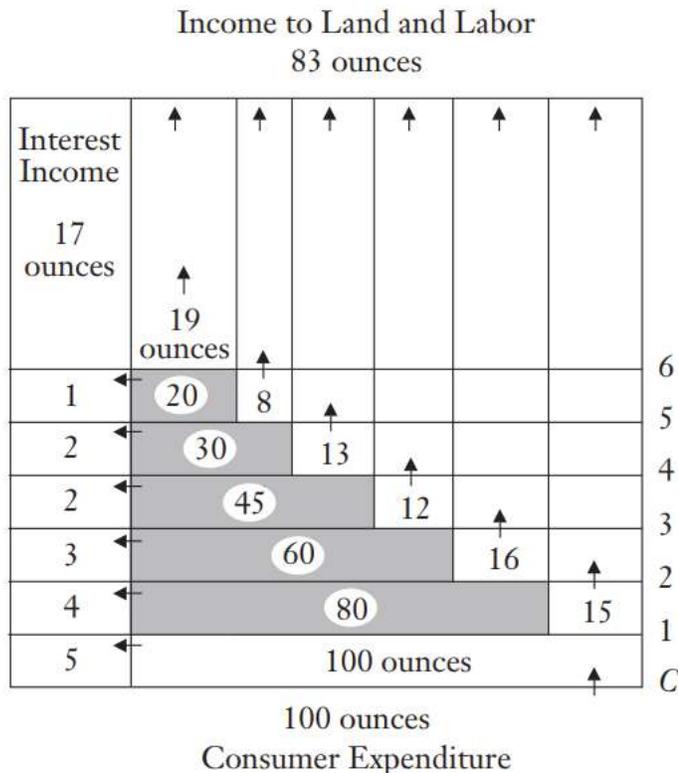


FIGURE 41. INCOME ACCRUING TO FACTORS AT VARIOUS STAGES OF PRODUCTION

was not primarily capital.

It turns out Menger *did* eventually focus on the notion of capital. In 1888 he wrote *Zur Theorie Des Kapitals* (or, *Towards a Theory of Capital*—a German version of which you can see here at Liberty Fund). However, this 1888 article is still publically unavailable in English. That's right, over 130 years have passed since the founder of a major school of economic thought concentrated on capital, and it is still basically unavailable to the English speaking intellectual community.

Fortunately, Professor Edward Braun from Germany, who reads German and writes in English, has translated significant passages of the Menger 1888 article and published them in articles of his own. This is one of them. Braun makes the argument that Menger was pretty clear. I'm posting the Abstract to Braun's article (linked above) here:

*The common interpretation of Carl Menger's take on capital theory rests upon a few sentences in his Principles of Economics. His later monograph on the topic, Zur Theorie des Kapitals (A contribution to the theory of capital), is more or less ignored, although it must be seen as a recantation of his earlier views. As it becomes clear in this work, Menger would have opposed all attempts to define capital as a heterogeneous structure of higher-order goods—A definition that is associated with his name today. In his opinion capital is a homogeneous concept stemming from accounting practices. The debate about Menger's view on capital does not only concern terminological points, but involves the subject matter of capital theory. A theory of capital based on Menger's later view would concentrate on the way the market economy is organized and not on technical characteristics of a multi-stage production process. [bold added]*

What's Braun saying here? He's saying that when Menger turned his attention to capital, he concluded decisively that capital is not heterogeneous and physical. Instead, it is homogenous and monetary.

F.A. Hayek, who apparently was aware of Menger's 1888 views, writes in the Introduction to Menger's

*Principles of Economics* that Menger thought capital was “the money value of assets with acquisitive purpose.”

For example, equity in a house that you use to purchase a car. That's capital. The value of a bank account deposit you use to secure a line of credit. That's capital. The cash value of a dividend-paying whole life insurance policy. That's capital. Capital is not the house itself, the checking deposit, or the life insurance policy. Capital is the value (denominated in money) of those assets after accounting for any debt owed on them. If your house would sell for \$200,000 and you owe \$125,000, then your capital, your equity, is \$75,000. Notice that we can actually perform calculations when we consider capital to be monetary in nature. That's because it is homogeneous, or of a like kind. Different quantities of capital are reckoned in the same unit, like physical-heterogeneous “capital” that is reckoned in different units across the various orders of production.

In my talk I point out that this idea of capital—as homogeneous and monetary—is the key idea underneath the concept of “banking.” In order to bank, you've got to have something to bank with! You've got to have capital. And in Nelson Nash's book *Becoming Your Own Banker*, where he lays out the financial strategy he calls the *Infinite Banking Concept* (IBC), he acknowledges this. After all, the word *capital* appears in one form or another 73 times in the 92-page book. In 72 of those uses, the meaning in context is obviously monetary. In the 73rd, the word *stock* appears in parentheses immediately after. It's obvious that Nelson was referring to the stock or the inventory of the company in this one case. Throughout the rest of the text, Nelson Nash has a Mengerian 1888 conception of capital.

Therefore, Nelson is an intellectual heir to Menger.

In fact, you might say—as I do in the talk—that *Becoming Your Own Banker* is a—if not the—work in applied Mengerian capital theory.

And that is what the *Infinite Banking Concept* is. It's a method to optimally build and deploy

capital—capital in the sense that Menger meant it in 1888.

Next I move to what this means for financial strategy. First, we have to understand the various ways of using capital. I suggest that you can only use capital in two ways: leverage and liquidation. To deploy the equivalent of the equity in your house, you either need to collateralize it and borrow from a mortgage lender or financing company (*leveraging* the capital value), or you need to sell (*liquidate* the capital asset) and use the funds to pay off your lender and to make your purchase.

What Nelson Nash shows in Part III of *Becoming Your Own Banker* is that *if you leverage optimally* (according to the *Infinite Banking Concept*), you can put yourself in a powerful, prosperous position. In other words, Nelson demonstrates that leverage is preferable to liquidation (paying cash)—if done right—when it comes to using capital.

Thus, in order to benefit from capital, we need to be able to *control* it. When it comes down to analyzing assets to see in which it is best to build capital, we want to look at control. Does the borrower maintain control of the capital when he leverages it, or not?

In contrast, in the world of *investment*, it's obvious that we explicitly, *intentionally forfeit* control over financial value. That's the whole idea! The investor gives up control of financial value in order to generate cash flow, a "capital" gain (upon sale), or both. This means that *capital* and *investment* are *categorically distinct*.

Yet, in the financial advisory world, what do we hear about? How much of the advice from the typical financial planner is concerned with intentional, strategic capital accumulation? Effectively zero. Perversely, what little capital accumulation the financial planner *does* advise consists of a meager "emergency fund." Despite the fact that the *purpose* of capital is to *use it*, we are told that what little capital we ought to accumulate (the emergency fund) we *should* not touch—unless of course, we have other option.

Instead, the vast majority (I mean, 98% or more) of conventional advice revolves around investment strategy. Therefore, the financial community effectively councils Americans to *minimize* their control over financial value. To make matters worse, the conventional planner will often advise that the individual "max out" his or her so-called *tax-qualified plan*. These are government-sponsored investment plans that add *an additional penalty* if the individual required and withdrew from the account prior to age 59.5 (in the amount of 10%). It is safe to say that not only does the financial advisory community advise *minimizing* control over capital, if they really had their way, the individual would drive his control over capital into the *negative* by suggesting that he or she should voluntarily seek and accept an additional state-mandated penalty for access to capital.

What's the result of all this?

Answer: the vast majority of Americans are *severely under-capitalized*.

Americans have almost no control over their own capital. And if you don't use capital under your ownership and control, you will rely on those who do. This is fundamentally why so many purchases in today's economy are financed through third-party lending. Consumer debt has skyrocketed, the total value of mortgage-debt is unprecedented, as is auto-loan debt, student-loan debt, credit card debt, etc. You name it, and Americans have financed it with third-party lending.

Consequently, Americans are exposed to the *cost of dependency on third-party lending*. What's this look like? It's everything we have become conditioned to believe is acceptable. Lengthy, time-consuming applications, physical collateral assignments, use restrictions, repayment schedules, hostile bill collections departments, reliance on bank personnel relationships, dependency on bank lending policy, high interest and fees (e.g. amortization, points, etc.). Cost of dependency on conventional lending is *the single greatest drain* on the resources of the modern American.

And the financial community says nothing about it.

Imagine if doctors paid no attention to diet, instead focusing only on illnesses. Imagine if auto mechanics paid no attention to oil system maintenance, instead focusing only on mechanical failures. Imagine if teachers paid no attention to course content, instead focusing only on how much fun students had. You get the idea.

However, I don't intend to neglect investment in the way conventional financial advisers neglect capital. To the contrary, with an appropriate understanding of capital, we are in an *enhanced* position to address optimal investment strategy.

Consider the opportunities to generate a return for two types of individuals: the *under-capitalized* and the *well-capitalized*. Let's take the case of the majority first: the *under-capitalized*.

Think of the list of investment opportunities the typical, *under-capitalized* individual faces. First, the tax-qualified 401(k) or 403(b) options. An employer may offer a selection of 10 to 20 or so options. Each of these options is *mass-marketed* at least nationally, and potentially globally, thereby exposing the investor to systemic risk (this is because the modern financial system is based on the commercial lending system of *fractional reserve banking*—a subject for another time).

These few, mass-marketed investment options are fairly homogeneous in nature—they're of a like-kind. Sure, the various mutual funds have varying allocation algorithms, some may be actively traded, others passively, but they're all "in the market" to one extent or another. The *actual, compounded* (as opposed to *average annualized*) return on these options vary year to year. In 2008, many mutual funds took a proper kick in the teeth of -50%.

The conventional financial adviser will say, "well that's alright, in general, if you stay in the market long enough, things will work out." The idea is that *in the long run*, you win. Astonishingly, what the conventional financial advisory world seems to miss is the fact that *in the long run*, *the long run becomes*

*the short run*. Look, if you're 70 years old, how much more long run do you have to go? For an older person, the so-called *long run* is a lot shorter than what it is for the young person.

And pray tell, what will the market be doing in 40 years? How about 30 years? The financial elite take to the airwaves after every major market correction and plead to consumers of their "advice" that "no one saw this coming." Well, even if that were true (it's not), why in the world would I then want to expose my nest egg to this risk that "no one" can see coming? Maybe you're starting to see my point.

In short, investment opportunities are *few, mass-marketed, homogenous, and systemically-risky*. As a special bonus, the under-capitalized is also exposed to the cost of dependency on third-party capital. Oh, and resources to engage in entrepreneurship? Forget about it. The under-capitalized employee has stacked the deck against themselves, and will most likely *remain* in their current industry. This presents a relatively higher degree of risk associated with a relatively high degree of labor specialization. If an individual lacks the resources (capital) to finance his or her transition to a new industry, say, when technological advancements cause increased substitution of machines and equipment for labor, then the cost of that transition will be higher. Put differently, opportunity for improvement for the under-capitalized is bad across the board.

Consider the opportunities that the well-capitalized confront. Everyone knows on some gut-level that "people with money" face a unique dilemma. The under-capitalized (those *without* control over financial value) will *beat the door down* of the well-capitalized to pitch this or that new investment or entrepreneurial opportunity. Think of the TV series *Shark Tank* where thousands (tens of thousands? Hundreds of thousands?) compete to get on the show and vie for the favor of the well-capitalized "sharks." In other words, for the well-capitalized, opportunity *comes to you*, whereas the under-capitalized must pay all sorts of costs and accept all sorts of risk to *seek out* profitable investment opportunity.

Furthermore, opportunity for the well-capitalized will likely be *personal*, if not *local* or even *exclusive*. Maybe the investment opportunity is investing in your friend's business. Maybe your neighbor is thinking of selling his perfectly rentable house. Maybe you and a co-worker are thinking of breaking out on your own. Whatever it may be, the likelihood for personal interaction between *investor* and *investee* produces the potential for *trust*, be it through past experience or the expectation of future, repeat interaction. Does the under-capitalized mutual fund investor know and trust his fund manager? Not likely. Even if he did, mutual fund managers turn over, on average, every five years, so even if he did know one manager, what're the odds he will know the next one, or the one after that?

Finally, unique, local, trust-based investment opportunities are also relatively more likely to be *highly profitable*. An investment in a company that doesn't exist yet, will generate much higher returns to the investor than one in your standard mutual fund. So if a "high rate of return" is really the holy grail of financial analysis, maybe we should be asking, "what is the best way to approach investing in the first place?" If we did so, we might wind up concluding that it is far better to approach investing *well-capitalized*.

So far, we have discussed the different views of capital: the modern Austrian view, versus the view expressed in Menger 1888. We expanded on the idea of capital as the money value of assets with acquisitive purpose. We saw that view of capital in Nelson Nash's *Becoming Your Own Banker* adheres to the Menger 1888 notion. This gives us the context we need to see that the *Infinite Banking Concept* is simply the best way to build and accumulate capital. Then we integrated the two distinct notions of capital and investment from the perspective of a generalized financial strategy. In other words, we made up for what the conventional financial adviser neglects, i.e. the role of capital, the individual's control over it, and how it affects our investment and entrepreneurial opportunities.

Let me clear up one thing: why is it that the IBC is

the optimal method of building and accumulating capital? Succinctly put, it is the only asset in which one can build capital whereby, when collateralized, the lender of funds is also the guarantor of the collateral. See, the issue in every other lending transaction in the world is that the value of the collateral is inherently uncertain. Something is only worth what someone else is willing to pay for it, and with most assets, we don't know what someone else in the future would be willing to pay.

Imagine if a mortgage lender could guarantee the future value of a home. Then, if the individual borrower failed to repay the mortgage, the lender could be certain that they could recoup their losses. But of course, no mortgage lender can guarantee the future value of a home, because no single actor in the real estate market can directly affect the future value of any property!

With the IBC and dividend-paying whole life insurance, this problem disappears. When you collateralize equity (called *cash value*) in one of these policies and receive money (in the form of a *policy loan*) from the lender (the life insurance company that sold the policy), the collateral (the cash value) is guaranteed by the lender (the life insurance company). It's as if the mortgage lender really could guarantee the value of the home. If a mortgage lender could guarantee the value of a home, then the lender wouldn't impose such high costs (in all the forms discussed above) on the borrower! This—the uncertainty of the value of collateral—is the source of the cost of dependency on third-party capital.

In other words, dividend-paying whole life insurance just so happens to offer the best terms of leverage to the individual. It offers the greatest level of control to the individual (there are other advantages too, like the tax treatment and growth guarantees, but these are fundamentally ancillary benefits). The way this manifests in practice is that the individual policy-owner/borrower doesn't have to fill out any lengthy applications; there are no use restrictions; there are no physical collateral assignments, no repayment schedules, no bill collections departments, no

reliance on bank personnel or bank lending policy, and so on. In other words, we eliminate the cost of dependency on third capital.

This means that the individual who adopts and implements the IBC eliminates the single greatest drain on his or her resources and positions him- or herself to become well-capitalized, thereby positions him- or herself to reap the benefits of the well-capitalized approach to investment and entrepreneurship.

In my talk at NNI I address some regulatory issues that agents should be aware of. The bottom line is that in the past, the life insurance industry has done a poor job of defending itself against colluding special interests. This has resulted in the implementation of unfavorable tax treatment for some life insurance contracts. Frederic Bastiat is alleged to have said (I'm paraphrasing) that "the worst thing for a good cause is not a skilled attack, but an inept defense." As an industry, we should be aware that the past accusation that what an individual who adopts the IBC is doing is reaping "investment returns without paying investment tax" is flawed on basically every level. Instead, we should remain steadfast that, no, what the adopter of IBC is doing is becoming well-capitalized. In fact, if anything, this will position the individual to *do better* in the investment world and therefore *pay even* more investment tax.

If you've made it through all of the above, bravo, you've really accomplished something. I will release the video of my talk when it is made available by NNI staff.

Thank you for your time and attention!

Click below to view the slides that accompany this presentation.

[https://docs.google.com/presentation/d/e/2PACX-1vRGyvs8uWlBmageZ4ZUdUBbtHHeMg9h-U9wgW\\_4hiP82xS\\_yOHdCxAKT1SYvVQNKi\\_P0fDJxgqgtzR1/pub?start=false&loop=false&delayms=3000](https://docs.google.com/presentation/d/e/2PACX-1vRGyvs8uWlBmageZ4ZUdUBbtHHeMg9h-U9wgW_4hiP82xS_yOHdCxAKT1SYvVQNKi_P0fDJxgqgtzR1/pub?start=false&loop=false&delayms=3000)

## The Government Shutdown Reveals Another Reason to Abolish the TSA

Ryan McMaken

The Transportation Security Administration, a federal agency, is facing a no-show problem with employees, as paychecks are put on hold during the partial government shutdown. This is reportedly leading to longer lines and security problems at airports nationwide. According to CNN,

Hundreds of Transportation Security Administration officers, who are required to work without paychecks through the partial government shutdown, have called out from work this week from at least four major airports...

TSA spokespeople, meanwhile, insist everything is completely normal although absenteeism has "increased by 200% to 300%," according to Marketwatch.

Not everyone was as sanguine about the situation as government officials. One frequent traveler complained "The lines were exceptionally longer than normal, especially for a peak departure time frame of 8 a.m. to 12:30 p.m."

Given that the feds admit more employees are skipping work, it's hard to believe that everything's humming along normally — unless workers are lowering security standards to get more people through the line quickly.

But, that, of course, is something the feds insist they would never, ever do.

In any case, the whole affair reminds us of just one of the many pitfalls that come with federalizing airport security and making it all part of one giant, nationwide federal bureaucracy.

TSA screeners are federal employees, and their salaries are paid out of a federal budget — of now more than 7 billion dollars. In fiscal year 2018, more than four billion of the TSA's 7.5 billion budget came from government appropriations, with the rest

coming from fees on passengers and the industry. Since 2017, the Trump Administration has proposed to increasing fees " to cover 75% rather than 40% of the Transportation Security Administration's costs."<sup>1</sup> But even if the Trump Administration were to get its wish, the TSA would still remain a federal agency with federal employees, and a substantial of its budget would still come from federal appropriations.

In other words, the next time there's a government shutdown, we'd be looking, yet again, at a situation in which the entire nationwide system of airports would be affected because a tiny number of politicians in DC couldn't agree on a nationwide budget.

It doesn't have to be this way. Nor were things this way prior to the federalization of airport security in the wake of the 9/11 terrorist attacks.

Thanks to the George W. Bush Administration, airport security was federalized only two months after 9/11, with Bush proudly declaring at the time: "For the first time, airport security will become a direct, federal responsibility." There were federal regulations in place dictating how security was conducted, of course, but the employees and the funding were largely decentralized in how they were distributed and used.

As a result, a federal shutdown under a system like this does not mean that the employees won't get paid or that "non-essential" personnel are simply sent home.

## The TSA Doesn't Keep Us Safe

In response, supporters of the status quo are likely to respond that the TSA "keeps us safe" and only a federalized version of airport security can work.

Unfortunately, for them, there is no evidence to support this position.

First of all, that there has been no serious and successful terrorist hijacking since 9/11 does not prove the effectiveness of the TSA. After all, the creation of the TSA is just one change since 9/11.

Indeed, 9/11-style hijackings were obsolete by the

afternoon of September 11, 2001. Their success rested largely on the fact that the airline industry and FAA regulators adhered to a policy of compliance when it came to hijackers. As a report from Stratfor notes:

Before 9/11, aircraft crews were trained not to resist hijackers but to comply with their instructions in an effort to calm the situation and land the plane. Once the aircraft was on the ground, hijackers would then either surrender or be killed by an aircraft entry team. The Federal Aviation Administration never dreamed that terrorists would commandeer an aircraft with the intent to use it as a weapon. Aware of this, the 9/11 attackers simply had to pretend to be typical hijackers to gain the crews' cooperation and take control of the aircrafts.

A compliance policy will never be used again:

But the advantage Mohammed [Atta] gained by shifting the hijacking paradigm was short-lived, as evidenced by the events that unfolded that morning aboard the fourth aircraft: United Airlines Flight 93.

The attackers who targeted the plane did not account for the fact that its passengers and crew were able to use their cellphones to talk to people on the ground. When they learned what had happened to the three other aircraft, they revolted and forced the hijackers to crash the plane before it could be used to target the U.S. Capitol.

In other words, a major reason that there haven't been any 9/11-type hijackings since 9/11 is that terrorists know people will react in a completely different way to a potential hijacking.

In the case of Flight 93, the hijackers only got as far as they did because the crew and passengers initially complied. Once the truth was learned, the situation changed dramatically. Now that 9/11 is common knowledge, not even initial compliance could be expected from terrorists.

Other factors include the placement of air marshals on some planes, and better security for cockpits.

The maintenance of an enormous corps of federally employed TSA employees has nothing to do with any of these factors.

And then there is the research which shows that the TSA has a 95-percent failure rate in detecting efforts by terrorists to place weapons on commercial flights. Dylan Matthews wrote at Vox in 2016:

The TSA is hard to evaluate largely because it's attempting to solve a non-problem. Despite some very notable cases, airplane hijackings and bombings are quite rare. There aren't that many attempts, and there are even fewer successes. That makes it hard to judge if the TSA is working properly — if no one tries to do a liquid-based attack, then we don't know if the 3-ounce liquid rule prevents such attacks.

So Homeland Security officials looking to evaluate the agency had a clever idea: They pretended to be terrorists, and tried to smuggle guns and bombs onto planes 70 different times. And 67 of those times, the Red Team succeeded. Their weapons and bombs were not confiscated, despite the TSA's lengthy screening process. That's a success rate of more than 95 percent.

Defenders of the TSA — much like defenders of the CIA and other "security" organizations — claim that the TSA surely succeeds in stopping terrorists quite often. Those successes, however, are secret and we can't know about them.

This sort of faith-based trust in government might be convincing for some, but it ought to strike most people capable of critical thinking as nonsensical.

The fact remains — if we exclude the hypothetical "secret files of amazing successes" maintained by government agencies — there is no empirical evidence that the TSA prevents terrorism, and even in theory, we can easily point to other factors that are much more important in the prevention of another 9/11.

On the other hand, the federalization of airport security does create a situation in which national politics can easily create a system-wide failure

in airport security that would not be possible in a system without the centralization of the TSA system.

1. For more, see page 20 of the TSA's budget documents: <https://www.dhs.gov/sites/default/files/publications/TSA%20FY18%20Budget.pdf>

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## The Nash Equilibrium Minimum Wage Is Zero

**It is only at this final state, of which there does not exist a government-imposed minimum wage level that the system can find its true equilibrium.**

Dave Sukoff

As the New Jersey legislature and governor debate the details of a hike in the state's minimum wage to \$15 an hour, it is worth taking a step back and contemplating one of the greatest thinkers in New Jersey history, Nobel Laureate John Nash. (Nash was the subject of the 2001 film *A Beautiful Mind*, starring Russell Crowe.)

In the most basic economic terms, a minimum wage is a price floor that distorts the supply-demand curve, thus creating an inefficiency. In layman's terms, the minimum wage reduces employment for less-skilled and less-educated workers by forcing employers to pay a wage that is higher than what they would ordinarily pay for a certain job. This is generally the reasoning against raising the minimum wage or even having one to begin with, as *The New York Times* argued back in 1987. Perhaps a better way to look at the harmful effects of the minimum wage is as a Nash equilibrium problem.

A Nash equilibrium involves a system in which

there are numerous participants, each with a strategy designed to maximize their own utility. Whether the participants cooperate or not, at some point they will each find a state in which no move makes them better off. It can be viewed as an iterative process. One person makes a decision that impacts the next, which impacts the next, and so on. This process continues until there are simply no more moves to make.

## Why Not Infinity Dollars?

The “Fight for 15,” as the minimum wage increase campaign has generally been referred to, is merely an arbitrary moniker with a nifty catchphrase. It sounds good. Let’s all fight for a \$15 wage. But why? Wouldn’t we prefer a “Sweet \$16”? Of course we would. But why stop there? How about “Takin’ Twenty,” or “Thankful for Thirty,” or “Begging for Benjamins”? They are all fairly arbitrary. If anything, we might as well simply use “Show Me the Money.” That is because where this part of the equilibrium problem ends is at infinity—just some vague concept of as much money as possible. After all, \$15.01 is better than \$15.00, and so on, and so on, and so on.

We saw similar logic in the 1998 film *There’s Something About Mary*. In a scene where Ben Stiller’s character picks up a hitchhiker, a discussion about the “8 Minute Abs” video sheds light on the faulty logic that raising the minimum wage is premised on. If you can get great abs in eight minutes, why not a seven-minute workout? But if you can do it in seven minutes, why not six? This would, of course, lead all the way down to zero minutes, and thus with certainty no ab workout. On the way back up, it leads to an infinite workout. And of course, the optimal workout time is based on each individual’s needs.

One can imagine the scene being about the minimum wage as opposed to an abs workout, with the hitchhiker offering up the great idea of raising the minimum wage to \$15 and Stiller responding with “Unless, of course, we raise the minimum wage to \$20.”

Sadly, the minimum wage is not a joke. It has real-world negative consequences for those who can least afford fewer job opportunities. *The primary purpose of a minimum wage is protecting those who would otherwise earn above that level at the expense of those who would otherwise earn less.* This was always the original intent of minimum wage laws. And today, whether nefarious or not, these laws have the same impact.

The minimum wage level, as we push the number to infinity, is simply a line reflecting who gets harmed and who does not. At some point, an employer simply cannot afford to hire an employee. At some point, there are simply no jobs to be had.

## Zero Dollars Is Best

Then we start to bring the number back down. First to the realm of real numbers. Then to numbers that could feasibly lead to actual employment. Then to numbers that start to allow the most people to participate. Then to numbers that do not exclude those most in need of work to be employed. And finally, we settle on the level that takes the decision out of the hands of the government. It is not some arbitrary number. Rather, it is zero. As in, there is simply no level of a minimum wage that can make sense when looked at as a Nash equilibrium problem, where we take logical steps from zero to infinity and then all the way back down to zero.

It is only at this final state, of which there does not exist a government-imposed—and arbitrary—minimum wage level that the system can find its true equilibrium. Only in this optimal state can every participant in the system determine at what level they are willing to work or offer employment based on their own ability and utility curve.

At any level above zero, a minimum wage has the potential to exclude someone from employment. At any level above zero, then, there exists the possibility of harm to people. At zero, that possibility simply does not exist. Do we prefer the Nash equilibrium in which every person is free to choose their own employment path? Or do we prefer allowing Governor Murphy and the New Jersey

legislature, or the federal government for that matter, to arbitrarily pick a number at which there are some winners but mostly losers—the ones who can afford it the least?

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## Bastiat Can Help You Understand the Root of Our Disharmony

**The French economist's timeless principles on social harmony and government rigidity.**

Gary M. Galles

Amid the hyperbole devoted to the partial government shutdown, Americans have heard the soap opera details of behind-the-scenes jockeying and Twitter smack-downs while being told how dire things are as a result. In fact, with all the blaming of opponents for extremism and unprincipled intransigence in preventing a resolution, you might think that the government status quo they are trying to get back to is the means to national harmony. That would be seriously mistaken.

The government we suffer from is the primary cause of our disharmony, which is why liberty requires a partial government shutdown.

Continually leveraging government power into ever-more areas where people's views dramatically differ expands how frequently some people's preferences are forced on others. That guarantees acrimony, not harmony. And our public servants in Washington could use some wisdom on that score. For that, they could turn to one of the most insightful observers of government's influence on social comity—Frédéric Bastiat, among history's ablest defenders of freedom, in his *Economic Harmonies*.

“All men's impulses, when motivated by

legitimate self-interest, fall into a harmonious social pattern...the practical solution...is simply not to thwart those interests or to try to redirect them.”

“Coercion...[has] never yet done anything... except to eliminate liberty.”

“Where do you...establish the acting principle of coercion?...if you entrust men with arbitrary power, you must first prove that...their minds will be exempt from error, their hands from greed, and their hearts from covetousness.”

“But it is not necessary to force into harmony things that are inherently harmonious.”

“Let men labor, exchange, learn, band together, act, and react upon one another...there can result from their free and intelligent activity only order, harmony and progress.”

“The question is whether or not we have liberty... not profoundly disrupted by the contrary act of institutions of human origin.”

“Social order, freed from its abuses and the obstacles that have been put in its way...[is] the most admirable, the most complete, the most lasting, the most universal, and the most equitable of all associations.”

“The laws of Providence are harmonious... only when they operate under conditions of freedom...Therefore when we perceive something inharmonious in the world, it cannot fail to correspond to some lack of freedom or justice.”

“The state always acts through the instrumentality of force...What are the things that men have the right to impose on one another by force?...I have no right to force anyone to be religious, charitable, well educated, or industrious; but I have the right to force him to be just: this is a case of legitimate self-defense.”

“If, therefore, the use of force by the individual is justified solely on grounds of legitimate self-defense, we need only recognize that government action always takes the form of force to conclude

that by its very nature it can be exerted solely for the maintenance of order, security, and justice. All government action beyond this limit is an encroachment upon the individual's conscience, intelligence, and industry—in a word, upon human liberty.”

“Accordingly, we must [turn]...to the task of freeing the whole domain of private activity from the encroachments of government.”

“Restrict the public police force to its one and only rightful function...from what source could come all our present ills...which teach the people to look to the government for everything...to the ever increasing and unnatural meddling of politics into all things.”

“[Many] causes of disturbances, friction, disaffection, envy, and disorder would no longer exist...it reduces evil to the smaller and smaller area left open to it by the ignorance and perversity of our human frailty, which it is the function of harmony to prevent or chastise.”

*Economic Harmonies* identified the principled defense of individual rights and freedom as central to social harmony and progress. But such freedom required government “exerted solely for the maintenance of order, security, and justice.” Every expansion beyond that narrow bound expands disharmony.

Politicians promise harmony and blame opponents for destroying it. But government acting as the ubiquitous dispenser of goodies and garnishments destroys harmony. So the fight in Washington is not the cause of division, and no temporary DC détente can eliminate it. The core fight is over how invasive, and thus how destructive of harmony, government will be.

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## Why Steve Jobs, not Bill Gates, Was the True Education Visionary

Apple's visionary motto of “Think Different” challenges the status quo, while Microsoft's “Empowering Us All” may just capture the next incremental change on a well-trodden path.

Kerry McDonald

When it comes to education reform, there are generally two camps: those who want to improve the existing mass compulsory schooling system through tweaking and tuning and those who want to build something entirely new and different. Not surprisingly, Apple co-founder Steve Jobs was in the “think different” camp, advocating for school choice and vouchers, while Microsoft's Bill Gates backed the Common Core State Standards and other incremental reforms within the conventional mass schooling model.

### The Efforts of the Gates Foundation

The Bill and Melinda Gates Foundation has funneled hundreds of millions of dollars into K-12 education over the past 20 years, including \$280 million toward Common Core, which people of all political persuasions came to despise for its standardization and government overreach. Earlier this week, the Gates Foundation announced an additional \$10 million to train teachers on “high quality” curriculum. The charity is on track to reach its goal of dedicating nearly \$2 billion dollars to K-12 education by 2022.

These huge philanthropic efforts, combined with the nearly \$700 billion a year that US taxpayers spend on K-12 mass schooling, means Americans spend more on education than any other country but with far more dismal results. Chipping away slowly at standard schooling may not be doing much good.

### Jobs Saw the Need for Disruption

Steve Jobs recognized this. He saw that true educational transformation requires disrupting the entire mass schooling model. As he did with his revolutionary Apple products, Jobs envisioned an

education system that is innovative, experimental, and individualized for each learner. In a 1995 interview with the Smithsonian Institution, Jobs asserted his support for vouchers and entrepreneurial educators:

I believe very strongly that if the country gave each parent a voucher for forty-four hundred dollars that they could only spend at any accredited school several things would happen. Number one, schools would start marketing themselves like crazy to get students. Secondly, I think you'd see a lot of new schools starting... You could have twenty-five-year-old students out of college, very idealistic, full of energy instead of starting a Silicon Valley company, they'd start a school. I believe that they would do far better than any of our public schools would. The third thing you'd see is, I believe, is the quality of schools again, just in a competitive marketplace, start to rise. Some of the schools would go broke. A lot of the public schools would go broke. There's no question about it. It would be rather painful for the first several years... But far less painful I think than the kids going through the system as it is right now.

For Jobs, vouchers were only one piece of the education transformation puzzle. He realized that an incremental approach to reforming the existing mass schooling model does not work because of the power structures and bureaucratic tendencies inherent in conventional schooling. In the same Smithsonian interview, Jobs said:

I'd like the people teaching my kids to be good enough that they could get a job at the company I work for, making a hundred thousand dollars a year. Why should they work at a school for thirty-five to forty thousand dollars if they could get a job here at a hundred thousand dollars a year? Is that an intelligence test? The problem there, of course, is the unions. The unions are the worst thing that ever happened to education because it's not a meritocracy. It turns into a bureaucracy, which is exactly what has happened. The teachers can't teach and administrators run the place and nobody can be fired. It's terrible.

## Two Different Experiences, Two Different Outlooks

The vastly different education policy approaches favored by Gates and Jobs may be due in part to their own childhood schooling experiences. Gates attended a private day school, Lakeside School, in Seattle, Washington, and said in 2005: "Lakeside was one of the best things that ever happened to me."

Jobs, on the other hand, had a far less favorable reaction to his public schooling. He recalled:

School was pretty hard for me at the beginning. My mother taught me how to read before I got to school and so when I got there I really just wanted to do two things. I wanted to read books because I loved reading books and I wanted to go outside and chase butterflies. You know, do the things that five-year-olds like to do. I encountered authority of a different kind than I had ever encountered before, and I did not like it. And they really almost got me. They came close to really beating any curiosity out of me.

While both of these tech moguls dropped out of college to start wildly successful businesses, their opinions on K-12 education policy reflect many of the differences that came to symbolize their respective companies. Apple's visionary motto of "Think Different" challenges the status quo, while Microsoft's "Empowering Us All" may just capture the next incremental change on a well-trodden path.

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.

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## George Washington's State of the Union Address Holds Lessons for the 21st Century

**It was a time when government knew its limits and its proper place, and the people did too.**

Lawrence W. Reed

A few million people will be watching when President Trump delivers his State of the Union Address to a joint session of Congress on January 29. I doubt I'll be one of them. The last State of the Union I watched from start to finish was literally 30 years ago, and I don't feel the least bit deprived—intellectually, spiritually, or otherwise.

The first State of the Union address was delivered in about ten minutes by George Washington on this very date—January 8—in 1790. At barely 800 words, it was the shortest of them all (which now number nearly 230). Like the federal government itself, the subsequent ones grew far more in size than in quality.

Bill Clinton holds the record for the longest State of the Union Address in US history—a stupefying one hour and 28 minutes of nothing that anyone remembers. That was in 2000. It broke the previous record, set by Clinton himself, just five years before.

Whether the country wants to hear a State of the Union or not, every president gives us one each year because the Constitution mandates it. How long it is and what ground it covers is up to each president. And he can make it as general or as specific as he chooses and as partisan or non-partisan as he desires.

### State of the New Union

Nostalgia prompted me recently to give Washington's first State of the Union a look. Any president who can get the job done in ten minutes, I figure, is worth paying attention to.

When Washington spoke on January 8, 1790, federal spending as a share of GDP was about 1.5 percent (it's 14 times that today). Federal debt was an estimated 30 percent of GDP, but it was on a path to

zero, which it reached by the 1830s. The new nation was at peace with a new Constitution in place, and most people wanted to get on with their lives. They expected the national government to tend to its limited business of keeping the country free, get it done at minimal expense, and otherwise leave them alone. Washington's address reflected that consensus.

He opened by congratulating the House and Senate for presiding over “the present favorable prospects of our public affairs.” He noted, in particular, the country's strong credit and the impressive degree of respect America had earned in the world. To keep things moving in the right direction, he said, would require of members of Congress their “cool and deliberate exertion” of “patriotism, firmness and wisdom.”

### Preserving the Peace

The most important matter deserving of the Congress's attention, Washington advised, was “the common defense.” That is so politically incorrect in our age when 80 percent of federal spending has nothing to do with defense and lots to do with redistributive transfer payments and interest on past debts. In 1790, our first president made his point in a single memorable sentence when he said, “To be prepared for war is the most effectual means of preserving the peace.”

Keep in mind that Washington was no foreign adventurer; when he left office, he warned against “entangling alliances” and mischievous interventions. To him, and most Americans of his day, the federal government's chief responsibility was to protect this nation, not a hundred others.

He suggested that the troops should be paid and the country should strive to be independent of foreign powers for its military supplies.

### Limited Government

After a few paragraphs about defense, he asked Congress to come up with a definitive process of naturalization for foreigners seeking US citizenship; to establish uniformity in currency and in weights and measures; to encourage the embrace of

inventions from home and abroad, and to tend to the creation of roads for delivering the mail.

Washington mentioned the importance of education, science, and literature but did not propose in his address any specific federal ventures in this regard. Noting that “Knowledge is in every country the surest basis of public happiness,” he urged in the same breath “a speedy but temperate vigilance against encroachments [on liberty], with an inviolable respect to the laws.”

He closed his address with these words:

And I shall derive great satisfaction from a co-operation with you, in the pleasing though arduous task of ensuring to our fellow citizens the blessings, which they have a right to expect, from a free, efficient and equal Government.

Wow! A State of the Union Address that didn't make promises that couldn't be kept, didn't try to buy anybody's vote with somebody else's money, didn't propose anything that violated the spirit or the letter of the Constitution; didn't mortgage our liberties with handouts; and didn't pit one class or group against another. How refreshing!

Keep it short and sweet, set the tone, focus on the fundamentals. That must have been the advice of Washington's speechwriter (himself). It was all over in ten minutes. The very thought of it makes me pine for the days when government knew its limits and its proper place, and the people did too. We were too busy building a nation to let a politician spend 90 minutes of our time telling us about it.

Hallelujah.

Lawrence W. Reed is president of the Foundation for Economic Education and author of *Real Heroes: Incredible True Stories of Courage, Character, and Conviction* and *Excuse Me, Professor: Challenging the Myths of Progressivism*.

## The Cure for Poverty

Henry Hazlitt

[Chapter 20 of *The Conquest of Poverty*, 1996.]

The theme of this book is the conquest of poverty, not its “abolition.” Poverty can be alleviated or reduced, and in the Western world in the last two centuries it has been almost miraculously alleviated and reduced; but poverty is ultimately individual, and individual poverty can no more be “abolished” than disease or death can be abolished.

Individual or family poverty results when the “breadwinner” cannot in fact win bread; when he cannot or does not produce enough to support his family or even himself. And there will always be some human beings who will temporarily or permanently lack the ability to provide even for their own self-support. Such is the condition of all of us as young children, of many of us when we fall ill, and of most of us in extreme old age. And such is the permanent condition of some who have been struck by misfortune — the blind, the crippled, the feeble-minded. Where there are so many causes there can be no all-embracing cure.

It is fashionable to say today that “society” must solve the problem of poverty. But basically each individual — or at least each family — must solve its own problem of poverty. The overwhelming majority of families must produce more than enough for their own support if there is to be any surplus available for the remaining families that cannot or do not provide enough for their own support. Where the majority of families do not provide enough for their own support — where society as a whole does not provide enough for its own support — no “adequate relief system” is even temporarily possible. Hence “society” cannot solve the problem of poverty until the overwhelming majority of families have already solved (and in fact slightly more than solved) the problem of their own poverty.

All this is merely stating in another form the Paradox of Relief referred to in Chapter 18: *The richer the community, the less the need for relief, but the more*

*it is able to provide; the poorer the community, the greater the need for relief, but the less it is able to provide.*

And this in turn is merely another way of pointing out that relief, or redistribution of income, voluntary or coerced, is never the true solution of poverty, but at best a makeshift, which may mask the disease and mitigate the pain, but provides no basic cure.

Moreover, government relief tends to prolong and intensify the very disease it seeks to cure. Such relief tends constantly to get out of hand. And even when it is kept within reasonable bounds it tends to reduce the incentives to work and to save both of those who receive it and of those who are forced to pay it. It may be said, in fact, that practically every measure that governments take with the ostensible object of "helping the poor" has the long-run effect of doing the opposite. Economists have again and again been forced to point out that nearly every popular remedy for poverty merely aggravates the problem. I have analyzed in these pages such false remedies as the guaranteed income, the negative income tax, minimum-wage laws, laws to increase the power of the labor unions, opposition to labor-saving machinery, promotion of "spread-the-work" schemes, special subsidies, increased government spending, increased taxation, steeply graduated income taxes, punitive taxes on capital gains, inheritances, and corporations, and outright socialism.

But the possible number of false remedies for poverty is infinite. Two central fallacies are common to practically all of them. One is that of looking only at the immediate effect of any proposed reform on a selected group of intended beneficiaries and of overlooking the longer and secondary effect of the reform not only on the intended beneficiaries but on everybody. The other fallacy, akin to this, is to assume that production consists of a fixed amount of goods and services, produced by a fixed amount and quality of capital providing a fixed number of "jobs." This fixed production, it is assumed, goes on more or less automatically, influenced negligibly if at all by the incentives or lack of incentives of specific

producers, workers, or consumers. "The problem of production has been solved," we keep hearing, and all that is needed is a fairer "distribution."

What is disheartening about all this is that the popular ideology on all these matters shows no advance — and if anything even a retrogression — compared with what it was more than a hundred years ago. In the middle of the nineteenth century the English economist Nassau Senior was writing in his journal:

It requires a long train of reasoning to show that the capital on which the miracles of civilization depend is the slow and painful creation of the economy and enterprise of the few, and of the industry of the many, and is destroyed, or driven away, or prevented from arising, by any causes which diminish or render insecure the profits of the capitalist, or deaden the activity of the laborer; and that the State, by relieving idleness, improvidence, or misconduct from the punishment, and depriving abstinence and foresight of the reward, which have been provided for them by nature, may indeed destroy wealth, but most certainly will aggravate poverty.<sup>1</sup>

Man throughout history has been searching for the cure for poverty, and all that time the cure has been before his eyes. Fortunately, as far at least as it applied to their actions as individuals, the majority of men instinctively recognized it — which was why they survived. That individual cure was Work and Saving. In terms of social organization, there evolved spontaneously from this, as a result of no one's conscious planning, a system of division of labor, freedom of exchange, and economic cooperation, the outlines of which hardly became apparent to our forebears until two centuries ago. That system is now known either as Free Enterprise or as Capitalism, according as men wish to honor or disparage it.

It is this system that has lifted mankind out of mass poverty. It is this system that in the last century, in the last generation, even in the last decade, has acceleratively been changing the face of the world,

and has provided the masses of mankind with amenities that even kings did not possess or imagine a few generations ago.

Because of individual misfortune and individual weaknesses, there will always be some individual poverty and even “pockets” of poverty. But in the more prosperous Western countries today, capitalism has already reduced these to a merely residual problem, which will become increasingly easy to manage, and of constantly diminishing importance, if society continues to abide in the main by capitalist principles. Capitalism in the advanced countries has already, it bears repeating, conquered mass poverty, as that was known throughout human history and almost everywhere, until a change began to be noticeable sometime about the middle of the eighteenth century. Capitalism will continue to eliminate mass poverty in more and more places and to an increasingly marked extent if it is merely permitted to do so.

In the chapter “Why Socialism Doesn’t Work,” I explained by contrast how capitalism performs its miracles. It turns out the tens of thousands of diverse commodities and services in the proportions in which they are socially most wanted, and it solves this incredibly complex problem through the institutions of private property, the free market, and the existence of money — through the interrelations of supply and demand, costs and prices, profits and losses. And, of course, through the force of competition. Competition will tend constantly to bring about the most economical and efficient method of production possible with existing technology — and then it will start devising a still more efficient technology. It will reduce the cost of existing production, it will improve products, it will invent or discover wholly new products, as individual producers try to think what product consumers would buy if it existed.

Those who are least successful in this competition will lose their original capital and be forced out of the field; those who are most successful will acquire through profits more capital to increase their production still further. So capitalist production

tends constantly to be drawn into the hands of those who have shown that they can best meet the wants of the consumers.

Perhaps the most frequent complaint about capitalism is that it distributes its rewards “unequally.” But this really describes one of the system’s chief virtues. Though mere luck always plays a role with each of us, the increasing tendency under capitalism is that penalties are imposed roughly in proportion to error and neglect and rewards granted roughly in proportion to effort, ability, and foresight. It is precisely this system of graduated rewards and penalties, in which each tends to receive in proportion to the market value he helps to produce, that incites each of us constantly to put forth his greatest effort to maximize the value of his own production and thus (whether intentionally or not) help to maximize that of the whole community. If capitalism worked as the socialists think an economic system ought to work, and provided a constant equality of living conditions for all, regardless of whether a man was able or not, resourceful or not, diligent or not, thrifty or not, if capitalism put no premium on resourcefulness and effort and no penalty on idleness or vice, it would produce only an equality of destitution.

Another incidental effect of the inequality of incomes inseparable from a market economy has been to increase the funds devoted to saving and investment much beyond what they would have been if the same total social income had been spread evenly. The enormous and accelerative economic progress in the last century and a half was made possible by the investment of the rich — first in the railroads, and then in scores of heavy industries requiring large amounts of capital. The inequality of incomes, however much some of us may deplore it on other grounds, has led to a much faster increase in the total output and wealth of all than would otherwise have taken place.

Those who truly want to help the poor will not spend their days in organizing protest marches or relief riots, or even in repeated protestations of sympathy. Nor will their charity consist merely in giving money

to the poor to be spent for immediate consumption needs. Rather will they themselves live modestly in relation to their income, save, and constantly invest their savings in sound existing or new enterprises, so creating abundance for all, and incidentally creating not only more jobs but better-paying ones.

The irony is that the very miracles brought about in our age by the capitalist system have given rise to expectations that keep running ahead even of the accelerating progress, and so have led to an incredibly shortsighted impatience that threatens to destroy the very system that has made the expectations possible.

If that destruction is to be prevented, education in the true causes of economic improvement must be intensified beyond anything yet attempted.

1. Nassau Senior, *Journal Kept in France and Italy from 1848–52*, London: Henry S. King, 2nd ed. 1871, Vol. I, pp. 4–5.

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## Authorized IBC Practitioners

<https://www.infinitebanking.org/finder/>

The following financial professionals joined or renewed their membership to our *Authorized Infinite Banking Concepts Practitioners* team this month:

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- John Blalock - Birmingham, Alabama
- Stephen Devlin - Vancouver, British Columbia
- Richard Gailey - Lake Mary, Florida
- Dennis Guy - Marianna, Florida
- Terry Hellenbrand - Waunakee, Wisconsin
- Don Hooser - Kailua Kona, Hawaii
- Paul Horsley - Hudson, Wisconsin
- Ron Luongo - Paoli, Pennsylvania
- Arkady Milgram - Los Angeles, California
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