

# **FREE ENTERPRISE AND POVERTY: CAUSE OR CURE?**

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## **Abstract:**

Poverty in general is created by governmental mismanagement. The solution to the problem is the free enterprise system. Markets reduce poverty by promoting incentives and rational economic activity. Governments exacerbate it by attacking private property, regulating business, and through taxation. The problem of black poverty stems mainly from the breakup, nay, the failure to form, of the black family. This, in turn, is traced to governmental welfare programs

## **Key words:**

Poverty, free enterprise, socialism, central planning, government regulation, laissez faire capitalism

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## **I. Introduction**

For the impatient, the short answer to the question of whether free enterprise causes poverty is that it does not. Rather, government intervention into the economy, and various socialistic welfare policies, are the villains of the piece. In section II we discuss the problem of poverty, and its causes, in general; section III is devoted to an analysis of issues that have a disproportionate effect on black poverty. We conclude in section IV.

## **II. Poverty in general**

Politicians are continuously holding hearings on the problem of poverty. Since they are in the mainstream, they continually arrive at the wrong answers for its cause, and adopt fascistic solutions for its cure. Worse, these initiatives cost millions of dollars or more, and thus exacerbate the very poverty they are supposedly fighting.

In 1776 Adam Smith wrote *An Inquiry into the Nature and Causes of the Wealth of Nations*. The politicians might do worse than cancel their meetings and read this book instead. In it Smith (1776) said that those countries that rely mainly on the free enterprise system of private property rights and the rule of law prosper, while those that do not are consigned to a life of grinding poverty. Modern day research (Gwartney, et. al., 1996) finds a statistically significant relationship not only between the degree of economic freedom in a country and its per capita income, but also between such liberty and income equality.

Smith was quite a bit too moderate in that he hedged on this basic insight with too many exceptions, too many concessions to government

(Anderson, G., 1997; Paul, 1977; Rothbard, 1987, 1995). But the general rule he articulated was as true in the 18<sup>th</sup> century as it is in our own, and applies as much to countries as to states and cities, indeed to any and all economies or political jurisdictions.

Why do markets work to alleviate poverty (Gilder, 1981; Hazlitt, 1973; Lee, 1985; Nash, 1986; Schall, 1990), and governments fail? One reason is the profit and loss system, the automatic feedback loop mechanism of free enterprise. If an entrepreneur does a bad job, people avoid his firm. If he does not mend the error of his ways, bankruptcy is the inevitable and usually swift result (Hazlitt, 1979). In sharp contrast, if a politician makes mistakes in satisfying a constituency, he can stay in office for up to four years; a bureaucrat, practically forever. The situation regarding pizza, pens and pickles, is pretty satisfactory; those who could not provide these goods at a competitive quality and price went broke. But what of the post office and the motor vehicle bureau? Poor service for decades, and nothing we consumers can do about it (Gwartney and Wagner, 1988).

A second reason is that no rational economic planning can take place in the absence of private property rights in the factors of production, a basic element of even quasi free enterprise economies. Without the purchase and rental/sale of land, labor and capital, market prices for these factors cannot be established. Without them, central planners are as at sea without a rudder. There is simply no objective way to determine, for example, if row boats should be made of usual materials for such items, such as plastic, wood, rubber -- or of gold and silver. All purely central planning is arbitrary. Without the Sears and Roebuck catalogues, and other windows into capitalistic economies, there is no way the U.S.S.R. could have lasted as long as it did as a semi viable economy (Boettke, 1991, 1993; Dorn, 1978;

Ebeling, 1993; Foss, 1995; Gordon, 1990; Hoff, 1981; Hoppe, 1989, 1991, 1996; Horwitz, 1996; Keizer, 1987, 1997; Kirzner, 1988; Klein, 1996; Lavoie, 1981, 1985; Lewin, 1998; Mises, 1975, 1981; Osterfeld, 1992; Pasour, 1983; Reynolds, 1998; Rothbard, 1971, 1976, 1991; Salerno, 1990, 1995; Steele, 1981, 1992.).

And there is also a third reason. This is the difficulty of the government gathering the knowledge with which to do economic planning. The White House would be simply inundated with information overload if *every* business in the country had to check with Planning Central before they could undertake even the most mundane of decisions. Moreover, much of the information known by the entrepreneurs “on the ground” is not the sort that can easily be transmitted to Washington D.C. It is, rather, knowledge concerning specific times and places and unique individuals. For example, which local supplier is the most reliable, and by how much more than the second best (Hayek, 1945, 1978, 1984). The free market, in this regard, is an institution which arises from human action, but certainly not from human design, at least not that of the central planning variety.

Why do free markets tend toward income equality, thus reducing the incidence not only of absolute but relative poverty as well? The only legitimate way to earn vast sums of money under free enterprise is by enriching others. Yes, Bill Gates, Sam Walton, Henry Ford and Ray Kroc make billions, but they do so by economically uplifting all those they deal with. If the masses of people did not benefit from dealing with Microsoft, Walmart, Ford and McDonalds, they would not continue to do so<sup>2</sup>. In contrast, in politics,

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<sup>2</sup> Nor is there anything magical about this. There is no guarantee that even the largest firms will long continue in business. When Ford introduced the unpopular Edsel, it lost millions and put its very existence into question ([http://www.failuremag.com/arch\\_history\\_edsel.html](http://www.failuremag.com/arch_history_edsel.html)). Chrysler *did* go broke due to

vast fortunes are made not by attracting customers, but by raising taxes and siphoning off the lion's share of them, or benefiting from regulation<sup>3</sup>. The wealth of the politician rises, and that of everyone else falls.

### III. Black poverty

But do not governments give money to the poor in the form of welfare? Doesn't that help the poor? First, only the crumbs go to the poor (Piven and Cloward, 1971). The rich, after all, run the government (Domhoff, 1967, 1971; Hoppe, 1990; Kolko, 1963; Mises, 1978; Oppenheimer, 1975; Raico, 1977; Rockwell, 2001), and it would take quite a bit more benevolence than they have for them to orchestrate things against their own interests.

According to Higgs (1995):

“The welfare system is another national disgrace. For decades, commentators of various political persuasions have recognized that our tax-funded welfare system promotes dependency, family dissolution, juvenile delinquency, and other pathologies. Since 1965, an increase of more than five fold (adjusted for inflation) in anti-poverty spending only subsidized the growth of a wretched underclass.

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entrepreneurial mistakes, and was only revived by fascistic government intervention in the form of a loan guarantee and other bailout measures (Henderson, 1980). A perusal of the Fortune 500 (<http://www.fortune.com/fortune/fortune500/>) every decade in the 20<sup>th</sup> century will reveal vast business discontinuities even at the very top. States Rockwell (2000) “... we have seen a virtual revolution occur in the Fortune 500, with old established firms being wiped out by younger, smaller, and more aggressive upstarts.”

<sup>3</sup> States Henderson (1999): “A young congressman named Lyndon B. Johnson built his family fortune from roughly zero in 1943 to at least \$14 million by the time he won his first election as U.S. President in 1964. About half the wealth derived from a license his wife held that allowed her to operate KTBC, a radio station in Austin, Texas -- regulated, of course, by the federal government. See also Caro (2002), Bresiger (2002)

“It would take little more than \$50 billion to raise every poor person above the official poverty line, yet the percentage of the population classified as poor hardly budges, while annual welfare spending amounts to four times that much. Where's the money going?

“You guessed it. The money goes to the planners, researchers, social workers, public health doctors, nurses, and technicians, public housing managers, community organizers, administrators, and assorted apparatchiki. Like the public school teachers, these people have strong political connections, vote in every election for candidates who support more welfare spending, and never fail to accuse would-be budget cutters of harming children.”

Second and far more important, what little money does go to the poor impoverishes them; it does not lift them out of poverty (Anderson, G., 1987; Anderson M., 1978; Block, 2001; Brown, 1987; Higgs, 1995; Murray, 1984; Olasky, 1992; Rothbard, 1998; Tucker, 1984). The key to understanding the direction of causation in this paradoxical situation is the family: anything that supports this vital institution reduces poverty; anything that undermines it, increases poverty (Anderson, 2000A; Carlson, 1991, tba , tba; Mises, 1981; Rockwell, 1999; Tucker, J., 1999, Tucker, W., 1984). Family breakdown is causally related to all sorts of poverty indices besides lack of money: imprisonment, lack of educational attainment, unemployment, lower savings, illegitimacy, etc.

And what is the effect of welfare on the family? To ask this is to answer it. As Murray (1984) has shown, the social worker makes a financial offer to the pregnant girl that the father of her baby cannot even come close to matching. But they do so on condition that this young man be out of the picture. A recipe for family disaster if ever there was one. Slavery was not

able to ruin the black family (poverty is disproportionately a black problem) but insidious welfare had that very effect.

There is a tale about the frog and the boiling water. If you throw the former into the latter, he will jump right out, relatively unharmed. It is as if he full well recognizes the danger. Whereas, if you place the frog in cold water, and slowly heat it up to the boiling point, his internal temperature clock is such that he stays in, and perishes. Slavery was to the black family what boiling water is to the frog; not a good thing, certainly, but the victim did not succumb to the danger. The black family was just about as strong as the white in the years following the War of Northern Aggression, but fell apart after Johnson's War on Poverty (Tucker, W., 1984).

However, the welfare system was far more insidious<sup>4</sup>. After it got started in the latter part of the twentieth century, not only was the black family rent asunder, it was failing, even, to form in the first place (Murray, 1984). It was something of a gradual process to undermine the social mores

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<sup>4</sup> International welfare, or foreign "aid," is no better at helping its recipients. First of all, it is not necessary that a poor country be helped by a rich one if it is to undergo economic development. Contrary to the shibboleths of the left, a nation can indeed lift itself up by its own bootstraps with no aid from others. Great Britain was the first country to burst out of the shackles of grinding poverty, and it did so, by definition, on its own, since there was none other, then, available to help it. It did so through the industrial revolution (Berg, 1992; Crafts, 1985; Deane, 1979; Floud and Johnson, 2003; Floud and McCloskey, 1994; Hayek, 1954; McKendrick, 1983; Taylor, 1975), the views of Dickens (<http://www.rvschools.org/rvhs/English/StudyGuides/GrExpect.htm>) to the contrary notwithstanding. Second, while the amount of government to government transfers of funds (a far more neutral term than foreign "aid") is relatively small for the donor nations, it is gargantuan compared to the budgets of the recipients. This makes it a matter of no little importance exactly *who* takes charge of these monies. This has the deleterious effect of turning the best and the brightest young people of the recipients away from things like entrepreneurship, engineering, medicine, etc., which lead to economic development, to becoming politicians and lawyers, which does not, but better enables them to share in these riches. Worse, it exacerbates inter tribal tensions, because the specific recipients of Western largesse can then engage in the 3 M's of foreign "aid": Mercedes for the rulers to ride around in, Monuments (sometimes statues of themselves, more often steel mills or air carriers which provide their goods and services at a multiple of the costs of importing them; they, too, do not like "outsourcing"), and Machine guns, the purpose of which is obvious. See on this Alesina and Weder, 2002; Bauer, 1981, 1982, 1984, 1987; Bauer and Yamey, 1957; Castle, 1957; Loeber, 1961; McNeill, 1981; Riddell, 1987; Rothbard, 1958; Thornton, 2002; Tucker, 1997; Vance, 2000

opposing out of wedlock children, but welfare programs succeeded in this task.

Similarly, social security weakens intergenerational family ties (Ferrara, 1982, 1985; Rockwell, 2004; Sennholz, 2004; Steinreich, 1996.). In the days before its advent, three and even sometimes four generations of a family were tied together economically, with the middle generation(s) financially supporting both the younger and the older ones. Afterward, the prevailing attitude came to be, “Why should we support granny, when the state will do so.” Of course, this “support” came from the funds of those who, before the advent of this program, happily kept granny in the family home. Now, to a greater and greater degree, she is shipped off to a warehouse for the elderly, with great harm to the family structure.

The “philosophy” behind social security, if we can dignify this fascistic program in that manner, was that people were too stupid, or short-sighted, to save for their old age. The government would step in and force them to do so, for their own good. But if they are so irresponsible, why should we allow them to vote for the government to do this great deed in the first place? If the state must do this for them, does this not demonstrate that they are unfit for the ballot box?

A paternalistic program that forced people to save more for their retirement years than they wished to do would be bad enough. But in actual point of fact, social security was far worse than that. For, instead of ensuring that each worker got *his own* money (plus interest) when he retired, this Ponzi scheme of a system orchestrated matters so that each succeeding generation received the savings of the one before it, and gave of its savings to the one behind. This system of massive theft “worked,” initially, when



there were very few retirees, and many workers supporting them. But, over time, the latter decreased, the former increased, and there were fewer and fewer savers supporting more and more workers. It is time, it is long past time, not only to end social “security,” but, also, to rescind the requirement that sovereign individuals be ordered to save on their own accounts. If they wish to do so, well and good; if not, it should be none of the government’s business. This is not poverty fighting; it is poverty enhancing.

Public housing came about as a result of the supposed “failure” of the residential housing market. Yes, it did indeed “fail,” but this was not due to any intrinsic flaw. Rather, this was the result of a plethora of unwise government policies, headed up by rent control (Baird, 1980; Block and Olsen, 1981; Block, Horton and Shorter, 1998; Block, 2002; Grampp, 1950; Hayek, 1981; Johnson, 1982; Lindbeck, 1972; Myrdal, 1965; Salins, 1980; Tucker, 1990). This policy, plain and simple, reduced the incentives landlords had to build more housing and maintain their present stock. It is no wonder there was a felt need to house the poor in many locales<sup>5</sup>.

But public housing was the wrong solution to a problem created by government in the first place (Anderson, W., 2000B; Bovard, 2000; Jacobs, 1961;). Given that it was aimed at the poor, an income level had to be established, such that people with incomes beyond that point were ineligible. But who is likely to either not be qualified for public housing in the first place, or to earn a raise while there, and thus be booted out? Intact families. Public housing, with its income cut off points, either evicts resident intact families, or bars them from entry in the first place. The remaining female

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<sup>5</sup> Even leftists, otherwise opposed to free markets and in favor of government intervention, have made an exception for rent control. For example, according to Lindbeck (1981, 213): “In many cases, rent control appears to be the most efficient technique presently known to destroy a city except for bombing.” And stated Myrdal (1981, 224): “Rent control has in certain western countries constituted, maybe, the worst example of poor planning by governments lacking courage and vision.”

heads of families are no match for gangs of teenaged boys lacking adult male role models. As a result, these places become hell-holes<sup>6</sup>, and have to be demolished<sup>7</sup>; not by foreign terrorists, but by their domestic economic equivalents, the housing authorities responsible for foisting these economic and social monstrosities on an unsuspecting public.

#### IV. Conclusion

The government is also a direct source of poverty. It's minimum wage and union legislation makes it difficult if not impossible for poor youth to get jobs. It's rent control makes cheap housing scarce. It tariffs make all basic necessities more expensive, and its subsidies to business have the same effect.

Want to cure black<sup>8</sup> (and all other) poverty? Reduce government interference with the free enterprise system.

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<sup>6</sup> As with rent control, so with public housing: there are those who ordinarily lambaste markets and advocate state regulation, who take a very different view in this case. For example, HUD Secretary Henry Cisneros stated (Bovard, 2000): "HUD has in many cases exacerbated the declining quality of life in America." And said former Democratic vice president candidate Al Gore (Bovard, 2000): "These crime-infested monuments to a failed policy are killing the neighborhoods around them."

<sup>7</sup> States Anderson, W. (2000B): "Urban planners, of course, saw these developments as a solution to the needs of poor workers. It was not long before it was obvious that public housing was not a solution, but an even greater problem. A case in point was the infamous Pruitt-Igoe development in St. Louis.

"Built in the 1950s, Pruitt-Igoe won architectural awards and the praise of utopians everywhere. However, as the welfare state grew, so did the number of non-working residents and single-parent families. Pruitt-Igoe became synonymous with crime in St. Louis, as the place became nearly unlivable. In 1972, authorities finally dynamited the rodent-infested structures to the ground."

For more on the Pruitt-Igoe debacle, see <http://en.wikipedia.org/wiki/Pruitt-Igoe>;  
<http://www.stltoday.com/stltoday/news/special/pd125.nsf/0/AB4B1191EB6948C186256E04006BBBCD?OpenDocument>

<sup>8</sup> See on this especially Sowell, 1975, 1976, 1981A, 1981B, 1982, 1983, 1994; Williams, 1982.

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