Democratic Capitalism, Volume II

The Way to a World of Peace and Plenty

Ray Carey
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Preface

The Human Mission

*It is not possible to run the course aright, when the goal itself has not been rightly placed.*  
*Francis Bacon (1561-1626)¹*

The human goal is to reach full potential based on the worth of each individual harmonized in an environment of trust and cooperation. Following these truths, common to natural law and religion, society can put the conducive circumstances in place and remove the impediments.

From the beginning, most individuals were not free of needs for food, clothing, shelter, and good health, nor were their minds freed by education to use reason. The urge towards freedom made progress possible, but it was persistently impeded by those who used coercion and violence to take a large share of the wealth.

Nations and religions contradictory the worth and potential of each individual and the environment of harmony by killing hundreds of millions for either perceived economic benefit or dogma.

Philosophers during the 18th and 19th centuries identified how economic freedom built up from the worth and potential of each in an environment of trust and cooperation, could eliminate material scarcity, distribute wealth broadly, and unite people in economic common purpose. Conducive circumstances were available then, and the impediments of concentrated wealth and violence among nations and people could be removed.

By the beginning of the 21st century the benefits of economic freedom and economic common purpose had been empirically confirmed by improvement in the lives of hundreds of millions of people. The impediments of concentrated wealth and violence among nations and people,

however, had not been removed.

The way to remove these impediments is clear, and the democratic power for reform is available. *Democratic Capitalism, The Way To a World of Peace and Plenty*, volume 1 and this volume 2 are offered to new leaders as the democratic capitalist solution.
Chapter 1

The Ideal, the Means, and the Process

"God who hath given the world to men in common, hath also given them reason to make use of it to the best advantage of life and convenience." 

John Locke (1632-1704)

From thirty years experience managing companies I knew that performance improved dramatically when people were free to participate in an environment of trust and cooperation. My confidence in the worth and potential of humans was not abstract theory, it was based on tens of thousands of specific opportunities in many countries to observe people functioning well when provided with the conducive circumstances.

During twenty years of study, I have found that the 18th century Enlightenment identified the way to peace and plenty: economic freedom that could feed, clothe, shelter, educate, and provide good health care and hope for all, and economic common purpose that could unite people and stop the violence.

The Enlightenment offered this ideal of indefinite human progress, the means to attain the ideal, and the process to specify the means and validate the ideal. For the next two centuries, economic freedom and economic common purpose were successfully tested but were impeded by concentrated wealth and violence. The intellectual community had failed to follow the Enlightenment’s truth-seeking process, failed to examine the specific means, failed to harmonize capitalism and democracy, and many even abandoned idealism. The folly and bloodshed that had dominated human history continued.

Late in the 20th century, more countries were adopting economic freedom and freed hundreds of

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millions of humans from extreme poverty. America, however, failed to lead the world in economic common purpose. Instead, ignorant and arrogant politicians tried to dominate the world based on nuclear bomb superiority. As a result, early in the 21st century, one-third of the world still lives in misery, the rest in violence, or fear of violence.

A rededication to the original mission of the Enlightenment can reposition America to lead towards economic common purpose and away from violence. An Enlightenment II can replicate the rigorous truth seeking that works so well in the sciences. Fragmented, specialized knowledge can again be integrated to improve the human condition. Information age technology can expedite a worldwide examination of hypotheses that debates, accepts, rejects, or refines to way to peace and plenty.

The first building block is the hypothesis that social progress begins by movement to the superior economic system. Validation of this premise is critical to releasing the energy and intelligence of millions of potential reformers. Once validated, the examination can proceed to specific propositions such as these:

- **Problem:** Capitalism depends on the discipline to invest for future gain instead of present consumption. Trillions of dollars of pension savings have gone into consumption by the financial capitalists, instead of into job-growth investment.

  **Solution:** Tax-free dividends for low-and-middle-income wage earners, a “capital wage” to be spent or reinvested. Hundreds of billions of dollars a year will be returned to the economy instead of wasted on stock buy backs and non-strategic acquisitions. This democratization of capitalism would encourage the spread of profit sharing and ownership plans; it would add income for the reciprocal purchases upon which free trade depends; and it would motivate wage earners to create more wealth.

- **Problem:** Speculators with borrowed money have caused asset inflation in stocks and real estate resulting in recessions that devastate the livelihood of ordinary people, after making the rich richer.

  **Solution:** Government accepts responsibility for prevention of asset inflation, as well
as price inflation, and controls it by taxes, bank reserves, stock margin reserves, and interest expense.

- **Problem:** Institutional investors use quarterly earnings per share to pressure companies to abandon long-term building plans for the sake of short-term earnings.

- **Solution:** Institutional investors honor their fiduciary responsibility to maximize the long-term retirement benefits of their customers, the wage earners, by changing the measurement of company performance from quarterly earnings-per-share to a three-year running average of sales, profits, and cash flow against predictions.

These simple reforms will put the world on the way to peace and plenty. Broad distribution of wealth at home will increase economic growth and change the relationship between capitalism and democracy from the traditional tension to harmony. With the reaffirmation of the American dream, the people will demand that their government give priority to economic common purpose, not military might, in the relations with other nations and cultures.

Young people everywhere will view the good life on the Internet, and powered by the innate urge towards freedom, they will pressure their governments to move to the benefits of economic freedom. Within a generation, improvement in the lives of people from a fundamentally moral system will spread to all parts of the world. Each generation will recognize the inevitability of peace and plenty and build on this momentum.

*Nature has set no limits to the realization of our hopes.*³ Condorcet, (1743-1794).

Condorcet’s optimism for social progress was based on how well his associates within the 18th century Enlightenment had integrated knowledge to improve the human condition. Since then, experience in many countries has verified that the way to plenty is economic freedom, and the way to peace is economic common purpose. Much of the world, however, is still full of misery and violence. Two billion humans try to live on $2 a day; 160 million humans were killed by

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governments during the 20th century; early in the 21st century, the violence has spread to cultures in which suicidal delivery of terrible weapons is celebrated.

Society should be embarrassed by this unnecessary failure. Violence always trumps reason in the short term, unless determination by nations and the structure of law are there to contain it. Economic freedom now functions at a fraction of potential because wealth is not broadly distributed, and economic common purpose does not unite the world because the priority is still military power. These impediments, in turn, are caused by mistakes by poorly trained leaders and lack of reform by poorly educated citizens.

The mission of the 18th-century Enlightenment was to find the optimum organization in human affairs by replicating in the social sciences the truth seeking that worked well in natural sciences. Their legacy is the ideal, the means, and the process to specify the means and validate the ideal. Although they provided the educational materials, the impediments continue, not for lack of solutions, but for lack of study.

This integration of knowledge, the Enlightenment way to a world of peace and plenty, was summarized by the Marquis de Condorcet (Marie-Jean-Antoine-Nicolas-Caratit), in his tenth stage of his Sketch for a Historical Picture of the Progress of the Human Mind.4 Like most of the Enlightenment, Condorcet’s truth-seeking discipline was developed as a scientist, he was a mathematician. Condorcet finished this extraordinary document while he was in hiding; shortly thereafter, he died in prison during the Reign of Terror.

Condorcet, the last of the French philosophes, was a protégé of Voltaire (Francois Marie Arouet 1694-1778), the first of the philosophes, who was banished to England early in the century for writing what he thought. A few years later, Voltaire brought back to France his appreciation of English Constitutional freedoms, Issac Newton’s (1642-1727) scientific discovery of order in the universe, Francis Bacon’s protocols to transfer scientific truth-seeking methods to the organization of human affairs; and John Locke’s affirmation of the inalienable rights of each individual, and government by the consent of the governed. Voltaire integrated the contributions

4 Goodell, op.cit.
of these 17th-century thinkers to help free the mind. Later, Adam Smith, (1723-1790), Condorcet’s friend, described in his Wealth of Nations.⁵ how to free of body of material needs

The way to peace and plenty was now clear, but the impediments of concentrated wealth and violence among nations had powerful momentum. Condorcet realised that the best hope to test and verify the way was in the new republic, America:

That happy land where freedom had only recently kindled the torch of genius, the mind of man released from the leading-strings of its infancy, advances with firm steps towards the truth.⁶

Thomas Paine (1737-1809), revolutionary free-thinker, examined the human march towards freedom in England, America and France, and called the democratic experiment in America a new beginning of history. He was typical of these public intellectuals who knew no borders. While their nations were at war, or preparing for war, they collaborated on ways to improve the human condition. Professor Immanuel Kant (1724-1804), for example, contributed thoughts on perpetual peace from Prussia, while Americans in Paris, Thomas Jefferson (1743-1826) and Benjamin Franklin (1706-1790), developed thoughts on structuring their new government. Condorcet described his friend Franklin as “a man who believed in the power of reason, and the reality of virtue.”⁷ Condorcet’s wife Sophie helped by translating both Smith’s first book, The Theory of Moral Sentiments, as well as Paine’s speeches to the French assembly.

Condorcet’s classical liberal manifesto

Drawing on the wisdom of many thinkers from many countries, Condorcet offered this manifesto:

Free trade, freedom of speech, freedom of press, the end of censorship, the end of slavery, the enfranchisement of women, universal free education, equality before the law, the separation of state and church, religious toleration, the adoption of a

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⁶ Goodell op cit. p. 227
written constitution with a written declaration of the rights of people embedded in
the constitution to insure the recognition of those rights, the establishment of a
representative or parliamentary form of national government, and local self-
government to encourage the independence and the participation of the peasants
in government.  

These words could have been written by Thomas Jefferson so closely do they reflect the
American Declaration of Independence, Constitution, and Bill of Rights. In the rest of the world
these freedoms were a hope, in America they energized and united people in an ethos in which
each generation expected to pass on a better life to their children, and they did.

Condorcet on concentrated wealth

Condorcet’s summary was not only about the liberal ideal but also specified the means to
neutralize the first impediment: concentrated wealth:

Any disproportion of wealth could not exist if civil laws did not provide artificial
ways of perpetuating fortunes; if free trade and industry were allowed to remove
the advantages that accrued wealth derives from any restrictive law or fiscal
privilege…if the administration of the country did not afford some men ways of
making their fortune that were closed to other citizens.  

We shall reveal other methods of insuring equality either by seeing that credit is no
longer the exclusive privilege of great wealth, or by making industrial progress more
independent of the great capitalists.

This volume 2 describes how trillions of mandated pension dollars should have made “industrial
progress independent of the great capitalists” as Condorcet expressed it, but most of the wage
earners’ capital is not being converted into job-growth investment.

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8 Goodell, op. cit, p. 162.
9 Ibid., p 231
10 Ibid., p.233
The Enlightenment thinkers knew that broad distribution of wealth was not merely a matter of fairness but was a key component of Smith’s economic dynamic that provided the spendable income to those whose purchases had the maximum multiplier effect. The added volume would then drive down costs and prices, allowing others to purchase, thereby adding more volume sustaining the economic perpetual motion machine. Smith extended this concept to globalization, or free trade, with conditions that would make it a universal benefit. Besides broad distribution of wealth, the conditions included peace, money that was merely a medium of exchange without influence on the commercial process, and control of the speculators, prodigals and projectors, as Smith called them.

Condorcet on war and violence among nations and people

Condorcet knew that Smith’s first condition for the success of free markets was peace, and he sensed that only economic common purpose could purge the violence that had dominated human history. Condorcet commented on this second impediment:

Gradually mercantile prejudices will fade away, and a false sense of commercial interest will lose the fearful power it once had of drenching the earth in blood and of ruining nations under pretext of enriching them. When at last the nations come to agree on the principles of politics and morality, when in their own better interests they invite foreigners to share equally in all the benefits men enjoy either through the bounty of nature or by their own industry, then all the causes that produce and perpetuate national animosities and poison nations’ relations will disappear one by one; and nothing will remain to encourage or even to arouse the fury of war.¹¹

Kant also knew that freedom cannot be functional without discipline, and so he offered in his “Eighth Thesis” the need for organization prerequisite to substituting law for violence:

A perfectly constituted State is the only condition in which the capacities of mankind can be fully developed, and also bring forth that external relation among

¹¹ Ibid., p. 244
States which is perfectly adequate for this end.\textsuperscript{12} This would force the States to the same decision (hard though it may be hard for them) that savage man was also reluctantly forced to take, namely, to give up brutish freedom and to seek quiet and security under a lawful constitution.\textsuperscript{13}

Condorcet anticipated a United Nations type of organization:

Organizations more intelligently conceived than those projects of eternal peace which have filled the leisure and consoled the hearts of certain philosophers, will hasten the progress of the brotherhood of nations, and wars between countries will rank with assassinations as freakish atrocities, humiliating and vile in the eyes of nature and staining with indelible opprobrium the country or the age whose annals record them.\textsuperscript{14}

What a wonderful vision! Two centuries later France and Germany, agreed to stop drenching their earth with the blood of each generation of young men, and formed the European Union. Condorcet’s optimism, however, is difficult to reconcile with the bloodiest, most violent century in human history, the twentieth; and with the continuation of this violence into the new century marked by September 11, 2001. How can the world in the grip of reciprocal atrocities unite in economic common purpose? Condorcet answered this question over two centuries ago: Only by actualizing an inversion, in which the standard of living throughout the world goes up, and violence goes down.

\textit{Tension between democracy and capitalism in the new American republic}

From the beginning in America, the democratic political system and the capitalist economic system were in tension. Millions of lives were improved, verifying the power of economic freedom, but the system functioned at a fraction of potential. Wealth became concentrated from the start by way of non-democratic privileges granted to the financial oligarchy. Despite George

\textsuperscript{13} Ibid., p. 420
\textsuperscript{14} Goodell, op cit p. 244.
Washington’s warnings, the nation was, moreover, unable to avoid the violence of European nations and, in time, copied their imperialism and priority for military power.

Alexander Hamilton (1757-1804), Secretary of Treasury in Washington’s first administration, built the country’s structure without which we probably would not have survived. “He knew that the European powers raised foreign loans in wartime and this inextricable linkage between military and financial strength informed all of his subsequent thinking.”15

With this mindset, Hamilton corrupted the democratic ideal of a country reflecting the wisdom of the people, and he corrupted the economic system by providing privileges for the wealthy and powerful. This hard working genius structured fiscal and monetary policies consistent with his elitist philosophy:

All communities divide themselves into the few and the many. The first are rich and wellborn, the other the mass of the people. The people are turbulent and changing, they seldom judge or determine right. Give, therefore, to the first class a distinct, permanent share in the government. They will check the unsteadiness of the second, and as they cannot receive any advantage by a change, they will ever maintain good government.16

Government requires the deliberate wisdom of a select assembly and cannot be safely lodged with the people at large.” 17

From the beginning, speculation with borrowed money was allowed in contradiction to the government’s obligation to control currency and credit for the general welfare. Protection against asset inflation was never accepted as a government responsibility, and, as a result, after the War of 1812 the country went into its first boom/bust cycle in stocks and real estate in which the rich get richer until the poor get poorer. The resulting panic of 1818 bankrupted farmers, put one-half million of the new urban workers out of work, and imprisoned thousands for inability to pay small debts. Since then the government goes to extremes to prevent price inflation that erodes the

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16 Ibid., p. 90.
17 Alexander Hamilton’s speech at the 1787 Constitutional Convention, Philadelphia, Pennsylvania.
asset value of the wealthy, but refuses to prevent asset inflation that has done more harm to more people. From Hamilton to Alan Greenspan, recent head of the Federal Reserve Board, the government has demonstrated that it does not regulate the finance capitalists, who handle the money, it protects them!

Thomas Jefferson, Secretary of State in the same first administration as Hamilton, recognized that the new democratic experiment was being profoundly corrupted by policies that would “enrich swindlers at the expense of the honest and industrious.” ¹⁸ Later, as President, Jefferson instructed his Secretary of Treasury, Albert Gallatin: “It is the greatest duty we owe to the safety of our Constitution to bring this powerful enemy to a perfect subordination.” ¹⁹ Jefferson failed to get control of the finance capitalists and presidents have failed since because concentrated wealth resulting from lobbied privileges means more riches for the politicians. The people sensed that currency and credit were being controlled for the speculators, not the general welfare, but lacked the financial sophistication to specify reform, then and now.

Jefferson’s frustration and Hamilton’s determination were major causes of the destructive two-party political system. Instead of a system in which candidates compete on how to implement an agreed agenda, America quickly adopted an adversarial and acrimonious system that represents two fundamentally opposite views of government: the Jeffersonian democratic ideal of government, “by the people,” and the Hamiltonian republican idea of government, “by the wealthy and powerful few.” Jefferson conditioned his optimism on universal, high-quality education and the belief that the people would get it right in time. Hamilton’s government by an elite copied the same error-prone government of monarchs and tyrants that had made European history a bloody failure.

The political debate should be about the best way to build and distribute wealth, and the best way to lead the world to the benefits of economic freedom to stop the violence. Fast forward to the election of 2006 in which the people rejected an imperial president and his small group of fascists. This rejection by the voters was critical, but the political debate was not about

¹⁹ Ibid., p. 62
America’s proper role in the world, nor was it about government privileges that concentrated wealth in record amounts. The 2006 debate was, instead, about minimum wages, stem cell research, abortion, and health benefits—all of which are important subjects, but none of which addresses America’s role as world leader towards economic freedom that can eliminate material scarcity, and economic common purpose that can stop the violence.

Marx’s contributions

In the middle of the 19th century Karl Marx (1818-1883) confirmed that capitalism had the productive capacity to eliminate material scarcity but was functioning at a fraction of potential because of concentrated wealth, one of the two impediments to human progress.

Marx, the atheist, found common cause with religion in the celebration of the worth and potential of each individual: “The free development of each is the condition for the free development of all.”20 This is one of two moral principles common to secular humanists and religions necessary to support human progress.

Marx also found common cause with religion in the environment of trust and cooperation that displaced alienation. This workplace culture of brotherly love is the second of two common moral principles.

Marx identified the way to eliminate the first impediment of concentrated wealth by the workers participating in ownership. Wealth was thus broadly distributed while the workers were motivated to produce more wealth.

Marx identified the way to eliminate the second impediment of violence among nations and people. He saw the benefits from this new mode of production spreading worldwide in a benign inversion in which the standard of living would go up and the violence would go down. According to Marx, in time, the Warrior State would become irrelevant and disappear.

Marx understood why the intellectual community had failed to assimilate Adam Smith’s vision of an end to material scarcity, they were wedded to political solutions and culturally conditioned

to reject economic solutions. Marx pointed them in the right direction: begin with the superior economic system.

The intellectual community after Marx compounded their error by adopting his critique of generic capitalism while ignoring his advice on where to start. The Marxists built tyrannical political structures in his name, did not change the work culture, and added to the violence. This intellectual myopia has precluded reform for a century-and-a-half since and is the prime reason that democracy and capitalism are still in tension and the world is still full of folly and violence.

*Mill avoided the Marxists fatal flaws and completed the definition of democratic capitalism.*

John Stuart Mill (1806-1873) endorsed the power of capitalism to eliminate material scarcity but avoided the fatal structural flaws of the Marxists by integrating Marx’s contributions with competition, private property, and skilled management thus completing the definition of democratic capitalism.

Mill saw the synergistic opportunities in capitalism and democracy raising the standard of living, elevating the spirits, and uniting people in a moral system:

> It is scarcely possible to rate too highly this material benefit, which yet is nothing compared to the moral revolution in society that would accompany it.”

The tension would be gone and capitalism and democracy in harmony.

The way to a world of peace and plenty was now clear and complete. It was an economic system that could eliminate material scarcity in the world and be a source of civic morality. The worth of each individual and their opportunity to reach full potential did not rely on an after life, but was a pragmatic secular opportunity. The culture of trust and cooperation was not some utopian dream but the hard-headed way to maximize commercial results, and the same time the way to improve performance in any human association from the family to the world.

*Gridlock*

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Early in the 21st century, the impediments are worse with wealth concentrated in record amounts and America trying to dominate the world. Democracy and capitalism are both corrupted because the lobby power of the financial oligarchy has produced a deeply flawed economic system, while the coupling of the military and fascists in government has moved America’s reputation in the world from most admired to most hated. The country’s direction is not that of the people, and the threat grows that, for the first time, a better world will not be passed to the next generation.

Many blame the state of the world on inexorable social forces, the inevitability of war, or “human nature” as though there is something “natural” about getting killed or maimed because of politicians’ errors. It should be simple: two moral principles to be observed- the worth of each individual and the environment of trust and cooperation; two conducive circumstances to be put in place-economic freedom and economic common purpose; and two impediments to be removed-concentrated wealth and violence among nations and people. The world becomes chaotic and impossible to manage because of the mistakes by leaders who do not understand that democracy works only by listening to the people, and capitalism works only when free market principles are not suspended.

America has abandoned its leadership towards freedom because of gridlock in these critical areas:

- **Political gridlock:** Instead of debating how we could reform the economic system to build more wealth and distribute it broadly, our polarized and superficial political parties debate more benefits from an already insolvent government. Instead of debating how to lead the world in economic common purpose, our political parties debate how to extricate ourselves from the results of previous errors.

- **Intellectual gridlock:** Famous professors cannot agree on the integration of knowledge to improve the human condition. Harvard professor John Rawls dismissed the Enlightenment mission of a comprehensive, philosophical doctrine founded on reason commenting that his political liberalism, “has no such ambitions.”22 Harvard professor Edward Wilson has said that the Enlightenment got it mostly right and that

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the culture war should be ended by treating the boundary between science and the humanities as unexplored terrain needing cooperative entry from both directions.23

- **Educational gridlock:** Famous educators cannot agree on the public responsibility of higher education. Derek Bok, former and interim president of Harvard, bemoans that in twenty years: “I cannot recall a single serious faculty discussion of how undergraduate education could do a better job of preparing students as citizens. The results of that neglect are all too visible.”24 Stanley Fish, distinguished educator and former Dean of Chicago University, wrote a *New York Times* editorial: “The task of educating students to be better citizens would deform (by replacing) the true task of academic work: the search for truth.”25

- **Philosophical gridlock:** A *Time* magazine cover raised again the old question: “God vs Science.”26 Why fight? Those with the mission of integrating knowledge to improve the human condition are interested in common rules that support human progress. The first is the worth and potential of each individual celebrated in religion, endorsed by Atheist Marx, and the moral foundation of democratic capitalism. The second is that performance improves in every human association in an environment of trust and cooperation. Benevolence, brotherly love, and a sense of unity are taught by religion, but thousands of companies succeed in the market place because their people function best in this culture.

_A logic trail on the way to peace and plenty._

In *Democratic Capitalism, volume 1*, I offer for examination ten hypotheses that integrate the wisdom of the Enlightenment, the visions of Marx, the refinements by Mill, and the experimental verification from subsequent experience. From these sources, the way to peace and plenty becomes clear. If the 18th century Enlightenment illuminated the way that subsequent generations

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24 Derek Bok, President Emeritus, Harvard University, Principal Address at the College of the Holy Cross, Worcester Mass. Reported in the Holy Cross Crossroads, September/October 1993. pp. 8, 9
26 November 13, 2006
failed to follow, then there must be a persistent failure of the truth-seeking process. That is the mission of Enlightenment II: A rededication to the process, and examination of the specific means. I predict that this examination will reaffirm the ideal, which is the American ethos: “Life, liberty, and the pursuit of happiness’ for all, and rediscover the specific means of economic freedom, and economic common purpose to reach the ideal.

To expedite a beginning to this examination I offer ten hypotheses that identify potential agents of change and their action agenda. The first five hypotheses are examined in volume one, the second five are more fully examined in this second volume.

Hypotheses:

# 1- Social progress is based on movement to the superior economic system. This starting point has yet to be assimilated by the intellectual community and this failure is the root cause of a world still full of misery and violence.

# 2- Democratic capitalism is the superior political-economic system. It motivates and rewards each to maximize broadly distributed wealth in an environment of trust and cooperation.

# 3-Economic freedom is a potentially universal system because it can improve lives in both authoritarian and democratic countries

# 4- Ultra-capitalism treats the wage earner as a disposable cost commodity and finance capitalism is dominant over, not supportive of, the job-growth economy. These perversions of free markets principles concentrate wealth and prevent unity through economic common purpose.

# 5- From the beginning the American banking system has limited the capacity of economic freedom to spread wealth and has caused recessions and depressions.

# 6- Political, economic, educational, and philosophical gridlock in America must be broken to open the way to peace and plenty
# 7- The quality of truth seeking must be improved by following the process of the 18th century Enlightenment.

# 8- A democratic republic can reflect the views of citizens only if universities educate them to understand their responsibilities.

# 9- Money managers’ fiduciary responsibility to maximize the wage earners’ retirement savings must change both company practice and government policies from short term and greedy to long term and patient.

# 10- After the American government is reformed in support of democratic capitalism, a world united in economic common purpose, free of want, fear, violence, and oppression, will become a pragmatic opportunity during the 21st century. The United Nations can then encourage national competitions in how well countries are improving the lives of their people measured by the UN Human Development Index.

America failed spectacularly to lead the world towards peace and plenty

At the end of the Cold War, America had a special opportunity to lead the world to peace and plenty. Countries from Eastern Europe to Asia were improving their economies and the lives of their people. China and India freed 500 million people from extreme poverty in a decade through economic freedom. Countries were regarding each other as commercial partners, not national enemies. China toured the world making commercial arrangements with the message: “Let’s get rich together!” The Information Age work culture needed participation in an environment of trust and cooperation as a competitive necessity. The Information Age also added productivity and communication opportunities to further unify the world. In America, mandated pension savings was a unique opportunity to meld the interests of capital and labor in a post-capitalist society. Democracy and capitalism could come into harmony and the world could benefit from strong, steady, economic growth that would leave no families behind.

America blew these opportunities. The capital flow from mandated pension funding did not produce the post-capitalist society because finance capitalists, the people who make money on money, the people who had traditionally exploited the wage earners’ labor, now learned how to
exploit the wage earners’ capital. American leaders lost not only prosperity at home, but also peace abroad because they did not listen to the people on its proper role in the world and went from team player to bully on the block. A few American fascists were determined to provoke enemies in order to rationalize the over one-half trillion dollars a year military budget. America stalked the world with the threat: “Do it our way, or else!” Finance capitalists lobbied their way into an economic system that concentrates wealth in obscene amounts; America fascists fumbled their way into an impossible war while becoming the world’s most hated nation.

*Try again, America!*

America, now, must search and find its roots to determine what economic system it will support and what foreign policy it will follow. The two are interdependent: Democratic capitalism maximizes wealth, and it does so in a moral environment that elevates and unites people. It can distribute wealth broadly at home and add income for reciprocal purchases to make free trade a universal benefit abroad. This coupling of material and moral benefits will reaffirm idealism in America, and eventually in the world.

The time for reform is getting short and will depend on the intellectual community doing their homework and finally getting the starting point right. It should not be that hard to find, Marx’s pointed it out. From this examination, it will be clear that economic freedom can provide food, clothing, shelter, education, good health care and hope for the world, and that economic common purpose can unite all people. Young people in Muslim cultures will view the good life on Information Age technology, and they will become a force for freedom in their own countries. It may take a generation, but the innate urge towards freedom cannot be denied. George Wilhelm Friedrich Hegel (1770-1831) saw this *Geist*, or spirit, moving the whole towards perfection:

The nature of spirit may be understood by a glance at its direct opposite-matter. As the essence of matter is gravity, so on the other hand we may affirm the essence, the subject of spirit, is freedom.27

Three German idealists in succession added their wisdom for the benefit of the Enlightenment

and humanity. First, Kant outlined the necessity to discipline freedom with law for perpetual peace. Next, Hegel saw the human urge to freedom moving the whole to higher levels through struggle and contradiction. Then, Marx found that the essential step for human progress was movement to the superior economic system, assimilated by the culture, with the political structure modified in its support. Over two millennia earlier, another wise man, Confucius said: “To attack a task from the wrong end can do nothing but harm.” 28 It is time to start at the right end.

Chapter 2

American Gridlock

*Hypothesis # 6: America is in an intellectual and political gridlock between those who support ultra-capitalism and those who are trying to use government to redistribute wealth. This gridlock prevents urgently needed reform of monetary, fiscal, and regulatory policies.*

Since the beginning of the American republic, the financial oligarchy has held both economic and political power. During the 20th century, the “Liberal” Democrats (collectivists) challenged this concentration of wealth and influence with growing democratic power promoting a poorly designed agenda to help people, and raised the percentage of the nation’s annual production (GDP) taken in all taxes from 3% to over 35%. They did not, however, reform the economic system, they did not prevent ultra-capitalism from dominating, and they wasted much of the money.

For over two centuries, America has fulfilled the liberal vision of social progress and individual freedom. Passing on a better life for the next generation has been a proud part of this environment of trust and cooperation. The future of this most successful experiment in human history of a country “of, for, and by the people,” however, is threatened. Both political parties are deeply flawed, and as a consequence the system is in gridlock. As long as the urgent need for reform is ignored, America will go into long-term economic decline, at home, and will fail to lead in economic common purpose abroad.

After the demise of communism, the world was ready to unite and get rid of the nuclear bombs

and other military waste. American leaders, failing to recognize this opportunity, led instead to more concentrated wealth and more coercive imperialism. If America continues on this path it will lose its economic superiority and will become irrelevant in world affairs. In the worst-case scenario, it will try to sustain its position in the world by military power, and the folly and violence will get worse.

How did the American Dream turn into this nightmare? Citizens allowed their country to drift away from policies based on the “will and wisdom” of the people filtered through the representative government of an “aristocracy of talent and virtue.” The economy is now centrally planned according to the wishes of Wall Street, although history shows that every country that allows finance capitalism to become dominant goes into irreversible decline. Imperialistic foreign policy is centrally planned by the military and American fascists, although history shows that every country that aspires to Empire fails. Tragic mistakes are the inevitable result confirming the views of American Founders who wanted to substitute the wisdom of educated citizens for mistakes by an arrogant few. Instead of diffused economic and political power, as intended by the majority of the Founders, concentrated wealth from government privilege now corrupts capitalism, and the money is then used to corrupt democracy. American citizens sense this failure. Usually about one-half vote and polls indicate that less than 18% approve of the job Congress is doing. In the 2006 election, however, citizens said “enough” and showed signs that they would take their country back.

Reform must begin with an understanding of the gridlock. Three economic-political systems compete in America. The first two, ultra-capitalism and collectivism, are seriously flawed but receive political and intellectual support, the first mostly from Republicans, the second from Democrats. The third system, democratic capitalism, has demonstrated superior performance, but receives little political or intellectual support. It survives on its economic and social logic rediscovered by each generation of democratic capitalists. The democratic majority must break the gridlock between the ultra-capitalists and collectivists by directing their political and money

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management representatives to support of democratic capitalism.

Citizens’ Choice

Ultra-capitalism is the combination of market fundamentalism, mercantilism that treats the worker as a disposable cost commodity, and finance capitalism that is dominant over, rather than supportive of the job growth economy. Ultra-capitalism’s ideologues of the liberation of capital markets proclaim laissez-faire philosophy at the same time that they contradict Adam Smith’s conditions for the success of economic freedom. Ultra-capitalism lobbies government privileges for subsidies, tariffs, and speculation with borrowed money, thus controlling currency and credit for the speculators instead of the general welfare. It takes credit for the wealth-creation capacity of economic freedom but ignores the reasons that economic freedom currently functions at a fraction of its potential. The work culture of ultra-capitalism is fear and intimidation; profits are maximized by suppressing wages and benefits. Mal-distribution of wealth, always the chief impediment of traditional capitalism, reached obscene levels during the last quarter century of ultra-capitalism. Wage arbitrage moves companies from country to country seeking the lowest labor cost and not providing the wage earner the spendable income for reciprocal purchases upon which free trade depends.

Ultra-capitalism is opposed by the reform-minded intellectual community; receives criticism from most of academia; and contributes to America’s negative international image. This exploitive capitalism hasn’t changed for centuries, nor has its support for the Warrior State. The two fatal flaws of ultra-capitalism are concentration of wealth at home and economic and military imperialism abroad.

Collectivism, since Marx, has been regarded as the alternative to capitalism. Its economic theory is to use government to control the inherent excesses of capitalism and to redistribute wealth. But ill-informed collectivists neither address Adam Smith’s conditions for the success of economic freedom, namely keeping money neutral and control of the speculators, nor do they examine the refinements of Smith’s system by Marx and Mill, consequently over 70 years of collectivism in America has been unable to reform capitalism. The fatal flaw of the collectivists is their preoccupation with government redistribution of wealth instead of addressing the flaws in the
economic system. The opportunity to build a foreign policy on promotion of economic common purpose is also lost.

During the 20th century, collectivism failed in their communist and socialist contracts to distribute wealth. During the same time, American collectivists increased the percentage of wealth taken by all levels of government in taxes by ten times. Money was wasted, and missions usually not accomplished because central planning inhibits the creation of wealth by its inability to assimilate complex, rapidly changing data, and it de-motivates people with its top-down structure. Despite its failures, collectivism survives in a form described by liberal economist-philosopher F. A. Hayek:

Socialists increasingly recognized the incurable economic inefficiency of central planning, collectivists then simply discovered that redistribution through taxation and aimed financial benefits was an easier and quicker method of achieving their ends.32

Describing Hayek as a “liberal” economic philosopher might confuse some as he is generally regarded as a conservative supporter of free markets. Hayek is a liberal in the classic sense of a believer in individual freedom, social progress, and reform. He matched his critique of collectivism with this one of conservatism:

Conservatism, though a necessary element in any stable society, is not a social program; in its paternalistic, nationalistic, and power-adoring tendencies it is often closer to socialism than true liberalism, and with its traditionalistic, anti-intellectual, and often mystical propensities it will never, except in short periods of disillusionment, appeal to the young and all those who believe that some changes are desirable if this world is to become a better place.33

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The economic guru both of Maggie Thatcher and Ronald Reagan, Hayek provided clarity on the pathologies of both collectivists and conservatives alike. Hayek understood that the function of government is to support free markets by keeping money neutral, control of the speculators, and no non-democratic privileges, in other words he understood the warnings provided in the 18th century Enlightenment summarized by Condorcet. Hayek advocated the usefulness of many other government functions, including the support of education and protection of the environment, but suggested that these missions can usually be accomplished better through financial incentives rather than punishing laws.

Collectivism has the support of the political left, reform-minded intellectuals, much of the popular media, and it receives general approval in liberal arts academia. It, however, contradict Karl Marx who tied social progress to movement to a superior economic system; based his economic system on the worth and potential of each individual; and predicted improvement in wealth creation after the work culture was changed from alienation to cooperation. Marx envisioned the world uniting in economic common purpose in which the standard of living would go up, the violence would go down, and the Warrior State would disappear. These visions of Marx are all contradicted by ultra-capitalism; they are honored in theory but contradicted in practice in collectivism, while integrated in theory and practice in democratic capitalism.

Democratic capitalism is the economic system that maximizes the creation and distribution of wealth through the participation of workers motivated by forms of ownership. The superior wealth creation and distribution capabilities of democratic capitalism can feed, clothe, shelter, educate and provide good health care for the world’s 6.4 fellow humans. Democratic capitalism distinguishes between market activities to be determined “in the natural course of things,” as Smith expressed it, and the vital responsibilities of government to be determined in a rigorous pragmatic way. The broad distribution of wealth in democratic capitalism has multiple benefits: it motivates the wage earner to innovate and produce, it adds income for those whose purchases trigger the multiplier effect, and whose reciprocal purchases make “globalization” a universal benefit.

John Stuart Mill identified the synergy among material benefit, the quality of life, and a moral environment in this democratic capitalist manifesto:
The other mode in which cooperation tends still more efficaciously to increase the productiveness of labor, consists in the vast stimulus given to productive energies, by placing the laborers, as a mass, in a relation to their work which would make it their principle and their interest—at present it is neither—to do the utmost, instead of the least possible, in exchange for their remuneration. It is scarcely possible to rate too highly this material benefit, which yet is nothing compared to the moral revolution in society that would accompany it; a new sense of security and independence in the laboring class; and the conversion of each human being’s daily occupation into a school of the social sympathies and the practical intelligence.\textsuperscript{34}

These words, written in 1848—the same year Marx and Engels published their \textit{Communist Manifesto}—marks a significant date after which forms of ownership participation have demonstrated superior performance but have not received the broad intellectual and political support needed to become the universal economic system. Tax incentives were passed into law in the early 1920s and again in the early 1970s when Senator Russell Long proposed and Congress passed 15 laws favoring ESOPs.\textsuperscript{35} These initiatives were overwhelmed by the lobby power of Wall Street whose privileges to concentrate wealth contradict the culture of worker ownership. Motivation and rewards from ownership are a vital part of a long-term, patient, democratic capitalism but fight for survival under short-term and greedy ultra-capitalism.

Despite the impediments, democratic capitalism has demonstrated such superior economic and social logic that by late in the 20\textsuperscript{th} century, over 25 million wage earners in America were participating in some type of ownership, and millions in other countries became owners as their countries privatized companies in their movement from tyranny to freedom. With the addition of ownership represented by wage earners’ pension and 401 (k) savings America now has the much announced “ownership society,” but the rewards are going to the handlers of the money, not the owners, the wage earners.


\textsuperscript{35} Employee Stock Option Plans
Jeff Gates announced *The Ownership Solution* in his 1998 book. Politicians of both parties provided testimonials, and one of the 20th century’s visionaries, Mikhail Gorbachev, former Russian Premier and author of *Perestroika*, wrote this:

Worker ownership focuses on the central issues that have to be addressed if the twenty-first century is to transcend the simplistic dilemma of capitalism versus socialism and create a new, sustainable civilization.37

Coretta Scott King, widow of Martin Luther King, Jr saw the same bridge that Gorbachev and politicians from both parties recognized:

Somewhere in between unbridled capitalism and the welfare state, there has to be a more just and equitable economic system which provides genuine opportunities for all citizens, while preserving incentives for investment.38

Mrs. King recommended examination of Gates’s “ownership solution” as “capitalism with a human face.”

Democratic capitalism continues to grow and demonstrate its superior capacity to build and distribute wealth, but it has been limited by the lack of assimilation by the intellectual community, by lack of support by political parties, by lack of institutional investors’ honoring their long-term fiduciary responsibility, by lack of visibility in education, and little visibility in the popular media. It is offered neither to Liberal Arts students as the way to improve the human condition, nor is it offered to Business School students as the way to manage for superior performance.

A Matrix Examined

The following comparison of competing systems makes clear that society will not progress through ultra-capitalism, the coupling of mercantilism and finance capitalism. It will not progress

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37 Ibid., Book jacket
38 op.cit.
through well intentioned but misdirected collectivism, it will move towards full potential only through the material and spiritual strengths of democratic capitalism:

**Wealth creation:**

*Ultra-capitalism* creates wealth through economic freedom but limits it in the work culture of fear and intimidation and by diverting capital from investment in job growth to speculation and consumption.

*Collectivism* limits the creation of wealth by legislating government intrusions in an attempt to micromanage industry. These programs frequently encourage a dependency condition. Collectivism fails to use its democratic power to reform capitalism in order to create more wealth.

*Democratic capitalism* creates the greatest amount of wealth because it motivates and rewards each to innovate and produce to their full potential in an environment of trust and cooperation.

**Wealth distribution:**

*Ultra-capitalism* believes in “trickle down” wealth distribution in the assumption that more wealth for the wealthy will help all people. It successfully lobbies government privileges that concentrate wealth. Insufficient spendable income limits the multiplier effect and reciprocal purchases needed to make free trade work. The result of both effects is the mal-distribution of wealth that, in turn, limits the creation of wealth.

*Collectivism* tries to redistribute wealth by government fiat, an inevitably inefficient approach that also limits the amount to be distributed through waste. Concentration by collectivists on the corruptions by ultra-capitalists diverts attention from the reforms that would create and distribute more wealth.

*Democratic Capitalism* through profit-sharing and ownership participation produces and distributes increased wealth, maximizes the multiplier effect at home, and adds income for reciprocal purchases critical for free trade abroad.
Social contract

Ultra-capitalism disdains any social contract between industry and society other than the mythical “trickle down” theory. Concentrated wealth in ultra-capitalism causes social tensions at home and frequently violence abroad.

Collectivism believes in redistribution of wealth by government to help individuals and compensate for the deficiencies of capitalism. Collectivism in all of its forms has had limited success in improving lives and no success in stopping the violence, in fact, its communist threat to ultra-capitalism resulted in more violence.

Democratic capitalism’s mission is to eliminate material scarcity in the world. Its capability to do so has been verified many times in many countries. Its mission includes improving the standard of living for all people as the only way to stop the violence.

Value system

Ultra-capitalism is individualistic, short-term, greedy, amoral at best, and frequently immoral. The expression “greed is good” is more a belief than a joke.

Collectivism’s mission is moral, but in too many cases the political structure erected in its behalf became tyrannical and immoral. Marx’s conversion of the work culture from alienation to cooperation implied a new morality never attained. Collectivists assume responsibility to control the effects of the immorality of capitalism with oversight and punishing laws rather than reform to the moral capitalism.

Democratic capitalism depends on an environment of trust and cooperation to innovate and produce to superior levels, therefore, democratic capitalism is moral at its core. As morality is not divisible, the company’s dedication to integrity includes relations with customers, employees, suppliers, and community. A concentration of democratic capitalist companies in an area has demonstrated an improved morality in the contiguous community measured by a reduction in crime and the cost of police protection.

Free trade
Ultra-capitalism lobbies both Congress and the World Trade Organization (WTO) for trading advantages in protectionist tariffs for manufacturers, subsidies for farmers, and deregulation for financial services. It has made globalization a target of protest because of practices that hurt instead of helped developing countries.

Collectivism is ambiguous but still tends to believe that protectionist tariffs saves jobs. It takes no position on the damage done to developing countries by the liberalization of capital markets ideologues because much of it was done by Democrats in the Clinton administration.

Democratic capitalism believes that free trade is the way to peace and plenty but that the transition is accomplished only by addressing all of the needs: education, infrastructure, rule of law, lack of corruption, available capital at modest cost, technology, and trained leaders. Democratic Capitalism upholds that the role of government in building an economy will change as the development proceeds. For example, mature countries should not have tariffs or subsidize farmers, but developing countries may need both for a time to allow industry and agriculture to build the skills and volume to compete

Smith’s conditions

Ultra-capitalism successfully lobbies government to contradict Smith’s conditions. Money is not neutral, it is excessively volatile and in excessive quantities that significantly affecting the commercial process. The speculators are not controlled, rather, they are provided privileges to speculate with borrowed money as much as ten times their own capital.

Collectivists are unaware of Smith’s conditions and consequently do not reform the economic system.

Democratic capitalism knows that observing Smith’s conditions of neutral money and control of the speculators, prodigals and projectors, as he called them, is key to building more wealth and distributing it broadly. Capital is not diverted to speculation.

Marx’s vision
Ultra-capitalism does not build up from the worth and potential of each; does not change the work culture from alienation to cooperation; does not position the superior economic system as the starting point for social progress; and does not promote economic common purpose as the alternative to Warrior State violence.

Collectivism does not integrate Marx’s visions into their agenda they only adopt his criticism of generic capitalism. Their agenda is redistribution of wealth by government not the creation and distribution of wealth by the superior economic system.

Democratic capitalism integrates the useful aspects of Marx’s vision: it builds up from the individual, it changes the work culture to trust and cooperation, it releases the innovation and productivity by motivated and rewarded workers; it believes that the superior economic system, democratic capitalism, can satisfy the material and spiritual needs of the world, and that economic common purpose can stop the violence. The integration by John Stuart Mill of Marx’s vision with private property, competition, and skilled management completed the definition of democratic capitalism.

Globalization

Ultra-capitalism believes in the American empire, big military expenditures, economic imperialism, and the inevitability of war and violence.

Collectivists are unclear about America’s position in the world and are intimidated by the military.

Democratic capitalists believe that the world can unite in economic common purpose and stop the violence. America’s role is as a strong team player helping developing countries improve the lives of their people. Democratic capitalists believes that once the world is visibly improving lives then America should lead in demilitarizing the world beginning with its enormous inventory of nuclear weapons.

Academic perception
Ultra-capitalism is held in contempt by most of the Liberal Arts professors while the short-term and greedy “American model” is celebrated in Business and Law Schools.

Collectivism is the political view of choice for the majority of professors but with little examination of the economic alternatives.

Democratic capitalism, the synergistic coupling of democracy and capitalism, is not examined in American education.

**Philosophy**

Ultra-capitalism is Hobbesian and non-democratic believing that people are murderous animals requiring control by an all powerful state. Ultra-capitalists believe that might makes right and that both commerce and geopolitics are zero-sum games, one wins, one loses.

Collectivism believes that a just society is possible only with a powerful state. It places more emphasis on what the state can do for people than providing the circumstances for people to do for themselves. Many collectivists are not true democrats in that they do not respect the wisdom of the people.

Democratic capitalism believes in the fundamental goodness and wisdom of people with industry and the state responsible for providing conducive circumstances. Democratic capitalism is Kantian in the belief that “perpetual peace” is possible. It believes that a rising standard of living is the only way to steadily to reduce the violence and points to the European Union as an example of economic common purpose stopping the violence.

**Unions**

Ultra-capitalism actively oppose them

Collectivists favor them.

Democratic capitalists are neutral. If the people want a union they may need one.

**Productivity**
Ultra-capitalism has passed on the productivity gains from the Information Age industries to the highest paid not to the wage earners whose compensation has been stagnant or declining for several decades.

Collectivism complains about the mal-distribution of wealth but does not recommend economic reform.

Democratic capitalism first stimulates more productivity from motivated wage earners and then shares if with them to sustain motivation while adding to aggregate demand for the benefit of economic growth

Inflation

Ultra-capitalism supports aggressive action to prevent price inflation that erodes the asset value of the wealthy and hurts the creditor class. It supports government officials who deny that the government can prevent asset inflation in real estate and stocks that have caused recessions and depressions and hurt millions of citizens.

Collectivism tries to add full employment to the Federal Reserve’s mission of price stability with little success. It has no position on asset inflation.

Democratic capitalism ties compensation increases to productivity and consequently is not a source of price inflation. Democratic capitalists know that asset inflation has been the cause of depressions and recessions, and this is evidence that the government does not, in fact, control currency and credit for the general welfare. Democratic capitalists would control asset inflation by bank reserves, margin requirements, interest rates, and taxes and points to other central bankers who recognize the economic threat from asset inflation.

Fiscal and monetary policies

Ultra-capitalism successfully lobbies tax cuts for the wealthy despite huge budget deficits. It successfully lobbies for the excessive liquidity and easy credit for speculation. The Crash of ’29,

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the Bubble Economy of the 1990s, LTCM, Enron and other scandals were all a result of the governments’ failure to limit easy credit.

*Collectivists* instituted progressive taxation but do not take a position on excessive liquidity or government protecting instead of regulating ultra-capitalism. The Democrats share responsibility with the Republicans for the easy credit that has caused such human suffering.

*Democratic capitalism* proposes tax-free dividends for low-and-middle income wage earners that would liberate the trillions of dollars of retirement savings held hostage by Wall Street. This priority in the distribution of surplus by companies would add hundreds of billions of dollars a year to aggregate demand both domestically and abroad. Democratic capitalists propose that asset inflation, caused by speculators with borrowed money, be controlled. Democratic capitalists believe that taxes that have been shifted from corporations and the wealthy to the middle class should be shifted back.

**Debt-savings**

*Ultra-capitalism* allows the government to build up record debt and encourages an economy based on record individual debt. America has a negative savings rate while China saves 40% of their GDP.

*Collectivism* try to win elections by promising more benefits from an already insolvent country.

*Democratic capitalism* will add tax revenues from stronger and steadier economic growth. It favors forced savings for medical, educational, and retirement needs from payroll deductions (similar to Singapore’s policy) The money would be in the control of the individual but would be invested in index funds at less than .15% annual cost, and in bonds used for environmental, educational and other infrastructure needs. These investments would add to economic growth and be coupled with deep cuts in military budgets.

*If democratic capitalism is so superior, why do we not use it?*

Why is democratic capitalism not the universal system in industry with its philosophy and protocols emulated by government at every level? The answer is myopia by the intellectual
community who are culturally conditioned to reject commerce as vulgar and social progress dependant on an economic solution as not worth consideration. This intellectual mind set first prevented the assimilation of Adam Smith’s conditions for free markets to work, and later prevented a synthesis of Smith, Marx and Mill which allowed exploitive capitalism to dominate both governments and commerce. There was no reason for this it was the mistakes of a few powerful people functioning in the confusion between ultra-capitalism and collectivism. Late in the 20th century an exhausted society seemed ready to unite in economic common purpose but the world’s most powerful nation did not recognize and respond to the opportunity.

The quality of civilization depends on the quality of knowledge; the quality of knowledge depends on the quality of truth seeking, the quality of truth seeking depends on the quality of education. This logic trail does not work, however, if knowledge is not integrated to improve the human condition. Most of contemporary, non-scientific knowledge is fragmented and specialized.

This lack of integration of knowledge for human betterment ignores the contributions of the 18th century Enlightenment who pointed the way to a world of peace and plenty summarized by the Marquis de Condorcet. Included in this extraordinary blueprint were specifics of Adam Smith’s economic freedom that could eliminate material scarcity, the structure and philosophy of a government of the people in the new Republic, America, and the proposed structure for perpetual peace by Immanuel Kant. The Enlightenment provided not only the ideal of human progress, but also, the means to attain the ideal, and the process, modeled after Newton and Bacon, to validate the ideal and specify the means.

The political and financial establishment, however, were never motivated to understand Smith’s conditions of neutral money and control of the speculators because most of them were enjoying the privileges from speculation with borrowed money. The reformers from the beginning have had a collectivist mind set and have offered government solutions instead of simply correcting the system to observe Smith’s conditions. This has gone on for over two centuries and is the basic cause of America now entering into decline. The solution has not changed, it is Smith’s economic freedom, including conditions that can feed the world, and economic common purpose that can unite the world and stop the violence.
Big mistakes - tragic consequences

In 2006, the folly and violence are getting worse. The intellectual community looks in all of the wrong places for answers, and untrained leaders continue to make incredibly bad mistakes. Human destiny in the 21st century is a quality control problem: do it right the first time, and stop the mistakes!

Management of economic freedom at home and economic common purpose abroad is relatively easy because decisions are decentralized, and management of change is comfortably within human competence. Conversely, central management of the economy to concentrate wealth causes social tensions and is by nature error prone, while efforts to centrally manage the world by coercion and violence is chaotic and even more error prone. Management of change in misadventures such as the Iraq war is beyond human competence.

If the American government had given priority to support of democratic capitalism at home and economic common purpose abroad, none of the following mistakes would have happened. All were violations of either democratic or economic principles, and if they had been avoided, the world would be well on the way to peace and plenty.

1953, Iran: The Dulles brothers, John Foster, Secretary of State and Allen, head of the CIA in Eisenhower’s new administration, sent Teddy’s grandson Kermit Roosevelt, to Iran with a big bag of money to topple the democratically elected Mossadegh, a superbly educated nationalist with a mission to bring Iran into modernity. Kermit succeeded.

Mossadegh had been honored by Time magazine as “man of the year,” calling him an “Iranian George Washington.” He offered the British the same 50/50 split of oil profits that the Americans had in Saudi Arabia; they refused; he nationalized the oil industry, and kicked the Brits out. They then talked the Dulles brothers into a “regime change,” courtesy of the CIA, based on phony Cold War claims of “communist threat” In a sham trial, Mossadegh was indicted, convicted, imprisoned for three years, and lived out his life in house arrest. He said that his crime was trying to free his country from colonial oppression.
Today, Iranian students know of America’s role in replacing their democratic leader with the imperial Shah, a puppet dictator. How many Americans know of this history and relate it to the present “Iranian threat?” Popular media articles on Iran start their current history with the taking of American hostages in 1978, not with America sneaking into Iran in 1953 to bribe enough rioters to dump their democratically elected leader.

Until this immoral, hypocritical violation of democratic principles, national sovereignty, and human rights, America was the only Western power that had not invaded the Middle East. The USA was positioned to partner with Iran and others in economic development. Instead, these actions initiated by a few arrogant and ignorant men put America on a violent course in the Middle East that is still gaining momentum.

1950-1973, Vietnam: All of these errors were repeated in Vietnam by four different presidents both Republicans and Democrats. None apparently knew that Ho Chi Minh was a nationalist who quoted verbatim from the American Declaration of Independence in his inaugural speech. None apparently knew that he was at the 1919 “peace talks” excited by Wilson’s pledges of national sovereignty only later to find out that it did not apply to Asia. His alleged communist connections were only because they were the only nation to communicate with him with respect.

Vietnam is a case study in the violation of the truth-seeking process proposed by the Enlightenment who had adopted Bacon’s dynamic, collaborative, and cumulative process. Robert McNamara, one of the architects of this American disaster, provided a retrospection of Viet Nam in *Wilson’s Ghost* that finally concluded that those who had promoted this tragedy shared a cultural conditioning that precluded the challenge and debate process necessary to find truth. This was a blatant violation of Bacon’s principle of collaboration that includes diverse opinions. The process was not dynamic because such opinions were not repetitively examined; and the process was not cumulative because presumably educated men did not understand the history of imperialism or the passion for national freedom from foreign domination. 54,000 young, innocent Americans and millions of Vietnamese were the victims of ignorant and arrogant men, whose successors would repeat the error.

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1971, Excessive volatility: President Nixon abandoned the Bretton Woods agreement and let the dollar “float,” that is, let the international money market determine its value. For the first time in commercial history, no international stabilizing monetary system was in place. Nixon had “closed the gold window” and America stopped converting dollars held by other countries into gold. Nixon made this momentous decision without challenge and debate, and with little understanding of its consequences. This caused the excessive volatility that allowed the world’s currency speculators to dominate global economics with daily trades of close to $2 trillion dwarfing all commercial transactions. According to Joel Kurtzman “It created enormous arbitrage possibilities and set the stage for the invention of a myriad of new financial products.” It uncoupled the “money” economy from the “real” economy of producing and selling things and put them out of balance. This egregious violation of capitalism’s need for neutral, non-volatile money and stability in the international monetary system aided the rise of ultra-capitalism in which currency speculation with borrowed money was a direct cause of reversing economic momentum in many emerging economies. It spawned unregulated Hedge Funds and derivatives that add liquidity for speculation and increase the risk to the entire economic system.

1974, ERISA: The government, through the Employee Retirement Income Security Act mandated the present funding of future pensions and created the greatest opportunity in the history of capitalism with as much as $100 billion a year available for investment. The law was poorly written, however, and converted the economy from long-term and patient to short-term and greedy ultra-capitalism with much of the money going into consumption by the finance capitalists instead of investment in job growth. Stock market analysts threatened punishment or rich rewards based on the daily price of the stock to make companies change their focus to quarterly earnings (e.p.s.). Although the wage earners had become the new capitalists, through their retirement funds, and therefore, the source of new capital, the rewards of capitalism were captured by the finance capitalists-an intolerable contradiction.

Investment in long-term growth has been sucked out of the economy by years of “downsizing.” Trillions of dollars have been wasted by stock buy-backs, and the annual compensation feast by

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Wall Street’ money “managers” as they move the pension money from one pocket to another. An opportunity was lost to not only invest in economic growth but also to invest in environmental, educational, and infrastructure needs.

Despite the original intention of ERISA to protect pensions, many public and private plans are not able to pay their obligations. Congress addressed the problem in 2006, but, again, did not ask whether the money would be going into investment or consumption. In typical Congressional form, the elected representatives of the people responded to the lobby power of the ultra-capitalists and made it easier for pension funds to “invest” in hedge funds. The peoples’ money is now going into high risk, unregulated, highly leveraged, hedge funds, previously available only to the very rich, a further violation of the fiduciary responsibility of the institutional investors. After enough hedge funds go broke, the people will not only have lost their pension money but as taxpayers will end up bailing out the easy-lending banks. We shall see a repeat of the S&L (Savings and Loan industry) scandal that began with a bad design by Congress and ended with wasting several hundred billions of dollars of taxpayers’ money for the bailout.

ERISA is an Act of Congress that caused the excessive liquidity that diverts capital to speculation and violates the precondition of capitalism to invest surplus capital for long-term gain, not short-term speculation.

1986, Nuclear Disarmament: After the demise of communism, no international enemies threatened. At that time, the world had an opportunity to replace the mentality of the inevitability of war, with the inevitability of peace from economic common purpose. President Reagan and Russian Premier Gorbachev came close to a sweeping nuclear weapons ban in Reykjavik in a 1986 summit meeting. “Only the panicked intervention of several presidential aides-some of whom advise the current U.S. administration (George W. Bush)-pulled Ronald Reagan back from the brink of agreement,” according to The Nation.

This tragic mistake blew this best opportunity to demilitarize the world, and let the prophets of violence prevail again. Now there are eight nations with nuclear weapons, four of whom, North

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Korea, India, Pakistan, and Israel, ignore the Non-Proliferation agreement. The world is one assassination away from terrorist access to nuclear weapons. The combination of weapons of mass destruction with young people eager to sacrifice themselves for their religious beliefs takes the threat to new levels. The threat will recede when America renounces military imperialism and starts to get rid of its bombs The threat will recede when the military-industrial complex stops trying to provoke new enemies in order to sustain their over one-half trillion dollars a year budget.

Gorbachev tried again in December 1988 by presenting his vision to the U.N. of “deep, unilateral arms cuts; rejection of ideology in international relations; and a call for a new world order of cooperation in solving such global problems as poverty, pollution, crime, and terrorism.” Again he lacked American support, an example of the domination of foreign policy by the military and American fascists determined for ideological and economic reasons to prevent the demilitarization of the world.

1991: Iraq dictator: Saddam Hussein was indebted to America for providing weapons to help him kill over a million Iranians in a long war, 1980-1988. When he presented his plan to the American ambassador to annex disputed territory from Kuwait, Ambassador April Glaspie gave him a green light, describing the action as a border incident not of importance to America. The first Iraq war caused by this mistake led to the billeting of 5,700 American forces in the Muslim Holy Land, a terrible insult to religious fanatics like Osama bin Laden. These two mistakes—another Western power invading the Muslim world, and the defiling of their Holy Land with infidel troops—set the stage for 9/11.

A CATO study on “Suicide Terrorism and Democracy” concluded:

The specific goal sought in almost all suicide terrorists campaigns in modern history is the same: to compel a democratic state to withdraw combat troops from

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43 Ibid., p. 35.

territory prized by the terrorists…suicide terrorism is mainly a response to foreign occupation rather than a product of Islamic fundamentalism.45

This meddling in the affairs of other countries, with little understanding of their culture, is a violation of America democratic principles.

1998, Ultra-capitalists reversed economic progress in emerging nations: Countries from Eastern Europe to Asia, late in the 20th century, were adopting economic freedom to improve the lives of their people. Instead of building on this positive momentum, however, America pushed ultra-capitalism on the world, derailed the Russian move to a free economy, and reversed economic momentum in Asian nations. For example, Indonesia the world’s most populous Muslim nation had reduced the percentage of its people under the poverty line from 40% to less than 10% in a few decades. Ultra-capitalists, with hot money rushing out and currency speculators rushing in, ruined that economy and put over 50% of Indonesians back below the poverty line in a matter of weeks.

This was a tragic example of ignoring Smith’s conditions for the success of economic freedom: money was not neutral, and the speculators were not under control. The Malaysian Prime Minister, Mahathir Mohammed, a Muslim, called America and “economic imperialist” and currency speculation “unnecessary, unproductive, and immoral.”46

The ideologues of the “liberalization of capital markets” had talked emerging economies into taking down their cross border capital controls to let “free capital seek its most efficient investment.” A good theory but in practice it was mainly borrowed money seeking its quickest speculative gain. These ideologues made an enormous mistake in using free market principles in finance capitalism and then suspending the disciplines with subsidies and bailouts. This is not Adam Smith’s economic freedom in which he described finance capitalism as a subtraction from the wealth of nations, a necessary administrative expense, why money had to be kept neutral, and why the speculators kept under control. Joseph Stiglitz, former Chair of Clinton’s Council of Economic Advisors and Chief Economist of the World Bank, described the ideologues of the

45 CATO Policy Analysis No. 582 Robert A. Pape, November 1, 2005
liberalization of capital markets as “the most important factor leading to the crisis” in Southeast Asia.

1999, Hedge Funds: Brooksley Bonn, Chair of the Commodities Futures Trading Commission (CFTC) recommended to Congress that derivatives and hedge funds be regulated. President Clinton’s “Working Group on Financial Markets” including Alan Greenspan, Chair of the FED, Secretary Rubin, of the Treasury, head of the SEC, and the new Chair of the CFTC rejected the proposal. Bonn’s lonely voice was silent, she had resigned after they had ganged up on her. The following year the “Commodities Futures Act” was passed further extending the use of borrowed money to speculate.

A year earlier Hedge Fund LTCM (Long Term Capital Management), needed a bailout when it lost $3.6 billion. LTCM had failed to hedge its bets; rather, it “went directional” and bet on Russian bonds, not anticipating a default. Forbes commented: “Meriwether (LTCM’s head) seemed to have a magic touch. What he really had was nerve-wracking leverage.” According to Roger Lowenstein “Incredibly Greenspan again downplayed the risks posed by rogue investors such as hedge funds. The Chairman’s credulity seemed to know no bounds” Greenspan was not trying to be funny when he testified that “Hedge funds are strongly regulated by banks who lend the money” He was being consistent with his role of protector, not regulator, of ultra-capitalism

In September of 2006, hedge fund Amaranth Advisors lost $6 billion of its total assets of $9.23 billion in a matter of weeks. Like LTCM it did not hedge, it “went directional,” this time on gas prices. Under increasing pressure to improve earnings, hedge funds do not hedge, that is make bets in both directions in order to be “market neutral,” they make bets that their horse will run in only one direction.

Gretchen Morgenson, New York Times columnist, curious about how Amaranth Advisors could lose two-thirds of their total worth in a couple of weeks asked the question “Where were the

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commodities regulators?” She answered her own question “By going back to Dec 15, 2000 the final day of the 106th congress, when a last-minute provision was inserted into legislation removing oversight from energy commodities traded on over the counter electronic exchanges. The provision was an early Christmas gift for a hard working lobbyist-Enron!”

It gets worse. Hedge funds that managed $257 billion ten years ago, now manage over $1 trillion and are attracting the peoples’ pension money. A headline in the WSJ announced: “Congress May let Hedge Funds Manage More Pension Money.” The original rationale for no regulation of hedge funds was that their customers were all sophisticated millionaires and they could understand the risk. Who will tell the people?

This is an example of the awesome lobby power of ultra-capitalism. The government not only violates the responsibility to control currency and credit for the general welfare, but government officials, both Republicans and Democrats, are lobbied to be protectors, not regulators, of ultra-capitalism.

*Populist agenda, where we go from here*

Are the people defenseless? No, they have the will and the wisdom, they have the political structure that is supposed to filter their wisdom, they have the votes, they have the Internet to expedite communication, they only need a *democratic capitalist* agenda and new leadership from either party to break America’s gridlock.

Do not expect help from the colleges and universities where knowledge is fragmented and specialized. They have lost the mission to integrate knowledge for social progress, and many even claim that education of citizens is not their responsibility.

Do not expect the money managers of your retirement funds to invest your money for your long-term benefit. They are the shock troops for ultra-capitalism who are violating their fiduciary responsibility. They are employed by the people, however, and will respond when enough

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pressure is applied to support a democratic capitalist agenda.

Do not expect to be informed by the popular media. Most news people are economically illiterate because the same colleges and universities that failed to educate citizens also failed to educate future journalists about economic matters affecting the country’s future.

You’re on your own but the task is not that daunting. We have economic freedom, including the all-important conditions for success, provided by Adam Smith. We have the summary of the classical liberalism of the 18th century Enlightenment by the Marquis de Condorcet; we have Marx’s visions and we have the integration of this vision with private property and competition by Mill. The blueprint to democratize capitalism is clear and time tested over two centuries, readily available for inquiring minds. It awaits examination by the people and determined application of reform.

The highlights of an agenda are:

- Stop speculation with borrowed money

- Provide a “capital wage” for all wage earners from tax-free dividends on pension and 401(k) savings

- Change the measurement of corporate performance to a three-year running average of sales growth, profits, and cash flow against management’s predictions

Is that all that’s needed? Three steps sounds too simple, but will have a profound effect. The control of speculation with borrowed money will prevent asset inflation and eliminate the recessions and depressions that have damaged millions of people. Tax-free dividends will activate the trillions of dollars now being held passive in the stock market and give the wage earner a secure double-digit return, half dividends, half appreciation. Tax-free dividends will make profit sharing and ownership plans so attractive to the wage earners that they will become nearly universal. Hundreds of billions of dollars a year will be returned to the people and to the economy, money that is now wasted on stock buy-backs and non-strategic acquisitions. The extension of this distribution of wealth abroad will provide the spendable income to make free
trade a universal benefit. The change of measurement of corporate performance will emancipate
good companies from the short-term earnings pressure and will return the stock market to its
proper function of moving savings into job-growth investment and away from speculation and
consumption by the finance capitalists.

This is the core agenda that will harmonize democracy and capitalism at home and
position America to lead in economic common purpose abroad. To accomplish this
new American revolution, the following ideas are presented as planks in a reform
platform, means for actualizing the three steps of economic reform described above:

# 1-Free Wage Earners’ Capital!

Wage earners have become capitalists from pension funding and 401(k) savings, but are not
receiving a return on their capital. Large dividends can free this capital by adding a “capital
wage” to the labor wage.

A company’s surplus should be reinvested and paid in dividends to grow the economy. Instead,
during the past quarter of the 20th century, over a trillion dollars was wasted on stock buy backs
that hyped the stock price and CEOs’ options, and acquisitions that make the deal-makers rich by
cutting jobs. Combined with exorbitant mutual fund fees, and quicker turnover of stock sales by
commission brokers, ultra-capitalism, (the kind that traditionally exploited the workers’ labor) is
now exploiting the workers’ capital.

Led by pension funds, companies should be pressured to maximize growth and dividends, and
the government should be pressured to make dividends tax-free for wage earners. A secure
double-digit return, balanced between annual income from dividends and appreciation in a
growing economy, will reward the working owners of capital, not the money handlers.

# 2-Stop Economic Cannibalism!

That capitalism, whose mission is making money on money, rather than job growth, now
dominates the American economy because of the stock market’s power to richly reward or
severely punish companies based on small changes in quarterly earnings per share (e.p.s.)
Enormous stock options are the coupling device between the stock market and CEOs that results in a feeding frenzy in compensation, sacrifice of profitable, long-term growth programs for short-term earnings, and the “downsizing” of millions of workers, treated as disposable cost commodities.

The solution to this economic cannibalism is deceptively simple. Wage earners should demand that money managers change the way companies are measured from short-term earnings per share to a three-year running average of sales growth, profits, and cash flow, compared to managements’ predictions. Accountability for sales shifts attention to long-term growth; and focus on cash flow against predictions assures integrity in the numbers. For example, this cash flow discipline would have identified the cancer at Enron early enough to minimize the damage to jobs and pensions.

# 3-Speculate with Your Own Money!

Speculators borrow hundreds of billions of taxpayer-insured dollars from regulated banks to leverage risky bets. Currency and credit is controlled not for the general welfare but for the speculators.

The Crash of ‘29 and the Great Depression, that nearly destroyed this greatest of democratic experiments, contained all of the lessons that if learned would have prevented subsequent economic damage including the Bubble of the 1990s. Specific events that damaged many -such as LTCM in 1998, and Enron in 2001, could have been avoided if the government would, in fact, control currency and credit for the general welfare.

During the 1920s, speculators quadrupled their borrowings to buy stock. AFTER the inevitable Crash, the government raised taxes, shrank the money supply, increased bank reserves, and curtailed loans to buy stock, the right moves at the wrong time. If government had used these same tools BEFORE the Crash, the Crash would not have happened, but the government always lets the rich get richer before the poor get poorer.

Daily speculation in currency alone is now over $2 TRILLION DOLLARS dwarfing all real commerce! The people, led by pension-fund managers, must demand that their government take
these preventive actions BEFORE speculators destroy more jobs, pensions, and the world’s economy.

# 4-Leadership to Economic Common Purpose

Late in the 20th century, countries were improving the lives of their people through economic freedom, the world was uniting in economic common purpose, and the violence was abating. The world then took a wrong turn that reversed economic momentum and caused social tensions and unprecedented violence. What went wrong?

America abandoned economic leadership for military might in an attempt to run the world but resulting in a spectacular failure of leadership. At home, bad capitalism lobbied laws that resulted in a short-term economy with record concentration of wealth. Abroad, emerging economies were devastated by uncontrolled hot money and currency speculation causing Muslim leaders to criticize America as an economic imperialist.

Through the pension fund managers, the people must lobby for laws that support economic growth and broad wealth distribution at home, and leadership towards economic common purpose abroad, including a capital wage in large tax-free dividends, a change in measurement of corporate performance from short to long term, limitations on borrowed money for speculation, and international monetary rules that balance hot money with long-term investment.

# 5 Tax Incentives for Good Capitalism!

Democratic capitalism maximizes the creation of wealth by releasing the innovation and productivity of people, and maximizes the distribution of wealth through profit sharing and employee ownership. Congress should legislate favorable tax treatment for democratic capitalist companies paid for by reductions in corporate welfare. With this encouragement, good capitalism would displace the bad capitalism that treats workers as disposable, sacrifices job growth for short-term earnings, and has concentrated wealth in record amounts.

Qualification for this tax advantage includes: demonstrable integrity and meritocracy, profit-
sharing and stock ownership plans for all, attrition and retraining instead of lay-offs, CEO base salary less than 35 times the lowest wage, stock grants instead of options with tax consequences for company and recipient, executive bonuses in company stock, no stock sales by executives or directors until retirement, reinvestment in growth and payment of large dividends instead of stock buy backs and non-strategic acquisitions, and financial reporting on long term sales, profits, and cash flow instead of quarterly earnings per share.

# 6-Break the Political Gridlock!

FDR observed that there was nothing wrong with the free enterprise system except that we had not tried it yet. Unfortunately, we have yet to try it because of political gridlock. Market fundamentalists, generally Republicans, loudly oppose government involvement while lobbying for government privileges to speculate with borrowed money and concentrate wealth. Collectivists, generally Democrats, angered by this wealth concentration, lobby government to redistribute the money as benefits. Each group sustains support by pointing out errors of their opposite.

Neither group focuses on eliminating impediments that prevent capitalism from generating more wealth and distributing it broadly, such as limiting easy bank credit for speculation that caused loss of jobs, wages, and pensions, activating the workers’ pension and 401 (k) savings by large tax-free dividends; and changing corporate accountability from short-term earnings to long-term growth.

Citizens can apply their democratic power to reform these government fiscal and monetary policies, and to assure that their money managers’ mission is not personal gain but, rather, maximum return for the workers.

# 7-Listen to Henry!

Capitalism succeeds when DEMAND from higher wages for low and middle-income workers matches SUPPLY. Purchases at this income level add volume, reduce cost and price, and spread wealth— an economic dynamic not matched by more wealth for the wealthy.
Henry Ford, watching his Model T cars rolling off the assembly line in 1915, figured out that unless he raised his workers’ wages way up to $5 a day, they could not afford to buy the cars. DEMAND could not match SUPPLY and sales would drop.

Globalization can unite the world in economic common purpose, but it has become a dirty word because most managers of global companies aren’t as smart as Henry was. They try to maximize short-term profits by suppressing wages and benefits, not by motivating workers to long-term superior performance with profit sharing and ownership opportunities.

Globalization will remain a source of friction until global companies pay enough, including incentives, so that workers can both cover basic needs and have money left over to buy products from other countries.

# 8-They’re Feasting on Your Pension!

Federal law in 1974 required companies to put money away to pay pensions. Based on stock market history, you had a right then to expect a 10% total return from 5% dividends, and a 5% increase in value of stocks.

What you got, instead, was a bubble market, companies without money to pay pensions, and 1% dividends. The handlers of your money, meanwhile, increased their personal wealth through revenues multiplying from $27 billion to $270 billion. Brokers collected commissions on stocks held on average less than a year, instead of the historical six years; fees for “managing” money went way up; and your money was used to acquire companies and fire workers.

Fix this rip-off by demanding that the financial motivations of the handlers of your money be aligned with your retirement needs! Instead of commissions and annual fees, pay for 5-year performance. This change will also move the stock market from short-term greed to long-term growth.

# 9-Federal Reserve Board’s Mission

Pension plans are $1.3 trillion short of money to pay retirees because the government failed to prevent the Bubble Economy, failed to protect dividend income, stimulated the housing bubble
with zero-cost money, and allowed companies to use fictitious stock prices instead of putting real
money away to pay future pensions.

The Fed fights price inflation aggressively to protect the wealthy, but denies responsibility for
asset inflation in stocks or real estate that hurts ordinary people. The Fed pumps borrowed
money into speculation, not job growth; deregulates finance but bails out bankers after dumb
loans; and stands by while companies walk away from pension obligations!

This Fed must change its mission from protecting Wall Street to helping Main Street. The
present mission is destroying the savings of the same people whose taxes will have to pay future
pensions. Democratic action must challenge the Fed to use available tools of taxes, bank
reserves, interest rates, and stock margin limits to control currency and credit for the general
welfare, that is, to prevent asset inflation.

# 10- Not More or Less, but Better Government

American collectivists increased the amount of national income taken in all taxes during the 20th
century from 3% to over 35%. Much of the increase was expedited by stupid wars that required
central micromanagement. Many new bureaucrats came to Washington during wars, but few left!
Wars between nations should be over but the military expenditures continue along with the
central micromanagement.

Your government should be reorganized on the philosophy and protocols of democratic
capitalism, that is, decentralization, participation, empowerment, and results-based, not rules-
based. The proliferations of laws that politicians love to take credit for, should be minimized by
adopting John Stuart Mill’s advice about “non-authoritarian government,” the promulgation of
useful information but not more laws. For example, instead of OSHA inspectors roaming the
country looking for infractions, worker safety can be improved through insurance costs and
taxes. Punishing the profit line has more effect than bureaucratic oversight.

# 11-Mother of All Lies

People are propagandized to believe that war is an unavoidable part of human existence rather
than an obscene contradiction to reason.

The killing by governments of 160 million people during the 20th century was not an historical inevitability; but it happened, rather, because of mistakes made by a few men with more power than reason. Prussian Field Marshall Moltke pushed the Austrians into attacking the Serbs, starting WW I; and American President Woodrow Wilson’s ignorance of economics at the 1919 “peace” talks led to Hitler and WW II.

American hawks now need to make an enemy out of China to rationalize the one-half trillion-dollar waste of the taxpayers’ money for military expenditures. Fighting terrorists does not require nuclear subs. If the hawks prevail in this new mistake, Americans will lose legs, arms, and lives in a contrived crisis to “protect” Taiwan as a matter of “national honor.”

China is doing well in its mission to improve the lives of their people though economic freedom, while lending America the money to fund our deficit. China is going around the world making commercial arrangements, while America goes around the world adding to its hundreds of military bases for hundreds of thousands of troops. America’s mission should be to lead the world in economic common purpose, not dominate the world with military might. Citizens must demand a foreign policy with this economic priority.

# 12-Repeal the Repeal!

Was anyone watching in 1999 when the Glass-Steagall Act was repealed? This law had been passed during the Great Depression because bankers were giving companies easy credit to do dumb things in order for their investment bankers to get deals with big fees.

The monster financial services company, Citi, demonstrated Wall Street’s lobby power when it was put together in anticipation of the repeal. Citi, with other big banks, immediately gave Enron easy credit to do dumb things in order for their investment bankers to get deals with big fees. Enron, the hedge fund on top of a gas line, was free to quadruple debt in five years to $13.6 billion.

After Glass-Steagall was repealed, thousands of Enron’s employees lost their jobs and pensions,
and many others lost their pension savings. Why has there been no democratic demand to repeal the repeal? Citizens should, at least, demand that their government regulate hedge funds before more jobs and pensions are destroyed.

# 13-Root Problem Solved

Economic freedom can satisfy basic needs of people, and unite nations and cultures in economic common purpose. To accomplish this, money must be merely a medium of exchange, and speculators must be kept under tight control. When these conditions are in place, wealth and political power will be diffused, and capitalism and democracy will be in harmony.

Conversely, when money is treated as a profit-making commodity, and speculators deflect borrowed money away from job growth, then wealth and political power will continue to be concentrated, capitalism and democracy will continue to be in tension, the world will continue to be full of violence, and the more than two billion people who live on less than $2 a day will continue to go hungry, be sick, and lead miserable lives.

Citizens fail to understand either the function of money or the need to control speculators because educators, at all levels, cannot teach what they have not studied: the interaction between capitalism and democracy. Once educators learn and teach the essentials of economic freedom, then citizens will know how to reform public policy to allow economic freedom to function at—for the first time—full potential.

# 14-Reaffirm Idealism!

A world of plenty is attainable in both democratic and authoritarian governments through economic freedom. When people live better, violence goes down, other freedoms follow, and the ideal of a world of peace is attainable. Improvement in the lives of people and their children is the only ideal common to all nations and cultures; consequently, economic common purpose is the only way to unite people.

This ideal is more attainable in the 21st century because the Information Age adds new levels of productivity, new communications technology making the world a global village; and is itself a
unifying influence. The world is ready to free the body of material needs, and free the spirit to reach full potential, once the impediments of concentrated wealth and violence are eliminated.

Citizens must vote for candidates who reaffirm the ideal that peace and plenty are attainable, that economic freedom is the means, and that economic common purpose is the way to unite people and stop violence.

# 15- Job Growth or Stock-Market Casino?

Capitalism is based on converting savings into investment. Since 1974, federally mandated pension funding provided an enormous savings-investment opportunity with as much as $100 billion a year looking either for investment in equity capital for growth companies or for purchase of bonds for infrastructure needs.

Most of the money, instead, went to the stock market, inflating prices, causing a feeding frenzy in executive compensation. CEOs were whipped into being one-trick ponies: Fire! Over a trillion dollars was wasted in a quarter century on stock buy-backs and acquire-and-fire deals. They also have the indirect effect of shrinking the supply of stock adding to the imbalance of demand from pension money to supply of stock creating an artificial push in the up direction.

The media loves to report on this casino. The talking heads report every few minutes with silly reasons for market movement, including futures, when the real reason is that more gamblers are buying than selling, or the opposite.

Wage earners, ask your money managers two questions: How much pension money is actually invested in the job-growth economy? How much did “managers,” brokers, and specialists take off the top pushing your money around?

# 16-An Enron Protector

After Enron and other scandals, Congress passed Sarbanes-Oxley, a typical “catch a crook” law that adds cost and solves little. Government’s own failure to control currency and credit for the general welfare allowed these disasters to happen. Only by limiting easy credit can they be prevented.
This has been the cause for every business-cycle boom-and-bust in American history. Why? Because your government treats money needed for job growth the same as money used for speculation. The resulting concentrated wealth concentrates political power; the former corrupts capitalism, the latter corrupts democracy by writing rules that privilege the few.

When government’s mission becomes truly the protection of jobs and pensions, it will use bank regulation to encourage job growth and limit risky speculation. When companies are required to project cash requirements for three years, the lack of control of speculation will become apparent, and the brakes will be applied by increasing the cost of money and bank reserves.

Wage earners, demand that your elected representatives limit easy credit. Do that and you will have protected your job and your pension.

**# 17-Warning, Bad Storm Coming!**

The American economy is in a financialization phase similar to a condition that ruined countries such as 16th-century Spain, 18th-century Netherlands, and 20th-century Great Britain. The manifestations include shifting taxes from capital to the middle class, treating wage earners as disposable cost commodities, and finance capitalism that is dominant, not supportive of commerce.

For example, since 2000, premium, floating-rate housing loans have grown seven fold to $450 billion for those whose who do not qualify for a conventional loan. As the Fed raises their rates, most borrowers will not be able to pay the addition to their mortgage payments. The banks say, “why worry?” because they have used credit derivatives to pass on the risk, a market that tripled to $8.5 trillion in 2004. Hedge funds are betting on increased foreclosures; your pension funds are betting that things will not be that bad. Many of the most vulnerable home owners were seduced into the floating rate loans with special deals and will lose their homes.

Wage earners must demand that their elected representatives regulate hedge funds and derivatives before runaway speculation destroys more pensions and the economy.

**# 18- Better Governance**
Corporate governance tends to “gotcha” type negative oversight intended to catch somebody at something. Here are three positive ways to improve corporate governance:

**Distribution of surplus:** Outside Directors of public companies should determine the distribution of surplus among growth, dividends, stock buy-backs, and non-strategic acquisitions. The first two should be favored because they help the job-growth economy. The latter two waste the surplus but are favored by CEOs under pressure to hype short-term earnings. Moving this responsibility away from the CEO to outside Directors can add a longer-term balance to corporate planning and help neutralize the short-term pressure.

**Compensation:** Compensation Committees composed of outside Directors should be responsible for the compensation practices of all employees in order to assure an internal logic and encourage performance bonuses and ownership opportunities. At present, most Committees respond only to consultants’ recommendations for additions to the executive smorgasbord that feeds the compensation frenzy and alienates the people.

**Internal audit:** Company integrity should be monitored by the Internal Audit Department that reports to both the CEO and the Audit Committee of outside Directors. The CEO should provide quick and visible action in response to any violation of company ethics; the Audit Committee must guarantee to Internal Audit an unrestricted access to all operations.

**# 18-American Leaders, Please Stand Up!**

Improvement in the human condition depends on an economic system that maximizes wealth by releasing the innovation and productivity of wage earners, and distributes wealth to the greatest number of people through profit sharing and ownership opportunities. Strong, steady economic growth can then provide government revenues for educational, health, and environmental needs. The name of the system that does all of this is democratic capitalism, an economic system superior to all others that raises profits by elevating the quality of life, unites people in economic common purpose, and can stop the violence.

This superior performance of democratic capitalism has been validated in companies and countries for over two centuries, but it is not yet universal because of the impediments of
concentrated wealth and violence among nations and cultures. Movement towards the superior system awaits rejection by Americans of short-term and greedy ultra-capitalism, and an understanding of why other nations reject America’s imperialistic effort to run the world. This is the agenda at home and abroad that most Americans desire. Political leaders who understand and present the potential of democratic capitalism will be elected and receive enthusiastic support in the reform of capitalism and foreign policy.

The results will be dramatic. Americans will respond to visible evidence of a fair society, a large increase in total wealth, and a broad distribution. Stronger and steadier economic growth will provide the tax revenues to help people and the environment. People will see their government by emulating democratic capitalism participation will function better at considerably less cost. The people will again participate in their own governance; and regain idealism in the process.

Once Americans have refined capitalism, restructured government, and regained idealism they will reposition American foreign policy to be a strong team player. From confidence in reformed economic freedom and excitement about the unifying power of economic common purpose America can show the way to peace and plenty. The fanatics will lose their support as young people in all cultures demand participation in the good life. In this world without national enemies, America can then lead in demilitarization, the guns can be finally be beaten into ploughshares. Democracy will demonstrate the capacity to correct itself aided by the arrival of new leadership that knows how to properly harmonize democracy and capitalism
Chapter 3
Institutional Investors: Agents Of Change

Every few hundred years in Western history there occurs a sharp transformation. We are currently living through just such a transformation. It is creating the post-capitalist society. Instead of the old-line capitalists, in developed countries pension funds increasingly control the supply and allocation of money. —Peter Drucker

During the last quarter of the twentieth century a new capitalism emerged as a global system with the potential to combine the capacity of capitalism to eliminate material scarcity with the Marxian ideal of broad wealth distribution. This new wage-earner capitalism, called either "pension socialism" or "employee capitalism" by Peter Drucker is here called democratic capitalism where labor and the source of capital become one.

Initiated by federal law requiring present funding for future pension benefits the ownership of public companies shifted dramatically to the wage-earner. American institutional investors—pension funds, mutual funds, insurance companies, banks, foundations, and university endowments increased their money to be managed from $673 billion in 1970, under $2 billion in 1980, to well over $12 trillion by the end of the century. Ownership of public companies by the wage-earners grew from under 15% to over 50%.

More extraordinary than the explosive growth of wage-earner capitalism by the end of the twentieth century was the reality that instead of resulting in a diffusion of economic and political power, wealth was more concentrated in the United States. Instead of public companies becoming more accountable for the long-term financial and social benefits of their majority owners, they adopted the goal of short-term earnings.


53 Drucker, op. cit., p. 82.

The paradox of more democratic ownership in contrast to more concentration of wealth and a less socially sensitive capitalism can be traced to an egregious government mistake. ERISA, passed by the US. Congress in 1974, misdirected trillions of dollars of the wage-earner's pension savings to Wall Street, and shifted momentum to short-term and greedy ultra-capitalism. The institutional investors helped ultra-capitalism, a/k/a "the American model" become dominant instead of developing a suitable mission, measurement, and accountability for this new form of capitalism.

The government failed to analyze alternative uses of this new flow of democratic capital. Instead they responded to the lobby power of Wall Street and sent most of it to the stock market. A new chapter in the book of making money from special government privileges was written.

*For the two centuries of the Industrial Revolution finance capitalism had exploited the workers' labor, now in the early stages of the Information Age revolution ultra-capitalism has learned how to exploit the workers' capital.* Instead of leading the world to the benefits of democratic capitalism, the institutional investors during the final decades of the twentieth century have become the shock troops for finance capitalism and forced ultra-capitalism on the world.

Peter F. Drucker spent most of the twentieth century analyzing the organization of human affairs. His more than one dozen books range from management, politics, economics, to society in general. Drucker, born in Vienna, educated there and in England, became a professor of politics, philosophy, management, and social sciences at American colleges, while being a student of Japan and Japanese art. Drucker commented on ultra-capitalism:

> What emerged from this frantic decade (hostile takeovers, leveraged buy-outs, downsizing, etc.) was a redefinition of the purpose and rationale of big business and of the function of management. Instead of being managed `in the best balanced interests of stakeholders,' corporations were now to be managed exclusively to `maximize shareholder value.'

This will not work, either. It forces the corporation to be managed for the shortest term, but that means damaging, if not destroying, the wealth-producing capacity of the business. It means decline and finally swift decline. Long-term results cannot be achieved by piling short-term results on short-term results. They should be achieved by balancing short-term and long-term needs and objectives. Furthermore, managing a business exclusively for the shareholders *alienates* the very people on
whose motivation and dedication the modern business depends: The knowledge workers. An engineer will not be motivated to work to make a speculator rich.\textsuperscript{55} 

The first priority for institutional investors is to examine the proposition that democratic capitalism maximizes long-term shareholder value because the system that maximizes the innovation and productivity of each should, as Marx proposed, add up to the system that maximizes the benefits for all. Exclusive concentration on short-term results will eventually be self-defeating as it destroys the motivation of those upon whom the long-term success of any enterprise depends.

\textit{In 1974, the U.S. government, undertook to protect workers' pensions, and created a long bull market as an unintended consequence.}

The profound change in the amount and direction of capital flow in the United States began in 1964 when Studebaker went broke, and thousands of employees under 60 years old witnessed the disappearance of their pension benefits. The legislators properly decided that this was not fair; led by Senator Vance Hartke, (D.- Indiana) Congress proceeded to work on legislation in response to the problem. After ten years, with the help of Senator Jacob Javitz, (R.- New York), ERISA (Employee Retirement Income Security Act) was passed and signed by Gerald Ford a few weeks after he became president.

The purpose of the law was to guarantee that a person's pension would be paid when earned, and many in Congress competed for the credit over this important new social legislation. The law requires that benefits be fully funded through trustees outside of company control. The sections of the law dealing with the personal liability of directors of companies scared them, for mishandling pension money in this new complex law might result in an attack on their personal resources. Whether the threat was real or perceived, directors were motivated for maximum insulation and discharged their responsibilities through a management committee who hired and fired money managers based on performance measured in quarterly and annual terms.

This was the genesis of the short-term earnings environment as the same performance time framework was passed onto company results. The quarterly and annual scorekeeping pension fund performance was usually based on the A. G. Becker median, a service that boy 1974 was measuring the performance of 3500 managed portfolios.

At the time ERISA became law companies had discretion on how much cash went into pension funding. Although an actuarially determined amount was charged against earnings, only a fraction of that was funded in cash. In effect, capital stayed in the company and was used for growth, dividends, or acquisitions.

Most pension plans were defined-benefit, that is, the company was responsible for paying workers a specific monthly benefit on retirement. Companies argued successfully that any gains on defined benefit money in the stock market was theirs, not the workers, because they guaranteed the pension no matter what the market did. As the market rose, companies were able to improve earnings by using the higher stock values in their actuarial assumptions to determine the amount of pension expense to be deducted from profits.

Gradually the defined-benefit pension plan was displaced by the defined-contribution plan where the worker and the company each contributed a specific sum to be invested to provide future pension benefits. Such forced savings are a sensible policy of government to maximize the citizens' future security; further, this defined contribution was attractive to companies because they were able to shift much of the cost to the worker. Cost-shifting by companies was aided by the 401-K tax law that allowed the individual to contribute in pre-tax dollars, another good government policy to encourage savings. By the time these features were added, the bull market had sufficient momentum to validate the stock market as the preferred investment and attracted substantially more liquidity. To a large extent it was a self-fulfilling prophecy, as the direction of the money was now fixed toward Wall Street and the favored investment was stock.

The government did not use this new source of capital from ERISA to democratize capitalism by buying shares in the company for the workers. In fact, the amount of money invested in the workers’ company was specifically limited to less than 10% of the pension plan assets based on the conventional wisdom of not risking too many eggs in one basket. The alternative, insuring basic pension benefits privately while using the money to fund company growth and building worker ownership at the same time, was apparently not considered.

In time, a growing sense of ownership would have changed the culture in most companies to democratic capitalism: Workers would have become more involved and motivated to innovate and produce. From this environment, profits would have been maximized, distributed broadly, and the persistent flaw of capitalism, concentrated wealth, would have lessened.
Instead of finding new ways to democratize capitalism, the government, encouraged by the strongest lobby force in Washington, directed the money to Wall Street and initiated the longest bull market in history. The effect of this excessive liquidity hitting the stock market, can be measured by comparative valuations of corporate earnings. Over a sixty-year period, the average stock price was valued at sixteen times earnings. A few years before ERISA, this value was as low as seven. By 2000, as the investable funds continued to grow, corporate earnings were valued over thirty, double the sixty-year average. In dot.com companies, the earnings multiple was infinity as in most cases there were no earnings. By late-2001, with corporate earnings declining, the multiple was still illogically in excess of twenty.

Many celebrated a new worker's capitalism, or as Drucker expressed it:

> If Socialism is defined, as Marx defined it, as ownership of the means of production by the employees, then the United States has become the most "socialist" country around while still remaining the most capitalist one as well. Pension funds are run by a new breed of capitalists: The faceless, anonymous, salaried employees, the pension funds' investment analysts and portfolio managers.56

This was a seismic shift in capitalism. For over the two centuries of the Industrial Revolution the coupling of democracy and capitalism had improved millions of lives, though it had been an imperfect process as both economic and political power were concentrated. Now that the wage-earner was the majority owner, the logical expectation was that economic and political power would be diffused. It did not work that way, however. The diffused worker ownership did not result in diffused economic and political power.

Two illusions persisted in this worker's capitalism. One, the perception that the money flowing to the stock market in some fashion is recycled to fund economic growth. With the exception of IPOs that fueled the dot.com bubble, this was rarely true. Ultra-capitalism rejects the dilution that comes from issuing more stock as a source of capital to grow on. Wall Street does not like dilution because while the additional shares may fund long-term growth, they also reduce the all-important earnings-per-share in the short-term.

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56 Ibid., p. 6.
The other illusion ignored the tidal effect of pension money. The tide of money that was rolling in would eventually roll out when the money was paid out in retirement. The hydraulic buy-pressure on the market will become a sell-pressure. This dramatic shift in the buy/sell dynamic will then be exacerbated by changing demographics as more and more people will be retired, and fewer and fewer working to provide the benefits.

The capital formation spawned by ERISA law has been enormous. About equally divided between public and private plans, it approached $100 billion in a year and at the turn of the century, with the inclusion of 401-K savings, totals over $4 trillion. One might assume that such a new source of democratic capital would solve the problem of low-cost patient capital to build companies, invest in education, infrastructure needs, and create jobs, but the architecture of the plan was such that the money went to financial capitalism. In this process it partially funded junk bonds used for takeovers and LBOs, built up mutual funds, financed speculation in derivatives, and helped fund real estate speculation. Excessive liquidity was combined with opportunities to borrow enormous amounts of money for speculation to multiply the values of artificial assets.

When ERISA required that money be taken out of the company and invested for a future purpose, an extraordinary opportunity was presented to democratize capitalism: The money could have been kept in the company for growth capital by buying shares for the workers. With the benefit of keeping this capital in the company, large dividends could have been paid annually, allowing the wage-earner the election of either taking the money for additional spendable income or reinvesting it in additional shares.

The mid-1970s was a time of great opportunity for the government to democratize capitalism. Congress was in the process of legislating this flow of capital through ERISA, at the same time Senator Russell Long's committee was proposing, and Congress was passing, tax laws that encouraged worker ownership through ESOPS. These activities could have been integrated with Social Security and medical benefits, all from pre-tax dollars, and all with substantial contributions from the wage-earner. Additional inducements could have been provided with tax-free dividends and long-term capital gains for low- and medium- income wage-earners. Various financial instruments, including convertible preferred stocks, combining the benefits of large dividends with potential equity appreciation, could have been designed for the new capital flow and the integration of the even greater flow of cash from Social Security.

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57 See Chapter 5.
None of this happened. Direct forms of worker ownership grew but without the benefit of favorable dividend and capital-gains taxes. Social Security obligations continued to be unfunded, medical costs continued to escalate to an incredible 15% of GDP (about double other mature economies) and the excessive liquidity that was directed to Wall Street changed capitalism to short-term and greedy. Although the damage was becoming more apparent in 2001, the political priority was not yet about how to change tax laws to encourage worker ownership but rather how to cut income taxes and eliminate the estate tax for the wealthy.

After the pension money pressure shifts from buy to sell, two other government errors will mature. First, Social Security has never put money away for the future obligations; it has been used to subsidize current government costs. The same phenomenon of more taking out and fewer putting in will be repeated in Social Security. In addition, the government does not apply the ERISA philosophy of present funding for future benefits to government pensions. If they did, the government, civilian and military pension funding obligation would be over $1 trillion, and "the funds needed to cover annual benefit payments by 2010 are expected to be $160 billion." 58

After ERISA provided the cash flow directed to the stock market, the media helped build short-term earnings pressure reporting that some managers of corporate pension funds were asleep at the switch! They had an epithet for these managers "closet indexers," (a large equity group with return based on averages) and needled "These closet indexers are sitting back playing it safe, yet charging fees commensurate with active management. But the jig may be up and these guys are feeling the heat." 59 The article says that these fund managers were either called on the carpet and warned to be more active or they were fired. This same article explains that fund managers had previously been motivated to be conservative and stay out of trouble.

A few months later, the pressure on fund managers increased: "Pension Fund Performances Are Rated as Poor Regardless of Type of Manager, Study Shows." 60 Only 22 of every 100 funds matched or exceeded the average annual return of the S&P 500 over a fifteen-year period. A conservative approach to investment was assumed because of a drop in stock participation from


75% of the total in 1972 to less than 55% in 1978 with the money moved to safer but lower return bonds.

Without any great effort, the Wall Street casino had a new source of capital. The speculative frenzy of 1929, with its easy margin requirements, drew individual investors, foreign money, and finally even big companies choosing the exciting rewards of speculative capitalism over the longer, laborious returns of democratic capitalism. The central monetary fact after the 1980s was the effect of additional pension funds creating a rising market that seemed to validate the logic of such investment. The competitive demand for performance was satisfied with the sustained buy-pressure driving up the Dow Jones from 750 in the early `70s to a high of over 12,000 in 2000. Pension fund managers traded accounts actively to prove the value of their fees against that terrible comparison, indexing. That is, investing in the average value of the stock market. The total amount of private and public pension plans for investment went from under $800 billion in 1979 to over $4 trillion by the turn of the century. In 1946, only 4% of the corporate equity was held by institutions, this increased to 13% in 1965, 24% in 1975, 36% in 1996, and over 50% in 2001. Trading volumes reached record levels, fund managers turned their entire portfolio over once every two years, adding an impression of expert selection while building broker commissions.

Originally, some in the media had criticized the money managers for being too conservative with the workers' pension money. Subsequently, they featured both arbitrageurs and money managers as spokesmen for new capitalism and monitors of "entrenched management." Others in the media warned that the changing dynamic had dangerous implications for the long-term health of the economy. A Business Week cover story questioned: "Will the Money Managers Wreck the Economy? Their short-term view derails companies' long-term plans."61 On the other hand, Ivan F. Boesky, later a convicted felon because of his financial actions, was quoted: "Executives think that by concentrating on their business alone, they're doing a good job. That's not true." Boesky's remark was accompanied by a full length picture of that gentleman striking a Napoleonic pose.62 A Prudential Bache executive said, "The typical investment cycle was three to five years in the 1960s. Now it's more a casino."63 Robert Monks, then chief ERISA administrator, later a "rock star" of pension investments and a governance activist, encouraged the institutions to do something about

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61 Business Week, cover story, August 13, 1984, p. 86, 93.

62 Ibid., p. 87.

63 Ibid., p. 88.
"entrenched management." Not knowing much about competition and how inarticulate unrepresented democratic capitalists really spend their day, the media jumped on this exciting new concept of how to make those fat cats accountable. Bigger even than the photo of Boesky, was the portrait of Monks looking solemn while pontificating that "pension fund managers should actively support takeovers that boost their portfolio value." Fortune described the "liquidity surge" and called the pension funds a major pipeline, pointing out that such pension funds, both large and concentrated, were having increased influence over the financial markets.

As the trillions of dollars piled up in Wall Street, the increasing power of the institutional investor could be gauged by the headlines in the financial media. In 1989: "Wall Street's New Muscle Men," in 1990, "Who's in Charge Here? Institutional Shareholders Are Gaining Clout," and in 1991: "Who Owns This Company, Anyhow!? Institutional investors are increasingly calling the shots in corporate America. Management doesn't like it."

The excessive liquidity from pension funding helped fund the takeovers in the 1980s and 1990s. The takeover artists learned to "downsize" quickly in order to get the funds for the "control premium" they paid to make the takeover. First, the company's assets, including pension funds, were used to collateralize the borrowings used for the takeover, then workers were fired in large numbers. Downsizing was an easy and seductive opportunity, fire people and the short-term earnings go up, of course.

The poster boy of ultra-capitalism is "Chainsaw" Al Dunlop. His success at Scott Paper made him a media celebrity, and he even wrote a book. His arrival at old-line appliance maker Sunbeam quickly caused a large increase in the stock price. His "turnaround" was impressive and generated approval from the financial media and analysts. The "turnaround" was a fiction, however, as Sunbeam eventually went bankrupt. In 2001, the SEC has a legal action against "Chainsaw Al" for "cooking the books" at Sunbeam, an extreme, sad and tragic story, but one of many that are less

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64 Ibid., p. 89.
65 Vivian Brownstein, "Where All the Money Comes From," Fortune, January 2, 1989, p. 75.
66 David Pauly, Newsweek, June 5, 1989, p. 45, 47.
extreme and less visible.

Some in government were aware of this growing distortion of capitalism, but the lobbying power of Wall Street was powerful enough to resist reform. Senator Howard Metzenbaum (D.- Ohio) observed: "When business needs cash for a merger of takeover, the pension plan is one of the first places they look." Many in the Senate recognized the monster that they had released in 1974 with ERISA so they proposed reforms that should have been integrated into the original plan. Lloyd Bentsen (D.- Texas), chair of the Senate Finance Committee proposed taxes on short-term trades of securities by the tax-exempt pension funds. This concept was as vital to capitalism in 1989 as it is in the new century. Use taxes to penalize and control short-term speculation and reward long-term patient capital. Both Nancy Kassebaum (R.- Kansas) and Republican Minority Leader Bob Dole announced support, but the effort failed in the face of lobbying by Wall Street, and state and corporate pension managers.

Despite increased ownership by the wage earners they had little opportunity to vote shares in the determination of corporate policy. The institutional investor assumed this prerogative and in the process, aided ultra-capitalism in becoming dominant with the perverted result that wealth became more concentrated.

As the social and economic damage from ultra-capitalism becomes more apparent, the political left will protest with the same lack of comprehension that they exhibited in 1974 when they missed an unprecedented opportunity to democratize capitalism. Following the usual paths, political pressure from the left will be for more government action, not correction of earlier mistakes. Collectivists, sensitive to the general welfare with sufficient understanding of the conflicting forms of capitalism, could have provided the countervailing lobby to Wall Street in 1974 and democratized capitalism.

Adam Smith defined the wealth of nations as the total production of goods measured by labor value. He defined financial transactions as a subtraction from the wealth of nations. He warned that money should be kept away from the "prodigals and projectors" whose speculative enterprises

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72 Ibid., p. 309.
artificially drove up values and diverted capital from productive purposes. If the available capital represented by present funding of future pension benefits were to be used in the capitalism defined by Smith, the funds would have been recycled as growth capital while providing workers an opportunity to enjoy the rewards of capitalism through dividends and equity accumulation. If dividends were tax-free and had priority over stock repurchase and non-strategic acquisitions, all but very high-growth companies could pay 6% dividends. Workers' equity would grow with dividend reinvestment and long-term appreciation. Liquidity would be provided by opportunities to borrow at 6% for homes or education.

The American Dream was built by millions of people who were willing to make present efforts for future benefits, in many cases their children's benefit. The new era of instantaneous expectations reversed this philosophy and permitted ultra-capitalism to demand more and quicker profits, and to dominate corporate goals. The future of many companies is being sacrificed for the present. When this cupboard becomes bare, many companies resort to accounting tricks, some illegal, to meet Wall Street's voracious appetite for quick profits. Management becomes simple and brutal: "Just give me the numbers, dammit!"

One might ask: If ultra-capitalism is so bad, why did this American model look so good for so long? The answer is that economic freedom in the United States has always been strong enough to overcome impediments although never reaching a fraction of full potential. Besides, the Information Age has added enormous productivity and growth and, finally, companies have been hocking the future in a desperate effort to continue short-term earnings.

Marx's axiom is repeated throughout this book: Social progress depends on movement to a superior economic system. The political structure must be organized to support the system that maximizes surplus and distributes it broadly. As the surplus is maximized only by the involvement of educated, independent thinking, wage-earners in an environment of trust and cooperation, the whole culture can be unified and elevated by reflecting these attributes inherent in democratic capitalism. Democratic capitalism is the superior economic system that can positively effect economics, politics and the culture. The institutional investors have the power and the responsibility to abandon ultra-capitalism and adopt democratic capitalism.

Too Little Too Late

Despite the damage done by excessive liquidity and ultra-capitalism spawned by pension funding,
the institutional investors demonstrated that they could be positive agents of change, as institutional investors used their growing democratic power to improve corporate governance. The perception that power balance between management and the Boards of Directors before the 1980s was heavily weighted to the CEO, was generally true. With the benefit of institutional pressure and Wall Street analysts, companies did become more accountable and most boards strengthened governance procedures. Some institutions made management more accountable by targeting poorly run companies based on a reasonably long-term record. In most cases their criticism was earned, and in many cases, action was provoked as outside directors took more responsibility. When the democrats took over the White House in 1992 they sensed the opportunities for institutional investors to extend their positive impact as agents of change. The democrats viewed the $2.3 trillion of pension investments, 40% of the nation's financial assets, as the people's money, with great potential benefit for long-term job growth. By then, however, finance capitalism was dominant and "shareholder value" not "stakeholders" had become the ruling principle supported by the financial media and business schools. While it was usually expressed as "long-term shareholder value," in practice long-term was a year, short-term the next quarter and the measurement was stock price.

More and more CEOs became later day mercantilists treating the wage-earner as a cost commodity. Many CEOs were enthusiastic "downsizers," many others were reluctant but pressured by the analysts' quarterly reports that criticized them for not laying off enough people. The returns from dominant finance capitalism were wonderful. Ordinary people could expect 12-15% annual appreciation of their money. If you could make the entry requirements of a million dollars with hedge funds you could "earn" 40% on your money in a year!

Along with all of this good feeling finance capitalism had been deregulated, market disciplines suspended, and taxes shifted from capital to the wage-earners. For those whose mission was making money on money it was the best of times.

Robert Reich, the new Clinton Secretary of Labor and Oleana Berg, Assistant Secretary for Pension and Welfare Benefits Administration made long-term job growth and the largest, safest pension benefits their mission. The ERISA pension money under their attention was $2.3 trillion, multiplied about eight times since 1975 and heading for over $4 trillion by the turn of the century.

Secretary Reich identified the democratic capitalist culture as the one that would maximize profits, jobs and benefits in the long-term. Reich did this working with CALPERS, the large California
state employee pension fund, on what was basically the democratic capitalist mission: to raise both productivity and the quality of life. CALPERS in turn used a consultant's study to confirm the relationship between wage-earner morale and company performance:

A 1996 survey of 3,300 employees by management consultants Towers Perrin found a dramatic rise in workforce disenchantment nationwide, particularly a feeling that managers ignore employees' interests after making decisions that affect them. The linkage between financial returns and people-responsive policies has simply become too obvious to ignore.\(^73\)

It seems strange that the capitalism of involved motivated and well paid workers of Adam Smith, the experimental confirmation of the superior performance from investing in people by Robert Owen, and the agreement by Marx and Mill that the involvement and reward for all would produce superior results needed confirmation by late twentieth century consultants. It is not strange, however, if democratic capitalism is not being presented in the business schools as the way to maximize profits.

Assistant Secretary Berg, who had served on the Board of CALPERS for several years, made an observation that linked the working culture and performance but also linked these with the stock price assuming that long-term performance was a relevant criteria:

We've begun to review the existing literature that explains the relationship between workplace practices and the corporation's performance. We are particularly interested in determining how these practices affect the company's financial performance. If, as we expect, a connection between high-performing workplaces and superior long-term financial performance exists this superior performance should be reflected in the stock price of such companies over the long run. It seems intuitively logical that investments in human capital should positively affect the performance of corporations that make such investments.\(^74\)

It seems strange that a 1984 graduate of Harvard Business School should be searching for literature


on the relationship of the working culture and performance, concluding "intuitively" that investment in human capital improves performance. The reason that it is not strange is that Harvard Business School gives democratic capitalist little attention but gives finance capitalism extra attention.

Berg was quite explicit in distinguishing between damaging short-term goals and appropriate long-term mission:

> Where pension funds fit into this picture is that, increasingly, the institutional investors in this country are *becoming the market*, in that they now are the major providers of investment capital as they grow larger. Our argument is that once you've become the market it doesn't make sense for individual funds to try to play or beat it on a quarterly basis. In fact, if we are too short-term oriented, we will hurt our ability to compete globally; we need capital that is invested for the long term. This is consistent with the need to develop high-performance companies, since we believe that such companies will be the superior performers in the global marketplace.\textsuperscript{75}

These observations, early in the first Clinton administration, indicate the right mission expressed with clarity. It was, however, too little, too late as the dominance of finance capitalism was nearly total in 1993. At the same time that Reich and Berg were articulating a democratic capitalist manifesto, President Clinton was joining Secretary of Treasury Robert Rubin in jawboning emerging economies into taking down all cross border capital controls. This action was correct in theory but disastrous in practice because of suspended market disciplines, no controls on "hot" money or leveraged speculation. Berg put her finger on the excessive liquidity from ERISA that caused short-term and greedy ultra-capitalism but, along with everybody else, did not expect the bull market to keep charging. The Dow Jones was about 5000 at that time, a stratospheric level compared to the 750 pre-ERISA, but nothing compared to the following rise to over 12,000.

Berg assumed that the efficient market would self-correct but while she identified the ERISA effect on the buy-sell relationship she understated the extent of the distortion.

> Part of the evolution in investment is stemming from the growth of pension funds. When funds were much smaller as a portion of investable capital, their effects on the

\textsuperscript{75} *Ibid.*, p. 29.
economy as a whole were not as significant as they're becoming. There has been a lot of concern recently about all the money going into stock mutual funds, for example, which has driven up prices in the marketplace. Again, it's supply and demand: As more money gets concentrated in one place, you have to think about other kinds of investments to get appropriate risk-adjusted returns, because you can't have more and more capital continuing to chase the same few investments without changing the risk-reward ratio for those investments.\textsuperscript{76}

With the domination by finance capitalism, all of this dialogue was abstract reasoning with limited application in the 1993 environment and even less limited for the next eight years. The long-term mission, no matter how compelling or how clearly stated, did not have a chance in the daily excitement about stock price.

In 2001, the damage from ultra-capitalism is becoming more visible making a shift to democratic capitalism with expanded worker ownership more urgent. The question remains: How bad will the damage have to be before the institutional investors and the business schools discover democratic capitalism as the way to maximize profits? For one of the few times in this book I have refrained from coupling the maximization of profit with elevated spirits, unified people and an end to violence as recognition of democratic capitalism as the way to superior profit performance alone fulfills the fiduciary responsibility of the institutional investors and the mission of the business schools.

If the analysis of alternatives had been pursued in 1974, the blow torch of money would not have been directed at Wall Street, upsetting the buy-sell dynamic, financial instruments would have been created for direct investment in infrastructure needs, wage-earners would have built an ownership position by direct investment in their companies, with basic pension benefits insured, and companies would have retained more capital to grow on.

\begin{quote}
*The institutional investors can be the agents of change that benefits the long-term return to their constituency and points the world toward peace and plenty.*
\end{quote}

The institutional investors as managers of money are responsible for identifying and supporting the superior economic system. If, in fact, social progress is dependent on movement to the superior

\textsuperscript{76} Ibid., p. 30.
economic system then the activities of the institutional investors have an important social dimension.

If the superior economic system can sustain interdependent world economic growth, if people and nations can unite in economic common purpose and stop the violence, then the institutional investors' actions can have a direct effect on leading to a world of peace and plenty.

The institutional investor has a direct responsibility to refine capitalism to its most effective form and to restructure government in support of the superior form of democratic capitalism. The institutional investors, however, have a corollary responsibility to help energize people to work hard for a common goal, that is to reaffirm idealism; and to help people and nations stop the violence by international law backed by multilateral force, that is to reposition foreign policy.

This full menu for the institutional investor assumes that Enlightenment II has validated these hypotheses and that educated citizens demand these actions by both their political and financial representatives.

The following analyzes the hypotheses, and action required in these four categories:

**Institutional Investors Can Help Reaffirm Idealism**

Institutional investors can be a significant influence in energizing people by verifying the common ideology of democratic capitalism. People need to learn again that there is an equal opportunity for all to improve their lives, that it must be an interdependent effort, that the worldwide goal of eliminating material scarcity and violence is attainable, and that realization of this agenda is no utopian scheme but the sober responsibility of the new generation.

This reaffirmation is the necessary antidote to the negativism and relativism that infected society throughout much of the twentieth century. The institutional investor can help the intellectual community realize that the obscene failures of the century past, and the tragedy of September 11, 2001, were aberrations, a series of leadership errors, due to faulty truth-searching. The institutional investor can help direct attention to the ideal that results in improved food, shelter, clothing, health, education, and hope.

Idealism has been abandoned by many based on the sorry record of the twentieth century. The new
transformation, however, is built from the individual up where, conversely, all of the twentieth
century failures were from top-down political structures. A society based on individual
development in a harmonious whole is universal in theory, and has been proposed by most religions
throughout history. The exciting difference is that it is now attainable in a smaller world aided by
the productivity and unifying influences of the Information Age.

The universal solution built up from the individual and capable of eliminating material scarcity was
also proposed by Karl Marx. Marx appreciated the record of capitalism in improving lives and he
anticipated a productivity explosion with greater wealth after the worker owned the means of
production. Marx proposed that recycling the surplus to the worker-owners would sustain
economic growth and avoid the repetitive economic damage caused by concentrated wealth.

Society has progressed through a struggle and contradictory fashion, but by the beginning of the
new century, two of the elements vital to Marx's ideal were in place: The productivity explosion
inherent in the Information Age, and worker ownership of the means of production in developed
countries. *The distribution of wealth consistent with worker-ownership remains to be completed.*

The specific means to broad wealth distribution are the *refinement of capitalism* and *restructure of
government*. The energy and determination applied to implementing these means will be
proportionate to the enthusiasm of those who embrace the ideal of sustained social progress through
movement to a superior economic system, defined here as democratic capitalism.

Idealism will be reaffirmed, and a common ideology evolve after an understanding of why Marx's
ideal failed. The reason is that Marx's ideal, based on releasing the enormous latent energy of
people when they are freed by the opportunity for full self-development, was compromised by the
political structures used as the means to his end. These political structures of communism,
socialism, and fascism corrupted and destroyed the ideal because, instead of freedom for self-
development, individuals were suppressed and frequently brutalized. Collectivism continues to
suppress initiative and suffocate the vitality of people.

An understanding of the reasons for the obscene events of the twentieth century is important and
should lead to recognition that during the twenty-first century it should be different. Most of the
elements of the ideal are in place, and that elusive goal of sustained social progress is very close to
realization.
As the future value of the wage-earners' money will be substantially affected by whether the twenty-first century is one of economic common purpose or more violence the institutional investor is obliged to influence government policy.

The ideal of economic common purpose will be met if the democratic capitalism culture with its broad wealth distribution is supported by the institutional investors and becomes the norm. The ideal of a world ruled by law enforced by multilateral actions of the U.N. will require persistent political action to change the existing aggressive unilateral policies of the United States.

The institutional investor represents the democratic power that can spread democratic capitalism where the resulting rising standard of living in all parts of the world will gradually build a sense of interdependence and displace animosities and violence. This world of peace and plenty has always been the ideal but in the twenty-first century it is attainable.

The institutional investors need to relate their support of democratic capitalism in specific terms to this ideal but they need to address the damage that ultra-capitalism has done to any sense of common ideology:

- Its concentration of wealth and visible excesses has caused social tensions and protest.
- The instabilities and volatility in the international monetary system have reversed economic momentum in many emerging economies displacing a growing sense of economic common purpose with a declining standard of living and social confusion.
- The continued concentration of wealth and visible excesses of ultra-capitalism has validated the view of many intellectuals that capitalism is exploitive. This has obscured democratic capitalism and prevented its support by much of the intellectual community.
- As the material and spiritual benefits of democratic capitalism become more visible it will stimulate more support from schools, religions and the intellectual community all vital to refreshing a sense of common purpose.

*Institutional investors can help refine capitalism.*

When the institutional investor identifies democratic capitalism as the way to maximize profits they
have a fiduciary obligation to applying its stockholder voting power to the distribution of surplus, in investment in more growth and in large dividends. These, in combination, will result in sustained economic growth and will shift the emphasis from the short-term earnings of ultra-capitalism to the combination of long-term earnings and annual income from dividends of democratic capitalism.

Drucker points out that wage-earners should now be the "main beneficiaries of the earnings of capital and of capital gains. But we have no social, political or economic theory that fits what has already become reality." It is the institutional investor's obligation to understand the theory and to put it into practice, it is democratic capitalism.

In post-capitalist society the wage-earner owns the means of production through the present funding of future pension benefits, 401-K savings, profit-sharing and stock purchase plans, and ESOPs. Some of the institutional investors invest union pension money that has an even clearer obligation to support democratic capitalism. University endowment funds, another source of institutional money, should have a special position as both the synthesizers of knowledge in this new transformation and the agents of change through their ownership.

In combination, these representatives of the new capitalism can initiate the transformation from command-and-control, hierarchial, and frequently fearful to the participation and contribution of the democratic capitalist culture. This will involve changing how business is measured, held accountable, and governed.

In this transformation of society, finance capitalism will undergo its own transformation from speculation to support of economic growth and new ventures in creative ways. Finance capitalism, with a mission to support democratic capitalism, can lead developing countries into ways to expand the legal structure of property and ways to free the morbid capital of the people for investment and participation in economic growth, a subject explored in depth by author Hernando de Soto.78

If we do not like short-term and greedy, what do we want to change it to? I propose the following measurement of corporate performance based on management's three-year projections: Sales growth, earnings per share, and cash flow, the latter divided into additional investment in growth

77 Drucker, op. cit., p. 78.

and dividends. A three-year period is selected because it gives time for managers to deliberately sacrifice the following year's earnings for an investment in greater growth and subsequent profit. Pragmatically, three years is also the longest time that institutions can accept for meaningful reporting. Sales growth is the key criterion for job growth, economic growth, full employment, and improvement in the standard of living.

Cash flow measured against a projection is an excellent way to measure company performance; it is simple and free of accounting practices that obscure performance. Distribution of surplus through dividends positions well managed companies in slow-growth industries to be highly regarded for a consistently high dividend. These companies are currently demeaned and their stock price punished by Wall Street. Companies distributing a large part of surplus in dividends would provide the stock market with a needed balance between high sales-growth companies and high yield companies, that is, large dividends. It is unrealistic to expect all companies, at all times, to have high-sales growth.

Except for start-up or extremely high-growth companies, most companies could pay a 6% dividend, and some slow-growth companies could pay more. Favorable tax treatment for low- and medium-income wage-earners would encourage greater use of profit-sharing and stock-purchase plans. The combination of profit-sharing, tax-protected dividends, and capital appreciation would stimulate productivity and innovation and make everyone a true capitalist. The resulting addition to spendable income for the wage-earner would sustain economic prosperity.

During the three-year measurement period stockholders would gain clarity on management performance by reviewing actual results against projections for the three criteria. The inclusion of cash as one criterion insures that managers will be accountable for both the profit-and-loss statement and the balance sheet, on the former, they are measured on sales and costs; on the latter, they are measured on cash management of such items as inventory and accounts receivable. One benefit of the technology of the Information Age is the opportunity to reduce the amount of cash tied up in the business, and in turn improve profits.

A grading system on the democratic capitalism culture.

Once the institutional investors are convinced that their responsibility for long-term value is best met by the contributions of all in an environment of trust and cooperation, that is, democratic capitalism, then they will need a grading system that measures how well existing or potential investments fit the democratic capitalist culture. The following is offered of such a grading system:
**Integrity:** Does the company have an explicit commitment to integrity in all business dealings written into its mission statement or charter? Are trust and cooperation stressed in all educational, training, and company communications? Are its actions consistent with this mission?

**Management Performance:** How well has management met its three-year forecasts for sales, profits, and cash?

**Distribution of Surplus:** Is the surplus reinvested in new growth and recycled into the economy through dividends? Does the company pay a 6% dividend? After reinvestment in greater growth, could the company pay a 6% dividend? Is management responsive to stockholders’ influence in determining the distribution of surplus?

**Profit-sharing:** Is there a sharing plan common to all and available to all?

**Ownership:** Is there a stock-purchase plan or ESOP? What percentage of all employees is participating? What is the percentage of participation projected to be in five and ten years? What percentage of the company’s stock is owned by all employees? What is this percentage projected to be in five and ten years?

**Democratic Capitalist Culture:** What is the evidence that the wage-earners are involved, participating, cooperating, and empowered?

**Meritocracy:** Does each associate have the opportunity for maximum self-development? What is the training and education budget calculated as a percentage of sales? What is the trend? How do associates have their potential tested and identified?

**Job Security:** Does the company have a best effort commitment to job security requiring restructure through attrition, retraining, and generous severance?

**Board of Directors:** Are there three or fewer insiders, including former executives, on the Board? Is there a diversity of backgrounds among the directors?

**Governance Committee:** Is this Board committee composed of all outside Directors? Does it participate in selecting new directors? Is there an annual performance review of the CEO and...
Directors?

Audit Committee: Is this Board committee composed of all outside directors? Does the head of the company's Internal Audit have a direct reporting responsibility to the Board Audit Committee? Does the company have a policy of changing outside auditors every five years? What is the percentage of consulting fees compared to auditing services paid to the outside auditors?

Executive Compensation: Is executive compensation based on an internal logic? Does the CEO participate in the same profit-sharing formula as all other associates? Do executives take all bonuses and dividends in stock? Are the executives expected to hold all their stock until retirement? In how many different compensation plans does the CEO participate?

Corporate Responsibility Committee: Is there a plan to encourage more participation by women and minorities in management? What is the plan, and what are the results and trends? What is the company's involvement in education and community activities? Are there any pending environmental hazards in company operations?

Performance Quality: Has the company utilized the microprocessor based distributed processing that now allows measurement and accountability in virtually all operations? Are there industry standards that measure excellence such as ISO or Six Sigma? Does the company participate? What is the performance record compared to expectations? Is there a way to rate overall quality performance against a peer group? If so, how does the company compare? What is the three-year trend?

Customers: Is there a method for ascertaining customer loyalty? What is the standard of measure of customer turnover? How does it compare to management's predictions or a peer group of other companies?

Associates' Morale: Is there a method for ascertaining associates' attitudes and morale? Can significant changes in morale be identified by specific location within the company? Is there a large spread from the best-morale location to the worst?

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Worker Safety: Does the Board review the safety program? What are the total costs of the program, insurance, and workers compensation awards? What are the trend lines?

Global Companies: Is there a formal policy and plan covering working conditions, including child labor and prison labor in other countries? Has the company analyzed the Mattel model, and will the company use similar audit procedures? Are there profit-sharing plans and ownership opportunities in all global operations?

The Mattel model covers all of the work practices in other countries that provoke criticism. The model includes unique outside auditing with the prerogative of the auditors to go public with their findings, if the company is not responsive. Included in the audit is the interviewing of workers by auditors who are not only fluent in the language of the workers but also in their dialects. These procedures are emphasized because many company mission statements lack this type of real-world follow through.

Freedom to perform based on decentralization and worker empowerment depend on discipline provided by sophisticated audit. Managers have broad delegation to perform, and the Board has the responsibility to measure and hold management accountable. In democratic capitalism, these broad delegations by the owners are supported by an audit process that includes all of the elements of the democratic capitalist profile. A clear understanding of the audit process is necessary for the institutional investor to judge the quality of the democratic capitalist culture.

The owners of public companies are now protected in theory by independent audit of the company's financial statements. This limited protection is, however, regularly compromised both by companies and by auditors. Auditors are often infected with the same greed as the corporations and they sometimes miss deteriorating circumstances in companies, and this failure severely hurts the stockholders. Auditors also sometimes compromise their objectivity by promoting their consulting business that grows larger and more profitable than their financial audit. In late 2000, the SEC (Securities Exchange Commission) completed a negotiation with the major audit firms and placed more responsibility on the Audit Committee of companies' Boards to prevent this conflict of interest.

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80 S. Prakesh Seth, Mattel Independent Monitoring Council for Global Manufacturing Principles, Audit Report 1999 (MIMCO), Zicklin School of Business, Baruch College-CUNY, 17 Lexington Avenue, New York, NY 10010.
To refine ultra-capitalism to democratic capitalism will require a thorough understanding of both the culture and the protocols of democratic capitalism by the institutional investors. It will also require an understanding of the profound damage done by several decades of ultra-capitalism including:

- The training of new leaders in many business schools in the culture of ultra-capitalism that treats workers as cost commodities, and gives exclusive emphasis on stockholders and short-term earnings.

- Wealth is concentrated in record amounts, not diffused consistent with the wage-earners' increased ownership.

- Instead of the democratic capitalism working culture of trust and cooperation, there is instead one of distrust, tension and individualism.

- Job security and a sense of loyalty are treated as anachronistic concepts in ultra-capitalism.

- Priorities for the distribution of surplus are mergers, acquisitions and stock buybacks, not growth and dividends.

- Executive compensation has escalated to hundreds of times the lowest grade. Any internal compensation logic has been abandoned and the sense of trust and fairness damaged or destroyed.

- Profits have been maximized, not by involving, motivating and rewarding all, but rather by firing people, cutting back on product development, research, training, maintenance, community activities and accounting tricks.

- Independent auditors have lost their independence by selling consulting services to ultra-capitalism and have been affected by the same escalation of compensation and gains on stock options.

- Short-term earnings pressure and a bull market have resulted in companies raising the "hurdle rate" limiting investment in new programs. The cost of equity has been assumed to be 12% or more, double what new equity would cost if new stock was actually issued.
• Deregulated banks have repetitively pushed so much short-term "hot" money into developing countries that this excessive liquidity led to imprudent loans for high-risk programs, speculation, and corruption.

• These weakened economies were thus set up for attack by speculators, real or perceived, that drive the "hot" money out of the country and collapse the value of the currency.

• Wage-arbitragers took advantage of the new lower wages caused by the devaluation to move manufacturing and, in effect, take advantage of the social and economic damage in order to improve profits.

• Global companies in many cases paid barely subsistence wages, ignoring the fact that free trade can be a universal benefit only when there is sufficient spendable income for reciprocal purchases.

• Wall Street executives led the excessive compensation parade, tens of millions of dollars annually, when deal making encouraged them to switch from advisory fee to percentage of the deal. Lawyers, accountants and corporate executives were stimulated to participate in ultra-capitalism where multi-million dollar annual compensation became ordinary.

*Institutional investors can help restructure government.*

The institutional investor can help *reaffirm idealism* and *refine capitalism* but they also should help *restructure government* in support of the superior economic system, democratic capitalism. Fiscal and monetary policies now lobbied successfully by finance capitalism must be modified to encourage the spread of profit-sharing, ownership plans, increased use of dividends for wealth distribution, significant reduction of borrowing for speculation, shift of taxes back from labor to capital reinstatement of market disciplines necessary to monitor free capital, leadership in the global codification of finance capitalism, and elimination of economic nationalism.

The long-term economic well being of the institutional investors' constituency depends on the structure, functions, and efficiency of the United States government. Institutional investors have a fiduciary responsibility and the potential political power to assure that the government shall promote the general welfare and support world economic growth.
At the beginning of the twenty-first century, the United States government was gridlocked between the collectivists and the finance capitalists. The former regulated things that should be free; the latter freed things that should be regulated. The collectivists raised total taxes taken and spent during the twentieth century from 3% to over 30%. Collectivists then tried to micromanage industry by telling them what ladders to use and which shoes to wear. The finance capitalists, on the other hand, convinced governments to take the controls off capital which, when coupled with floating the dollar and suspending market disciplines, resulted in a few years in international speculation that dwarfed commercial transactions.

It is good government to promulgate information about safe shoes and ladders; it is bad government to pass laws on those subjects and then micromanage their application.

This power-sharing by the collectivists and the finance capitalists has resulted in an extraordinary waste of the taxpayers' money and extraordinary concentration of wealth. The extraordinary waste has resulted in a taxpayers' revolt that prevents critical investments in adequate education for millions of youths and infrastructure. The extraordinary concentration of wealth contradicts the new reality that the major source of capital is now the wage-earner. The social tensions caused by this abandonment of the democratic promise for many, and the accumulation of great wealth for the few, will, in time, damage or even destroy both democracy and capitalism.

If this view seems too cataclysmic, recall that the Great Depression, only seven decades before, almost destroyed the U.S. democratic experiment. Consider the killing and misery since the Great Depression while the world has been learning, the hard way, that more freedom works better than less freedom. Now, at the beginning of the new century, most of the world is struggling to move to economic freedom. It will be tragic if the United States fails to provide the leadership towards economic common purpose and an end to violence.

This power-sharing by the collectivists and the finance capitalists has taken a long time to develop. Consequently, the corrective lobby power of the people, including efforts by the institutional investors, will need a program that is comprehensive, integral, and patient. The political process may happen one step at a time, but each action needs to be within a full context of socio-economic theory.

Whether the citizen's agenda is developed by the universities, a new or reformed political party, the institutional investors, or by a collaboration, an enormous political constituency is ready to be
energized by a program truly developed for the general welfare. This potential political constituency includes wage-earners, democratic capitalists, entrepreneurs, unions, civic groups, young students, and all intellectuals who believe in the opportunity for a better world. Young politicians from either party will recognize this agenda as the way to social progress, and the way to get elected.

Instead of government by this majority, the United States government during the twentieth century has evolved into the dysfunctional form described by Aristotle (Chapter 10). Instead of government representing the will and wisdom of the middle class it is government gridlocked between the extremes of representing the wealthy or representing the poor.

The agenda for restructuring government includes:

*Tax laws:* Democratic capitalism needs support by the elimination of double taxation on dividends, and reduced long-term capital gains taxes for participants in profit-sharing and ownership plans.

*Leveraged Speculation:* The government should regulate and reduce borrowings for speculation.

*Excessive Liquidity:* In the control of currency and credit for the general welfare, the government must prevent excessive liquidity from damaging the economy as ERISA has done and as the overlending of hot money has done to emerging economies.

*Democratic Capitalism Culture:* The use of Information Age measurement and accountability technology can be used to convert bureaucratic government to a process where government people are responsible for results and citizens are responsible for participation. Huge savings on administrative costs can be redirected to social programs and tax reduction.

*Shift Taxes from Labor to Capital:* Reverse the trend since 1980 of moving taxes from capital to labor. Tax speculation for two benefits: Raise government revenues and mute speculation. In the last quarter century, payroll taxes increased from 12% to 33% of total government tax revenues. During this same time capital gains taxes for the wealthy and the average corporate tax rate declined.⁸¹

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Standardized Global Banking Practices: America should provide the leadership to discipline the lending of short-term "hot money" that first overfunds growth and then flees so quickly that it damages whole economies.

Reinstate Market Disciplines: Free capital depends on the monitoring influence of market forces which are compromised by insurance, subsidies, and bail-outs.

Lobby Support for FASB: The Financial Accounting Standards Board (FASB) needs help from the institutional investors in their efforts to insure financial discipline, better disclosure, and integrity in financial reporting. The institutional investors should neutralize the lobby efforts of ultra-capitalism.

Eliminate Corporate Welfare: All types of subsidies should be phased out as intrusions on the free market with taxpayer money. These include subsidies to farms and oil companies.

Favorable Domestic Tax Rates: To encourage the spread of democratic capitalism, institute favorable tax rates for companies who qualify in their practices as democratic capitalist.

Eliminate Subsidies and Tax Havens for Multinationals: Capitalism depends on freedom of choice to produce anything, anywhere. This choice is compromised by tax laws, subsidies, and loan guarantees.

Favorable Tax Rates to Make Free Trade a Universal Benefit: Free trade depends on freedom to move operations but it also depends on sufficient spendable income to make reciprocal purchases. Tax laws should favor companies that meet working condition standards and distribute wealth through profit-sharing and ownership plans.

Direct Solutions to the Problem: Governments should discriminate in fiscal and monetary policies between speculation and commerce. For example, when the Federal Reserve Board identified "excessive exuberance" on the stock market as an inflationary threat, the FED should have raised brokers' margin requirements from 50% to 75%. Instead the FED raised interest rates that hurt the economy and ordinary people.

In the 1920s, and again in the 1970s, considerable Congressional interest focused on the benefits of worker ownership. Favorable tax treatment for ESOPs, along with the later 401-K feature that
allowed employee savings from pre-tax dollars, resulted from this government interest. Although these plans in the United States and abroad have grown, they would benefit from additional tax encouragement.

Institutional investors should prioritize dividends as the most important way to distribute corporate surplus, second only to reinvestment in growth. Along with an expansion of ownership plans, dividends could become an important part of broad wealth distribution, and large sustained dividends would become a reason for rating companies highly. Dividends are wonderfully flexible, some recipients would spend the added money with a beneficial multiplier effect on the economy; others would reinvest the dividend as patient capital for the company to grow on. Capital gains taxes should reward long-term investment and penalize short-term speculation. Zero or modest capital gains taxes for employees who hold their company stock until retirement would help spread these plans.

Institutional investors ought to know the answer to the following question: Which benefits the economy and, in the long term, the stockholder more: Distribution of surplus cash in dividends or use for stock buy-backs? If the answer is dividends, then why do tax laws favor stock buy-backs? Institutional investors should influence the tax laws to favor dividends, not stock buy-backs.

Big, successful global companies accumulate enormous amounts of cash. Toyota, at the end of 1998 was sitting on about $20 billion in cash, while the Japanese economy was starved by lack of consumer demand. At the same time, IBM was hyping its stock with a stock-buy-back program, $23 billion and climbing. Would not this surplus help the economy and the IBM stockholder better through distribution as dividends or investment in growth? In early 2001 the Japanese government changed their laws to allow companies like Toyota to use their hoards of cash for stock buy-backs! American institutional investors should learn from two decades of Japanese economic stagnation what the Japanese have yet to learn that consumer demand supported by large dividends is crucial to sustained economic growth. Stock buybacks have little beneficial multiplier effect on the economy.

Distribution of surplus has a social dimension that deserves more scrutiny than the next quarter's earnings per share. Presently, these questions are settled on the basis of Wall Street preferences. Wall Street loves big cash piles that can be used for lucrative deals, an attraction for a takeover attack, or stock buy-backs. Wall Street does not give dividends a high priority because they are not quickly translated into higher stock prices.
To reduce total taxes below 25% of the nation's GDP should be a goal of a citizen's agenda, supported by the institutional investor, as it forces attention on the enormous waste in present bureaucracy. This emphasis will force an integration of Information Age technology and finally, it will force a decentralization of functions to the lowest level with full use of participatory democracy. It will force recognition that the government cannot waste hundreds of billions of dollars on persistent mistakes like the Savings and Loan scandal.

This proposed structure of government would be dependent on a philosophical shift to the democratic belief in the capacity of individuals to participate and contribute freed from the suffocation of centralized management. This attitude shift will affect not only the size of government but also how the government involves their workers away from the bureaucracy described by Alexis de Tocqueville: "It covers the surface of society with a network of small complicated rules. The will of man is not shattered, but softened, bent, and guided ... it does not tyrannize, but it compresses, enervates, extinguishes and stupefies."\(^{82}\)

To *refine capitalism and restructure government* the institutional investor needs to help understand how to neutralize the effects of ultra-capitalism lobbied for so many years by Wall Street. These deep root problems include:

- Profits are privatized for the few with losses nationalized to the taxpayer. The Savings and Loan fiasco described in Chapter 7 should be required study.

- Hedge funds are unregulated and regulated banks do not provide the requisite discipline nor are they disciplined for not doing it. The LTCM fiasco described in Chapter 7 should be required study.

- FASB and the SEC are responsible for integrity in financial reporting but ultra-capitalism has corrupted the process to the extent that famous investor Warren Buffet commented: "CEOs have come to the view that it is okay to manipulate earnings to satisfy what they believe are Wall Street's desires."\(^{83}\)

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• **Stock options:** FASB has recommended various ways to charge profits for options providing some discipline to the number of shares allowed. Presently options are a "freebie" without cost to the company or the recipient at time of award. Consequently, the number of options awarded has grown by several multiples and helped couple the CEO's interest with Wall Street in stock price and deals, not long term growth.

• **Change Pooling-of-interest accounting:** Mergers and acquisitions can be motivated by strategic reasons, personal greed, or as the only remaining way to keep the stock price high. Pooling-of-interest accounting allows the acquiring company to ignore the premium paid over the book value of the acquired company which is then placed on the balance sheet as "goodwill" that has to be charged against profit over time.

• **Mark derivatives to market:** Banks have no obligation to correct their balance sheets to the current value of derivatives. The simple accounting rule for valuing items on the balance sheet is "cost or market, whichever is lower." The U.S. government lectures other countries about better disclosure but it opposes FASB efforts to get better disclosure on derivatives.

• **Level the playing field for restructuring:** When ultra-capitalist companies announce a downsizing or acquisitions, they are able to write off many future costs in one "big bang." The company defines a continuing "core" business, with the rest subject to "restructuring." It is a wonderful pill that makes management headaches go away quickly. The SEC is trying to exert more control, as this pulling in of future costs into a present write-off, lowers the quality of earnings which should be of significant interest to the institutional investor. A democratic capitalist company that chooses to "restructure" to a lower level of employment because of market changes, does so by attrition, retraining, and optional retirement on favorable terms. This approach takes longer and requires a deliberate investment, but it sustains the trust between the company and its wage-earners. The government and Wall Street combine to penalize this approach, as no beneficial tax write-off is allowed.

• **Oppose megamergers.** The U.S. government has relaxed opposition to major mergers. In time, this policy will hurt the economy as many companies use merger and acquisitions as their last-ditch effort to sustain or improve their stock price. Many companies with a high P/E multiple can acquire companies with a lower P/E and by that fact alone improve earnings. This has a negative effect on the long-term economy and should be a matter of interest to the institutional investor.
• **Reinstate Market Disciplines:** The bailout of Continental Illinois in 1984\(^{84}\) established the "too-big-to-fail" policy. The repeal of Glass-Stegall in 1999 encourages enormous financial service companies and a "really too big to fail" policy.

*The institutional investor can help reposition foreign policy.*

If the institutional investor in the U.S. is committed to *reaffirm idealism, refine capitalism* and *restructure government*, then the *repositioning of foreign policy* will follow. Once institutional investors recognize the opportunity for the United States to lead the world in economic common purpose, to eliminate material scarcity and violence, it will be recognized that this mission is mutually exclusive with political hegemony, an arms race, and a cop-of-the-world posture.

The institutional investor has the potential democratic power to not only counteract the lobbying of finance capitalism but also to counteract the xenophobic, militaristic, Cold War mentality that now dominates U.S. foreign policy. Institutional investors have a fiduciary responsibility to do this to protect their constituencies' investment from war and waste. Institutional investors have a democratic obligation to do this because the majority of citizens support movement towards economic common purpose, strengthening of the U.N., and an end to violence.\(^{85}\)

American leaders must recognize the new world realities. They include an end of imperialism and political hegemony by one or two super-powers. New realization should include the shocking reality that China will challenge the United States as the world's largest economy during the twenty-first century. This oldest civilization that has been generally free of imperialistic ambitions will now have the economic resources to engage in an arms race, *if that is the direction that the United States chooses*. Several generations of politicians' mistakes have already made a China matter, Taiwan, into a U.S. concern. Without a countervailing lobbying force these mistakes escalate into "national honor," where mistakes cannot be admitted, leaving war as the only alternative.

At the beginning of the new century the United States is trying for world political hegemony while ignoring the need to reposition its military and foreign policies consistent with new realities. The

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U.S. policies to fight two wars simultaneously, to be cop-of-the-world, while providing weak support for the U.N. are all counter to the democratic will and wisdom of the American people. It is not disinterest in foreign policy by the American people, as some suggest, it is the fact that the political parties do not include it adequately in their political agenda.

A paradigm shift in foreign policy is overdue, and it can be expedited by institutional investors. Their long-term fiduciary responsibility is to identify those broad historical developments that will affect the future value of their constituencies' money. Institutional investors who reaffirm the ideal of social progress through economic common purpose, will consistently oppose foreign policy that is based on the pessimism that war is inevitable.

William Grieder sees an "opening in history:"

> An opportunity to reinvent international relationships and to reach, with distant societies, a higher plateau of shared goals. Americans have the capacity to help fashion that different future and lead others to see the potential. Our democratic values and generous spirit are fully resonant with progressive objectives for the world at large.\(^{86}\)

The institutional investors are positioned to encourage the United States to move to a position of moral and economic leadership. With a powerful constituency of wage-earners, entrepreneurs, unions, universities, and democratic capitalists, institutional investors have both the brain power to develop the ideas and the political power to make it happen. New leaders will absorb the ideas and become excited by the potential political power. Grieder believes: "The American people are ready to hear something different. They await a real debate. Politicians who describe the new global realities honestly and offer plausible, forward-looking responses will find themselves becoming the party of the future."\(^{87}\)

The ideal is a world enjoying a rising standard of living, a developing sense of unity, better health and education, and all of these combining, in time, to eliminate violence. This is an attainable ideal only with U.S. leadership, a U.S. that can adjust to these new realities to become a team player, a

\(^{86}\) Ibid., p. 169.

\(^{87}\) Ibid., p. 184.

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strong leader on the team, but still a team player.

Early in the new century, time was running out for the U.S. to modify its position. Lethal finance imperialism had ravaged Asian economies in 1997 with the resulting social chaos that would continue for years. In Europe, the United States is determined to lead NATO whose mission of containing Russia is finished, but the U.S. will not accept that reality. Already included in the damage is the devastation in Yugoslavia, partly because the U.S. was determined to exclude Russia from the process, the only country with a long history of influence over the Serbs.

At the beginning of the new century and millennium, a philosophical battle is ongoing in the United States between those who see the world moving toward the economic common purpose of free markets greatly expedited by the Information Age, and those who believe, sadly, that the future will mirror the past. The former see a decline of violence as people enjoy a rising standard of living, better education, and are united by new technology. The latter see a more violent world as more people have more terrible weapons, bombs, chemicals, and germs, that can be easily delivered anywhere. The United States will play a pivotal role in which direction the world turns, and the institutional investor can be pivotal in determining U.S. policy.

The shocking attack on America on September 11, 2001 would seem to validate the pessimistic view but it can be turned into a unique opportunity for unity among nations. The world's history of violence has been primarily among nations. This terrorist threat is shared by all nations and can be the catalyst for a strong U.N., and the rule of law backed by multilateral force.

Support by the institutional investors for world opportunities from economic freedom would include a foreign policy that prioritizes economic leadership, maintains a strong military capability, abandons political hegemony, and participates only in multilateral actions in containing violence. By the end of the twenty-first century the world's level of affluence, health, and education will render violence a rare event. Until that time cooperative force must be available.

Institutional investors can be central to the development of the citizen's agenda directed to economic freedom and the multilateral rule of law. Politicians of both parties should be responsive to this most effective coupling of democracy and capitalism. Young, more idealistic politicians will recognize democratic capitalism as the citizen's agenda and the way to a world of peace and plenty as well as the way to get elected.
The citizen's agenda for foreign policy would include:

- A mission to turn the tragedy of the September 11, 2001 attack on America into an opportunity to unite the world first to eliminate terrorism and then in economic common purpose by building the power and prestige of the U.N. as the source of international law backed by multilateral force.

- A selection of U.N. multilateral action to eliminate terrorism as a strategic alternative more likely to win the war than unilateral or a U.S.-led coalition. A direct U.S. response is warranted but the question is not what response is warranted but rather what strategy is winnable.

- *The Moral Imperative*: Establish as a major goal of U.S. foreign policy, and indeed of foreign policies across the globe, the avoidance in this century of the carnage—160 million dead—caused by conflict in the 20th century.\(^8^8\)

- *The Multilateral Imperative*: Recognize that the United States must provide leadership to achieve the objective of reduced carnage but, in doing so, it will not apply its economic, political, or military power unilaterally, other than in the unlikely circumstances of a defense of the continental United States, Hawaii, and Alaska.\(^8^9\)

- Europeans should be responsible for their own stability and defense. NATO should be terminated. Over 117,241 American soldiers including 4,994 in Portugal\(^9^0\) would be brought home from Europe.

- In high-risk areas such as the Balkans, the Europeans, including Russia, will become responsible for containing violence through U.N. action. Any U.S. participation would be through this U.N. action.

- The U.S. abandons efforts at political hegemony in Asia, and would encourage Japan, China,
India, and Indonesia to promote stability and balance in the region. U.S. interests would be maintained through U.N. actions, 110,695 American troops would come home.\textsuperscript{91}

- America realizes that a holy war, a \textit{jihad}, with the Muslims is unwinnable, and that the memories of reciprocal atrocities will go away slowly through a proactive plan for economic common purpose resulting in a rising standard of living and better education. Over 11,000 American forces in Arab countries are considered a religious insult and a stimulant to terrorism. The U.N. should assume responsibility for assuring stability when requested by Arab governments.

- U.S. leads in demilitarizing the world, including, in time, the elimination of \textit{all} nuclear weapons. The U.S. is by far the world's greatest exporter of weapons of mass destruction and should reverse position to lead in global disarmament. The military-industrial complex, aided by those who consider violence an unavoidable part of the human experience, will continue to advocate massive military spending unless a powerful cohesive force of citizens recognizes the urgency: "The startling fact is that nuclear arms control is faring worse in the first days of the twenty-first century than it did in the last days of the Cold War."\textsuperscript{92}

- The United States encourages the U.N. to reform the Security Council to add more members to the existing five, U.S., Russia, Great Britain, France and China, and substitutes a 75\% vote for the present veto by any one of the five.

\textit{Summary}

The problems that stand in the way to twenty-first century peace and plenty have a common solution: democratic capitalism. The problems are concentrated wealth, terrorism and force, not law, in the relations among nations. Democratic capitalism maximizes surplus and distributes it broadly relieving the concentration of wealth impediment. Democratic capitalism has the capacity to eliminate world material scarcity, elevate and unite people and by demonstrating this gradually substitute law for force.

\textsuperscript{91} Ibid.

\textsuperscript{92} Jonathan Shell, "The Folly of Arms Control," \textit{Foreign Affairs}, Vol. 79, No. 5 (September/October 2000) p. 27.
All of these good things are possible if the institutional investors develop and implement a citizen's agenda. The universities, unions, religions, and civic groups have the same opportunity and responsibility but only the institutional investors have it as their fiduciary responsibility.

Finance capitalists have always used government privileges to exploit the worker's labor and concentrate economic and political power. Despite the recent diffusion of capital, "pension socialism," in Drucker's words, the finance capitalist has learned how to exploit the worker's capital. Contrary to logic, the diffusion of economic power has not resulted in a diffusion of political power because finance capitalists have gained control of OPM (other people's money).

Institutional investors are positioned to stop this aberration. They can change how companies are measured and held accountable; they can influence the government's fiscal and monetary policies; and they can move the world's dominant economic system from ultra-capitalism to democratic capitalism.

The promise of Marxism was the development of each individual to full potential, but Marx's theory in practice was displaced by the suppression of individual freedom. Democratic capitalism is built on the same economic logic that the whole is maximized as the sum of each individual's reaching full development. Democratic capitalism, however, is an extrapolation, a refinement of the existing structure that requires no radical and risky changes. Democratic capitalism should excite intellectuals for the same reason that Marxism excited them: a promise of secular progress. However, the same default of the intellectuals, namely their ignorance of economics, governance, and people, that supported Marxism and resulted in great social damage, however, can prevent democratic capitalism from becoming the socio-economic-political model for the twenty-first century. Intellectual fatigue, caused by the failures of the twentieth century, makes enthusiastic adoption of any plan for secular perfection suspect, particularly any plan with the word "capitalism" in it. For these reasons, the responsibility of the institutional investor is even greater. They have to be engaged in and provoke a process that can synthesize the ideal of democratic capitalism as attainable and can identify the means economic to that end.

The elected representatives of the people in the U.S. democratic republic have abandoned their commitment to reflecting the will and wisdom of the majority. This was anticipated by the founders who warned that the natural evolution in government was away from the people and toward bureaucracy and special privilege. Democratic citizens have to be alert and active in insuring the limitations of power, but they first need education and a more cohesive political force that
transcends the gridlocked political parties. The universities and the institutional investors can collaborate in developing the agenda and applying the political pressure to make it a reality.

If the human species fails again to reach its potential in the new century, future historians will indict leaders in the United States for sustaining the adversarial, violent world by demonizing countries like China and Russia. These countries were trying to make the long, difficult move from tyranny to freedom, from misery to a decent standard of living. They had reason to count on moral and economic leadership from the United States. If the U.S., instead of providing leadership and assistance, continues to search for enemies to rationalize its military expenditures, the world will be doomed to another century of folly and violence, except that now there are more people with more terrible weapons easily delivered anywhere. The September 11, 2001 attack on America may be the shocking event that forces the United States to build on the common ground with Russia and China.

We must trust the will and wisdom of the people. Let institutional investors, aided by the universities, respond to the people with the first workable secular plan in human history that can eliminate material scarcity worldwide, elevate spirits, unify people, and end the violence. Definition of this secular plan for unlimited social progress requires the collaboration of many people with time, energy and optimism. It requires people who can make the connections that validate the ideal and identify the means. Most of all it requires a profound optimism about the potential of the average person when provided with the proper circumstances.
Chapter 4

Needed: New Philosophers For A New Age

The dichotomy will be between "intellectuals" and "managers," the former concerned with words and ideas, the latter with people and work. To transcend this dichotomy in a new synthesis will be the central philosophical and educational challenge for the post-capitalist society.  

—Peter Drucker, 1993, age 83

Comprehensive philosophical and moral doctrines cannot be endorsed by citizens generally, and they also no longer can, if they ever could, serve as the professed basis of society.  

—John Rawls, 1993, age 72

Based on a lifetime of experience, celebrity author and consultant Peter Drucker sees society being transformed by the Information Age to a superior economic system in which workers are educated, involved, contributory, and rewarded as owners, in other words, democratic capitalism.

Based on a lifetime of study, celebrity author and philosophy professor John Rawls rejected any universal plan for social progress. Drucker proposed that progress will depend on how well the thinkers and doers collaborate on the analysis and the action plan. Rawls said it could not be done. This latter view is disappointing since Rawls, in 1971, had challenged the utilitarians with his concept of a society based on the rights and opportunities of each individual, including the


least advantaged. Phrased in terms of political philosophy, the early Rawls advocated the greatest individual development of all in a harmonious whole, in other words, democratic capitalism.

Drucker's wisdom and experience was drawn from many sources; his knowledge was multidisciplinary, his experience multi-faceted, his area all parts of the world. Rawls' wisdom was based mainly on single-discipline scholarship practiced inside a university. Drucker oriented social progress to a superior economic system. Rawls oriented it to a superior political arrangement.

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I share Drucker's optimism, but the new synthesis by new philosophers must not only define the means to realize the new opportunities but must also neutralize the damage from anti-idealists. What shall we call this new generation of philosophers? Noosphereans,\(^{96}\) Global Villagers,\(^{97}\) Digital Age philosophers, Information Age philosophers, Post-Post-Modernists, Neo-Idealists, Post-Capitalists? No matter what we call them, they will celebrate the new century and the new millennium, examining the convergence of philosophy, religion, science, economics, governance, and law.

The prophet of convergence, Teilhard de Chardin, was a Jesuit priest, scientist, (paleontologist), and philosopher of enormous optimism about humans and their potential. Decades before the advent of the microprocessor and the internet, Teilhard foresaw the world unified by new technology. Teilhard described the process: "Like the meridians as they approach the poles, science, philosophy and religion are bound to converge as they draw nearer to the whole."\(^{98}\) Teilhard coupled convergence of science, religion, and philosophy with the emergence of a vision of all people united by technology and spirit.

Emergence led to the Divine Milieu,\(^{99}\) a perfect world. It represented the fulfillment of human yearnings since antiquity, now enhanced with a new pragmatism. Teilhard described emergence:

To those who can use their eyes, nothing, not even at the summit of our being, can escape this flux any longer because it is only definable in increases of consciousness. The very act by which the fine edge of our minds penetrates the absolute is a phenomenon, as it were, of emergence.\(^{100}\)

What Teilhard foresaw is coming to pass in individual freedom for full development in a

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\(^{96}\) "Noosphere," coined by Teilhard de Chardin, means human structures and activities pervading the biosphere.

\(^{97}\) Marshall McLuhan (1911-1969), a professor at the University of Toronto and student of Teilhard de Chardin, used "Global Village" as the locale for unification of new technology and the human spirit.


\(^{100}\) Teilhard, The Phenomenon of Man, op. cit., p. 220.
harmonious whole that is both the means and the end in this newly practical philosophy. In a world rapidly becoming unified through computers and telecommunications, the forces for freedom and a better life are transcending the traditional power structures. The political abstraction of the sovereignty of the people is becoming a reality; the organization of human affairs is becoming more democratized.

As more and more of the world's citizens are touched by the unification phenomenon, Teilhard felt that they would then realize that they were not just "an erratic object in a disjointed world." On the contrary, Teilhard exclaimed:

I doubt whether there is a more decisive moment for a thinking being than when the scales fall from his eyes and he discovers that he is not an isolated unit lost in the cosmic solitudes, and realizes that a universal will to live converges and is hominized in him.\textsuperscript{101}

Teilhard's works were not published until after his death in 1955. The Catholic Church was not comfortable with his integration of evolution and creation, although Teilhard said that the integration would lead to a perfect secular world that would be at the same time the realization of the divine plan. Teilhard placed humanity in this context:

Man is not the centre of the Universe as once we thought in our simplicity, but something much more wonderful, the arrow pointing the way to the final unification of the world in terms of life. Man alone constitutes the last-born, the freshest, the most complicated, the most subtle of all the successive layers of life.\textsuperscript{102}

Teilhard's vision was similar to that of Condorcet who had summarized the work of the Enlightenment at the end of the eighteenth century (Chapter 3). They were both French, both

\textsuperscript{101} Ibid., p. 34.

\textsuperscript{102} Ibid., p. 224.
scientists, both shared an optimism about the potential of each person and of society in general. Condorcet penned much of his optimism while in a French prison getting ready to die during the Reign of Terror; Teilhard wrote much of his vision while banished from his beloved Paris to China because of his controversial views. Personal hardship could not suppress the joy of these two French philosophers in their sense of unity and the possibilities for the human species.

Condorcet's vision was partly realized through the improvement of millions of lives during the Industrial Revolution. Teilhard's vision has a better chance at fulfillment, for the Information Age Revolution will exceed the economic growth and productivity of the Industrial Revolution, and, beyond that, is itself a force for global unification. Both the Industrial Revolution and the Information Age Revolution added multiples of productivity that give to all the opportunity to live better. The benefits of the Industrial Revolution, however, were limited because the traditional power structures continued to dominate in their essentially feudal mode. Financial gains were made from the productivity of capital investment while foregoing the greater gains possible through investing in human capital. The command-and-control structure of government needed to fight wars was applied to commerce. The predatory nature of world imperialism among the Western powers was copied in the exploitation of workers. Capitalism was strong enough to improve lives, but it was an imperfect process that sustained the historical concentration of wealth, and it never approached the potential available through involving the people and sharing the improvement.

The Information Age revolution is based on cognitive power, not manual labor, and requires the full involvement of people. Investment in human capital is no longer a choice; it is a necessity. A company cannot compete without educated, independent-thinking, involved people. Peter Drucker provided the context for this transformation from ultra-capitalism to democratic capitalism:

"We are trying to straddle the fence, to maintain the traditional mind-set, in which capital is the key resource and the financier is the boss, while bribing knowledge workers to be content to remain employees by giving them bonuses and stock"
options. Bribing the knowledge workers on whom these industries depend will simply not work. The key knowledge workers in these businesses will surely continue to expect to share financially in the fruits of their labor. But the financial fruits are likely to take much longer to ripen, if they ripen at all. And then, probably within ten years or so, running a business with (short-term) "shareholder value" as its first, if not its only, goal and justification will have become counterproductive. Increasingly, performance in these new knowledge-based industries will come to depend on running the institution so as to attract, hold, and motivate knowledge workers. When this can no longer be done by satisfying knowledge workers' greed, as we are now trying to do, it will have to be done by satisfying their values, and by giving them social recognition and social power. It will have to be done by turning them from subordinates into fellow executives, and from employees, however well paid, into partners.  

In Drucker's extraordinary vision democratic capitalism will no longer be a choice, it will be mandated by competitive forces. Economic logic will prevail because commerce can no longer succeed by investing in physical capital only; capital must be invested to involve the people.

Teilhard was similarly excited about human potential, but whereas Marxism had pursued the goal through collectivism, Teilhard emphasized personal responsibility:

For whatever extraordinary solidarity we have with each other in our development ..., each of us forms, nonetheless, a natural unit charged with his own responsibilities ... It is we who save ourselves or lose ourselves.  

This individual development within a harmonious whole, with emphasis on personal responsibility, is the foundation of human affairs beginning in the individual person, reaching to the family, to the company, to the country, to the world.

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104 Teilhard, Divina Milieu, op. cit., p. 141.
The traditional power structure has impeded the spread of democratic capitalism during the past two centuries. Democratic capitalism grew by demonstrating its economic and social logic, but it has been a stunted progress with three steps forward, two back. Now, with the Information Age revolution, democratic capitalism is both an economic necessity and an influence toward unifying people. Teilhard knew that social progress needed such a focus:

Man will continue to work and to research so long as he is prompted by a passionate interest. Now this interest is entirely dependent on the conviction, strictly undemonstrable to science, that the universe has a direction and that it could, indeed, if we are faithful, it should, result in some sort of irreversible perfection. Hence comes belief in progress.

As soon as we try to put our dreams into practice, we realize that the problem remains indeterminate or even insoluble unless, with some partially super-rational intuition, we admit the convergent properties of the world we belong to. Hence, belief in unity.\textsuperscript{105}

This new age where people come together to improve the human condition deems disconnected with the reality of a world dominated by violence punctuated by the tragic event of September 11, 2001 and its aftermath. Social progress through unity, however, is still a pragmatic opportunity. By improving all lives democratic capitalism will gradually build a sense of interdependence and crowd out the memories of reciprocal atrocities.

\textsuperscript{105} Ibid., p. 284.
The world can then be sufficiently unified by economic common purpose to improve all lives and eliminate violence while simultaneously retaining all of its wonderful cultural diversity. The momentum will be self-perpetuating as more and more people are educated and lives continue to improve. Information Age technology makes it possible to reach every nation, every tribe, with educational materials, including the best practices for good health and the most productive techniques of agriculture. An extraordinary delivery system is now coming into place. An enormous library of knowledge, audio and visual, is available that needs only translation. The costs of this program are large but infinitesimally small when compared to continued misery, illiteracy, bad health, environmental damage, and war.

The Information Age transformation is presenting fresh opportunities for society. The vision was captured at mid-century by Teilhard and restated at the end of the century by Peter Drucker. Although human history has demonstrated both extraordinary progress and inexplicable failure, these visionaries have seen new opportunities emerging through a collaboration between the "thinkers" and the "managers." The optimism of the late-eighteenth-century Enlightenment to find the way to human progress through a scientific truth-searching process has survived two centuries of disappointment to be restated by new optimists in Enlightenment II, an improved opportunity through the Information Age transformation.

*The Twentieth Century: Celebrity philosophers abandon the search for a comprehensive secular doctrine.*

Many philosophers in the late twentieth century were depressed by the events of the twentieth century, both the record violence and the failures of top-down reform ideologies: Fascism, communism, and socialism. Many proclaimed that God is dead, idealism is abandoned, social progress is a pejorative term, traditional values are illusions, the only thing alive are nihilism, relativism and for many, despair.

Isaiah Berlin (1904-1998) Fellow of All Souls (Oxford), Fellow of New College, Professor of Social and Political Theory, and founding president of Wolfson College, won the Erasmus,
Lippincott, and Agnelli Prizes; as an exponent of the history of ideas, and as a defender of civil liberties, he received the Jerusalem Prize. In 1957, British Prime Minister Harold MacMillan recommended Berlin for knighthood for "talking." Although Berlin never wrote a book, he was a worldwide intellectual celebrity for his lectures and essays. He was also one of the leading intellectual quitters who proclaimed the Enlightenment to have been wrong, that there is no all-encompassing natural order, and that the search for it is a waste of time.

Berlin wrote:

> Utopias have their value. Nothing so wonderfully expands the imaginative horizons of human potential, but as guides to conduct they can prove literally fatal ... If one really believed that a single solution is possible, then surely no cost would be too high to obtain it; to make mankind just and happy and creative and harmonious forever, what could be too high a price for that? To make such an omelet, there is surely no limit to the number of eggs that should be broken. That was the fate of Lenin or Trotsky, of Mao and for all I know, of Pol Pot.¹⁰⁶

Berlin was following the consistent error of social commentators who begin with a top-down political arrangement, "the notion of the perfect state as the proper goal of our endeavors."¹⁰⁷ In this he was right, for these notions do not work, and do end up with a combination of state coercion, violence, and many broken eggs.

John Rawls, a Harvard professor of philosophy in the 1960s, published *A Theory of Justice*,¹⁰⁸ material that he had used for years in his courses. This book made Rawls one of America's leading philosophers, a response that took the author by surprise. Over two hundred thousand copies of the book have been sold in the United States, and it has been translated into 23 languages. Some five thousand books and articles have been written that deal with Rawls'

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¹⁰⁷ Ibid.

¹⁰⁸ *op. cit.*
theories in whole or in part.

Twenty-two years later, Rawls wrote *Political Liberalism* in which he shared Berlin's explicit rejection of the Enlightenment's view that a process of scientific reasoning could discover the best order for human governance:

> Whether there is or ever was such an Enlightenment project (finding a philosophical secular doctrine, one founded on reason and yet comprehensive), we need not consider it; for in any case political liberalism, as I think of it, and justice, as fairness as a form thereof, has no such ambitions.\(^{109}\)

The conclusion of Berlin and Rawls, that it is impossible to organize human affairs rationally is a reaction to the failure of alternative political systems. Their intellectual fatigue resulted from the collective failure to perfect society by an elite design: it did not work; *ergo*, it cannot be done. The alternative, that it did not work because the structure was wrong and untrained leaders made huge mistakes, they apparently did not consider. Many intellectuals suffer from a profound ignorance of ordinary people, of their potential, and of what organization is appropriate to encourage them to reach their potential. Philosophers like Berlin and Rawls approached the problem from the wrong end, and came to a wrong conclusion.

Berlin, Rawls, and many others thus recommended that the search for a common ideology be terminated and replaced with *pluralism*, defined by Berlin as "the conception that there are many different ends that men may seek and still be fully rational ... our values are ours, and theirs are theirs."\(^{110}\)

Berlin, Rawls and others who reject a common ideology that can unite and elevate, think in terms of a political order. Politicians are interested in politics, philosophy professors are interested in philosophy. Philosophers need an epiphany to see that the answer lies in the economic, not the


political, system, and that cultural reform will emulate democratic capitalism. It is this superior economic system that is the solution to the mystery of human progress. New politicians, motivated and instructed by new philosophers, can then lead the way.

The intellectual default of the left at the time of Marx and Mill was caused by the same factors that are now causing the default of those like Berlin and Rawls, who abandon the search for social progress because of insufficient understanding of democratic capitalism and its potential. Paradoxically, this failure lies in the epistemological process of the philosophers. Many who have dedicated their life to philosophy start, however, by rejecting knowledge as the power for social benefit with reasons that are inherently anti-intellectual. The humanists do not understand that the bridge to science is first to copy the truth-searching process. The humanists also tend not to be multi-disciplinary in their scholarship, and they habitually communicate and debate only with those who share their scholarly background. While many liberal-arts professors are suspicious of the sciences, almost all of them are contemptuous of capitalism. If, as proposed, democratic capitalism is the "single solution," it does not get scrutiny, both because "single solutions" in general are rejected and because any form of capitalism as "a single solution" would be regarded as not worth consideration.

Despite Berlin's rejection of utopian visions, he came close to defining common purpose, for he described the universal goals that transcend all cultures:

All men sought the satisfaction of basic physical and biological needs, such as food, shelter, security, and also peace, happiness, justice, the harmonious development of their natural faculties, truth, and somewhat more vaguely, virtue, and moral perfection.111

Berlin also understood that the urge to eliminate impediments to reach these goals was inherent in the human spirit:

111 Berlin, op. cit., p. 245.
The conviction that once the last obstacles, ignorance and irrationality, alienation and exploitation, and their individual and social roots, have been eliminated, true human history, that is universal harmonious cooperation, will at last begin in a secular form of what is evidently a permanent need of mankind.\textsuperscript{112}

Berlin described specific human needs and the human urge to attain them. While rejecting utopia, Berlin summarized a structure capable of attaining utopia:

> It would follow that the creation of a social structure that would, at the least, avoid morally intolerable alternatives, and at the most promote active solidarity in the pursuit of common objectives, may be the best that human beings can be expected to achieve, if too many varieties of positive action are not to be repressed, too many equally valid human goals are not to be frustrated.\textsuperscript{113}

The early Berlin thus had described the human need for a common ideology as well as its specific goals. The goals were all products of an economic system that would have to be honest and fair in order not to offend many cultural values. Berlin had stepped up to the door marked "democratic capitalism." He failed to knock and enter because he had neither understanding nor interest in economics.

Berlin later described his epiphany that "shocked his earlier faith" when he discovered that the Machiavellian view of "a ruling class of brave, resourceful, intelligent, gifted men" who knew how to seize opportunities and use them, is incompatible with "Christian virtues of humility, acceptance of suffering, unworldliness, and the hope for salvation in an after life."\textsuperscript{114} Berlin was correct, for these two are incompatible, but why did he treat them as the only alternatives? Berlin concluded from this limited examination "that not all the supreme values pursued by


\textsuperscript{113} \textit{Ibid.}

mankind now and in the past were necessarily compatible with one another.\textsuperscript{115}

Berlin concluded that the universal human aspirations for food, clothing, shelter, security, happiness, morality, and justice for all, could not be attained by either the Machiavellian philosophy or Christian secular passivity. They could be attained, however, through a system that couples brave, resourceful, intelligent people with Christian and other religions' virtues of honesty and compassion.

Before he declared defeat and retired from the field, in Rawls' earlier work he validated the concept of social idealism when he proposed a comprehensive doctrine for a just society based on two principles:

First: Each person is to have an equal right to the most extensive scheme of equal basic liberties compatible with a similar scheme of liberties for others.\textsuperscript{116}

His first principle was basically a restatement of the social ideal "life, liberty and the pursuit of happiness" according to the American Declaration of Independence. Rawls, like Berlin, came close to identifying "democratic capitalism" as the common ideology for social justice.

Rawls' second principle proposed that inequalities of wealth and authority are just only when they are part of a structure that provides benefits to the most disadvantaged: Social and economic inequalities are to be arranged so that they are reasonably expected to be to everyone's advantage, and attached to positions and offices open to all.\textsuperscript{117}

Rawls was proposing that the structure provide for a meritocracy of talent and virtue that also elevates the least advantaged. However, instead of greedy and individualistic meritocracy, Rawls described individual development of all in a harmonious whole, the fundamental

\textsuperscript{115} Ibid.

\textsuperscript{116} Ibid.

\textsuperscript{117} Rawls, Political Liberalism, op. cit., p. 53.
governance principle of democratic capitalism.

Rawls' second principle calls attention to how well the weakest link can be motivated and trained. A structure to encourage the greatest self-development of the least advantaged through education, training, and motivation, would lead to a comprehensive plan for the greatest development of all.

Ultra-capitalism, with CEO's annual compensation in the tens and hundreds of millions of dollars, could not pass Rawls' second principle. Such compensation could not be rationalized as necessary for the benefit of the least advantaged, and in fact it damages the harmonious environment in which the least advantaged could prosper.

Rawls' second principle is not merely abstract theory. If it were a guiding principle of American political life, we would recognize the large overdue obligation to millions of youths who have not been given the minimum benefits of education, training, and motivation. Many end up on account of minor drug charges as part of the growing prison population. Why Rawls abandoned the search for a common ideology is not clear. Perhaps with his orientation to political solutions, he was discouraged by how thoroughly special interests contaminated the democratic political process.

Throughout the second half of the twentieth century, philosophic relativism has eroded the search for any common ideology. Moral relativism rejects any moral value as universal; epistemological relativity rejects the integrity of knowledge; metaphysical relativism even rejects reality as objective. Instead of using relativism as part of the epistemological process, some have treated it as a final answer.

Engineers will remind us that everything has a tolerance, and there are no absolutes. Social progress, however, requires only improvement, not perfection, in applying the few rules based on individual freedom and reciprocity among people. This universality is demonstrated by the similarity among the few rules that are derived from three different points of view: The natural
order based on innate human characteristics, a rational order designed and tested by human reason, and the plan for secular perfection common to most religions.

The search for a "comprehensive philosophical doctrine," as Berlin and Rawls called it, had gone through four phases and at the turn of the twenty-first century it was entering a fifth. The first phase in Western civilization until the Middle Ages was theological domination. Next the pendulum then swung too far to confidence in human reason exclusively. The third phase was a recognition by some that truth-searching is an imperfect process best pursued through contributions from multiple sources: Reason, experience, tradition, and faith. The Post-Modern phase was a rejection of the mission, believing that there is no way to reach the illusory secular goal. The fifth phase, emerging in the new century, is a convergence of the sciences, humanities, economics, business, law, philosophy, and religion. Drawing on a full range of knowledge, properly organized, new philosophers can define how the growth, productivity, and unifying influence of the Information Age in a more democratic world can improve all lives and stop the violence.

The architecture of knowledge of these new philosophers will have to be both broad and deep: Broad in that all disciplines must be represented in order to find a holistic plan for human betterment, deep because the failure thus far of the best thinkers in history demonstrates how elusive the solutions are. More thinkers, more cooperation, and more interactions are needed to explain why society still functions at a fraction of its potential, and what steps are necessary to attain full potential.

The following historical references are part of an understanding of why folly and violence, not peace and plenty, have dominated human history.

*For over four thousand years, force has dominated reason in the relations among nations.*

Hammurabi (2113-2081 B.C.) was at first a successful warrior who brought order out of the incessant local warfare in lower Mesopotamia. He then drew up 285 laws and inscribed them in
a public place for participation by all. When order had replaced violence and society was based on justice under law, Hammurabi then addressed the general welfare by investing in infrastructure, both human and physical. He dug canals, stored grain against famines, lent money at no interest to stimulate commerce, and prevented exploitation of the weak by the strong. Broad wealth distribution and better education improved the standard of living and stimulated momentum in all branches of knowledge:

No one looking at the site of ancient Babylon would suspect that the hot and dreary wastes along the Euphrates were once the rich and powerful capital of a civilization that almost created astronomy, added richly to the progress of medicine, established the science of language, prepared the first great code of law, taught the Greeks the rudiments of mathematics, physics, and philosophy, gave the Jews the mythology which they gave to the world, and passed on to the Arabs part of that scientific and architectural lore with which they aroused the dormant soul of medieval Europe.\(^\text{118}\)

This exemplary society lasted only a short time. Eight years after Hammurabi's death, Babylon was invaded and pillaged by the Kassites, a tribe of mountaineers from the northeast border. These invaders, probably European immigrants, conquered and ruled in ethnic and political chaos for centuries. Society had advanced quickly, but it was brought back to barbarism even more quickly. Over the four thousand years since, benevolent governments and the rule of law have been repeatedly destroyed or displaced by predatory forces.

The only way that predatory actions can be contained is through cooperative force by other nations. For some such as xenophobic American politicians, however, cooperation implies an intrusion into "national sovereignty" and is therefore rejected. In other words, the containment of violence remained unresolved early in the twenty-first century. The attack on America illuminated for many that unilateral actions are regarded as an arrogant use of power, in contrast to cooperative action through an improved U.N.

500 BC: Confucius presented a template for the proper organization of human affairs.

Confucius, (552-479 B.C.) a humanist searching for ways to benefit the general welfare, provided the world with a template for the organization of secular life. The elements of the template were few and simple. They included the worth of each individual, self-development in a harmonious whole, broad educational opportunities, civic order in the state, moral discipline in the individual and family, equality of opportunity, broad wealth distribution, meritocracy in the selection of leaders, and an end to violence.

Confucius grew up in the state of Lu, part of modern Shantung. He came from a noble family, but his father died when Confucius was three, so he grew up in poverty. "I was of humble station when young, that is why I am skilled in menial things." He worked first as a tax collector and started a lifetime of study of the causes of poverty and oppression. His government career included: Master of Crime (Police Commissioner), Assistant Superintendent of Public Works, and Chief Magistrate. A renowned public servant and idolized by the people, he nevertheless grew tired of public service, left office, and spent thirteen years travelling China with his students.

As a scholar, Confucius had learned of cultures that changed from a tribal society, over which the influence of spiritual beings was almost total, to a secular society, in which human ingenuity was challenged to build a better life. Confucius adopted and passed on the view that human destiny is dependent on one's own good works and thoughtful action.

As a boy and a man, Confucius studied the old master, Lao-Tze, who long before had written a book in two parts, "the Tao and the Te." Confucius had learned that Tao, the way of the universe, and Te, the way of life, are one. Human life in its essentially two-some yin and yang is part of the rhythm of the world. In that cosmic Tao, all the laws of nature form together the substance of reality. As Aristotle, would later do, Confucius began by studying the nature of

Confucius' early humanist code was directed to individual self-development, but he also integrated recognition of a supreme being, "It wasn't until I was fifty that I understood Tien Ming, the decree of Heaven, one of the things a gentleman stands in awe of." Modern religion and humanism have engaged in a lengthy cold war, each perceiving in the other threats to its theology. Confucius ignored whether the supreme being were a creator, the ultimate truth, or society's goal; he focused instead on the common means that illuminate "the way" to temporal happiness. Beyond that, Confucius cautioned his students not ask about the spirits when they did not even understand life.

In the Book of Great Learning, Confucius's students passed on his blueprint for temporal society, basing state and world order on the family unit and on the individual's effort to find knowledge through a rigorous thought-process based on personal integrity:

The ancients who wished to manifest their clear character to the world would first bring order to their states. Those who wished to bring order to their states would first regulate their families. Those who wished to regulate their families would first cultivate their personal lives. Those who wished to cultivate their personal lives would first rectify their minds. Those who wished to rectify their minds would first make their wills sincere. Those who wished to make their wills sincere would first extend their knowledge. The extension of knowledge consists in the investigation of things. When things are investigated, knowledge is extended; when knowledge is extended, the will becomes sincere; when the will is sincere, the mind is rectified; when the mind is rectified, the personal life is cultivated; when the personal life is cultivated, the family will be regulated; when the family is regulated, the state will be in order; and when the state is in order there will be peace through the world. From the Son of Heaven down to the common people, all must regard cultivation of the personal life as the root or

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120 Ibid., p. 29.
During a lifetime of teaching and learning, Confucius had outlined this common philosophy of meritocratic governance based on individual development within a harmonious whole. However, Confucius specifically addressed the two greatest impediments to social progress: Concentration of wealth and violence among nations. Confucius proposed broad wealth distribution as fundamental to social harmony.

The centralization of wealth is the way to scatter the people, and letting it be scattered among them is the way to collect the people. They produce wealth, disliking that it should be thrown away on the ground, but not wishing to keep it for their own gratification. Disliking idleness, they labor but not alone with a view for their advantage. In this way, selfish schemes are repressed and find no way to arise, robbers, filchers and rebellious traitors do not exist.

Confucius also knew that a world of law, not violence, begins with trained and virtuous leaders. He was realistic that the elimination of violence would be a long process.

When the great principle prevails, when the world becomes a republic, they elect men of talents, virtue, and ability; they talk of sincere agreement and cultivate universal peace. After a state has been ruled for a hundred years by good men, it is possible to get the better of cruelty and do away with the killing.
Chinese philosophers had no confusion about war. Mencius (371-289 B.C.), one of Confucius' interpreters, denounced war as a crime against humanity. "There are men who say `I am skillful at marshalling troops, I am skillful at completing a battle.' They are great criminals, there never has been a good war."¹²⁶ A prophet of universal love, Mencius marveled that a thief who steals a pig is condemned and punished, while an emperor who invades and appropriates a kingdom, enslaving the citizens, is called a hero and made a model to posterity.

The Chinese philosophers over two millennia ago put war into proper context as a scandal and embarrassment to the human race. It kills, and maims people, and does severe economic damage. One of the greatest dangers to realizing the benefits of global democratic capitalism is war. War is a failure of leadership, mistakes made by a few poorly trained men. War will be eliminated, according to Confucius, only after men and women "of talents, virtue, and ability talk of sincere agreement and cultivate universal peace."¹²⁷

350 BC: Aristotle defined the process by which the study of the nature of things would indicate their full potential and the circumstances required to attain it.

Young Aristotle (384-322 BC) came to Athens in 367 BC to study with Plato, then in his sixties, for the next twenty years. Aristotle was a model for the Enlightenment process as he used systematic truth-searching, which he called "logic," to understand the nature of things, which he called "physics," to understand the principles of social association, which he called "ethics."¹²⁸

Aristotle's lifetime of scientific investigations came naturally to him because his father was a doctor. Among his many disciplines Aristotle was a biologist who searched in every growing process for its essence, purpose, or end, believing that an understanding of the growth potential was prerequisite to identifying the circumstances necessary for its attainment. With the right circumstances the process would result in the perfect plant from the best nutrition, and the animal

¹²⁶ Durant, op. cit., p. 685.
¹²⁷ Ibid., p. 673.
reaching potential excellence in its body and limited associative skills. Humans reach full potential, according to Aristotle, when they achieved excellence in mind, body, and extensive associative skills.

Aristotle defined the terms and integrated logic, physics, and ethics in the process that could find the best organization of human affairs, and the necessary circumstances for each and all to reach full potential. This challenge that Aristotle accepted was the same challenge taken up by the Enlightenment of the eighteenth century, and it is the contemporary challenge before Enlightenment II. The challenge is a three-part responsibility: First, for humans to use their reason to define their full potential individually and collectively; secondly, for humans to use their reason to define the requisite circumstances and impediments to be eliminated; thirdly, for the thinkers and managers to cooperate in reforming the circumstances needed to move toward the ideal. The ultimate good for the human species is still pending the successful application of this process.

Aristotle had the multi-disciplinary knowledge to define the political structure that could allow the humans to reach their potential. In his effort to find the best, Aristotle's examinations included a study of 158 constitutions. The quality of Aristotle's truth-searching was, however, compromised by the realities of violence among nations and states and by slavery as the mode of production. For example, Aristotle's pupil Alexander the Great was considered "great" for his ability to invade and subjugate whole nations killing, raping and pillaging in the process. Although Aristotle freed his slaves in his will, he defended slavery as a proper institution to be supported by the state.

Aristotle returned to Athens in 335 BC and set up his Lyceum near Plato's Academy, dedicated to the examination of nature. Aristotle specifically rejected all three of Plato's waves of reform: Women with equal rights for leadership, dissolution of the family unit in favor of the state, and centralized government by guardians directed by philosophers. Aristotle believed that the emancipation of women was too radical to work. He believed in the family and did not believe that the state could properly raise children. Aristotle's state structure rejected the oligarchy of the
rich and the democracy of the poor, believing that government controlled by extremes would be unable to serve the general welfare. Aristotle favored a state managed by the middle class who, whether through ability or good fortune, had been given the most conducive circumstances for their development, and were people most likely to extend to others the opportunities from those circumstances. Aristotle designed a structure that prevented concentration of power from either the political right or left, that would leave the state in the control of the "special interests."

Aristotle described the process and state structure through which the human species could reach potential but his society could not provide the circumstances. Slavery, concentrated wealth, oppression of women and violence among nations were all so institutionalized in Aristotle's society that humans were able to reach only a fraction of their potential. Socrates, in Plato's Republic, had rejected, in theory, the "might is right" theory of government but in practice, the predatory society had the momentum of history and economic motivation on its side.

Aristotle in Politics129 described the association of people in a state structure that would provide the circumstances allowing each to reach full potential. In Ethics, Aristotle described how the individual could seek excellence both in personal talents and in social cooperation. In this goal of individual development in a harmonious whole, Aristotle proposed four primary elements: Courage, temperance, justice, and practical reason. In each case, Aristotle emphasized that it was practical intelligence, wisdom, or "street smarts," that was crucial to moderating the extremes of the other three attributes. Courage was a virtue, except when rash or foolish; temperance was a virtue in the enjoyment of pleasures, but not in excess, justice was the obligation to give each their due, but that elusive goal could be met only when wisdom defined the "golden mean."

Aristotle, "the philosopher of common sense," likened the pursuit of excellence to learning how to play the flute. In both cases, it takes training and practice and the first effort will inevitably prove inexpert. This seems obvious except in contemporary society, where do young people train and practice making their contributions to a harmonious whole?

129 Ibid.
1250 AD: Thomas Aquinas attempted to combine knowledge from faith and reason.

Thomas Aquinas (1225-1274) undertook the task of integrating knowledge from many cultures drawing on Jewish and Muslim philosophers as well as Christian. The common denominators of these philosophers were prodigious work covering the multi-disciplinary spectrum of science, humanities, medicine, philosophy and religion with profound study of Aristotle referred to as "The Philosopher." Included in this assimilation were the works of Muslim philosopher Avicenna (Abu Ali al-Husein ibn Sina) (980-1037 AD), Muslim philosopher Averröes (Abu al-Walid Muhammad ibn Rusho) (1126-1198 AD), and Jewish philosopher Maimonides (1135-1204 AD).

Avicenna, who lived in what is now Iran and Iraq, wrote over 100 books, including medical texts that were used in Europe for the next 500 years. Averröes was also a renowned physician and author of a medical text in Latin. Like his father and grandfather before him, Averröes was also the Chief Justice of Cordoba, Spain. He was known as the "Commentator" for his knowledge of Aristotle, as he had been commissioned by the Emir to write a clear exposition of Aristotle's works.

Maimonides, called Moses, was born nine years after Averröes in Cordoba, also the son of a scholar, physician and judge. Maimonides and his family left Spain after the invading Berbers demanded that all convert to Islam. Maimonides later became a famous rabbi and a scholar in biblical and rabbinical literature, medicine, mathematics, astronomy, and philosophy. As Aquinas would attempt to do a century later, Maimonides attempted to reconcile Greek philosophy with religious dogma and provoked a battle among Jews between strict orthodoxy and philosophy similar to battles among the Christians and Muslims. Violence and book burning in this struggle was common to all religions.

These philosophers of the eleventh to thirteenth centuries were pioneering the bridging of their faiths and reason. Harmonizing the beliefs of Aristotle with the revealed truths of their religions
was challenging as most religions believed that the world was created and the soul immortal, while Aristotle believed the opposite. It is not surprising that the works of these thinkers, and Aquinas after them, were attacked, but they were eventually accepted by that part of religious communities concerned with the temporal human condition who recognized that there was little contradiction between the advice of religion about secular conduct and the Aristotelian process. The necessity in all cases was to determine the nature of things, animals, and humans; to determine the limits of the growing process; and then to identify the circumstances that would allow growth to full potential. The circumstances included, for example, visions of brotherly and sisterly love and unity of purpose that were both religious and philosophical.

Aquinas made a major contribution by packaging the illuminations from so many brilliant people from so many different cultures. It was a good start in bridging faith and reason, a task still as important and still not complete. Aquinas’ *Summa* helped free the minds to be applied to improving the human condition but it was still too early to propose individual autonomy and economic freedom for all. Sixteen hundred years after Aristotle, Aquinas repeated the defense of slavery as a proper institution deserving support from the establishment, the subservience of women, accepted violence among nations, but added death for heresy to the list of barbaric practices.

*Early-Seventeenth Century: French and English philosophers pursue human betterment through the power of knowledge.*

Rene Descartes (1596-1650), French mathematician and philosopher, and Francis Bacon (1561-1626), English statesman and philosopher, shared the mission of applying the power of knowledge to improving the human condition. Descartes and Bacon felt that the material then presented by the educational system was confused, and the process by which it was attained was badly flawed. Having restated their belief in the ideal of social progress, both men recommended ways to improve the process.

Rene Descartes was the son of a prosperous lawyer, educated by the Jesuits, studied and traveled
in many parts of Europe. In 1628, he moved to Holland where he spent most of his life but died in Sweden where he had gone to be tutor to the Queen.

Descartes was part of the freeing of the mind from theological domination at the same time that his work was inhibited by the authority of the church. Many were revolting against the Aristotelian-Scholastic curriculum arrived at by a confusion of reason and ecclesiastical authority. The assimilation done several centuries earlier by Aquinas had been used primarily for the education of clerics, now it was being attacked by reformers and skeptics.

Recognition that truth is not certain and that the process is relative and subjective, was as old as philosophy itself, but now the church used the skeptics to support their authority with the argument that if truth could not be reliably ascertained by reason then it had to be provided by faith.

Descartes tried to improve on both Plato and Aristotle with extensive efforts in both metaphysics, including proofs of the existence of God, and physics, with investigations into an amazing variety of things, including crop failures, refraction in optics, and the effect of altitude on atmospheric pressure. Descartes' contemporary, English philosopher Thomas Hobbes, thought that Descartes should have stuck to physics as his metaphysics were confused by the separation of mind and body.

Descartes undertook to build an architecture for finding truth and accumulating knowledge in the belief that great benefits would accrue to society from humans' becoming "the masters and professors of nature." Nevertheless he straddled science and religion by affirming that reason "does not prevent us from believing matters that have been divinely revealed as being more certain than our surest knowledge."

Like Descartes, Galileo (1564-1642) also affirmed fidelity to the authority of the church, but his material on the validity of the Copernican theory was so thorough and convincing that he was condemned in 1628 and spent the rest of his life under house arrest. When Descartes became
aware of this he hid a major work from publication until after his death.\textsuperscript{130}

Descartes proceeded to outline a structure for truth-searching accompanied by moral maxims to live by. His \textit{Discourse on Method} includes "accepting nothing as true which I did not clearly recognize to be so," "to divide up each of the difficulties that I examined into as many parts as possible," "to carry on my reflections in due order," meaning to conquer the simple, then to move on to the more difficult, a building-block technique, and "to make examinations so complete and reviews so general that I should be certain of having omitted nothing."\textsuperscript{131}

Although Descartes is still criticized as the father of rationalism, that is, the belief in reason as the exclusive source of knowledge, he started his search for truth on values dependent on not only reason but on experience and tradition.

Before commencing to rebuild the house which we inhabit, to pull it down and provide materials and an architect, unless we have also provided ourselves with some other house where we can be comfortably lodged during the time of rebuilding, so in order that I should not remain irresolute in my actions while reason obliged me to be so in my judgments, and that I might not omit to carry on my life as happily as I could, I formed for myself a code of morals for the time being, which did not consist of more than three or four maxims, which maxims I should like to enumerate to you.

Among Descartes' maxims was "to obey the laws and customs of my country, adhering constantly to the religion in which by God's grace I had been instructed since my childhood."\textsuperscript{132}

Descartes is most famous for, "I think, therefore, I am," however, his dedication was more truth-searching than skeptical.


\textsuperscript{131} \textit{Ibid.}, p. 16, 19, 20.

\textsuperscript{132} \textit{Ibid.}, p. 18.
I did not wish to imitate the skeptics who doubted only for the sake of doubting, and intended to remain always irresolute. On the contrary, my whole purpose was to achieve greater certainty and to reject the loose earth and sand in favor of rock and clay.  

Descartes combined in his career the work of a mathematician, philosopher, and teacher. Englishman Francis Bacon was a philosopher, lawyer and politician. He worked for years on the Great Instauration, his statement on how to renew and restore the method for accumulating knowledge. In 1620, Bacon published Novum Organum, featuring his new experimental method of confirming truth. Bacon, the humanist and author, pursued a busy career and became a member of Parliament in 1584. Between 1607 and 1618, he held successively higher positions up to Lord Chancellor, but he was then disgraced and exiled from the court by his political enemies who charged him with a conflict of interest in his acceptance of gifts.

Bacon faulted education both for the process and the content arguing that its mission was not the improvement of society through intelligent leadership or informed citizenry. His Novum Organon was a direct attack on the educational establishment in which Aristotle's Organon was a standard text. The curriculum that reached back centuries was directed to clerical education, and Bacon thought that it mixed religion and reason to the confusion of both. As a result, university work was increasingly irrelevant for the rapidly growing population of young men in training for politics and commerce.

While Bacon's attack was on the Aristotelian curriculum as interpreted in seventeenth-century Scholasticism, his influence was in fact a return to a more authentically Aristotelian investigation of things in search of the essence, the growth potential, the favorable circumstances, and the impediments. Bacon agreed with the inductive approach of learning from experience, testing the resulting generalizations, and then moving onto higher levels of generalization. Bacon accommodated relativity and subjectivity in truth-seeking, by building a process that was

133 Ibid.
**dynamic, collaborative, and cumulative:** Dynamic because it was a reiterative process that was constantly modified by new or improved knowledge; collaborative because it required representatives from all scholarly disciplines and diverse cultures; cumulative because it was a building-block process in which each verified block provided a new level on which to build new knowledge.

Bacon attacked superficiality in the thought process:

The primary notions of things which the mind readily and passively imbibes, stores up and accumulates, are false, confused, and over-hastily abstracted from the facts ... whence it follows that the entire fabric of human reason which we employ in the inquisition of nature, is badly put together and built up, like some magnificent structure without any foundation.\(^{134}\)

Let him correct by seasonable patience and due delay the depraved and deep-rooted habits of his mind; and when all this is done and he has begun to be his own master, let him use his own judgment.\(^{135}\)

Bacon presented two books of *Aphorisms Concerning the Interpretation of Nature* and *The Kingdom of Man*. The first book contained over 100 aphorisms, many of them still relevant for contemporary philosophers. Bacon insisted, for example, that the end must be clear before defining the means.\(^{136}\)

It is not possible to run the course right when the goal itself has not been rightly placed.\(^{137}\)

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\(^{135}\) Ibid., p. 27.

\(^{136}\) Ibid., Aphorism, lxxxi, p. 56.

\(^{137}\) Ibid., Aphorism, lxxxi, p. 57.
Bacon, who warned against excessive abstract theory, was the intellectual ancestor of David Hume in anchoring reason to what works in practice:

Roads to human power and to human knowledge lie close together, and are nearly the same, nevertheless, on account of the pernicious and inveterate habit of dwelling on abstractions, it is safer to begin and raise the sciences from those foundations which have relation to practice and let the active part itself be as the seal which prints and determines the contemplative counterpart.\textsuperscript{138}

For Bacon, the final step in the process was experimental verification, "a course of experiment orderly conducted and well built up."\textsuperscript{139}

Bacon's repeated theme was that the ability of the human species to maximize opportunities is dependent on the quality of the knowledge. Bacon emphasized the axiom that errors of knowledge will lead to mistakes in operation. The process fails again when mistakes in operation lead to new theory instead of a search for the original error. When the original theory was superficial and poorly thought out, feedback from the inevitable mistakes in operation analyzed in a similarly faulty process, then leads to additional faulty theory.

Bacon reasoned from nature in order to find appropriate rules for human action:

Human knowledge and human power meet in one; for where the cause is not known, the effect cannot be produced. Nature to be commanded must be obeyed, and that which in contemplation is as the cause is in operation as the rule.\textsuperscript{140}

Between Descartes and Bacon, an architecture for the development, organization, and validation of knowledge, started long before by Aristotle, was refined. Like truth itself, the architecture had

\textsuperscript{138} Ibid., Second book, \textit{Aphorism} iv, p. 89.

\textsuperscript{139} Ibid., \textit{Aphorism} lxxxii, p. 57.

\textsuperscript{140} Ibid., \textit{Aphorism} iii, p. 28.
to be constantly analyzed and refined. The process had worked well in the sciences, but it has had only partial success in the governance of human affairs, where reason has had to battle traditional domination by predatory forces and autocratic rule.

After Descartes and Bacon, Western intellectual development followed two imprecise paths, one in the Greek tradition, where rational contemplation of the ultimate truth of things is "the highest attainment," the other in the Roman tradition, where the practical aspects of human existence are "a larger and more significant whole in relation to whole ends. Our philosophic apprehensions should be viewed as subordinate though still very valuable means." This difference could also be summarized, with a large tolerance for error, as the difference between the continental rationalists, such as Descartes, and the English empiricists, such as Bacon, Hobbes, and Locke.

_Eighteenth Century: The Enlightenment uses the systematic thought process of Aristotle, Descartes, and Bacon to define the means for the best organization for human affairs._

The meritocracy of Confucius did not exist in Western culture. In Aristotle's society the mode of production was slave-based, in Aquinas' it was serfdom. Until the eighteenth century, Western society remained largely static with little opportunity for either freedom or mobility for the majority. Many people were persecuted or killed for religious beliefs, many were imprisoned for writing what they believed to be true.

All of this began to change during the life of Francois Marie Arouet Voltaire (1694-1778) and his protégé Condorcet. Voltaire energized the intellectual movement in Europe toward the freedom to think and to act. In his *Tenth Stage* (see Chapter 3), Condorcet summarized the just society as defined by the Enlightenment.

The son of an affluent family, Voltaire studied with sons of the nobility at the Jesuit College in

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142 Ibid.
Paris. Soon after, Voltaire began his attacks in plays, prose, and poems and he came under constant surveillance and threat. François Marie Arouet was not known as Voltaire until his first time in the Bastille in 1718. After another episode, instead of the Bastille, Voltaire was banished to England in 1726. During his three years in England, Voltaire refined his social philosophy and broadened his knowledge through study of John Locke's empiricism and theory of inalienable rights for all, and of Newton's extraordinary contributions to science. The relative freedom of individuals under the English constitutional monarchy impressed Voltaire, as did the growing affluence resulting from the early stages of the Industrial Revolution. In England at that time, commerce was respected, not demeaned, by a growing middle class and even some of the nobility.

Voltaire returned to the Continent with a broadened understanding of potential social progress based on the integration of scientific advances, individual freedom, economic freedom, and political freedom. In combination, these seemed to be the circumstances that gave promise for humans to reach their potential. The progress that Voltaire observed in England was relative, as wealth in England was still concentrated and the workers crowded into the cities in poor living conditions not as good as some French serfs. Voltaire later broadened his knowledge and experience with several years living at the court of Frederick William II, King of Prussia with whom Voltaire had a difficult relationship for over forty years.

Voltaire and others of the Enlightenment in their wide-ranging curiosity discovered the Chinese culture and Confucius. Voltaire developed a great respect for the philosophy and structure of China and wrote extensively about their society. He called China: "the finest, the most ancient, the most extensive, the most populous and well-regulated kingdom on earth."¹⁴³ Although much of the knowledge of the Chinese came by way of the Jesuits, the Enlightenment presented the Confucian ethic as a moral code for secular society developed from reason and experience.

Most thinkers of the French Enlightenment, conditioned by their antagonism towards the oppressive church-state structure, were either deists or atheists. Others, like the German

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Immanuel Kant, however, saw commonality between the morality developed for the secular existence from reason and that derived from religion. Kant felt that reason and religion were complementary, not competitive.  

The Enlightenment's most ambitious production was *The Encyclopédie*, an enormous effort to capture and codify all knowledge. While many made contributions, the two who worked the longest and the hardest under constant harassment were Denis Diderot (1713-1784) and Jean Le Rone d'Alembert (1717-1783). Diderot came from a middle-class family and studied at the Jesuit College in Paris. He gave up early thoughts of being a priest and chose the life of a thinker and writer. D'Alembert was abandoned as an infant, raised by a step-mother, and studied at the University of Paris. He also dedicated his life to intellectual pursuits, usually living in poverty. A scientist, he did important work in mathematics and calculus; his d'Alembert Principle" became a well-known theorem helpful in mechanical calculations. Most of the Enlightenment, including Voltaire, were scientists or involved in scientific investigations. They followed the Aristotelian tradition of studying the nature of things, a discipline that they then carried over into the analysis of society. From an understanding of the nature and potential of any growing process, they could then identify the circumstances necessary for an organism to reach its full potential, including the human species.

The French authors of *The Encyclopédie* honored those from whose intellectual momentum they derived courage and information. D'Alembert, for example, observed: "At the head of these illustrious personages should be placed the immortal Chancellor of England, Francis Bacon, whose works, so justly esteemed deserve our study even more than our praise."  

D'Alembert and Diderot were in regular communication with Voltaire and well schooled in Newton's scientific advances beyond those of Descartes, who, they felt, had been hampered by religious persecution or, at least, critical attention. D'Alembert nevertheless described the movement toward freedom stimulated by Descartes, who dared to show to alert mines how to

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free themselves from the yoke of Scholasticism, opinion, authority, in a word, from prejudice and barbarism, and by this revolt, of which we today gather the fruits he rendered to philosophy a service perhaps more difficult than all those that it owes to his renowned successors.\textsuperscript{146}

Claude Adrien Helvétius (1715-1771) was one of twenty children of a physician to the king and queen of France, a connection that later kept Helvétius out of prison. Helvétius studied with the Jesuits and, inspired by Voltaire whom he met shortly after college, dedicated his life to study and writing. Helvétius spent many years at home with his family writing \textit{De l'Espirit} (On Intelligence). The men of the Enlightenment were well versed in economics and included material on the Phisiocrats and \textit{laissez-faire} theory in the \textit{Encyclopédie}. Helvétius was part of the\textsuperscript{111} Enlightenment but was also a wealthy man, who wrote with special authority on the persistent impediment of concentrated wealth:

\begin{quote}
The almost universal unhappiness of men and nations arises from the imperfections of their laws, and the too unequal partition of their riches. There are in most kingdoms only two classes of citizens, one of which wants necessaries, while the other riots in superfluities.

If the corruption of the people in power is never more manifest than in the ages of the greatest luxury, it is because in those ages the riches of a nation are collected into the smallest number of hands.\textsuperscript{147}
\end{quote}

In 2001, in the United States, as the damage from speculating with borrowed money is becoming more apparent, the feeding frenzy in executive compensation worsens, and the concentration of wealth breaks new records, Helvétius' words have a threatening echo.

The constant battle and occasional imprisonment over the material in the \textit{Encyclopédie} exhausted Diderot and d'Alembert and eventually caused them to withdraw but not before the first volume

\textsuperscript{146} Ibid., p. 637.
\textsuperscript{147} Ibid., p. 689.
of the Encyclopédie was published in 1765.

Shortly before his death in prison during the Reign of Terror, the last of the eighteenth-century French Enlightenment philosophers, the Marquis de Condorcet, summarized the French architecture of the rational ordering in human affairs. Condorcet saw the accumulation of knowledge, both scientific and social, as a step-process in which matters requiring profound thought by genius are captured and made simple for many. He saw the process expedited by commercial progress and education. As the standard of living improved, more people would become educated. Condorcet emphasized the necessity of including women in this process, to form a broader base of world citizenry with sufficient education to absorb the contributions of their predecessors. From this broader base, the probabilities would be improved that new genius, whether male or female, would extend knowledge to a new level. This is the way it has worked in science, but to the shame of the intellectual community, it is not the way it has worked to define the rational organization in human affairs. Condorcet described this intellectual ratcheting process:

The truths whose discovery has cost the most effort, which at first could be grasped only by men capable of profound thought, are soon carried further and proved by methods that are no longer beyond the reach of ordinary intelligence. If the methods that lead to new combinations are exhausted, if their application to problems not yet solved requires labors that exceed the time or the capacity of scholars, soon more general methods, simpler means, come to open a new avenue for genius.

We shall point out how more universal education in each country, by giving more people the elementary knowledge that can inspire them with a taste for more advanced study and give them the capacity for making progress of it, can add to such hopes; how these hopes increase even more, if a more general prosperity permits a greater number of individuals to pursue studies, since at present, in the most enlightened countries, hardly a fiftieth part of those to whom nature has
given talent receive the education necessary to make use of their talents.\textsuperscript{148}

The broad-based educational opportunities for both men and women envisaged by Condorcet have come to pass in the mature economies. The building-block process in identifying, verifying, codifying and promulgating knowledge applicable to improving the human condition, however, remains to be done. This is the mission of new philosophers of Enlightenment II to benefit from Information Age technology to identify the best organization for human affairs on a worldwide basis.

Voltaire, and in effect the whole Enlightenment, was honored for his impact on French society when he returned to a hero's welcome in Paris shortly before his death in 1778. The ability of the Enlightenment to move from abstract theory to action was demonstrated when Voltaire's passion for toleration was reflected later in an edict on toleration by King Louis XVI in 1787. Although other reforms of the state were proceeding, based on the advice of Condorcet's friend Turgot, the king's financial minister, Louis XVI unfortunately vacillated once too often between reform and the Queen's and nobles' defense of privilege. The revolution became bloody and ugly.

\textsuperscript{148} Marquis de Condorcet, final chapter of \textit{The Sketch}, "The Tenth Stage, the Future Progress of the Human Mind" from Edward Goddell's \textit{The Noble Philosopher} (Buffalo, New York: Prometheus Books, 1994) p. 236.
Eighteenth Century: Adam Smith proposes economic freedom as the key to eliminating worldwide material scarcity.

In 1776, the American Declaration of Independence proclaimed the mission of "life, liberty, and the pursuit of happiness." In the same year, Adam Smith described the means to this end: Economic freedom through private property; competition; involved, well paid workers; and the technology of the Industrial Revolution. This combination would drive costs and prices lower, opening up new markets whose additional volume would add more wage-earners, more purchases, and even lower prices. Smith felt that self-perpetuating growth depended on surplus being distributed to the wage-earner for purchases, rather than to the wealthy whose purchase of luxuries and portfolio investments had little economic benefit. Smith also specified control of the "prodigals and projectors" to prevent them from deflecting capital to speculation, thereby making money high-cost, scarce, volatile, and impatient, all inversions of the money needed to make Smith's vision work.

Adam Smith was very much a part of the Enlightenment. Drawing on his background in moral philosophy, the study of the Phisiocrats and their *laissez-faire* theories in France, and an understanding of the productivity potential of the Industrial Revolution, he proposed in *Wealth of Nations*\(^{149}\) in 1776 an economic system capable of eliminating material scarcity. For the first time in human history, there was an alternative to nations and people battling over finite resources.

The human duality of individual appetite and ambition in combination with the instinct for social cooperation could be found by following Aristotle's study of the nature of things. With Smith's proposed economic system, the circumstances changed radically. Instead of predatory appetites trampling on social cohesion, there was a system that worked best through cooperation. In theory, the economic motivation for violence among nations and people was over. In theory, the productivity and growth potential of this new economic system would distribute wealth broadly. The two major impediments to improving the human condition were eliminated. Nations would

no longer have to use force against other nations to improve the circumstances of their people; instead they would improve their circumstances cooperatively through free trade. No longer did the few have to concentrate wealth by impoverishing the many; all would gain from the cooperative growth of the new system.

Following the Industrial Revolution, the progression of knowledge among an increasing number of educated women and men became possible when democratic opportunities made a free and comfortable life available for many instead of only for the few. Until the eighteenth century, the motivation for gathering knowledge about governing human affairs had been constricted by the realities of poverty and social immobility. Many had been destined to an existence closer to the animal than to the noble, because a rational order was impeded by predatory forces. This changed gradually as more freedom was forced into the process.

In the Western world, economic freedom began to demonstrate its power to improve lives. The intellectual community had available an epistemological process initiated by Aristotle assimilated by Aquinas, refined by the architecture of Descartes and Bacon, plus the ratchet effect of accelerating knowledge described by Condorcet. The intellectual community had the benefit of Condorcet's summary of the Enlightenment's agenda for a just and prosperous society. Smith's summary of the economic system that could eliminate material scarcity, and the American Declaration of Independence that proclaimed the right to "life, liberty and the pursuit of happiness," for all.

The "thinkers" now had an architecture of knowledge that defined the ideal of eliminating material scarcity and violence along with specific definition of how to couple democracy and capitalism as the means to that end, and finally considerable verifications that these means, competently applied, could reach that ideal.

Nineteenth Century: Karl Marx and John Stuart Mill propose ways that Smith's economic system could reach full potential by involving and motivating the workers.

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Ibid., pp. 225-251.
Like Smith before them, Marx and Mill followed the Aristotelian process by studying the nature of people at work and recognized that the growing industrial process could reach full potential only by changing the circumstances, the work culture, the nature of things.

By the mid-nineteenth century, capitalism had demonstrated its ability to improve lives, but it was functioning at only a fraction of its potential. In 1848, Karl Marx identified the reason: Capitalism had enormous productive capacity to eliminate material scarcity worldwide, but capitalism's distribution of surplus was so concentrated that most people did not have the money to buy what capitalism could produce.

Marx pointed out that during an economic decline, this flaw of capitalism accelerated the downward cycle, as lost jobs and wage cuts further reduced demand. Marx believed that worker ownership was the solution because workers would be motivated to maximize surplus that would then be distributed broadly. Marx felt that this superior economic system would supersede capitalism.

John Stuart Mill, in the same year 1848, in the same city, London, also proposed worker ownership as the method of balancing capitalism's demand with supply. Mill, however, had a better understanding of the management of change than did Marx, so he grafted his refinements onto the existing system of private property and competition. By combining management skills with more productive workers in a new work culture, Mill would reach the same end but avoided Marx's structural mistakes that later caused such tragic results.  

John Stuart Mill had been superbly educated in many disciplines. As a teenager, he discussed economics with David Ricardo, and social theories with Jeremy Bentham, who were both friends of his father. Mill was also a man of experience, having worked for the East India Company and served in Parliament.

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Marx, building on the idealism of his German predecessors, Kant and Hegel, added his theory of dialectical materialism, and concluded that social progress would depend on a superior economic system that would distribute wealth broadly and lead to a classless, non-alienated society. Marx spent years, most of it holed up by himself in the library of the British Museum, integrating his economic theories with his social theories. Marx had little practical experience; he worked for a living only occasionally as a writer or journalist.

Mill had been trained like a scientist in rigorous truth-searching protocols. He understood the management of change, and from this perspective he proposed profit-sharing and worker ownership as a democratic extrapolation of capitalism that could solve the problem of the maldistribution of wealth. Marx, however, was an angry radical with only vague ideas about how to reach his ideal. Knowing little about the management of change, he proposed solutions that would tear down the whole structure, political, economic, and religious.

Subsequently, reformers proved as a group to be closer to Marx's profile than to Mill's; they too suffered from limited experience and inadequate knowledge of finance and economics. They were neither equipped nor trained to present an agenda for reform that had much chance for success. The intellectual left had ignored the Aristotelian process, the architecture of Descartes and Bacon, the economics of Smith, and Condorcet's summary of the Enlightenment. Instead, they followed Marx's shallow, emotional, unworkable solutions. This enormous process failure led the world into a wrong turn with tragic results. Throughout the twentieth century, governments would kill 160 million people, mostly innocent civilians.\(^\text{152}\)

Both Adam Smith and John Stuart Mill made success of the economic democratic system conditional on promotion of the general welfare by a supportive government and the subordination of the financial system to the building and selling of things. Although this superior economic system was defined with great specificity, it was neither sufficiently examined by academia nor offered for examination to students who would later lead companies and countries. As Marx observed, the intellectual right supports the existing economic system

and tends to sustain it beyond its economic logic. During this time, the intellectual right did defend the status quo while the intellectual left sought radical alternatives. The correct answer, democratic capitalism, was left to the trial-and-error efforts of managers with a democratic vision.

Marx and Mill had different ways to put in place the circumstances conductive for each individual to reach their full development in a harmonious whole. The work culture is described as empowerment, and decentralization, and is based on investing in human capital. It is the work culture based on the dual nature of people providing opportunity for individual development within a harmonious whole. It is the work culture necessary in the Information Age in order to release the cognitive, not manual, power of the people.

These educated, independent-thinking, involved people are, at the same time, the profile of the ideal citizenry needed to make democracy workable. Is it possible that commerce, thus transformed, can become the source of values, an example of morality in action to be emulated by the other elements of the culture? Why not? Marx was right about many things, and this watershed event is no more than confirmation of his theory: "The writers of history have so far paid little attention to the development of material production, which is the basis of all social life, and therefore of all real history." 153

The Information Age Revolution is based on the most elementary truth about the organization of human affairs: The opportunity for the fullest development of the individual within a harmonious whole. The ideal of society reaching its full potential as the sum of individual development is right out of the Communist Manifesto: "In place of the old bourgeois society, with its classes and class antagonisms, we shall have an association, in which the free development of each is the condition for the free development of all." 154

Twentieth Century: Ludwig von Mises described why capitalism was failing to reach full


potential: The greedy few were able to dominate the uninformed many.

Ludwig von Mises was one of the Austrian economists and a mentor to Friedrich Hayek. Later in America, von Mises became known as a conservative economist because of his support of economic freedom. In 1912, however, Mises wrote of how government policies dominated by financial capitalism caused economic damage and damaged social cohesion. Mises described the deliberate deflation in Great Britain after the Napoleonic wars which restored the asset value of the wealthy to pre-war levels by putting people out of work, cutting wages, and raising prices.

Calamitous economic hardship resulted from this deflation; they stirred social unrest and begot the rise of an inflationist movement as well as the anti-capitalist agitation from which after a while Engels and Marx drew their inspiration.155

The same philosophy of protecting the asset value of the wealthy by victimizing the people is used every time the economy is damaged by either war or the excesses of ultra-capitalism. Mises, the economist honored by conservatives, provides this example of why government fiscal and monetary policy must be designed by representatives of the people, not by representatives of finance capitalism.

This same brutal practice was copied in the United States after the Civil War with the same results. After World War I, Great Britain followed this policy again. John Maynard Keynes pointed out that not stabilizing the monetary position at the inflated level of 1920 gave Great Britain a decade of unemployment.156 These are examples of how wealth is persistently concentrated through government privilege and, in turn, is an example of why social tensions are provoked instead of economic freedom reaching its full potential.

Mises following the tradition of the Enlightenment made these observations about the process


failure in the rational search for truth:

The main objective of praxeology and economics is to substitute consistent correct ideologies for the contradictory tenets of popular eclecticism. There is no other means of preventing social disintegration and of safeguarding the steady improvement of human conditions than those provided by reason. Men must try to think through all the problems involved up to the point beyond which a human mind cannot proceed farther. They must never acquiesce in any solutions conveyed by older generations, they must always question anew every theory and every theorem, they must never relax in their endeavors to brush away fallacies and to find the best possible cognition. They must fight error by unmasking spurious doctrines and by expounding truth.157

Mises analyzed humans free to make their choices in one of his books appropriately titled Human Action. He fulfilled the Enlightenment vision by applying his multi-discipline wisdom to the combination of economic freedom, the search for the rational order, and a warning about the damage from dogma, whether from the left or the right of the political spectrum.

Friedrich Hayek warns that the movement away from individual freedom toward state control is the "Road to Serfdom."

The political left has never learned enough about economics and finance to understand how the political right was concentrating wealth through government privileges. Instead of following the Aristotelian process of studying the growth potential of the system, defined by Smith and refined by Marx and Mill, the political left indulged their Platonian instinct for central control by an elite. Coopting growing democratic power, they attacked concentration of wealth by taxing and redistributing it. During the twentieth century, this process of collectivism in the United States raised all taxes as a percentage of the GDP from 3% to over 30%.

Hayek wrote *Road to Serfdom* in 1946, describing how the movement then underway in Europe and the United States would lead from socialism to fascism. Hayek's book shocked and angered most of the intellectual community, but his theory has been validated historically since by the loss of freedoms in forms of collectivism and consequently, the failure of all systems of extreme central control.

Both the collectivism on the left and the concentration of wealth by the right derive from government privilege. Both prevent the economic system of Smith, Marx, and Mill from reaching full potential. These privileged systems are not only impediments to reaching full potential but they polarize and gridlock the process preventing real reform. It is this impasse that needs the probing analysis of Enlightenment II that will result in a citizens' agenda for reform.

Conservatives' high opinion of the works of Mises and Hayek in most cases fails to focus on their monetary views. Capitalism's need for low-cost, ample, non-volatile, patient capital could be fulfilled, in the opinion of Mises and Hayek, by free banking monitored and punished by all the usual forces of competition. In the absence of free banking, however, government policies have to provide the kind of capital that promotes economic growth and prevents privileges for speculation. The present fiscal and monetary system in the United States, however, is the worst of both worlds: It privatizes the profits and nationalizes the losses. This would not fit the Austrians' definition of free markets.

Conservatives are pleased with Hayek's espousal of *laissez-faire*, but they tend to overlook his litany of government responsibilities that go beyond *laissez-faire*. Hayek's role for government includes virtually every liberal mission, though he emphasized that it is the means to the end that needs debate, not the end itself. Hayek also characterized conservatism as "paternalistic, nationalistic, power-adoring, a defender of established privilege and closer to socialism than true liberalism."\(^{158}\)

Hayek had a clear view of why elitists fail at governance when they use their energy to seek

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alternative social orders through political solutions rather than trying to improve their understanding and use of the underlying principles of the economic system. From Hayek's study of these principles, he became an exponent of "spontaneous order" and a critic of collectivism which does not work well and leads to tyranny as subsequent events proved. Hayek's "spontaneous order" was the alternative to central planning in which a superior commercial order arose from the free, spontaneous choices of millions of people.

Hayek understood that the extraordinary improvement in lives had been accomplished by economic freedom, but he also understood that a higher standard of living generated new demands to sustain and broaden the progress:

Wherever the barriers to the free exercise of human ingenuity were removed, man became rapidly able to satisfy ever widening ranges of desire; and while the rising standard soon led to the discovery of very dark spots in society, spots which men were no longer to tolerate, there was probably no class that did not substantially benefit from the general advance. At this moment, when the greater part of mankind has only just awakened to the possibility of abolishing starvation, filth and disease; when it has just been touched by an expanding wave of modern technology after centuries or millennia of relative stability; even a small decline in our rate of advance might be fatal to us.159

These phenomena place special urgency on an Enlightenment II. Violence among nations and concentration of wealth, the twin impediments to the superior economic system reaching its full potential, no longer have any economic logic and should be terminal. The momentum of history, including its ugly features, however, is great. Hayek pointed out that in our smaller world of instant communication, most people develop an impatience for the good things in life. When, instead, their living standards decline, as they have done at the end of the twentieth century in Indonesia and Russia, two of the world's most populous nations, the people will not stand for it for very long. If true reform does not position democratic capitalism to eliminate material

159 Ibid., p. 20.
scarcity, elevate spirits and unify people then new waves of violence will be provoked. The tragic events on September 11, 2001 give added urgency to these observations.

Jean-Francois Revel places economic freedom ahead of political freedom in the transition away from tyranny. Revel exhorts intellectuals to assume their proper responsibilities.

At the beginning of the twentieth century, there was optimism that violence among nations would be displaced by the rule of law. There was similar optimism that growing democracy was diffusing political power and would inevitably result in a diffusion of economic power. The intellectual community however failed in the process of identifying the means to these ends. The people did not use the growing democratic power to eliminate the impediments because they were not informed. As a result, the twentieth century, measured in terms of people killed by governments, was the worst failure in human history. This failure did not, however, cause many in the intellectual community to recognize their process failure; instead, many abandoned the search for the best organization for human affairs.

French intellectual Jean-Francois Revel, author of over twenty books and a former editor and director of L'Express, reminds us that while totalitarian governments are founded on systematic mendacity, democracy depends on citizens' free choices based on the free flow of truth. Revel explains the central paradox of the twentieth century, the bending and warping of the truth in democratic countries because of ideological or intellectual laziness. Revel also explains why economic freedom will lead to political freedoms whereas political freedoms do not always lead to economic freedom. Revel points out that without improving food, clothing, shelter, health and education, political freedoms can be a cruel illusion.

Revel discriminates between authoritarian states and totalitarian states. Authoritarian states may not have all political freedoms but can choose an economic life that is largely autonomous and

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161 Ibid., pp. 155-6.
encourage freedom in philosophy and the arts. A totalitarian government "by definition is a cast-iron monopoly of politics, the economy, and the culture for the benefit of a self-appointed oligarchy."\(^{162}\)

Revel recognized the world movement to free markets at the end of the twentieth century but reminded us of a similar optimism for a better world at the end of the nineteenth century that failed to foresee the corruption of the twentieth-century by totalitarian governments. Likewise, at the end of the twentieth century, many intellectuals were ignoring the reasons for the implosion of central planning, underestimating the unifying effect of the Information Revolution, and still treating unexamined capitalism as the enemy. This myopia may predestine the twenty-first century to more folly and violence, unless new philosophers can present a rational plan for citizens' consideration.

Revel in his numerous books has provided an important concept to be integrated into the process of moving from tyranny to economic freedom. He emphasized that in the difficult management of change, priorities have to be arranged properly. This should be obvious, but in a politicized, superficial environment, American politicians seek political benefit by criticizing other countries' "human rights" violations without placing them within the context of a long, broad process. China is an example of such criticism where an ongoing movement from tyranny and a low standard of living to economic freedom, and a higher standard of living has been criticized for human rights abuses. The first priority in any country is sufficient food, clothing, shelter, education, good health, hope, and economic freedom serves these fundamental needs. Revel cautions us to understand the process, including the inevitable transition to political freedom by the educated, independent-thinking people required for economic freedom to work.

Revel also addressed the intellectual process failure that is threatening the world movement to freedom. He faults his fellow intellectuals for allowing their personal psychological urges to dominate their intellectualism and render them incapable of the function upon which society depends:

Everything thus boils down to the erroneous way in which the elusive problem of the "function of the intellectual in civil society" is usually posed. How can the intellectual be the rudder of society if he proves himself incapable of playing this role in his own thinking? How can he be a teacher of honesty, rigor, and courage for the whole of society when he is dishonest, inexact, and cowardly in the very exercise of intelligence? Still, I venture to hope that we have finally reached the end of an era during which so many intellectuals strove above all to place mankind under their ideological domination, and that we are entering a new epoch in which they will at last settle down to their true vocation, which is to place knowledge at the service of human beings, and not simply in the scientific and technical domains. This transition from the old era, when sterilization of knowledge was regarded as the norm, to a new age is not simply one possible choice among others: it is a necessity. Our civilization is condemned to abide by its underlying principles, or else it will regress toward a primitive stage where there will no longer be a contradiction between knowledge and behavior, knowledge in the meantime having disappeared.

Revel and others have examined the intellectual community's failure to fulfill its truth-searching role in society, first by promoting a terribly flawed agenda, collectivism in its extreme forms, and subsequently by denying that any agenda was possible. Revel emphasized that this failure contaminated the whole educational process and led to an impasse at the end of the twentieth century. The hope for a world united by economic common purpose can be realized only when the educational process presents to the best young minds an ideal, the means to attain it, and the empirical evidence that it works.

_Pope John Paul II celebrated diverse cultures synthesizing faith and reason for the common good._

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163 Revel, _The Flight From Truth_, op. cit., p. 363.
164 Ibid., p. 387.
Karol Wojtyla had been a student of philosophy in his homeland, Poland, when he became a priest. He understood that faith must constantly challenge reason to continue the confusing task of finding truths applicable to secular progress: "Reason needs to be reinforced by faith in order to discover horizons it cannot reach on its own."\textsuperscript{165} In 1998, Pope John Paul II marked his twentieth anniversary as pope with his celebration of these interdependent forces in \textit{Fides et Ratio, Faith and Reason}.

John Paul II respected cultural diversity, sensing that philosophy emanating from these many sources would find common ground:

Philosophy is directly concerned with asking the question of life's meaning and sketching an answer to it. Philosophy emerges, then, as one of the noblest of human tasks. According to its Greek etymology, the term philosophy means "love of wisdom." It is an innate property of human reason to ask why things are as they are, even though the answers which gradually emerge are set within a horizon which reveals how the different human cultures are complementary.

Philosophy's powerful influence on the formation and development of the cultures of the West should not obscure the influence it has also had upon the ways of understanding existence found in the East. Every people has its own native and seminal wisdom which, as a true cultural treasure, tends to find voice and develop in forms which are genuinely philosophical.\textsuperscript{166}

From the tragic events of the September 11, 2001 attack on America a new understanding can emerge from the East and the West, from the cultural diversity honored by the pope.

John Paul II summarized the damage done by reason gone astray in three categories: Trying to confirm revealed truth by reason, the development of a secular religion, communism, from

\textsuperscript{165} Pope John Paul II, Encyclical Letter \textit{Fides et Ratio, on the Relationship Between Faith and Reason}, no. 67, given in Rome at St. Peter's, September 14, 1998.

\textsuperscript{166} \textit{Ibid.}, no. 2.
reason, and finally reason that denies its own capacity to harness knowledge to improve the human condition:

Some representatives of idealism sought in various ways to transform faith and its contents, into dialectical structures which could be grasped by reason. Opposed to this kind of thinking were various forms of atheistic humanism, expressed in philosophical terms, which regarded faith as alienating and damaging to the development of a full rationality. They did not hesitate to present themselves as new religions serving as a basis for projects which, on the political and social plane, gave rise to totalitarian systems which have been disastrous for humanity.\textsuperscript{167}

As a result of the crisis of rationalism, what has appeared finally is \textit{nihilism}. As a philosophy of nothingness, it has a certain attraction for people of our time. Its adherents claim that the search is an end in itself, without any hope or possibility of ever attaining the goal of truth. In the nihilist interpretation, life is no more than an occasion for sensations and experiences in which the ephemeral has pride of place. Nihilism is at the root of the widespread mentality which claims that a definitive commitment should no longer be made, because everything is fleeting and provisional.\textsuperscript{168}

Pluralism in its celebration of the richness, meaning, and pride in various cultures should be as much an enemy of \textit{nihilism} as democratic capitalism which celebrates how all cultures can unite in economic common purpose. Pluralism, or multiculturalism, is based on minority groups participating fully in the economic-political system while maintaining cultural identity. In this emphasis, pluralism is consistent with the democratic capitalistic fundamental of \textit{all} having the opportunity for full development in a harmonious whole. Pluralism is an emphatic restatement of the democratic promise of life, liberty, and the pursuit of happiness. It is vital, however, to

\textsuperscript{167} Ibid., no. 46.

\textsuperscript{168} Ibid.
recognize that whereas pluralism restates the end, it is democratic capitalism that provides the means.

Descartes spent his life defining a process to lead to truth. He lived in an age, however, of intellectual tyranny when people were not free to follow their reason or collaborate with others in the use of reason. At the beginning of the new century and millennium in most parts of the world, restrictions to the free use of reason disappear as countries move toward economic freedom. Religious fanatics in some parts of the world do still suppress freedoms, including particular force against women. They are applying a form of tyranny purged from most cultures several centuries ago.

Paradoxically, some contemporary intellectuals have converted their social and political beliefs into a quasi-religion where any argument with the authority of their beliefs is not met with curiosity and debate but rather with reflex emotion, threats, and insults. Ignored in this new form of intellectual tyranny is Mises' advice:

The problems involved are purely intellectual and must be dealt with as such. It is disastrous to shift them to the moral sphere and to dispose of supporters of opposite ideologies by calling them villains. It is vain to insist that what we are aiming at is good and what our adversaries want is bad. The question to be solved is precisely what is to be considered as good and what as bad. The rigid dogmatism peculiar to religious groups and to Marxism results only in irreconcilable conflict. It condemns beforehand all dissenters as evildoers, it calls into question their good faith, it asks them to surrender unconditionally. No social cooperation is possible where such an attitude prevails. 169

*Some new philosophers reaffirm the mission of the Enlightenment and, at the same time, reaffirm idealism.*

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The means and the end will be clear when new philosophers rebuild the rigorous truth-searching disciplines that this most vital subject, the future of the human species, demands. Superficial thinking and dogma contradict the intellectual quest in contrast to philosophical offerings in this century from those trained first in scientific truth-searching disciplines. Teilhard de Chardin, a renowned paleontologist, and Edward O. Wilson, a Nobel-Prize-winning biologist were also multi-discipline philosophers who used rigorous truth-searching protocols required by science to gain knowledge relative to improving the human condition. Many humanists on liberal arts faculties reject science as too mechanistic, too deterministic, to be useful in the broad area of human affairs. Many with this attitude betray a flawed epistemological process. Their single-discipline scholarship disables them from finding the multi-disciplinary solutions required in complex human affairs; nor do their methods force them into a fuller examination.

Roger Kimball, an author and editor also examines the anti-Enlightenment attitude:

It is a curious irony that self-creators from Nietzsche through Derrida and Richard Rorty are reluctant children of the Enlightenment. In his essay `What is Enlightenment? Immanuel Kant observed that the Enlightenment's motto was sapere aude, `Dare to know!' For the deconstructionist, the liberal ironist, and other paragons of disillusionment, that motto has been revised to read "Dare to believe that there is nothing to know." The Enlightenment sought to emancipate man by liberating reason and battling against superstition. It has turned out, however, that when reason is liberated entirely from tradition, which means also when it is liberated entirely from any acknowledgment of what transcends it, reason grows rancorous and hubristic: it becomes, in short, something irrational.

To the extent that Enlightenment rationalism turns against the tradition that gave rise to it, it degenerates into a force destructive of culture and the manifold directives that culture has bequeathed to us. Like so many other promises of emancipation, it has contained the seeds of new forms of bondage. Philosophy

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has been an important casualty of this development. It is no accident that so much modern philosophy has been committed to bringing us the gospel of the end of philosophy. Once it abandons its vocation as the love of wisdom, philosophy inevitably becomes the grave-digger of its highest ambitions, interring itself with tools originally forged to perpetuate its service to truth.¹⁷¹

Others have translated sapere aude with more of a challenge: Have courage to use your own reason.

Edward O. Wilson, Harvard professor and winner of both a Nobel and a Pulitzer prize for science and literature, explained that the title of his book, Consilience,¹⁷² means the unification of knowledge, and he selected this rare word as more precise than "coherence." Wilson proposed a vision similar to Teilhard's of the social progress possible through the unification of knowledge. He identified single-discipline scholarship in academia and the under-prepared media as serious impediments to the unification of knowledge requisite to the rational organization of human affairs:

The root cause of the problem: ... the overspecialization of the educated elite. Public intellectuals, and trailing close behind them the media professionals, have been trained almost without exception in the social sciences and humanities. They consider human nature to be their province and have difficulty conceiving the relevance of the natural sciences to social behavior and policy. Natural scientists, whose expertise is diced into narrow compartments with little connection to human affairs, are indeed ill prepared to engage the same subjects. What does a biochemist know of legal theory and the China trade? It is not enough to repeat the old nostrum that all scholars, natural and social scientists and humanists alike, are animated by a common creative spirit. They are indeed creative siblings, but they lack a common language. There is only one way to


¹⁷² Edward O. Wilson, Consilience, the Unity of Knowledge (New York: Alfred A. Knopf, 1998).
unite the great branches of learning and end the culture wars. It is to view the boundary between the scientific and literary cultures not as a territorial line but as a broad and mostly unexplored terrain awaiting cooperative entry from both sides. The misunderstandings arise from ignorance of the terrain, not from a fundamental difference in mentality.173

Wilson could have added economics, finance, law, and principles of governance to the disciplines not integrated with liberal arts in the search for truth about the human condition.

Many intellectual leaders have rejected the challenge of the Enlightenment and abandoned the search for a unifying force. Others attack any value system; everything to them is relative. The pluralism that means, "Make up your own value system, one is as good as another," is a negative influence. The pluralism that insists on "full participation in the dominant economic-political system by all groups and cultures," is a positive influence.

173 Ibid., p. 126.
Edward Wilson describes the confusion:

All movements tend to extremes, which is approximately where we are today. The exuberant self-realization that ran from romanticism to modernism has given rise now to philosophical post-modernism (often called post-structuralism, especially in its more political and sociological expressions). Post-modernism is the ultimate polar antithesis of the Enlightenment. The difference between the two extremes can be expressed roughly as follows: Enlightenment thinkers believe we can know everything, and radical post-modernists believe we can know nothing.

Edward Wilson defended the Enlightenment in specific terms:

I believe that the Enlightenment thinkers of the seventeenth and eighteenth centuries got it mostly right the first time. The assumptions they made of a lawful material world, the intrinsic unity of knowledge, and the potential of indefinite human progress are the ones we still take most readily to our hearts.  

Wilson continued with his criticism of those who rejected the Enlightenment's mission:

The philosophical modernists, a rebel crew milling beneath the black flag of anarchy, challenge the very foundations of science and traditional philosophy. Reality, they propose, is a state constructed by the mind, not perceived by it. In the most extravagant version of this constructionism, there is no "real" reality, no objective truths external to mental activity, only prevailing versions disseminated by ruling social groups. Nor can ethics be firmly grounded, given that each society creates its own codes for the benefit of the same oppressive forces. If these premises are correct, it follows that one culture is as good as any other in the expression

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174 Wilson, op. cit., p. 8.
of truth and morality, each in its own special way. Political multiculturalism is justified; each ethnic group and sexual preference in the community has equal validity. And, more than mere tolerance, it deserves communal support and mandated representation in educational agendas, not because it has general importance to the society but because it exists. That is, again, if the premises are correct. And they must be correct, say their promoters, because to suggest otherwise is bigotry, which is a cardinal sin.\textsuperscript{175}

Wilson attacked on all fronts and angered the defenders of a rights-based society so thoroughly that they poured water over Wilson's head after he finished speaking, chanting "He's all wet!" Tom Wolfe described the attack on Wilson as "one of the most remarkable displays of wounded Marxist chauvinism in American academic history."\textsuperscript{176}

A whole generation of sensitive people has been weaned on a combination of multiculturalism, pluralism, relativism and nihilism. A rights-based society was an extrapolation of the vital civil rights movement. Antagonism to the establishment was an extrapolation from opposition to the Vietnam War. Relativism and nihilism are products of the obscene wars of the twentieth century. All of these are productive social pressures until they displace the unifying influence of a common ideology.

Edward Wilson examined deconstruction:

Post-modernism is expressed more explicitly still in deconstruction, a technique of literary criticism. Each author's meaning is unique to himself, goes the underlying premise; nothing of his true intention or anything else connected to objective reality can be reliably assigned to it. His text is therefore open to fresh analysis and commentary issuing from the equally solipsistic world in the head of the reviewer. But then the

\textsuperscript{175} Ibid., pp. 40.

reviewer is in turn subject to deconstruction, as well as the review of the reviewer, and so on in infinite regress. That is what Jacques Derrida, the creator of deconstruction, meant when he stated the formula *Il n'y a pas de hors-texte* (There is nothing outside the text). At least, that is what I think he meant, after reading him, his defenders, and his critics with some care. If the radical post-modernist premise is correct, we can never be sure that this is what he meant. Conversely, if that is what he meant, it is not certain we are obliged to consider his arguments further. This puzzle, which I am inclined to set aside as the "Derrida paradox," is similar to the "Cretan paradox" (a Cretan says "all Cretans are liars"). It awaits solution, though one need not feel any great sense of urgency in the matter.  

This put-down may be appropriate but intellectuals' support of a new social ideal and their contributions to identifying the means to the end is an urgent matter. Democratic capitalism needs the understanding and support of these brilliant people, both optimists and pessimists who are truly sensitive to the human condition. Deconstruction is the latest iteration of the skeptic philosophy and should be part of the continuous process of truth seeking. Greek philosophers both before and after, challenged Plato's and Aristotle's agreement that ultimate truth was attainable. Protagoras (481-411 BC) had proclaimed that all truth, beauty and goodness are relative and subjective; Phyrro (360-300 BC) agreed. David Hume repeated this skepticism in the eighteenth century. Skepticism, then and now, is a vital part of the challenge and debate nature of truth-seeking.

Skeptics are correct: There are no absolutes, perfection is not attainable. Each individual sees, hears, feels, smells, and tastes with imperfect senses, and reasons with a culturally conditional mind. But what does any of this have to do with finding the best way to improve the human condition, a relative goal? What works well can be clear, if not perfect. Reason is a powerful tool, when wielded by a sufficiently culturally diverse group in collaboration across the full range of scholarly disciplines. This continuous

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177 Wilson, *op. cit.*, p. 41.
process has been the mission of truth-seekers throughout history and is now the mission of Enlightenment II.

Late twentieth century philosopher sees Teilhard's convergence and Drucker's synthesis coming into place.

Friedrich Turner, Professor of Arts and Humanities at the University of Texas at Dallas has predicted a synthesis of religion, art, and science, as a third option in the culture war between the left and the right:

Huge changes have recently occurred that offer good prospects for peace and steady economic development. World communism has collapsed, and with it the economic and political appeal of socialism. The age of information economics has begun. The computer is multiplying the power of the brain as the steam engine and internal combustion engine multiplied the power of the body. Reproductive technology, together with increased human longevity, has made it possible for societies to survive without consigning one whole sex to the work of reproduction and nurture, and thus the talents of women have become available for other tasks. Chaos theory, ecological thinking, and an enlarged and deepened conception of evolution have revolutionized the sciences by making plausible a nonlinear creative potential to counteract the modernist conception of the universe as deterministic and decaying. Much of the erstwhile Third World has transformed itself into bustling capitalistic democracies. Together, these forces spell the end of an old world-view, that of modernism and postscript postmodernism, and the beginning of a new. But these changes are still in their infancy, or even in utero, and they are tragically vulnerable to the forces that oppose them. A new era has begun, but it faces the baleful resentment of those who cling to the late-modernist and postmodernist era that gave it birth.178

Turner proposes an emerging "radical center" with a new view of value that can transcend the zero-sum view of both the left and the right. According to Turner, the intellectual left believes that:

This natural value can be extracted from nature only by painful labor, that it is distributed among human beings either through coercive control by a ruling class/race/gender or through liberating struggle against that control.179

Turner believes that the intellectual conservative right shares this "shrinking pie" view but with a different emphasis: "Natural value is a diminishing stock pile that is distributed by the invisible hand of the market, a just process that cannot be disrupted without economic damage."180

This zero-sum world described by Turner is contrary to Adam Smith's dynamic for wealth creation. Turner understands this, and he describes the radical center realizing both self-perpetuating growth and elevated spirits:

Value is continually created by the natural universe, that it is not a shrinking pie, and that human beings can share in and accelerate the growth of value through work which may be delightful, if disciplined.181

Turner senses this transformation towards a vaguely defined democratic capitalism:

As our technology enables more perfect and multidimensional forms of communication, as machines take over the drudgery, the labor basis of

180 Ibid., p. 5.
181 Ibid., p. 6.
value is being replaced by an information basis of value; and this in turn will be replaced, perhaps, by an emergent kind of value which is hard to define but as a kind of embodied grace.\textsuperscript{182}

With "embodied grace," Turner is close to describing democratic capitalism that maximizes surplus and eliminates material scarcity \textit{by} elevating spirits.

Because of the lack of academic visibility of democratic capitalism, professors such as Turner, have been left looking elsewhere for the moral system:

Unlike the tendency of \textit{laissez-faire} capitalism, the regime of evolutionary hope would not reductively boil down all higher motivations to intelligent materialistic selfishness, but would recognize the equal reality of nobler impulses.\textsuperscript{183}

Even optimistic academicians share this bleak view of a generic capitalism that ignores the democratic capitalism that maximized surplus by elevating spirits described in 1848 by John Stuart Mill:

Yet it (the material benefit) is nothing compared to the moral revolution in society that would accompany it; a new sense of security and independence in the labouring class; and the conversion of each human being's daily occupation into a school of the social sympathies and the practical intelligence.\textsuperscript{184}

Since many humanists have either abandoned or attack a secular ideal, a new social coalition needs assistance from religious thinkers. The values in the best coupling of democracy and capitalism are common with those of religion, both sustaining a belief in

\textsuperscript{182} Ibid., p. 6.
\textsuperscript{183} Ibid., p. 268.
\textsuperscript{184} Mill, \textit{op. cit.}, p. 789.
secular progress. Turner places religion in this powerful perspective:

Syncretism: The incorporation within higher and deeper religious ideas of the tenets, theologies, and observances of all the religious traditions, together with the new revelations that continuously pour forth from the sciences. Religion would be at the leading edge of science. Traditional religious concepts and metaphors would be recognized as culture-bound, partial, but valid formulations of the evolutionary direction we should take and have in general been taking, and as the missing component of social hope.\textsuperscript{185}

\textit{Summary}

The fall of Babylon to invaders has become a pattern repeated during the following four thousand years. As societies become more civilized, affluent, and comfortable, less civilized tribes or nations invade for their economic benefit, raping and killing in the process. Later, nations used force for economic exploitation of weaker nations. This economic imperialism has been extended worldwide by the Western nations during the last four centuries, but it began to end after World War II. New philosophers should have the opportunity to seek the optimum arrangement for human affairs in the twenty-first century free of this impediment of imperialism where nations subjugated other nations.

Although national imperialism is terminal for lack of economic logic, new philosophers will still have to grapple with the reality that law in the relations among nations has not yet displaced force. This residual effects from centuries of imperialism can be eradicated through economic common purpose, rising affluence, better education, and a willingness of U.N. members to collaborate in the use of force to discipline those still trying to use force for their purposes.

Many argue that violence and the domination by the human animal over the rational

\textsuperscript{185} Turner, \textit{op. cit.}, pp. 268-9.
human is inherent in the species. I believe strongly that bloody human history is due to the failure of the reasoning process to be reflected in action through the democratic will of the people. During the twentieth century, enormous progress was made in the standard of living for many, and growing democratic freedoms responding to human urges and human reason. In contrast, one-hundred and sixty million people killed by governments during the same century reflected not inherent evil but rather demonstrable errors in the reasoning process that led to tragic mistakes in action.

Confucius presented an arrangement for human progress: A secular code of morality, personal responsibility, and meritocracy in the selection and training of leaders. Confucius specifically identified violence among nations and concentration of wealth as the impediments to human progress that could be purged in time by talented and virtuous leaders. China deliberately abandoned imperialism in Asia in the sixteenth century to focus on internal development, but later China was unable to avoid force among nations. This Confucian society was dominated by Western nations and Japan for centuries.

Aristotle added a great deal to the process of truth-seeking beginning with the investigation of the nature of things, proceeding through the identification of full potential, circumstances needed, and the impediments to be eliminated, in order for the growing process to reach full potential. Aristotle's society was dominated, however, by slavery, inequalities, and violence among states; consequently, the rational organization of human affairs developed by his process had little chance for broad implementation.

Aquinas packaged Aristotle and a composite of religious teachings from Christianity, Islam and Hebrew. Aquinas' culture, however, was more barbaric than Aristotle's. Besides a continuation of forms of slavery, and violence among nations, books and people were burned for heresy.

Descartes and Bacon added significantly to the architecture for finding truth including Bacon's dynamic, collaborative, and cumulative process to harness knowledge. While the epistemological process was improved by the efforts of these philosophers, the European continent was in a state of confusion between faith and reason. Instead of
cooperating in the development of a common, secular, moral code, religion assumed the authority to place the world at the center of the universe and kill anyone who disagreed.

The eighteenth-century Enlightenment assimilated the wisdom of many, including for the first time the Chinese, and outlined an organization of society based on reason and experience. The Enlightenment proposed the elimination of war, international law among nations, political democracy, and broad wealth distribution. Besides an improved definition of the means to the goal of social progress, the Enlightenment demonstrated the power of ideas by toppling the political tyranny of the church-state combination, and the intellectual tyranny of limiting freedom to think and write. The new freedoms provoked by the French Enlightenment were opposed by the defenders of the status quo, and the transition turned into the violence of the French Revolution.

During the eighteenth century, the momentum toward intellectual, political and economic freedom had become irresistible. In Scotland, Adam Smith drew on this momentum, his knowledge of moral philosophy, and the technology of the Industrial Revolution to declare that material scarcity was no longer a necessary part of human existence. The implications were enormous. No economic logic could any longer be claimed for violence among nations. No economic logic could any longer be claimed for concentration of wealth. For the first time in human history, a practical way had been found to neutralize the twin impediments to the attainment of full human potential.

At the middle of the nineteenth century, both Karl Marx and John Stuart Mill concluded that Smith's system for eliminating material scarcity had been experimentally verified. They agreed, however, that the capacity to produce was not properly matched with the capacity to consume. Consequently, wealth was still concentrated and the potential for improving all lives and social cohesion was not being realized. Both recommended worker-ownership as the refinement of capitalism that would maximize the surplus and distribute it so that it would sustain economic growth. In Mill's proposal, workers would accumulate ownership by purchase and profit-sharing in stock. As this included a financial sacrifice by the worker in order to acquire stock, the motivation to think and act
like an owner was assured. Marx did not understand management of change and proposed tearing down all of the infrastructure in order to introduce a new system.

The work of Smith, Marx, and Mill contains the educational material crucial for new philosophers because an understanding of the way to maximize and distribute wealth democratically is fundamental for anyone who aspires to make a contribution to social progress. To assume responsibility for new opportunities, new philosophers must do their homework in economics and finance in order to have a functional understanding of the practical means for human progress.

An important part of this education is an understanding of how and why Marx and his followers made such egregious mistakes by failing to understand the correct dynamics of Smith's proposal. An understanding of this history is likewise necessary to understand how Marx's vision of individual development and the decline of the warrior state retrogressed into tyrannical governments that caused the tragic events of the twentieth century.

By the middle of the nineteenth everything was in place for humans to make dramatic progress toward comfort, freedom, elevated spirits and unity. The wisdom of the earlier philosophers had defined the intellectual process and outlined the rational order. It was the responsibility of the philosophers of that time to integrate the contributions of Smith, Marx, and Mill that specified the means that made the ideal a practical possibility for the first time. Its implementation would require modification of political structures and changes in the culture in support of this superior economic system. Enlightenment II new philosophers must understand how that opportunity was lost resulting in another century and a half dominated by the same concentrated wealth and violence among nations. Enlightenment II new philosophers must examine why citizens were not educated and leaders trained at that time to implement the apparent reforms.

At the end of the twentieth century, despite the end of imperialism, the advent of the Information Age, and the evidence that economic freedom improves lives, the world was
still, incredibly, dominated by the twin impediments of violence among nations and concentrated wealth. The world's presumptive leader, the United States was gridlocked intellectually and politically by the left and the right. In the twenty-first century, new philosophers have a greater responsibility than ever before to identify the correct reforms and purge these impediments because these obstacles to human progress have now lost all economic logic. Their roots are now more shallow, so they can be more easily pulled up and discarded.

The political gridlock in the United States had been anticipated by Aristotle when he warned that the state should not be under the control of either the rich, concentrating and protecting their wealth, or of the poor, trying to take it away. According to Aristotle, only the middle class could design and support a system that produces and distributes wealth in such abundance that everyone's needs are filled.

Twentieth-century philosophers and economists, Mises and Hayek, are helpful to new philosophers because they described the pathologies of both the conservatives and the collectivists that gridlock the system. Mises described techniques used by the financial oligarchy to concentrate wealth. New philosophers need to understand these intrusions on economic freedom in order to design protections against continued exploitation. Hayek described the damage that collectivists do to wealth creation and individual freedom, with their governments of the elite trying to redistribute wealth. Although Hayek is usually described as a conservative economist he was, in fact, a true liberal whose belief in the power of freedoms was coupled with specificity in the means for governance according to liberal principles.

Some late twentieth-century philosophers did damage because they opposed the concept of the Enlightenment just at the time when the mission of human betterment had become practical and the impediments to social progress could be eliminated. New philosophers must understand that philosophers who abandon idealism because of the failures of the twentieth century are repeating the error of many intellectuals in mid-nineteenth century when they chose Marx's radical structural change instead of Mill's evolutionary
refinement. The error then, and now, is reformers using new democratic power to redistribute wealth instead of influencing government to reform capitalism through fiscal and monetary policies. New philosophers need to understand that this persistent error is caused simply because reformers do not understand the government policies necessary to refine capitalism in ways that maximize the creation and distribution of wealth. The political power available to counteract the lobbying of finance capitalism and collectivism is enormous, the reformers need only the agenda of democratic capitalism to energize and organize this power.

New philosophers need to engage the post-modern deconstructionists in Enlightenment II as the latest generation of skeptics who move beyond their proper function in the truth-seeking process. Bacon called this the *dynamic* part of the process where, for example, the hypothesis that social progress depends on movement to a superior economic system requires challenge, debate and analysis of experience to validate the hypothesis. Similarly, the hypothesis that democratic capitalism is this superior economic system that can eliminate material scarcity, elevate spirits, and unify people, requires extensive analysis of experience presented as experimental verification.

The common denominator among the post WWII visionaries and optimists such as Teilhard, Drucker, Wilson and Turner is the call for synthesis, or a bridging of disciplines. New philosophers will realize that as knowledge becomes deeper it becomes narrower. The extraordinary range of disciplines by earlier thinkers, such as Aristotle, Descartes, Voltaire, Condorcet, Smith, and Jefferson, is rarely replicated now. All the more reason that the process has to be *collaborative* as Bacon described it. With knowledge more fragmented and specialized, Enlightenment II can succeed only if representatives from all disciplines make the process a simultaneous teaching and learning experience. Because truth-seeking is relative and subjective, as the skeptics point out, *collaboration* is therefore required to neutralize individual cultural conditioning.

Multi-disciplinary truth searching for the improved organization of human affairs is not a
precise science. Human history is not about small misses, it is about incredible folly and violence. Aristotle provided an appropriate tolerance of error for this effort with this observation:

It is the mark of an educated man to look for precision in each class of things just so far as the nature of the subject admits; it is evidently equally foolish to accept probable reasoning from a mathematician and to demand from a rhetorician scientific proofs.186

N v Enlightenment II will labor in a time when the circumstances are propitious for humans to move from functioning at a fraction of potential towards full potential. The slavery that dominated most societies up to the nineteenth century is gone in most forms; the imperialism that dominated the world until the mid-twentieth century is over; concentrated wealth no longer has any economic logic. As nations improve the comfort and education of their people through economic common purpose, they will substitute law for force in their relations. As democratic capitalism comes to be better understood, the protectors of privilege will come to understand that more wealth can be produced for all through collaboration instead of exploitation whether domestically or internationally. The new Reign of Terror that escalated so tragically on September 11, 2001 will be terminated when citizens understand how to move the world away from ultra-capitalism toward democratic capitalism. Enlightenment II will learn how to use the technology of the Information Age to codify building blocks of knowledge. Universities around the world can cooperate and compete in a process that will present each succeeding generation with a new plateau from which to launch their improvements. Universities will compete in the sense that part of the truth seeking process will be the resolution of differences among universities or groups of universities. This is the cumulative process, the building block approach described by Bacon, and later Condorcet, that has been applied to great benefit in the sciences but not yet applied to the rational organization of human affairs.

The world's most powerful nation, the United States, will benefit from Enlightenment II because an understanding of democratic capitalism will break the political and intellectual gridlock between the left and the right. Economic freedom, the capacity to maximize wealth, and the emphasis on personal responsibility are politically and intellectually attractive to the right, while the opportunities for all, meritocracy, and broad distribution of wealth are attractive to the left. After finance capitalists and the institutional investors recognize that long-term accumulation of wealth is best accomplished through democratic capitalism, only the speculators will support ultra-capitalism. After the collectivists realize that their mission is best accomplished by democratic capitalism, only those motivated by power will support collectivism.

The challenge for new philosophers in Enlightenment II is to validate the goal and specify the means. New philosophers can identify the kinetic opportunities to redirect the collectivists' energies into workable ways to improve lives; and they can redirect the creative energies of finance capitalists, shorn of special privileges, to support of world economic growth. In this assimilation and repackaging of existing forces the new philosophers will engage in "the rational investigation of the truths of being, knowledge or conduct," leading to "a system of principles for guidance in practical affairs." \(^{187}\) In other words, the new philosophers will be true philosophers.

Chapter 5

Conservatism, Collectivism or Liberalism

Socialists increasingly recognized the incurable economic inefficiency of central planning; collectivists then simply discovered that redistribution through taxation and aimed financial benefits was an easier and quicker method of achieving their aims.

— F. A. Hayek188

Conservatism, though a necessary element in any stable society, is not a social program; in its paternalistic, nationalistic, and power-adoring tendencies it is often closer to socialism than true liberalism, and with its traditionalistic, anti-intellectual, and often mystical propensities it will never, except in short periods of disillusionment, appeal to the young and all those others who believe that some changes are desirable if this world is to become a better place.

— F. A. Hayek189

The system that can eliminate material scarcity, elevate spirits, unify people, and stop the violence, democratic capitalism, is the means to the goals of the political philosophy of liberalism. Liberalism believes that the human species is functioning at a fraction of potential and that progress can be made toward full potential by encouraging individual development in an environment of cooperation and trust. The circumstances required for each and all to reach full potential include economic freedom, political freedom, rule of law, equal rights and opportunities, no special privileges, tolerance, progress,


representative government and the diffusion of economic and political power. It was the philosophy of the eighteenth century Enlightenment, of Adam Smith's economic system, and of the government structured by the American founders. This economic-political-philosophical system demonstrated in practice during the last two centuries that it was the means to free the mind, body and spirit.

Collectivism, the political philosophy dedicated to improving the human condition through the actions of the state, is a twentieth century phenomenon and includes communism, socialism, and central governments that collect and spend more than 25% of the nation's production. Collectivists confuse the analysis of competing political philosophies because they have coopted the term liberal while contradicting many of its principles. Collectivists do not have the liberals' optimism about people and their potential for participatory democracy and as a consequence build up the state. Collectivists do not try to reflect the will and the wisdom of the people because they believe in Plato's philosophy of governance by an elite. Collectivists treat capitalism as a generic enemy, ignore the conflict between democratic capitalism and short-term and greedy ultra-capitalism and as a result promote new government actions instead of correcting earlier government errors. Many collectivists engaged in the culture war with the conservatives contradict the liberal principle of tolerance because many revert to intellectual tyranny in pursuit of their agenda.

Hayek emphasized that in the competition among political philosophies the argument is not about the goals but about the means, not about the concepts but about competent execution. Open-minded collectivists who espouse liberal goals should examine Hayek's advice about the means to their end:

The advocacy of policies which in the long run cannot be reconciled with the preservation of a free society is no longer a party matter. That hodgepodge of ill-assembled and often inconsistent ideals which under the name of the Welfare State has largely replaced socialism as the goal of the reformers needs very careful sorting out if its results are not to be very
similar to those of full-fledged socialism. This is not to say that some of its aims are not both practicable and laudable. But there are many ways in which we can work toward the same goal, and in the present state of opinion there is some danger that our impatience for quick results may lead us to choose instruments which, though perhaps more efficient for achieving the particular ends, are not compatible with the preservation of a free society. The increasing tendency to rely on administrative coercion and discrimination where a modification of the general rules of law might, perhaps more slowly, achieve the same object, and to resort to direct state controls or to the creation of monopolistic institutions where judicious use of financial inducements might evoke spontaneous efforts is still a powerful legacy of the socialist period which is likely to influence policy for a long time to come.  

Health care and environmental pollution are examples of this point. Collectivist programs, centrally planned and micromanaged, are high-cost and frequently ineffective. Liberal plans use tax incentives to shift responsibility to individuals or companies, and can be lower cost and more effective.

Conservatism is the political philosophy that honors traditional values, protects the established order and resists change. Although conservatism in theory, supports many of the elements of freedom contained in liberalism; conservatives, like collectivists, are not true democrats as many do not believe in the ability of people to participate in their own governance.

Conservatives believe in economic freedom as long as the freedoms include the privileges that have always allowed them to make money on money and concentrate economic and political power in the process. At the end of the twentieth century American conservatives, with support by many collectivists, have accomplished an

190 Ibid., p. xxxiv.
extraordinary lobbying act by convincing the government to extend the concept of laissez-faire to making money on money and at the same time successfully lobbying the government to suspend the market disciplines that laissez-faire depends on.

Friedrich Hayek is a favorite of conservatives because of his support of economic freedom and spontaneous order combined with his understanding of the pathologies of collectivism. For these reasons, Hayek's description of conservatism should be analyzed carefully by open-minded conservatives:

In the struggle against the believers in the all-powerful state the true liberal must sometimes make common cause with the conservative, and in some circumstances, he has hardly any other way of actively working for his ideals. But true liberalism is still distinct from conservatism, and there is danger in the two being confused. A conservative movement, by its very nature, is bound to be a defender of established privilege and to lean on the power of government for the protection of privilege. The essence of the liberal position, however, is the denial of all privilege, if privilege is understood in its proper and original meaning of the state granting and protecting rights to some which are not available on equal terms to others.¹⁹¹

Conservatives in theory support the established order and traditional values, but, in practice support the traditional privileges that allow them to make money on money. Until recently this form of capitalism resulted in concentrated wealth that impeded world economic growth, later in the twentieth century, however, it grew to a size that threatened the world's economy.

Until the seventeenth century the conservative philosophy of protecting the existing order dominated. Monarchs had tyrannical power, even Divine rights, the structure was top-

¹⁹¹ Ibid., p. xxxvi.
down, command-and-control and static. The majority of people were uneducated, the work done by slaves, serfs or wage-slaves. The European warrior state that evolved in the seventeenth century was an extrapolation of this primitive social structure where governments were structured to attack or defend. Concentrated power allowed the state to control, coerce, and frequently exploit the people. Emperors were economically motivated to attack other nations, steal their riches and enslave their people.

Demonstrating that tyranny cannot forever suppress the human urge toward freedom, liberalism began to change society in the seventeenth century. The freeing of the mind can be traced from the seventeenth century when Descartes advanced the humans' capacity to use reason to improve their circumstances. In time the freeing of the mind produced the technological progress of the Industrial Revolution where multiples of growth and productivity began to free humans from primitive needs.

Descartes was a mathematician who believed what he could prove. His rationalism evolved into modern forms of constructivism, the idea that the ideal is reached through a design of the perfect state. David Hume and Adam Smith were critics of rationalism as they believed that understanding human action, not human design, was the key to social progress. Ultimately it is a question of what works best. *Liberalism* as the philosophy, and democratic capitalism as the means, frees the individual to develop and contribute whereas both *collectivism* and *conservatism* restrict human freedom. The social progress produced by spontaneous order from human freedom still depends on a human design of the state but in this case it is a state where powers are limited and the design is for maximum freedom. F. A. Hayek, the great proponent of spontaneous order, still endorsed functions of the state similar to the *collectivists*. In Hayek's design, however, the state aided the individual in participating in their own development. It was government *of, for and by* the people.

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In the seventeenth century, Englishman John Locke wrote of the inalienable rights of all humans and the need for government of their choice. England led the way in limiting the powers of the monarch with their constitutional monarchy that encouraged Enlightenment thinkers from Voltaire to Jefferson. The new liberal philosophy was the foundation for the American democratic republic that successfully showed the world the benefits of freedom. Jefferson's respect for independent thinking, educated, virtuous farmers emphasized self-development as part of the foundation. Voltaire's lifetime devotion to tolerance emphasized the necessity to position individual development within a harmonious whole. During the eighteenth century the traditional tyranny over mind, body, and spirit supported by conservatism was thus challenged by the liberalism of "life, liberty, and the pursuit of happiness" of the American Revolution and "liberty, equality, and fraternity" of the French Revolution a few years later.

By the end of the eighteenth century the goals of the liberal philosophy were clear and the means specified. Adam Smith had shown the way to economic freedom and a rising standard of living for all. Thomas Jefferson and the founders had put in place the political freedoms that complemented the economic freedom. Voltaire had spent a lifetime emphasizing tolerance of the views, religion, ethnicity of others as fundamental to liberalism. Voltaire's protege the Marquis de Condorcet summarized these liberal principles in his Tenth Stage (Chapter 3). The way to a world of peace and plenty was clear at the beginning of the nineteenth century and was supported by growing democratic momentum where the people were sovereign. Both Adam Smith and Thomas Jefferson were emphatic that according to liberal principles government must not intrude on individual and economic freedom, but they were also clear that the government was responsible to assure good education and health for all citizens. Smith was also clear that money must be a stable medium of exchange, capital for investment must be patient, and that speculators must be controlled by the government in order to sustain economic growth. Beyond that, Smith joined Jefferson in sensitivity to government's tendency to grow too large:

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Little else is requisite to carry a state to the highest degree of opulence from the lowest barbarism, but peace, easy taxes, and a tolerable administration of justice; all the rest being brought about by the natural course of things. All governments which thwart this natural course which force things into another channel or which endeavor to arrest the progress of society at a particular point are unnatural, and to support themselves are obliged to be oppressive and tyrannical.194

Adam Smith was later translated incorrectly as the conservative defender of generic capitalism, even the apologist for greed. Not true; Smith was a liberal not a conservative. Beatrice Webb reflected in 1886:

The Political Economy of Adam Smith was the scientific expression of the impassioned crusade of the eighteenth century against class tyranny and the oppression of the Many by the Few. By what silent revolution of events, by what unself-conscious transformation of thought did it change itself into the 'Employers' Gospel' of the nineteenth century?195

Beatrice Webb's celebration of Smith's liberalism was supported by Carl Menger, the first of the Austrian economists who later included Ludwig von Mises and F. A. Hayek. Menger commented, "There is not a single instance in A. Smith's work in which he represents the interest of the rich and powerful as opposed to the poor and weak."196

German professor Immanuel Kant knew that the liberal movement from violence to economic common purpose and freedom would reach full potential only if there was a cooperative attitude and structure among nations. Proof that there was no longer a need


196 Ibid.
to battle over finite resources was not sufficient if the new structure was not powerful enough to suppress the traditional use of force for perceived national purpose. Kant proposed a moral imperative in respect to the rule of law displacing war:

Reason from its throne of supreme morally legislating authority absolutely condemns war as a legal recourse and makes a state of peace a direct duty, even though peace cannot be established or secured except by a compact among nations.197

Experience had demonstrated that all freedoms depend on discipline and that similarly an improving world through economic freedom depends on international law to expedite commerce and prevent violence. Any law to be effective must be reasonable and serve the general welfare, but ultimately it has to have an element of coercion that gives real meaning to law. At the world level this coercion must represent democratic agreement and multilateral action.

By the middle of the nineteenth century the economic and political freedoms of liberalism had validated its capacity to improve the comfort and quality of lives. The world seemed poised to release the latent power of people and accelerate momentum towards individuals, companies, and governments reaching full potential. By mid-century, however, it was apparent that the conservative resistance to change, and protection of privileges, was impeding the momentum of liberalism and limiting its benefits. Although democratic power was growing it was not used to reform the concentration of power from government privileges, and the diffusion of economic and political power was limited. Both John Stuart Mill and Karl Marx proposed emancipating the worker through economic freedom. This liberal solution would increase the workers’ contribution to the creation of wealth as well as their participation in the increased surplus. Marx and Mill both believed that greater worker ownership would purge the inherent flaw of capitalism that had persistently concentrated wealth. Mill extrapolated his refinement upon the capitalistic system of private property and

competition. Marx, on the other hand, had little knowledge of how to relate the task to be accomplished with the resources of time, money, and trained people required, and consequently based his reform on tearing down the entire infrastructure. Marx was a collectivist designing the perfect state; Mill believed in liberalism, an evolutionary progress through spontaneous human action.

Many in the intellectual community were excited by Marx's legitimate criticism of capitalism and initiated forms of collectivism as their response. These collectivists used liberal slogans but abandoned their liberal obligation for reform by ignoring Mill's solution. Instead of limiting the powers of the state consistent with the liberal philosophy of Smith and Jefferson, the collectivists steadily added to the powers of the state.

During the twentieth century liberalism continued to demonstrate its ability to improve lives. In many companies variations of Mill's worker participation were tried with success. Democratic capitalism received a new thrust with the advent of the Information Age whose dependence on the cognitive power of the people made the democratic capitalism culture a competitive necessity. The validity of these liberal principles was confused however, because the collectivists continued to use the word in support of their statist contradictions. Despite continued evidence that the goals of liberalism could be attained through the means of democratic capitalism, the system continued to function at a fraction of potential as conservatism was able to sustain its government privileges and share political power with the collectivists. In mid-twentieth century, the world seemed to be moving toward communism and socialism as the social contract that eliminated the contradictions and excesses of capitalism. Most of the intellectual community in capitalist countries such as Great Britain and the United States regarded this movement towards collectivism and away from conservatism as inevitable progress.

Socialism and communism, more extreme forms of collectivism, became the dominant philosophies, but later in the twentieth century the fatal flaws of central planning became apparent. These systems, founded on noble purpose, were unable to deliver on their promises and instead caused extraordinary economic and social damage. They failed
because they contradicted the basic human urge for freedom and most of the principles of the freedom philosophy of liberalism. People deprived of freedom did not produce and innovate and the central state proved a poor substitute for individual spontaneous choice in economic planning.

Although the events of the twentieth century had demonstrated that central planning in all forms works poorly, collectivism persisted in its effort to extend the powers of the state. This can be measured by the percentage of the nations' total production taken in all taxes. Before World War I, none of the nations in Europe took more than 15% of its wealth in all taxes; federal, state, and local; in the United States it was about 3%! At the beginning of the twenty-first century, taxes in Europe ranged from 50% to 63%, and are over 30% in the United States. By comparison, Singapore, one of the world's most prosperous nations, collects about 18% of its nation's production with social programs depending heavily on personal responsibility and forced savings.

Reporter Peter Brinelow identified the late twentieth-century surge of collectivism:
"Fueled by optimism about what governments could accomplish, the industrial nations embarked on an orgy of government spending. The optimism has faded, but the orgy is not over." 198

The events of the twentieth century provided empirical evidence that more freedom works better than less freedom. Combined with the failure of communism and socialism this encouraged many to feel that the world was moving toward economic freedom and economic common purpose, even an *End of History*. 199 The celebrating was premature, however, collectivism continued gaining strength in a less visible but more insidious form with the state making additional intrusions on economic and political freedoms. Hayek described this collectivist regrouping after the failure of communism and socialism to pursue their philosophy through taxation and redistribution of wealth for social purpose:

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The defeat of the onslaught of systematic socialism has merely given those who are anxious to preserve freedom a breathing space in which to reexamine our ambitions and to discard all those parts of the socialist inheritance which are a danger to a free society. Without such a revised conception of our social aims, we are likely to continue to drift in the same direction in which outright socialism would merely have carried us a little faster.\footnote{Hayek, Road to Serfdom, op. cit., 1956 preface, p. xxiv.}

Hayek was right again. Measured by the amount of the nation's wealth collected by the government, then redistributed in the directions of their choice, this collectivist momentum has continued. In the 1980s, conservative President Ronald Reagan was the sworn enemy of collectivism, but the best his administration could do in eight years was to slow the momentum.

In the decade before the Reagan administration federal government spending was $2 trillion. By 1990 it was over $1.2 trillion. It was estimated that "in 2000 total federal, state, and local government spending was $2.75 trillion; as government regulation cost $1.1 trillion, the total cost of government intervention was $3.86 trillion. In other words, the portion of the nation's real income consumed by government was a staggering 45.4 percent.\footnote{Patrick Basham, "It's the Spending Stupid." CATO Briefing papers #64, July 16, 2001, p. 5. Government spending figures based on U.S. government budget, fiscal year 2002; regulatory expenses based on a Washington University Study.}"

It is these huge numbers, the rate of growth in the twentieth century, and lack of application of Information Age technology to bureaucratic operations that gives me confidence that the government could reduce expenditures to under 25% of the GDP and, at the same time, do a more effective job in health, education, and environment.

Early in the twenty-first century, collectivism and conservatism energized each other by examining the excesses of the other but united in sharing political power. \textit{Liberalism}
continued to demonstrate its economic and social logic but became dominated by the power concentration of the *collectivists* and *conservatives*. Both Democratic and Republican political parties in the United States have abandoned *liberal* principles in practice. Individual freedom and responsibility are in retreat while the size of government continues to grow despite the rhetoric. The political gridlock is matched by a culture war between the *conservatives* and *collectivists* using liberal jargon, although this culture war is also marked by abandonment of *liberalism*. Tolerance so precious to Voltaire is ignored and in its stead are versions of intellectual tyranny in the universities that are supposed to be the seats of true *liberalism*. The process of truth seeking initiated by Aristotle, refined by Descartes and Bacon and completed by the Enlightenment is replaced by superficialities and anger.

Hayek commented on how thoroughly the *collectivist* in the United States had kidnapped the proud term liberal:

> In the United States, where it has become almost impossible to use  
> ’liberal’ in the sense in which I have used it, the term ’libertarian’ has been used instead. It may be the answer; but for my part I find it singularly unattractive. For my taste it carries too much the flavor of a manufactured term.\(^{202}\)

Hayek went on to describe his frustration at finding an appropriate substitute to *liberalism* to describe the system favoring free growth and spontaneous social evolution. Perhaps *liberals* have tried too hard to find a substitute rather than refusing to give up the term. It is harder for a *collectivist* to define *liberalism* in a way consistent with their philosophy than it is for a *liberal*. A battle over the definition and use of the term *liberal* by the *collectivists* and liberals can force needed examination of their differences. The political philosophy that inspired the Constitutional Monarchy of England, the American and French Revolutions should not be surrendered without a battle. In fact, examination of the meanings of *conservatism*, *collectivism* and *liberalism* should be a part of citizen

education at all ages. Nothing is more fundamental to the success of a democratic republic than clarity and adherence to the citizens' political philosophy.

Where the collectivists stole the good word liberal for their statist purposes, the conservatives stole the good words free markets in order to obtain privileges to make more money on money in the shortest time. These are not word games because at the beginning of the twenty-first century the collectivists continue to extend statist central administration at the expense of individual freedoms, while the conservatives support the dominance of ultra-capitalism at the expense of economic freedoms.

The conservatives are right about many things but are frequently so rigid and righteous that the real debate is never joined. The collectivists have admirable goals but continue to ignore that reform requires understanding of the superior economic system, and how to purge the privileges that concentrate wealth. The conservatives claim to have won the intellectual battle based on economic freedom, but ignore the two billion people living in misery, and the escalating social tensions caused by the visible greed of ultra-capitalism. The collectivists search for a new identity not recognizing that it is liberalism in its original form.

The world made a bad turn in the late nineteenth century because it adopted collectivism and failed to reform capitalism supported by the conservatives. The bloodiest century in human history was the result. Early in the twenty-first century, the means to a near perfect world has been identified and validated, but the United States is leading the world in another bad turn by supporting the wrong capitalism, a contributing cause to the attack on America on September 11, 2001. Collectivists, who share political power, have yet to learn enough about fiscal and monetary policies to institute needed reforms. If the facts were known and presented the political constituency available to support this reform would be a large majority, as they would embrace a rededication to the original principles of liberalism. Politicians of both parties who so love polls would still find near unanimous citizen support for these principles of the liberalism of the founders:
• Economic freedom
• Political freedom
• Rule of law
• Tolerance
• Representative government
• Limited government
• Equal opportunity
• No special privileges that concentrate wealth
• Broad wealth distribution that sustains economic growth
• Universal education

_A matrix examination of how the competing philosophies of conservatism, collectivism, and liberalism affect government, economics, and the culture._

This matrix examination is not based on precise definitions but rather general tendencies. Hayek argued that _conservatism_, _collectivism_, and _liberalism_ are not, as popularly presented, positions on a political spectrum from left to right, but are rather competitive and in many respects mutually exclusive concepts. At the end of the twentieth century these competitors could be measured and held accountable presumably with the superior performer becoming the surviving political philosophy for the twenty-first century, and the new millennium. On the record _liberalism_ should be the dominant philosophy as it is the cultural and political foundation for the successful American democratic experiment and the economic foundation that has demonstrated the optimum creation and distribution of wealth.

• _Government_

_Political power:_ The _collectivists_ concentrate political power and use it for their social missions. Conservatives concentrate political power and use it to concentrate wealth. _Liberals_ seek to limit and diffuse political power. The _conservatives_ and _collectivists_ combine in a government by the "special interests." Aristotle warned about any
government dominated by the extremes of wealth or poverty believing that it would be unable to serve the general welfare. The United States has evolved into that political trap. The middle class, preferred by Aristotle as the group best able to serve the general welfare, is usually ignored in the political process because the majority has no Washington lobby. The majority can, of course, vote but the agenda has already been defined by the "special interests."

*Forms of government:* A democratic or authoritarian government can be liberal in the practice of economic freedom. Authoritarian governments with a dedication to economic freedom, in time will move to political freedoms. *Conservatives* proclaim the benefits of minimum government and economic freedom but in practice use government to concentrate wealth. *Collectivists* steadily grow the size and scope of centrally administered government.

*Missions of government:* *Collectivists* believe the mission of government is improving the human condition, in practice they see no limits to government micromanaging this mission. *Conservatives* believe that free people can improve their own lives if the government gets out of the way. They contradict this mission by successfully lobbying special privileges. *Liberals* believe that the mission of government is to support economic freedom by discriminating between what should be controlled, the monetary system, and what should not be controlled, commerce. *Liberals* believe the government is responsible to help provide the education, good health, and economic opportunities for each to fully participate, and to help those whose cannot participate in the benefits of economic freedom.

*Participatory democracy:* *Liberals* and *conservatives* regard it as the low-cost, effective way to accomplish social objectives. *Collectivists* prefer state directed programs. Participatory democracy has demonstrated its superiority over top-down programs when government does *with* people not for people. Participatory democracy is an old concept in the American culture but has gradually disappeared as state directed programs drive it out and people are seduced away from personal responsibility. In many cases the rigid
rules of bureaucracy suffocate cooperative programs.

In the 1830s Tocqueville anticipated this slip from democracy into bureaucracy:

> When the government covers the surface of society with a network of small complicated rules, the will of man is not shattered but softened, bent, and guided; men are seldom forced by it to act, but they are constantly restrained from acting. Such a power does not destroy, but it prevents existence; it does not tyrannize, but it compresses, enervate, extinguishes and stupefies a people till each nation is reduced to nothing better than a flock of timid and industrious animals, of which government is the shepherd.\(^{203}\)

**Tax and fiscal policies:** Conservatives understand these matters in depth and join with Wall Street representatives of both parties to design policies for their benefit. Most collectivists do not understand these policies and instead of reforming them for better wealth creation and distribution they concentrate on taxing and spending. The economic freedom of liberalism depends on tax and fiscal policies that support democratic capitalism and purge the privileges of ultra-capitalism.

*Laissez-faire*, also known as the "market economy:" Conservatives support it, collectivists oppose it. Liberals believe that it works well in building and selling things if the government provides a medium of exchange that is stable, and capital for investment, that is patient. Conservatives have perverted *laissez-faire* into "free capital roaming the world" by deregulating at the same time that market disciplines have been abrogated, the result threatens world economic growth. Collectivists use *laissez-faire* or the "market economy" as shorthand for the excesses of ultra-capitalism and in support of more government action. Most collectivists do not have the education or the interest to trace the excesses that they target to bad government policies. The result is a further proliferation of government mistakes instead of correction of earlier mistakes.

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Efficiency of governments: Liberalism is the most efficient form of governance because it releases the productivity and innovation of motivated people. With liberalism both commerce and government are structured to provide opportunity for the greatest individual development in a harmonious whole. Collectivism is inefficient because it cannot assimilate and act on information centrally, and it suffocates the spirit and vitality of the people. Conservatism is inefficient because finance capitalism, that it supports, concentrates wealth and deflects capital to speculation. The feeling of unfairness from wealth concentration causes social tensions, demotivates people, and prevents a sense of common purpose.

Nationalism: Many conservatives are nationalistic and xenophobic. Hayek felt that nationalism was shared between conservatives and collectivists: "It is this nationalistic bias which frequently provides the bridge from conservatism to collectivism." Liberals may be patriotic but are tolerant for other nations or cultures to be free to improve the lives of their people in the manner they chose. In 2001, both conservatives and collectivists are supporting a nationalistic American foreign policy based on unilateral actions and protection of unexamined "sovereignty." This policy will hinder the multilateral influence of the U. N. just as it destroyed the League of Nations after World War I. It is a policy that contributed to the September 11, 2001 tragedy.

Imperialism: Hayek commented on how many conservatives manage to be anti-international and imperialistic at the same time:

Only at first does it seem paradoxical that the anti-internationalism of the conservative is so frequently associated with imperialism. But the more a person dislikes the strange and thinks his own way superior, the more he tends to regard it as his mission to "civilize" others—not by the voluntary and unhampered intercourse which the liberal favors, but by bringing them the blessings of efficient government.204

Hayek's description was applicable to conservative views that dominate American foreign policy at the beginning of the twenty-first century.

*Militarism:* As nationalism is a bridge between *collectivism* and *conservatism*, support of military power is a natural extension for both. Many *conservatives* believe that the future will mirror the past and that war and violence are unavoidable. Many collectivists oppose military spending, in theory, but support it anyway as to oppose it would be political suicide. Politicians know that people respond to a common cause but stimulating nationalistic emotions have been the traditional common cause of politicians. *Liberalism* recognizes a dangerous world but differs by believing that a world of peace and plenty is possible and that economic common purpose and education can phase out the violence. During the transition multilateral military power is still a necessity.

*Economics*

*Wealth creation:* *Collectivists* impede the creation of wealth through government intrusion in the commercial process and by not reforming finance capitalism. *Conservatives* impede the creation of wealth by lobbying policies that abrogate the market disciplines that the free markets depend on and with special privileges, such as leveraged speculation, that deflect capital from economic growth. *Liberals* encourage economic freedom and through the economic system consistent with its principles, democratic capitalism, release the latent power of people to maximize the surplus.

*Wealth distribution:* *Collectivists* loudly oppose the concentration of wealth and seek government ways to redistribute it instead of reforming the government policies that allow it. *Conservatives* concentrate wealth for greedy purposes and use it to sustain their privileged position. *Liberals* distribute wealth broadly through democratic capitalism where participating and contributing wage-earners share in the improvements that they have produced. This broad distribution sustains motivation and places spendable income with those whose purchases have the greatest multiplier effect benefiting further.
economic growth.

*Free trade*: Conservatives support free trade as long as the principles of ultra-capitalism are applied, that is, treating the worker as a cost commodity and concentrating wealth. Some *conservatives* favor protectionism when short term gains are threatened. *Collectivists* are also ambivalent, some recognize the benefits of raising the standard of living in other countries, but many concentrate on lost jobs domestically and inferior working conditions in other countries. *Liberals* recognize free trade as the economic common purpose that can displace violence in the world if there is broad wealth distribution. Neither *conservatives* or *collectivists* support democratic capitalism with its addition of spendable income for reciprocal purchases that could make free trade a universal benefit.

*Culture*

*Common ideology*: Many believe that society needs a common ideology to sustain and improve itself. *Conservatism* helped the American democratic experiment succeed with its emphasis on freedom, personal responsibility, education, traditional values, and hard work. Despite an improving standard of living, however, most Americans recognized an unfair distribution of wealth that contradicts the positive parts of *conservatism*. *Collectivism's* mission is dedicated to improving the general welfare, a common ideology, but in practice instead of purging the imperfections of capitalism, *collectivism* tries to solve the unfair distribution of wealth by taxing and spending it. In this process instead of stimulating a sense of common purpose *collectivism* produces an adversarial environment and erodes the sense of personal responsibility by conditioning many to a victims' complex. *Liberalism* was the common ideology that resulted in the extraordinary success of the American democratic experiment. At the beginning of the twenty-first century it is obscured by the power sharing of the *conservatives* and the *collectivists* but *liberalism* is still the common ideology of the majority of people and can again be the uniting force.
**Attitude about people:** Collectivists construct a government to control individual lives. By their actions they demonstrate that they do not value highly the abilities of ordinary people to participate in their own governance. The conservative view began with Alexander Hamilton in which a power structure of finance capitalists ran the country and avoided the confusions of the role. Hayek understood this view:

The conservative rests on the belief that in any society there are recognizably superior persons whose inherited standards, values, and position ought to be protected and who should have a greater influence on public affairs than others.\(^{205}\)

The *liberal* is not an egalitarian but believes in an aristocracy of talent and virtue who, however, must prove their merit and the right to lead in a competitive environment with equal opportunity for all and privileges for none.

**Equal Opportunity:** The *collectivists* have a static view that all differences in social condition that lead to unequal opportunities are solvable by top-down government solutions. This approach has a poor record because in many cases it encouraged a victim's attitude that eroded the sense of personal responsibility. The *conservative* ignores the realities of social condition and believes that everyone does have equal opportunity if they only work hard enough. The *liberal* has a dynamic view that the first priority is economic freedom that maximizes surplus and distributes it broadly steadily improving all lives. This priority, however, does not exclude government responsibility for the health and education of people to fit them to use their opportunities, nor does it exclude helping those unaided by economic growth.

**Rule of law:** All three philosophies support the rule of law but the collectivists and conservatives use it to extend and protect privileges. The liberal believes that the rule of law is the foundation for freedom but that laws can be dangerous things if not limited.

**Social progress:** The *collectivists* believes in social progress and are willing to design a
detailed plan to make it happen. Many conservatives fears change and believe that the future will repeat the past with war and violence inevitable. The liberal believes in social progress that will occur in a spontaneous way if people are free and the state limited. The liberal believes that the economic common purpose that will evolve from this process can eliminate material scarcity and gradually stop the violence.

*Enlightenment:* The collectivists interpreted the eighteenth century Enlightenment as a challenge to rationalize a central structure to manage human affairs. The conservative regarded the Enlightenment as a radical challenge to the traditional structure of church and state. The liberal believes that the Enlightenment proposed a truth-searching process adopted from science to ascertain the best organization of human affairs. The liberal believes that this epistemology, in place of the superficial, politicized present process, will bring people to the simple combination of economic freedom and a government dedicated to its support.

*Tolerance and diversity:* It is the nature of both collectivists and conservatists to have an evangelical view of their own beliefs and a distrust or disinterest in other views. Hayek described those who have the "diffidence to let others seek their happiness in their own fashion and to adhere consistently to that tolerance which is an essential characteristic of liberalism."206

*Religion:* Many conservatives support religious views as part of the traditional values that have been responsible for the success of the American democratic experiment. Many collectivists support a rights based society by passing laws instead of improving opportunities. Both are rigid, righteous, and evangelical and create a culture war. Liberals follow the lead of the Founders where both Republican Jefferson and Federalist Adams were honored for their opposition to religious intolerance. Hayek felt that:

> What distinguishes the liberal from the conservative here is that, however profound his own spiritual beliefs, he will never regard himself as entitled

206 Ibid., p. 407.
to impose them on others and that for him the spiritual and temporal are different spheres which ought not to be confused.207

Coming from France, where the Church and State had recently been uncoupled in a violent fashion, Tocqueville recognized the continuing benefits from its separation in the new republic:

Religion nevermore surely establishes its empire than when it reigns in the hearts of men unsupported by aught besides its native strength. Liberty regards religion as its companion in all its battles and its triumphs, as the cradle of its infancy and the divine source of all of its claims. It considers religion as the safeguard of morality, and morality as the best security of law and the surest pledge of the duration of freedom.208

*Intellectual Community*: At the end of the twentieth century the conservatives claimed to have won the intellectual debate because economic freedom had demonstrated clear superiority over the central planning of *collectivism*. The conservatives did not acknowledge that the form of capitalism that protected their privileges was concentrating wealth in record amounts and had caused a decline in the standard of living in most countries. *Collectivists* were on the defensive as they knew that central planning failed. As they had never learned how to correct government mistakes that allowed ultra-capitalism to flourish they suffer an identity crisis and search for a "third way."

The *liberal* philosophy is now more compelling than it was even at the time of Smith and Jefferson because by the twenty-first century all of its tenets had been experimentally verified. Despite this, American citizens had allowed *liberalism* to be crowded out of the political debate and agenda by the conservatives concentrating wealth and the *collectivists* concentrating political power. *Liberalism* is not dead, it is just sleeping waiting for the American people to wake it up and put it back to work.

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207 Ibid., p. 407.

208 Tocqueville, op. cit., p. 44 (fuller quote in Chapter 3).
Most collectivists sustain a hatred for unexamined capitalism and contradict the term intellectual by not analyzing the conflicting forms of capitalism. This examination would lead to government mistakes that allow the excesses of ultra-capitalism but collectivists gravitate toward government solutions not identification of government errors.

Multiculturalism and Pluralism: Collectivists treat these as the new secular religion. Conservatives tend to regard them as part of the relativistic attack on traditional values. Liberals believe that all people should have the opportunity for full participation in the benefits of economic freedom and that the state has obligations in promoting good health and education to this end. Liberals agree with conservatives in emphasizing personal responsibility and are sensitive to the proper relationship of "rights" and "opportunities." Collectivists subscribe to the pluralism that gives equal validity to different and sometimes opposing ideas and values. Conservatives believe in the efficacy of traditional values. Collectivists tend to think in relative terms, conservatives in absolute terms. Liberals believe that there are no absolutes but that careful use of the best truth-seeking process will validate that an ideal world is attainable and identify the general means to attain it.

Summary

For most of the two-century American success story there has been sufficient freedoms, both political and economic, to improve lives. During that same time, however, liberalism has been in retreat, conservatism sustained its privileged position while collectivism gained political power. At the beginning of the twenty-first century, however, the dynamic among these competing philosophies is not encouraging. The shared political power of collectivism and conservatism is adding more government, reducing individual liberty, concentrating wealth in record amounts, and allowing finance capitalists to dominate the economy. The will and wisdom of the people, based on original liberalism that should be reflected by their representatives in public policy is being ignored. Hayek explained that Hitler was able to gain power in Germany in the
1930s because the conservatives and collectivists found political advantage in sharing power. A similar power sharing is going on in the United States at the beginning of the twenty-first century.

The threat to the American democratic experiment from collectivism is slow and insidious. The threat to the world's economy from ultra-capitalism supported by both conservatives, and tacitly by collectivists, is however urgent. Many countries have had encouraging economic momentum reversed by ultra-capitalism, the protestors are becoming more numerous, and the terrorists are adding new dimensions to the violence.

For over two decades the United States has been flaunting ultra-capitalism as the "American model." Enemies of the United States have been confirmed in their view of American exploitation by an economic system devoid of social contract in which all wage-earners have been treated as an expendable cost commodity and in which the only motivation is making money on money, quickly. Ultra-capitalism supported by both conservatives and collectivists is a contradiction to the liberal philosophy because it depends on special privileges and impedes the opportunity for hundreds of millions around the world to enjoy economic freedom.

During the Cold War, America frequently violated liberal principles by supporting non-democratic governments and by refusal to participate in democratic actions by the U.N. Both of these were understandable tactics during a confrontation with a country with an avowed purpose of world domination.

After the end of the Cold War the United States did not have leaders with the vision to lead to a new world by a return to liberal policies. America continued to support oppressive governments and refrain from democratic participation in the U.N. The country that demonstrated to the world how to couple democracy and capitalism to improve lives was instead celebrating an economic "American model" that concentrated wealth in record amounts, supported governments that denied freedom to their citizens, and continued to avoid participation in democratic judgments and actions by the U.N.
Because the United States leaders lacked vision of the unique opportunities for liberalism in the new century, it engaged in non-liberal actions that threatened the opportunities.

Many were united in a sense of common purpose after the tragic events of September 11, 2001. The world was reminded of this powerful force that should be harnessed in normal times to improve all lives through economic common purpose. It remains to be learned how to capture this precious spirit other than in wars or disasters. It should not be hard to find, it is the liberalism of the Founders, and is still the political philosophy of the majority.

The following chapter traces the United States history in various events where conservatism, collectivism, or their combination, caused social and economic damage that could have been prevented by staying true to liberal principles.
Chapter 6

Power Failures (Arrogance) and Process Failures (Ignorance)

The American democratic experiment launched in the late eighteenth century was the greatest opportunity in history for humans to reach full potential. The country had land, enormous resources, and hard working people who believed that they could make a better life. The American Founders assimilated the inalienable rights of each individual from Englishman John Locke, diffusion of political power from the mixed republic of Frenchman Baron Montesquieu, economic freedom and universal education fundamental to a democratic society from Scotsman Adam Smith.

The experiment was successful improving the lives of hundreds of millions of people and validating the eternal contract where each generation was able to pass on a better world to their children. America became the model for the world, the "light on the hill." It was, however, an imperfect experiment as it departed from its original liberal philosophy and allowed impediments to limit its success to a fraction of potential.

Early in the nineteenth century non-democratic privileges were given by the government to financial capitalists that allowed a concentration of wealth that has persisted since. During the twentieth century, collectivists tried to redistribute wealth by taxation and central administration. At the end of the twentieth century, America had an opportunity to lead the world toward the benefits of economic freedom but failed. In combination, these errors limited the creation and distribution of wealth that could have eliminated worldwide material scarcity.

The mistakes that have been made that prevent America and the world from reaching full potential have been both power failures and process failures. Power failures are the arrogant usurpations of government for non-democratic purposes. Process failures are due to ignorance because of imperfect methodology in truth-seeking.

Power failures include:

- Failure to limit government privileges in fiscal and monetary policy that results in
concentration of wealth.

- Failure to limit the growth of government.
- Failure to participate with other nations in order to substitute law for violence.

Process failures include:

- Failure of reformers to learn how to couple democracy and capitalism for the greatest benefit for the general welfare.
- Failure of reformers to learn how to eliminate the privileges that allow the concentration of wealth that slows economic growth and causes damaging swings in the economy.
- Failure of leaders to understand that broad wealth distribution is necessary to sustain economic growth and make free trade a universal benefit.
- Failure of leaders to understand a new American world role as economic team leader, not cop-of-the-world.

These matters have been analyzed in previous chapters. This chapter gives examples of power failures and process failures over two centuries of the American democratic experiment. Mistakes, by definition, are correctable. It is hoped that this litany of avoidable error will encourage a rededication to the liberal philosophy and a new interest in democratic capitalism as the means to correct mistakes and lead the world toward full potential.

1818: The first economic recession in the new republic followed a pattern repeated since with the government providing privileges for finance capitalism in exchange for funds to fight the War of 1812, followed after the war by lack of government control of speculation with borrowed money, followed by the rising value of artificial assets, followed by the decline of the whole economy, followed by government actions that victimized ordinary people in order to repair the damage to the financial system. In other words, the new republic had imported the conservative financial oligarchy from Europe with all of its associated corruptions.
This episode is an example of all three impediments. The War of 1812 was a particularly stupid war with the emerging political parties fighting over whether to go to war with France or England and with the Europeans unable to settle differences by law. It was a power failure with the financial oligarchy lobbying laws that allowed them to concentrate wealth and make strikes illegal; and of liberals, Jefferson and Madison, unable to structurally limit this concentration of economic and political power.

1820: The British conservatives managed government monetary policy in order to restore the asset value of the wealthy to pre-Napoleonic wars levels. This was accomplished by hurting the ordinary people through cutting wages, causing unemployment, and raising prices. Von Mises wrote that the resulting social tensions set the stage for the emergency of Marx.²⁰⁹

This episode is an example of the economic dislocations caused by war and the control of government by the financial oligarchy to concentrate wealth. This power failure was not hard to do at that time as there was limited democratic political power and little comprehension of what the conservative establishment was doing. The social tensions provoked food riots much like the current attacks on globalization, that is, a process failure in identifying root causes.

Post-Civil War: The finance capitalists used their power to copy the brutal British practice and restore the asset value of the wealthy to pre-war levels. In order to make this action less visible they took longer to accomplish it. The conservative establishment had made huge amounts of money funding the war; they then successfully lobbied government to purge the effects of war-inflation on their assets, a power failure.

1896: The political defeat of the Populist party after two decades of trying to democratize the source of capital was an example of the political power of conservative process and the inability of the reformers to design and vote for a political agenda to provide workers and farmers access to capital. The Farmers Alliance was unable to obtain working capital from private banks despite their willingness to collateralize their farms. Conservatives regarded them as a threat to the status quo, wanted to destroy them, and did. The Farmers Alliance was unable also to get direct government assistance, a power failure in face of the lobbying

power of finance capitalism.

*World War I:* At the beginning of the twentieth century, most were optimistic that the liberal principles would prevail and that the world was becoming a better place with improving lives and the rule of law minimizing violence among nations. Senator Patrick Moynihan (D. New York) summarized this mood:

> The idea of a world by law is as old, almost, as the idea of law itself. But it was only with the latter part of the nineteenth century that it came to be seen as a practical vision and as a reasonable choice that governments might make in determining their own behavior. It is probably fair to say that at the turn of the twentieth century most statesmen in the west expected such a future for the world. It was part of the prevailing optimism of that time, and closely associated with the confident expectation that liberal democracy—with its great emphasis on law as the arbiter of relations among citizens with equal rights—would become a near universal form of government.²¹⁰

This optimism was shattered in 1914 by World War I when the rule of law proved too weak to protect the world. According to historian A. J. P. Taylor, the German, Chancellor Bethmann, the Austria-Hungarian Foreign Minister Count Berchtold, and Russian Foreign Minister Sazonov, without the constraints of either domestic or international law, started the war by daring each other in an international game of "chicken."²¹¹ Once the war had started no one knew how to stop it. While the leaders fumbled around for years, tens of millions were trapped in the trenches and either killed or wounded, including one-quarter of young Frenchmen.

This game of "chicken" was set in motion by the actions of German Kaiser William II whose jealousy of his English relatives’ naval power stimulated German armament. In time, the British did not allow a new powerful German navy to challenge their world hegemony.

According to historian Donald Kagan:

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His mother was the daughter of Queen Victoria. William came to detest her domination of his father, her preference for English over German ways, her liberal policies ... He always suspected that the British did not take him or his country quite seriously and that they accorded neither due respect and these prejudices had important consequences.212

Despite some optimism for a world of law, power was still in the hands of capricious men whose actions would result in millions of deaths, untold human agony, and severe economic damage. The world was not rational, it was out of control. The bloodiest century in human history was launched on its mad course by this power failure.

Post-World War I: At Versailles, in 1919 four men dramatized the opportunity to learn from the mistakes and put the world back on the road to peace and plenty. The French leader, Clemenceau, however, was understandably vengeful, the American President Wilson was full of impractical idealism, John Maynard Keynes could not get the leaders to heed his economic advice and Ho Chi Minh was barely visible. Woodrow Wilson's "Fourteen Points" encouraged the Germans to believe that the talks would be productive, not punitive, but Wilson's Points were treated by the rest of the participants as unrealistic propaganda.

John Maynard Keynes could see the dangerous mistakes being made in the reparations agreement that would make World War II inevitable. Keynes resigned from the British team and went home to write a book on the subject.213

Another relatively young man at Versailles, Ho Chi Minh was later to become the long-time independence leader of Vietnam who defeated both the French and the United States in Vietnam's quest for independence. Ho was deceived by Wilson's "song of freedom,"214 that is, he had the erroneous idea that Wilson's ideal of sovereignty for all nations included the Asians and an end to European colonialism. Ho presented requests that were close to "life, liberty, and the pursuit of happiness," but was ignored. The reparations agreement imposed on Germany and continued imperialism in Asia set the stage for the horrors of World War II and later the Vietnam War.


While Woodrow Wilson championed liberal principles, he is a case study in process failure. In the words of his biographer:

Wilson had little time to ponder deeply on the economic causes of war ... from the beginning of the peace process he had relegated economic matters to subordinate places ... Woodrow Wilson's first love was politics, not economics.  

Wilson's instincts were noble but his training inadequate, with his flaws including no understanding of economics, management of change, and, surprisingly for a politician, little ability to develop consensus or merchandise his ideas. Wilson died trying to get the League of Nations approved by the United States Congress. He was defeated in this effort by his political enemy, senator Henry Cabot Lodge, (Rep. Mass.).

The forces thus set in motion early in the century predestined further failures. The reparations agreement forced on Germany, together with the ineptitude of the Marxists in governing during the 1920s, allowed Hitler to take control of Germany. In Russia, Lenin stole the revolution but he died a few years later, turning Russia over to Stalin's long terror. R. J. Rummel's scorekeeping of "twentieth-century democide" recorded 20,966,000 killings for Germany and Hitler, including the ultimate horror, the Holocaust, and 61,911,000 for Stalin. All can be traced to the power failure that allowed World War I to happen and the process failure that resulted in "peace" terms that made World War II inevitable.

Russian Revolution: Russia, after the 1919 revolution, demonstrated the fatal flaws of collectivism in a dramatic and bloody way. Marx had correctly identified concentrated wealth as an inherent contradiction in capitalism and had correctly identified the solution, broader distribution of wealth by greater participation in ownership by the worker. Marx's emancipation of the worker, in practice, however, became their enslavement under a new form of state tyranny. The fatal flaws were central administration that doesn't work and statist governments that suffocated the people. This was an enormous process failure by many reformers around the world who were excited by an attack on capitalism but neglected


to learn how to refine it.

**Twentieth Century Imperialism:** The rejection of the best efforts of Ho Chi Minh at Versailles demonstrated that the Western powers were not ready to give up the presumed benefits of imperialism. The world was still dominated by predatory actions and power failures. Asia was still regarded as an opportunity for colonization. This is one thing that has changed in the early part of the twenty-first century as imperialism in its original form is terminal for lack of economic and social logic. Unfortunately, the United States had led in a new form of financial imperialism that can have the same negative effect on world economic growth and world peace. This is a power failure that allows a few to dominate policies; it is a process failure because reformers fail to learn how to modify policies.

**Humans use new technology for barbaric purposes:** The first bomb was dropped on Arab civilians near Tripoli by an Italian pilot on November 1, 1911. World War I later extended the use of planes and bombs as a new level of barbarism. The killing of innocent civilians escalated during the twentieth century to the fire bombing of whole cities, to the nuclear destruction of hundreds of thousands in Japan, to the planned destruction of villages, to the "Surgical strikes" in undeclared wars. Early in the twenty-first century religious fanatics combined pilot, plane and jet fuel in the attack on America.

These events demonstrated a world dominated by power and violence lacking a process to identify how to stop the violence.

**The Crash of 1929 and the Great Depression:** Collectivists claim that the crash and depression exposed the contradictions in capitalism and an enlightened government stepped in to save the country. Conservatives claim that the New Deal did not work and that it was only the production demands of World War II that brought the country out of the depression. The liberal view is that it was conservative government privileges to speculate with borrowed money during the 1920s that caused the crash and that it was conservative policies to regain "fiscal integrity" that exported the damage from Wall Street to Main Street. The liberal view is that the damage was so severe that the government had to take extreme damage control actions. Not surprisingly many of them did not work well. This syndrome of few making enormous amounts of money speculating followed by many

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suffering from the cure is being repeated by the IMF around the world. After finance capitalism nearly destroys the system by speculation, bankers fix the banking system only by cutting wages, raising prices, causing unemployment, stopping loans, and reducing government spending. The liberal view is that if the government had fulfilled its responsibility to control leveraged speculation the crash would not have happened or would have been of a magnitude that the draconian measures that caused the Great Depression would not have been required. This disaster was another failure to control the power of finance capitalism because the reformers failed to understand the process.

**World War II:** During the 1930s there were three incidents that led to a war that could have been avoided by a strong League of Nations. The first was the invasion of Manchuria by Japan, the next the invasion of Abyssinia by Italy, and finally the actions by Germany:

The watershed between the two World wars extended over precisely two years: Post-War ended when Germany reoccupied the Rhineland on 7 March 1936; pre-war began when she annexed Austria on 18 March 1938.218

On September 18, 1931 Japan occupied Manchuria, a part of China but not in perfect control. China appealed to the League of Nations who had no power and whose members were distracted by economic difficulties. Great Britain was a Far Eastern power but not inclined to act. The United States was not a League member, had trade relations with Japan and had signed naval treaties that gave Japan hegemony. A League commission condemned Japan "for resorting to force before all peaceful means were exhausted. The Japanese withdrew in protest from the League of Nations."219

Mussolini had been in power since 1922 but chose 1934 to avenge a humiliating defeat of Italy by Abyssinia in 1896. Abyssinia was a member of the League of Nations and appealed its case: "It was the death blow to the League as well as to Abyssinia. Fifty-two nations had combined to resist aggression; all they accomplished was that Haile Selassie lost all of his country instead of only half."220

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219 Ibid., p. 68.

220 Ibid., p. 95.
The people in Great Britain were strongly in favor of collective security and in support of
the League of Nations but from the moment that Neville Chamberlain became prime
minister in 1937 things changed. Chamberlain was a conservative who "had no faith in the
hesitant idealism associated with the League of Nations." Chamberlain and many British
statesmen tended to regard Nazi Germany as the bulwark of Europe against the Bolshevism,
or collectivism, of Russia. Chamberlain was also sympathetic with the problem of 6 million
Germans in Austria and 3 million in Czechoslovakia. Hitler became convinced that the
British would not fight over solutions to these problems. Hitler's grand plan was directed
toward Russia and it was a shock to him when Britain declared war.

Hitler could have been stopped in 1936 by a well-armed France, a well-armed Great Britain,
certainly by the two of them. But these countries had been gutted by World War I and had
demilitarized. The correct response to Hitler was collective security, international law, The
League of Nations. Hitler bluffed successfully because he understood the disarmed
condition and the mood in England and France. He would have never bluffed into a resolute
League of Nations to the shame of the United States. As monstrous a mistake as the
American boycott of the League of Nations was, it will be dwarfed, if, early in the twenty-
first century, the same sloganeering about "sovereignty" prevents the United States from
supporting collective security by the U.N. The twenty-first will be another century of folly
and violence except only worse with a few terrorists who can deliver nuclear, chemical and
biological weapons anywhere, anytime. (This was written over a year before the September
11, 2001 attack on America.)

In the build up to World War II, government mistakes were rife, both power failures and
process failures. The reparations agreement was a mistake; American actions on tariffs and
pulling capital out of Germany were mistakes; continued imperialism in Asia was a mistake;
and the deliberate reduction of military strength by England and France was a mistake. All
of these mistakes could have been compensated by the League of Nations if it had
determined support of all nations backed up by cooperative military power. The United
States aborted that opportunity by refusing to participate. The power of the people had been
usurped by a few xenophobic congressmen.

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221 Ibid., p. 134.
Post-World War II: The argument that the bloody twentieth century was the result of avoidable errors can be demonstrated both by analyzing the power and process failures and by evidence of other leaders doing it right. After World War II the United States used its power and money to repair the ravages of war and set the world on the way to economic growth and better lives for many. The Marshall Plan was one of America's proudest moments because President Truman, General Marshall, and other leaders understood history and economics well enough to make the right moves, a process success. Any criticism that it was self-serving, and in time helped the U.S. economy, misses the point, for mutually beneficial results are the essence of economic common purpose.

The United States provided the money and encouragement but left the management up to leaders in their own countries. Some argue that bureaucratic collectivists, both American and German, tried to micromanage the German recovery but Ludwig Erhard, Finance Minister and later Chancellor, was too strong and understood free market principles contained in the liberal philosophy too well. Erhard had combined the right process, the proper use of power and propelled the German "economic miracle."

The economic recovery that put the social structure back in place in both Germany and Japan demonstrates what can be done when the national mission is exclusively economic and not dissipated by an arms race and geopolitics. The German recovery also demonstrated that economic freedom in liberalism works better than the state control of collectivism: Germany's economy grew over 8%, while Great Britain, pursuing socialistic policies at that time, grew one-third of that rate.

1960s Vietnam War: 54,000 young Americans and millions of Vietnamese of all ages were killed, and many more wounded by a colossal process failure. This was confirmed by Robert McNamara, Secretary of Defense at the time. In McNamara's book *Wilson's Ghost* he describes how the government team searching truth and determining action failed the process. There was imperfect collaboration as the team did not include those with an empathetic understanding of dominant nationalism, not communism, in the motivation of vietnamese leaders and people. Lacking the collaboration, that is team members representing all points of view, the process was neither sufficiently dynamic nor reiterative in the assimilation of the truth about Vietnam.

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McNamara compared the Vietnam experience to the Cuban missile crisis where nuclear war was avoided because the team included a former Russian ambassador who provided an empathetic understanding of Russian leader Nikita Khrushchev.

McNamara has provided a self-critical examination that should serve as a case study for citizen education and leadership training. The Vietnam tragedy should never have happened. The damage from this process failure can be measured in lives lost; it is more difficult to measure the effect on American idealism and sense of common purpose but it was severe.

President Lyndon B. Johnson in secret tapes examined in a book by historian Michael Beschloss223 confirmed that the Gulf of Tonkin incident never happened. It was this alleged attack by North Vietnamese on two U.S. destroyers that stimulated Congress to give Johnson authority in 1964 to significantly expand the war. These tapes reveal that Johnson knew that the war was unwinnable at the same time he was sending more young Americans half way around the world to be killed and hurt.224

Why did Johnson and later President Richard Nixon prolong an unwinnable war? It was politically unacceptable for America to say we made a mistake, declare defeat and walk off the field. The conventional wisdom was that such actions would compromise our world power. Instead we continued to kill Americans and Vietnamese in a war that many young Americans and most of the rest of the world knew was a tragic error.

Vietnam was both a power failure (arrogance) and a process failure (ignorance). It was a misuse of power when capricious leaders were able to take actions unrestrained by domestic or international law. It was a continual process failure because the legislative branch along with the executive branch had insufficient understanding that the prime motivation of the Vietnamese was nationalism. Most did not know that Ho Chi Minh quoted directly from the Declaration of Independence in his inaugural address.

**NATO Expansion:** Late in the twentieth century the United States led in the expansion of

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NATO to three countries contiguous to Russia. These actions took full advantage of a weakened Russia and were provoked by residual conservative feelings about communism. In this area of aggressive geopolitics the conservatives can still get bipartisan support from the collectivists as the label "soft on communism" still has political currency. As communism fades into history those with the hawkish attitude that war is inevitable are restating the expression to "soft on defense" as they search for new enemies.

One of the contributing factors to World War II was the feeling among Germans that after World War I they had been betrayed in the peace negotiations. Robert McNamara, Secretary of Defense in both the Kennedy and Johnson administrations, describes both Russia and China feeling betrayed by the United States early in the twenty-first century.

Wilson's ghost has already appeared in the twenty-first century, as Russia and China have become increasingly suspicious of the United States and the West for having betrayed them, reneging (as the Russians believe) on commitments not to expand the NATO Alliance on Russia's western border, and (as the Chinese believe) on commitments to avoid supporting independence for Taiwan.225

The prescient subtitle to McNamara's 2001 book is Reducing the Risk of Conflict, Killing and Catastrophe in the 21st Century!

George Kennan was the original architect of Soviet containment at the beginning of the Cold War. Kennan commented on the NATO expansion:

I think it is the beginning of a new Cold War. I think the Russians will gradually react quite adversely and it will affect their policies. I think it is a tragic mistake.226

The Russians, Kennan observed, were depicted during the U.S. Senate debate on NATO as still eager to invade Western Europe:


Don't people understand? Our differences in the Cold War were with the Soviet Communist regime. And now we are turning our backs on the very people who mounted the greatest bloodless revolution in history to remove the Soviet regime.\textsuperscript{227}

The attack on America has fused the interests of America and Russia and may be permanent and strong enough to neutralize these mistakes which misuse American power because of a process failure to think through America's proper role in a new world.

\textit{Post Cold War-Russia:} An extraordinary opportunity for world peace and economic growth opened up in 1991 when Russia completed a bloodless revolution under Mikhail Gorbachev and prepared to move toward economic freedom. Scholars, economists, finance capitalists, government policy-makers, and journalists from the United States rushed in to dominate the design of the Russian transition. It was a process failure of enormous magnitude. In simple terms, they did not know what they were doing. The result has been an economic disaster and an unnecessary human tragedy. Ten years after the failed attempt, the situation was as follows:

\begin{itemize}
  \item Russia experienced the worst peacetime industrial depression in the twentieth century.\textsuperscript{228}
  \item For the first time in history, a fully nuclear-ready country had been destabilized.
  \item Anti-Western sentiment had never been so strong or widespread in modern Russia as it was at the end of the twentieth century.\textsuperscript{229}
  \item The economic catastrophe in combination with pushing NATO into three countries contiguous with Russia gave the enemies of freedom in Russia a strong position.
  \item Because of the economic breakdown, the possibility of nuclear disasters increased because nuclear missile sites and nuclear submarines could neither be maintained nor
\end{itemize}

\textsuperscript{227} Ibid.


\textsuperscript{229} Ibid., p. 32.
decommissioned properly.

- Russia's desperate need for hard currency increased the possibility of sale of nuclear, biological, and chemical weapons to other nations.

- U.S. actions increased pressure on Russia, China, and India to collaborate as the superpower antidote to the United States.

How could an opportunity to assist Russia in its movement to economic freedom end in an economic catastrophe and a political relationship with threatening consequences? The cause of this process failure was yet another erroneous instance of Americans acting and advising in arrogance and an appalling ignorance of the management of change and of democratic capitalism. As ultra-capitalism dominates the domestic U.S. market, it is not surprising that its corruptions were exported to Russia. In America a favorite buzz word of ultra-capitalists is "creative destruction," the Russian equivalent is "shock therapy." In this mood, according to Stephen Cohen, each error: "further undermined aspects of the seventy-year-old Soviet order—institutional, economic, human—that could have been building blocks of a reformed Russia but were instead destroyed."230

Cohen found it difficult to "explain the equally large failure of American scholars, at universities and think tanks, whose careers were devoted to the study of Russia."231 This is the process failure of the so-called experts who work from a too narrow and too shallow a range of knowledge and experience. They failed to study Edmund Burke, the eighteenth century English statesman whose notable understanding of management of change has stood the test of time. Burke predicted the social chaos from the French Revolution because they tore down too much of the structure too fast.

There were many contemporary examples, the study of which could have helped avoid the Russian debacle, including the successful transition of Singapore to economic freedom, or the long, costly conversion of East Germany to economic freedom by the competent and wealthy West Germans. The experts also ignored the example of little, financially illiterate, impoverished Albania in the early 1990s, moving in months from centuries of tyranny

230 Ibid., p. 37.

231 Ibid., p. 17.
through revolution in the name of political freedom, to uncontrolled speculation, and then social anarchy. \textsuperscript{232}

\textit{China-U.S. Relations in the Twenty-First Century:} The same need of enemies colors the \textit{conservative} attitude toward China. They are joined, however, by \textit{collectivists} chanting \textit{liberal} slogans about human rights abuses without any understanding of the improvement in human rights by the difficult movement by China towards economic freedom.

Although the United States has overwhelming military superiority over China, thousands of nuclear armed missiles instead of a few hundred, for example, the U.S. still finds it necessary to spy on China with slow coastal planes, fast high-altitude planes, and satellites. The perception that the U.S. must maintain hegemony in Asia, watch China, and keep 37,000 troops in Korea is all part of a process failure to understand how to use power as a team player in the new century.

In April 2001, a U.S. spy plane collided with a Chinese fighter plane and was forced to land in China territory. The incident was front page news for weeks and gave the military hawks a good opportunity to stimulate anti-Chinese feeling while most of the media served as midwives in a propaganda onslaught. Why it is a matter of national interest for the United States to fly spy planes along the China coast as not examined, neither was the presumption that the U.S. must sustain hegemony in Asia.

China's conversion to economic freedom has raised the standard of living of more people and democratized more villages than any transition in history. Eventually, economic freedom will lead to political freedom. Management of change from tyranny to freedom in a country of 1.3 billion people is complex and takes time. China is making the conversion slowly and carefully in contrast to Russia who accepted U.S. advice to move quickly that resulted in an economic and social disaster.

American leaders did not understand that World War II was the end of Western imperialism in Asia; that error led to Vietnam with all of its tragic consequences. Now, instead of applauding China's steady movement to freedom, while being patient with its faults, American leaders still do not understand the forces of history. China will challenge the

United States as the world's largest economy during the 21st century. It will now have the resources to resist the humiliations by Western nations that have regularly occurred during the past two hundred years.

The U.S.-Taiwan Relations Act of 1979 was negotiated and signed in the middle of the Cold War when communism still had aspirations for world domination. Communism failed and communist countries like China began the long process toward economic freedom as it was clear that this was the only way to improve lives. Despite this dramatic change in circumstances, the U.S. leaders in 2001 are still referring to the 1979 Taiwan Relations Act. Following its terms, ambiguous as they may be, can be construed as "national honor." This is the same slippery slope starting with earlier agreements that brought the U.S. into war with Vietnam. Young people can be killed and hurt, again, because of the process failure of uncomprehending leaders and the media.

China faces a difficult transition. While it has made great progress it has to grapple with the reality of government tax revenues of only 13.6% of GDP, a fraction of the American-European pattern. This does not provide a big safety net for the dislocations caused by privatization.

As reported in *The Economist*:

> Yet over the past 20 years or more, for all its obvious faults, the world's biggest Communist Party has also conspired to increase the GNP of the world's most populous country more than seven-fold, lifting many millions of Chinese out of poverty.

> China's central government receives a paltry 13.6% of GDP in taxes, nowhere near enough for the reforms of education, pensions and welfare it plans.233

Chinese leaders understand that economic freedom is the only way to improve lives in the Information Age. Economic freedoms will gradually produce political freedoms. The last thing China desires with its small tax revenues is a big budget for a military build-up. That

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233 "As China changes, the Communist party must change with it or perish." *The Economist*, June 30, 2001, p. 9.
will happen only in response to American uncomprehending belligerence, a power failure and a process failure.

1990 Iraq: On July 25, April Glaspie, the U.S. ambassador to Iraq, went to a meeting with Iraqi officials in Baghdad and was surprised to find that she was meeting with Saddam Hussein. Communicating through the Iraq translator the ambassador encouraged Hussein to settle the problem with Kuwait peacefully but made it clear that the U.S. regarded it as a border disagreement between Arab states in which the U.S. had no opinion or position. Eight days later, Iraq invaded Kuwait.\(^{234}\)

The result of this process failure was the Gulf War, a stunning victory for President George Bush but the beginning of over a decade of economic sanctions that resulted in the malnutrition of Iraqi children and high-level bombing that killed other civilians.

The terrorists of September 11, 2001 claimed that these American actions had killed one-half million Iraqi children, probably an exaggeration but any deaths of children are unacceptable and the U.S. had provided its enemies with a propaganda cause to inspire more hate.

Actions have consequences. Was the misinformation and misdirection by a poorly informed ambassador in 1990 the cause of the terrorists' attack in 2001. Obviously not, but it was part of a continuing process failure and it was a contributing cause.

1990s: American/U.N. confusion about who, when, where, and how to use force in Yugoslavia and Africa.

In January 1990, the Yugoslavia Communist League disbanded. The march from tyranny to economic freedom was spreading from Eastern Europe. First Slovenia became independent with the encouragement of Germany and without any opposition from the U.S., then the movement moved south through Croatia, Bosnia, and Kosovo, in each case the desire for independence was opposed by Serb leader Slobodan Milosovic's plan for Serbian dominance. Croatia fought on the German side against the Serbs who fought on the Russian side in World War II. Both had memories of reciprocal atrocities in the battles between

\(^{234}\) Terence C. Jeffrey, "Do We Need War With Iraq?" *Human Events*, week of October 29, 2001, p. 7.
European Christians and the Orthodox Slavs. Bosnia was different, this was a battle between the Serbs and Muslims and became, not a battle but genocide. Kosovo was a further extension of Serbian ethnic cleansing of the Albanian Muslims.

Yugoslavia provided a case study in the inability of the U.S. to be integrated into a U.N. effort to preserve peace. The success of every complex task depends on attitude, the capacity to respect the views of others, to listen, and then to cooperate. Most world leaders in nations and the U.N. did not like the American attitude which they thought to be: "The smug, remote, superpower whose attitude on most things was don't call us, we'll call you, and by the way, we'll make all the important decisions."\(^{235}\)

The "Powell Doctrine" became a popular concept. It was promulgated by General Colin Powell when he was Chief of Staff during the Gulf War and was based on the bad experiences from the Vietnam War. Powell was later Secretary of State in the George W. Bush administration. The doctrine went back to fundamentals emphasizing that the mission, the resources to accomplish the task, the communication among parties, and an exit strategy all had to be clear and the execution of high quality. As basic as these concepts were they were all violated continuously during the decade of the Yugoslavian devolvement. There were at least eight parties involved, each with a different agenda, including U.S. politicians, U.S. military, U.N., NATO, Great Britain, France, and Germany. Other European Community nations were involved to some extent as NATO members but Russia, the only nation with influence over the Serbs, was deliberately excluded.

At the core the problem was that the U.S. which had pioneered democratic principles such as, "one person, one vote" was unwilling to participate in democratic actions in the U.N. Xenophobic congressmen considered any "world order" an infringement on "national sovereignty," as they defined it, forgetting that in a democracy the people are sovereign.

Human history confirms that all freedom must have a discipline. At the government level there must be law and structure for freedom to flourish. This is particularly true at the world level where the lack of law and structure has resulted in continuous violence among nations and people. The American people understand this and polls have shown large majority support for the U.N.

Any opportunity for congressional support for multilateral action with the U.N. received a severe blow in 1992. With typical confusion of mission and who was doing what to whom, American soldiers were sent to Somalia on a humanitarian mission and then killed and desecrated by being dragged through the streets with American people watching on live television. David Halberstam commented:

American help, if it came at all, would come later rather than sooner, and it would come smaller rather than larger. It was also a tragedy for U.S.-U.N. relations, always fragile, but increasingly important if the United States was to become involved in peacekeeping missions in marginal parts of the world. The Congress hated it. Mitch McConnell, an influential Republican senator, was quoted as saying, `Creeping multilateralism died on the streets of Mogadishu.'

Yugoslavia was also too little, too late, and too uncoordinated. Early and emphatic action could have stopped Milosevic, just as it could have stopped Hitler in the 1930s, but Americans would not join in U.N. actions. For a considerable time American air power was not used because the Europeans demanded that the U.S. also put troops on the ground along with the rest of them. After Somalia, the threat of `body bags' was too great.

American unwillingness to cooperate in multilateral actions with the U.N. in 1995 contributed to over 800,000 Tutis being murdered by the Hutus in Rwanda. Halverstam commented on bureaucracy in the midst of genocide:

Americans were supposed to help out with material. Armored personnel carriers were to be sent to Rwanda to enable the U.N. troops to get around the country. But their movement through the pipeline was deliberately impeded by debates over the terms of the lease, the color of the APCs, and what kind of stenciling they would have.

*Jesse Helms vs. the U.N.*: On January 20, 2000 Republican Senator from North Carolina,

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Jesse Helms addressed the United Nations Security Council. Helms presumed to speak for the American people, and at the same time apparently, the executive branch. Helms warned that the U.S. overdue bill of $926 million would be paid only "upon the implementation of previously agreed common-sense reforms." He concluded his remarks by saying that he "wanted to be candid with you," if the U.N. did not shape up it could result in "eventual U.S. withdrawal."

The world has been dominated by violence throughout history because of the inability to put in place international law backed up by multilateral action. Republican senator from Massachusetts Henry Cabot Lodge killed the opportunity after World War I when he led the charge to keep the U.S. out of the League of Nations. At the end of the century American citizens are allowing another Republican senator to undermine and insult the U.N.

Robert McNamara was Secretary of Defense during the Vietnam war and has spent the rest of his life trying to understand how this great country went so wrong. He was later President of the World Bank and has combined these experiences in *Wilson's Ghost* to recommend specific U.N. reforms, for example:

The Security Council must be expanded, become more representative, and the veto of the (current) five members must be phased out and replaced with decision making by a `qualified' majority—for example, 75 percent.\(^{238}\)

McNamara knows that the confusion begins with the U.N. and that any opportunity for close cooperation will need change. After the September 11 attack on America the sense of world common purpose is good, the opportunities for U.N. reform better, and more Americans are aware of the necessity to modify our world position from unilateral arrogance to strong team player.

*Late twentieth century*: Ultra-capitalism, the ultimate effort to concentrate wealth became dominant in the late twentieth century. The two impediments to a world of peace and plenty, concentrated wealth and force not law in the relations among nations were both made worse by the increasing dominance of ultra-capitalism. Wealth was concentrated in the U.S. in record amounts but the most tragic damage was the effect of ultra-capitalism on

emerging economies, many of which were growing at rapid rates. All over the world hundreds of millions of lives were being improved until lethal finance capitalism struck reversing economic momentum and provoking political and social tensions.

Lethal finance imperialism is defined as conservative privileges that includes excessive liquidity where too much uncontrolled short term or hot money overheats an economy with money going into increasingly risky projects and speculation. This excessive liquidity that puts an economy into overdrive is assisted by the suspension of market disciplines. Insurance bailouts and subsidies over a period of a few decades have lowered the sensitivity of lenders to imprudent loans. These market disciplines were suspended at the same time that finance capitalism was deregulated and, pressured by the United States, traditional protections such as cross-border controls of money were torn down. Weaknesses developing in the economy attract the highly leveraged speculators who can cause a precipitous drop in a local currency. By now the power of these leveraged speculators to overwhelm the defensive efforts of central banks to defend currency is so well known that sometimes just the threat of a speculative attack will drive a currency's value down. After the damage the bankers follow the usual script of hurting ordinary people in order to regain "fiscal integrity," that is, wages drop, unemployment goes up, prices go up and the state is constrained from spending money to help people and the economy recover.

In the 1990s Francis Fukuyama in his End of History239 proposed a world after the demise of communism moving toward economic freedom and improving lives. Samuel Huntington in The Clash of Civilization240 saw instead a world devolving with ethnic and religious animosities among more angry people with more terrible weapons causing violence and economic and social upset. Indonesia was a model for Fukuyama's thesis until the out of control international financial system destroyed their economic momentum and made them, instead, a model for Huntington's thesis.

1997: Indonesia 40-10-50: Indonesia was one of the Asian tigers moving smartly toward economic freedom with rapid growth rates steadily improving lives and building a sense of common purpose. In a few decades the number under the poverty line decreased from 40% to 10%. After lethal financial imperialism, ultra-capitalism, struck, in a few months the

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number went back below 50%. The fragile political structure collapsed and the ethnic and religious tensions that had been declining in inverse ratio to the improving standard of living then erupted.

Indonesia is the world's fourth most populous nation. With 225 million people it ranks behind only China, India and the United States. It is also the world's largest Muslim country.

Hundreds of thousands of unemployed youths are being recruited by terrorist groups, including representatives of Bin Laden.

In early October 2001 a group of young Indonesian men met at a safe house on the outskirts of Jakarta. Recruits of a militant Islamic group called Hizbulloh Front, they had come to get training in hand-to-hand combat.241

According to their leader, when they are ready they will sweep all Americans out of Indonesia "because of your government's arrogance you cannot safely live in Indonesia."242

It is doubtful that the members of the Hizbulloh front understand how the combination of uncontrolled hot money, leveraged speculation, deregulation at the same time that market disciplines were suspended, and a lack of a stabilizing mechanism in international currency have caused their economic and social chaos. It is doubtful that they understand that once a country goes into economic decline, IMF based actions make the financial structure better but make the social problems worse.

Like the globalization protestors, young people in Indonesia sense that the U.S. led short-term and greedy ultra-capitalism has caused their country to go backwards economically and socially. The reality that it is more a series of avoidable mistakes, a process failure by the United States government instead of a conspiracy, is of no interest.

Is ultra-capitalism the direct cause of the terrorist attack? No, but it is a contributory cause.


242 Ibid.
It is now a direct cause of social tensions that can make Osama Bin Laden's dream of a worldwide Islamic revolution more likely.

Indonesia's economic and social disaster and its potential Islamic threat is an enormous process failure. American citizens have let Wall Street lobby their government for policies and privileges that caused their economic catastrophe. In late 2001 there is no evidence yet that citizens, leaders, reformers, media, universities, civic groups and the institutional investors are examining the process failure to work out corrections to the continuous misuse of lobbying power by ultra-capitalism.

1997: Albanian Anarchy: This small country of over 3 million people on the Adriatic Sea has a history of domination: Greeks, Romans, Byzantines, Turks, Italian fascists, Russian communists and finally ultra-capitalism. Typical of the Balkans most of the north is Christian and the south Islamic.

When Albania emerged from almost a half-century of Stalinist isolation in 1991 the United States took a sudden interest in its fortunes. At that time neighboring Yugoslavia was sliding into violent disintegration and the Bush administration saw Albania as a potential foothold in the Balkans.243

The United States had an opportunity to help a small country move from tyranny to economic freedom. Instead the U.S. followed its usual pattern of buying an election for Sali Berisha, a hand-picked candidate. It was a bargain as it only cost $8 million.244 Subsequently, various military activities were pursued; air bases, NATO exercises, Albanian officers training in the United States, etc.

Economic development was left to the ultra-capitalists and the new stock market quickly went to uncontrolled speculation. Poor citizens actually believed that in this new wonderful world of capitalism they could "earn" 18% a month by investing in stocks.

Inevitably the speculation climaxed and crashed with Albania descending into the Hobbesian state of utter anarchy, which seldom happens to a

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244 Ibid.
European country. Armed mobs have ransacked stores, unruly soldiers have stolen cars at gunpoint, foreign nationals have been evacuated by helicopter from embassy compounds, and rebels have stolen some 100,000 light arms from government arsenals.245

The Albanian people were protesting over the collapse of the fraudulent investment scheme, the Albanian version of the Ponzi Scheme,246 where new money is paid out lavishly to earlier investors stimulating more new money until the fraud runs out of time. "Albanians, infuriated by their bosses in a huge swindle, turn violently against their government."247

The Albanian tragedy illustrated how easily a stock market can become a gambling casino motivated by instant riches. Albania copied the American raging bull stock market. It was the Albanians' first view of economic freedom and it looked beautiful. Alternate ways of investing patiently with strong annual dividends and modest appreciation was not a part of the U.S. advice.

Albania was both a power failure and a process failure of two types. After the fall of communism the U.S. arrogantly expected to run the world and use any opportunity to expand its military presence. Albania was a process failure because American leaders were ignorant of the proper role of the United States after the end of the bipolar confrontation, and it was a process failure because the American government was ignorant of the damage done by ultra-capitalism in comparison to the economic and social benefits available from democratic capitalism.

1998: A Muslim Prime Minister speaks out against a new form of Western economic imperialism: Prime Minister Mohammed Mahathir was responding to the reversal of economic momentum in his and other "Asian tiger" countries. It appeared to Mahathir to be a flaunting of financial power for the usual greedy purposes. He was partly right but the real cause was a process failure. World powers led by the United States had been unable to cooperate on a new world financial architecture. As a result there was little control of lending hot, short-term money for long term investment, and there were unavoidable

245 Ibid.

246 Bruce W. Nelan, op. cit., p. 32.

247 Ibid.
consequences from simultaneously deregulating banking while suspending market disciplines. After 1971 when President Nixon floated the dollar, there was no world monetary stabilizing mechanism for the first time, and leveraged speculation was out of control, dwarfing world commerce. The power failure allowed ultra-capitalism to export its damage worldwide; the process failure continued, with the reformers unable to understand how to fix the problem.

2001: *Unilateral America*: Before the September 11, 2001 attack on America, the news was full of examples of a United States not trying to be the world's moral and economic leader, not trying to make the U.N. the strong agency of international law backed by cooperative force, instead the United States was pursuing unilateral actions, disappointing allies, and causing hatred among enemies:

Anthony Lewis reported:

In 1969 President Nixon announced the development of biological weapons ... He then led the way to a 1972 treaty banning the development, production or possession.

This week President Bush wiped out eight years of effort on a protocol to enforce the 1972 treaty. President Bush's response was the same as bowing out of the Kyoto agreement on global warming, the United States has a better way.

Lewis latter commented:

Once again, under his presidency, the United States was all alone on a global issue. So it was, also, last week on an effort to negotiate limits on small-arms sales that feed civil wars and terrorism. Underlying Mr. Bush's response on these matters there is a failure of vision. He takes a parochial view, driven by ideology and a narrow sense of where American interests lie. But in today's close-knit world our interests cannot be so easily separated from global needs.  

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President Bush's administration also would not participate in ratification of a treaty creating the International Criminal Court and was ready to set aside anti-ballistic missile agreements with Russia.

The *New York Times* commented:

> As the world's strongest economic and military power, the United States has a compelling interest in helping to expand and shape international law on matters from arms control to the environment to criminal accountability. Mighty as it is, Washington cannot expect to lead the way to a less dangerous, more law-abiding and environmentally sustainable world from the sidelines.249

All of these examples of U.S. unilateral arrogance were reported in 2001, before the September 11 attack.

*The Will and Wisdom of the People*

This will and wisdom of the people evidencing a greater awareness of new world realities has been reported in many ways. One opinion poll indicates that 86% of Americans in 1996 believed that the United Nations should play a much bigger peacekeeping and diplomatic role than it did before the Gulf War. 85% believed that the countries of the world should act together, not on their own, to deter and resist aggression. 83% believed that the United Nations should tax international arms sales and redeploy money to famine relief and humanitarian aid.250

In another poll (October, 2000) 65% favored the idea that "a permanent U.N. force be created that is made up of individual volunteers ready to be sent quickly to conflict areas to stop the violence." 69% versus 17% favored the idea of voting for a presidential candidate who supports a stronger U.N. to help keep the international peace, protect the global environment, and combat world poverty.251

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250 Grieder, op. cit., p. 171.

These are the matters that will determine whether the twenty-first century is one of peace and plenty or more folly and violence. It is clear from these examples during the 1990s that the right answers are unlikely to come from the political process affected as it is by both arrogant power failures and ignorant process failures.

An Enlightenment II however can produce an agenda independent of the superficial, polarized political process. With the benefit of new communication technology the people can become truly sovereign and the country will be run by representatives who accurately filter the will and wisdom of the people, just as the founders intended.
Chapter 7

The Federal Reserve and The Crash of ‘29

1913: Beginning of the Federal Reserve

The panics were easy to blame on the Morgan interests who manipulated stock markets and took enormous fees for capital formation and were expected to stabilize currency but occasionally choked it off. Nationally chartered country banks were required to maintain their reserves in 47 reserve cities who, in turn, kept their reserves in three central cities, mainly New York but also Chicago and St. Louis. When the crop working capital demand hit the country banks drew down reserves from the 47 who, in turn, drew from the three central reserve banks. If the demand continued, Morgan could raise rates or decide not to respond. They could organize syndicates or, with enough time, get the requisite gold from Europe. When none of this was done, somewhere a country bank would fail as depositors panicked and a “run” began. In fractional reserve banking, when most want their money, it’s simply not there. While Morgan and the privileged made money when the system worked and made money when it failed, the problem was not simple greed, it was systemic because of immobile reserves and inflexible money supply tied to gold.

The Panic of 1907 scared Wall Street and created the environment for the Federal Reserve. The repetitive nature of the problem resulted in country banks trying to hoard reserves in anticipation of Wall Street’s eventual turn down. This hoarding created such a problem that a New York bank failed and J.P. Morgan had to make a personal plea to President Theodore Roosevelt to get the government to pump money into the system to avoid massive failure, which they did.

Because of these repetitive failures, the Federal Reserve was created in 1913. Woodrow Wilson used populist rhetoric in his 1912 campaign but when elected, with...
economic understanding, deferred to the financial experts. The bill, drafted by an economist on the staff of Representative Carter Glass of Virginia, was basically the same as that developed by the heads of National City (now CitiBank), Morgan and Kuhn Loeb. It solved the currency crises by a privately controlled network of regional reserve banks that would be given government powers. Wilson didn’t understand the banking experts, but he didn’t trust them either, so he insisted on the creation of a Federal Reserve Board in Washington appointed by the President to represent the public interest. After all, he had campaigned against “a concentration of the control of credit which may at anytime become infinitely dangerous to free enterprise.” He’d had fights with wealthy trustees when President of Princeton that gave early evidence of his inability to either merchandise views or attain consensus. He was unfortunately never reluctant to pursue a course without sufficient dialogue or opposition. He regarded this as personal courage, but it ultimately led to the debacle at the Versailles peace talks and his physical destruction.

The Federal Reserve was a good example of unintended consequences. Wilson was advised that the government had to take action to prevent these regular liquidity panics. As a reformer, he thought that this action would finally take control away from Financial Capitalism. In reality, Democratic Capitalism was doing very well despite the impediments caused by the deficiencies of Financial Capitalism. William Grieder quotes historian Gabriel Kolko describing the industrial expansion going on throughout the country. “From 1900 to 1910, 70% of the new funds for manufacturing were generated internally, making the corporations more independent of finance capital.” Without the benefit of tax laws or a comprehending government, democratic capitalism was financing most of its own growth. Changes then and now in investment tax credits, dividends, capital gains and creative engineering of the flow of funds from pension plans, could have made democratic capitalism free of the markups, monstrous errors and other impediments of Ultra-Capitalism.

President Wilson thought he was leading the fight against privileged interests with his insistence on the hybrid approach of public-private with the public represented by those
recruited and appointed by the President. In fact, his unintended consequence was a repackaging of the control by the banking interests, without diffusion of financial power. The money reforms protected the old order and money still would not be neutral. Alternatives for capital formation to encourage the growth of democratic capitalism were probably not even considered as this constituency was not represented. William Grieder emphasized the inherent contradiction between the sovereignty of the people and the function of the Federal Reserve. These non-elected officials decide on how the economy would grow, they made political moves, particularly before elections, and make decisions between protecting wealth and creating jobs sustaining the time honored and destructive nexus between Government and Financial Capitalism. The overwhelming majority in Congress who voted for Wilson’s plan had created a new management system that would, in time, replace gold as the regulator. With its influence on money supply and interest rates, it was a throttle regulating the entire economy through fiat money.

The costs of World War I resulted in the usual government sham of financing by currency debasement but, in this case, it signaled the end of the gold standard, though no one knew it at the time. The U.S. held on until it suspended gold convertibility in 1933. Without the gold standard, the mission of the Federal Reserve changed from being a protection against liquidity crises to managing the money supply and, in effect, money value. It evolved into a central monetary administration assuming sovereign power. For a while it monitored the world’s exchange when, after World War II and the Bretton Woods conference, the U.S. dollar replaced 2500 years of some type of gold standard. In 1972, President Nixon cut currencies free, resulting in present currency speculation now dwarfing commercial exchange.

Stable currency to expedite commerce needs consistent protocols on supply, cost of money, deficits and taxes in all countries. This is impossible when politicians are using currency manipulation for economic nationalism and speculators make or lost hundreds of millions, occasionally billions, guessing what the politicians will do. It would be hard to design a world monetary policy with more risk and further from the economist’s dream of neutral money.
In 1920, the Federal Reserve created its first depression in the name of sound finance. The costs of the war had inevitably caused a 15% inflation as the national debt went from $1 billion to $27 billion. The Federal Reserve raised the discount rate to a record level of 7% and kept it there for 18 months. Commodity prices fell 50%, plunging farmers into destructive circumstances. Manufacturing fell by 42% and unemployment rose to 11.9% with four million people were out of work. Bank failures rose from 63 in 1919 to 506 in 1921. The wealthy were happy to see their assets restored to prior value, although most had increased assets substantially in real value during the war. This was the first event that exposed the Federal Reserve abandoning their stated mission to accommodate “the needs of commerce and industry” and instead accommodating the financial interests. Their action did protect the purchasing power of the retired with meager assets and on fixed income but this small part of the population has always been used as the attractive message in support of unfair distribution to the wealthy. There are other techniques to protect this group.

This humanitarian concern for protecting the income of the elderly was good merchandising, but the true trade off was the asset value of the wealthy vs. the jobs of many. The circumstances in the early 20s anticipated the disastrous events of 1929 and the great depression, The interventionist techniques were tariffs, money supply, and taxes with no methodology to discriminate between democratic capital and speculative capital. The tariff actions of 1921 did serious damage to world trade and set the stage for the larger disaster of Smoot Hawley in 1932. While easy money during the 20s helped support the eventual speculative craze, the manufacturing section was free enough and prospered with increasing volume and many reduced prices, but this democratic capitalism deflation was obscured by the inflationary effect of easy credit for speculation.

In 1927, Benjamin Strong of the New York Fed, for a decade the country’s most powerful banker, responded to a European committee seeking easier credit in the U.S., presumably to loosen the credit crunch in Europe. England had been in a poor economy most of the 20s due primarily to a decision to return to the gold standard and peg the
pound at its earlier value, an action taken in 1925 by Winston Churchill as Chancellor of the Exchequer. John Kenneth Galbraith, in his book, “The Great Crash, 1929,” observed that economics was never Churchill’s strong point and there’s no record of reproach for this damaging government action. Strong felt that additional easing was appropriate as there were signs of a slow down in manufacturing. Several hundred million more dollars were pumped in and were almost immediately sucked into the vortex of speculative capitalism.

In the early 20s, brokers’ loans totaled less than $1½ billion financing the purchase of stock on margin then using the rising stock value as collateral to borrow more money to buy more stock. By 1926, brokers loans increased to $2½ billion, $4 billion in June, 1928, $5 billion by November and close to $6 billion by year end. This enormous hydraulic flow was coming from all directions as it was easily available at a 12% interest rate. It was an early version of the hydraulic flow from savings accounts into Broker’s CDs, then into S&Ls and finally into a black hole of high risk adventures that happened during the 80s. In the late 20s, banks could borrow from the Federal Reserve at 5% and loan at 12%. Money flowed into New York from all over the world. Companies even started loaning their surplus cash into this speculative craze. During 1929, Standard Oil of New Jersey contributed $69 million a day, Electric Bond and Share averaged over $100 million a day. Some, like Cities Service, sold securities and loaned the proceeds. Why not? It seemed easier than finding new ways to build things. The buying pressure was so great that the investment bankers created new products for sale such as investment trusts, a packaging of bonds and stocks. In 1927, trusts sold $400 million worth of securities during 1929, they sold about $3 billion. In 1995, mutual funds are the hot commodity confirming the ability of speculative capitalists ever since the Dutch tulip craze to find a commodity to accommodate the buying urge.

The government and the FED seemed to regard this out of control situation as an exercise in free market. It did not then and doesn’t now use available tax, currency, and credit techniques to encourage productive capital and discourage speculative capital. It made limited moves on margin or interest rates and indulged in a few verbal warnings. The
free market builds and sells things with money being the medium of exchange. How the money machinations of Wall Street can be regarded as an exercise of free market principles is a triumph of merchandising over truth. The FED had the controls but not the will or the wisdom to use the. The record of selective laissez-faire, suspending government intervention only during the speculative phase, was kept intact. Speculative Capitalism Caused the Crash of ’29; the Hoover Administration Intervened with Three Mistakes that Converted the Crash into the Great Depression.

Once again during the 20s, the government was unable or unwilling to discriminate between expansion and speculation. The government was partnering with corrupted Financial Capitalism by acts of commission and omission. Capital was increasingly directed to the Prodigals and Projectors while Democratic Capitalism was largely internally funded. The productive economy was driving prices down but Financial Capitalism and government inflation absorbed this productive deflation and inflated from there.

After the inevitable climax and crash of artificial assets, the other estate went to work. The media loves the visibility, excitement and instantaneous nature of the stock market. It ignores the reality that the stock market has little to do with the productive sector. The market has only two motivations: greed and fear. Whenever the fear prevails resulting in a crash of artificial assets, the media reports it in a way that exports the fear of the general economy. Aided by Hoover’s errors, it worked in 1929-32 when people stopped buying and manufacturers trimmed inventories. The media tried to export the crash in 1987, but it didn’t happen because of the lack of similar government errors and the continued buying pressure form institutional liquidity such as pension money.

Once it was clear that the system was heading into a depression, Hoover either initiated action or allowed Congress and the Federal Reserve take action to:
1. Raise personal taxes to record progressive levels (63%) with retroactivity that pulled cash out of accounts exacerbating the banking crises.

2. Passed the most protectionist law in U.S. history with quick devastating effect on world trade.

3. Reversed the easy money of the 20s at the wrong time. During 1930, the Federal Reserve decreased money by 4.2%, speeding up to 7.1% reduction in 1931 and 12.3% in 1932, provoking deflation and reduced demand.

The crash of ’29 and the Great Depression a case study of continuing epistemological failure. By now, the facts should be well known and provide clarity to be used in current decisions but that is not the case, the events are still confused with lies and myths. There are many books that provide clarity. John Maynard Keynes in “General Theory” describes the antics of the market as a game of musical chairs. John Kenneth Galbraith gives emphasis on the flow of speculative cash in “The great Crash 1929” but ignores the intervention. Ronald Nash in “Poverty and Wealth,” lines up the four main myths and analyzes/destroys each. Jude Wanniski details all of the forces before and after in “The Way the World Works.” Continuing damage is done however by liberals that describe the Crash and Great Depression as caused by the laissez-faire policies of Hoover, later corrected by Roosevelt’s enlightened intervention. In their view, this was the watershed even confirming the inherently destructive cycle of the free market and the necessity for government intervention to minimize the hurt to society due to this flaw. All not true, the government made mistakes with monetary policies that allowed the inherently destructive cycle of Speculative Capitalism followed by intervention damage control that exported the crash of artificial assets to a destruction of the general economy. The problem was not a matter of choosing the correct political abstraction, it was mistakes of omission during the 20s, followed by mistakes of commission after ’29. The common denominator was failure of leadership. Before his seduction by the collectivists, Roosevelt
campaigned against Hoover leading us toward socialism, opposed insuring bank deposits, promised a balanced budget, and felt that the free economy was a great system, but hadn’t been tried yet!

1929 Smoot Hawley Being Debated

The Republican party was determined to help the farmer who was suffering from a worldwide shift to low cost producer and mechanization. This was a classical economic shift where government intervention shouldn’t happen. A “no risk, no hurt” system can’t exist but both would be minimized if the situation was left to self-correcting capabilities of the free economy. “Old Guard” Republicans favored protective tariffs on all agricultural products but both Democrats and “progressive” Republicans opposed Senator Borah of Idaho who presented a resolution reflecting the “sense of Senate” against extending protectionism beyond agriculture, and the resolution failed 39 to 38. The stock market assumed that the non-voting senators would favor free markets and anticipated eventual victory for the anti-tariff forces moving from 281 in March to 347 in July to 381 in September.

October 29: The market gyrates as Senate debates tariffs. Great attention given to such as casein, a product made from skim milk and used in the manufacture of glue and slick paper. Was it a farm product or industrial? The House left the rate at 2½¢/lb., the Senate Finance Committee bumped to 3½¢/lb. The question was what the full Senate would do. Adam Smith would have fainted at this intrusion.

Oct. 23-24: Market off 21 points and goes into Black Thursday panic. Senator Shortridge, on behalf of dairymen, tries to get casein up to 8¢/lb. Compromise made at 5½¢/lb. Fifteen tariff schedules under review affecting 20,000 items.

Nov. 13: Tariff bill daily news with the question whether to be killed or passed, Dow down to 198. Hoover is silent on tariff but cuts personal income tax rate by 1%. By end of December Dow back to 263. 1930 Stock market recovers to 294 in April. Foreign
interests express horror over potential tariff, urge that bill be killed.

British India points out that a 1000% increase in tariffs on cashews will destroy their industry and also points that the U.S. does not produce cashews.

Greece’s minister calls attention to America’s first place in Greek imports and that proposed tariffs will significantly reduce Greece’s purchasing power to buy American goods.

Italians are more passionate, and think that the U.S. is trying to structure an export/import equation that will allow them to corner the gold market. They reciprocate with tariffs ranging from $815 on a Ford to $1,660 on a Chrysler Imperial. By November, Italian car agencies are out of business and the Ford assembly plant closed. U.S. car windows are spat upon and tires punctured.

June 15: Hoover breaks silence and says he will support the tariff bill. National Association of Manufacturers says it will “bring a breath of relief to all industry and all business.” Big labor approves. Tough combination: big government, big business, big labor. Stock market starts slide to a low of 41 on July 8, 1932.

1929-32: Hoover’s interventionist damage control makes problems worse and the long and deep recession foreordained. Federal Reserve reduced money supply by 30% between 1929 and 1932, leading to reduced demand and deflation. Over 5,000 banks go under with deflation reducing purchasing power and unemployment peaking at 25%. In 1933 there were innumerable personal bankruptcies. The classical economist would describe falling prices and falling wages as the self-correcting feature of the free market. Hoover took all possible action to keep both prices and wages up. Agricultural price supports resulted in larger crops and surpluses with no market.

1932: American exports were down by almost two-thirds, $5.5 billion in 1929; $1.7 billion in 1932. The tax increase in 1932 was the largest in the history of the nation.
Real gross national product fell by 14.8% in 1932.

1932: Federal Reserve action: Basically nothing, they followed earlier conventional wisdom that their function was to add money to the system during growth and the withdraw during recession. Hoover didn’t control their action or inaction while they confirmed their defacto mission of financial interests over jobs. From 1929 to 1932, money disappeared as foreigners took back their loans in anticipation of Smoot Hawley. Billions of dollars of bank debt was liquidated by defaults and bankruptcies as U.S. money shrunk by one-third. Hoover lamented that the Fed became “a weak reed to lean upon in time of trouble.” The 1992 version is “pushing on a string.” There is almost unanimous expert agreement that this was tragic human error as the Fed should have given the economy the equivalent of electro shock with infusions of money. They didn’t. Some suggest if Benjamin Strong had not died in 1928, leaving a decision vacuum, things would have been different. But, if true, this is a perilous system to be so dependent. Most of Hoover’s advice after a decade of government intrusion was now free economy. Let the system self-correct. Andrew Mellon, Treasury Secretary, was particularly emphatic in the need for a good purging process, “liquidate labor, liquidate stocks, liquidate the far, liquidate real estate.” The fact that the purge would destroy farmers and result in 25% unemployment of those most distant from the speculative frenzy was unfortunate but irrelevant. Workers were merely a variable in the equation. Amazingly, after another half century workers are still a variable as putting them out of work is the conventional weapon against inflation.

The story is actually worse. The Federal Board chairman in Washington, who at the time did not have central control, pleaded in 1931 for the reserve banks to pump money into the system, but they did the reverse. Finally, in April 1932, Chairman Eugene Meyer, with the support of Morgan and others, prevailed and $100 million a week was pumped into the system for eleven weeks. The transfusion was bringing the patient back to health. The Chicago Fed and Philadelphia Fed, however, led a successful campaign to abandon this initiative and resume the contraction. The reason, expanded money supply drove down interest rates on government securities, the major source of large bank
earnings at the time. A few months later, a third wave of bank failures swept the country.

The reforms implemented during the thirties in the Federal Reserve had two things in common: an appearance of solving a problem and the usual ratchet effect of initiating a bigger problem. Some of the moves:

1. Deposit insurance of $5,000—a good idea to fight bank runs. Now up to $100,000 and in the S&L scandal, high rollers were using the $100,000 at multiple locations. Roosevelt warned that deposit insurance would be a disaster and a burden on taxpayers—he was right.

2. Federal Reserve centralized control

3. Glass Steagall separated commercial banking and long term investment banking with controlled interest on deposits allowing government to engineer how banks make money.

4. No cabinet officers ex-officio numbers of Federal Reserve Board purportedly distancing it from politics.

5. Government debt securities replaced short term commercial notes as the medium for Fed action. This seemingly innocuous action, in time, integrated the interests of Fed and Financial Capitalism with a proportionate increase in distance from democratic capitalism.

_The Financial Predators and Government Errors Opened Door to the Collectivists._

The Great Depression truly drove the country close to revolution. The people were again remote witnesses to the excesses of the twenties but then the direct
victims of both the excesses and government error. Their leaders had failed them, not due to uncontrollable events, but due to inadequate training. Wilson didn’t know what he was doing when he created the Federal Reserve, and Harding, Coolidge and Hoover didn’t know the difference between growth and speculation, between overproducing and overtrading. They were descendants of Madison and Monroe who supervised the first Crash in 1818-19 for basically the same reasons. The unwitting legacy from the protégés of Jefferson was a monetary system with an inverted mission of serving the privileged at the expense of the general welfare. Rather than the free banking of Adam Smith disciplining the system or direct government control, the country ended with the worst of both worlds: enough government intervention to insure constant errors from the adversarial political process with enough freedom to allow the predators to plunder the system.

The Collectivists were on a roll worldwide in the early 30s. Stalin, Mussolini, and even Hitler were becoming role models for those with the Platonian conceit. The failure of leadership in the U.S. opened the door wide for their social construct. Most if it failed but World War II obscured this allowing contemporary liberals to blame the 1930’s problem on free markets and give the recovery credit to Collectivism. Anyone still doing this should have their intellectual’s card punched as this theory can’t stand even a little inspection.
Chapter 8
A Case Study in Bad Government:
The Savings and Loan Disaster

_The Savings-and-Loan Fiasco Cost Taxpayers About One-Half Trillion. It combined Flawed Monetary Policy Favoring the Few with Bad Legislation, Worse Execution._

From the time Jefferson lost the battle to the financial aristocracy, the country has suffered cycles of speculation, followed by impoverishment of the farmer and job-loss by workers. The pattern never changed. A few gained riches in both directions, while the worker and farmer were hurt in the up and devastated in the down, the monetary system was so flawed that occasionally it couldn’t even fund the seasonal demand to get crops to market. Democratic Capitalism, however, proved to be powerful enough to overcome the impediments and the country went on flourishing.

During the twentieth century, the flaws in the monetary system were combined with the accelerating growth of big government to produce mistakes of gargantuan proportions. The Savings and Loan disaster in a case-study for new leaders, to help them understand root causes and the disaster in the century, the earlier two being the ’29 Crash and subsequent Depression, and the misdirection of $2.6 trillion in workers’ pension money to speculative capitalism. In each case, mistakes were made in a flawed structure producing a flawed process. After each speculative craze reached its inevitable damaging conclusion, the process continued with a new generation of politicians producing a new generation of mistakes. The people sensed failure of leadership but didn’t know how bad it was.

On October 15, 1982, President Reagan signed the Garn-St. Germain Act. Two hundred people were invited to the Rose Garden for this “Most important legislation for financial institutions in 50 years.” Two years into his first term, the President apparently felt that he was honoring his campaign pledge to get the government off peoples’ backs in order
to allow the private sector to grow and create jobs. He was, in fact, sustaining a disaster and giving deregulation a bad name.

Back in 1932, President Franklin Roosevelt had threatened to veto a bill that would provide government insurance for bank deposits of $2,500, later $5,000. He felt then that it was a dangerous abrogation of market place disciplines and would inevitably encourage risky business decisions with the financial damage paid for by prudently managed banks. He was later convinced by his advisors that the panicky banks runs could only be stemmed with such extreme damage-control legislation.

The new law didn’t have a “sunset provision phasing out such protection after the crisis and there was no effort to insure on a risk-oriented basis. (At the time the Garn-St. Germain bill was being designed in the early 1980s, such insurance deposit had increased to $40,000. As the bill was being expedited to conclusion, the persistence of an industry lobbyist was rewarded with having the insured level increased to $100,000 without limitation on the number of locations.

A modest protection for the small depositor, controversial as that was, was now converted to an insured financing vehicle for “prodigals and projectors”, as Adam Smith called them. Deposits were not only insured, there was no relation between risk and reserve. A trillion-dollar obligation had been added to the U.S. economy. This mistake cost about half that, all dumped onto the taxpayer.

Thrifts were started in the mid-nineteenth century as a way for people to pool assets to help expedite home-buying. The banks were too engrossed in commercial lending to service the home mortgage market thoroughly. Government incentives could have helped add this to the existing infrastructure, but they were lacking. This simple thrift idea, modeled after similar institutions in England, worked well. Supported by a steady economic growth, home ownership in the U.S. reached record levels, with 2/3 of families owning their own homes during the twentieth century.
In due time government regulation crept in. Regulation Q had mandated a maximum 5.25% interest payment on bank savings. Paul Volker’s term as Chairman of the Federal Reserve in the late 1970s saw his uncoordinated attack on inflation driving interest rates up to as high as 20%. This quickly exposed the fundamental flaw in the now-regulated S&L, an inversion of the normal banking principle. The were borrowing high-cost monthly short, to invest in low-return long. Putting the industry in a destructive economic vise. It might be educationally beneficial to analyze what would have happened if there had been no regulation, or what other alternatives could have been explored. The original mission was low-cost, available home mortgages. Because of uncoordinated government intervention the mission now became, save the S&Ls.

During the S&L decade of the 80’s, Danny Wall was the central figure. He had worked for a Savings and Loan in Salt Lake City and came to Washington as chief administrative aide to Senator Jake Garn (R-Utah). In 1989, the Wall Street Journal described him as “The S and L Looter’s Waterboy.” If Wall was the “waterboy,” then the S&L lobbying group, the U.S. League of Savings Institutions, was the coach. In 1985, Senate records show the waterboy’s taking 30 trips paid for by the coach. The same article described this former assistant city administrator in Salt Lake City becoming chairman of the Federal home Loan Bank Board, a clear case of Peter Principle.

In 1980, the Senate Banking Committee addressed the predicament that the S&L industry was in due to uncoordinated government intrusion earlier. There was a low level of interest on deposits, based on Regulation Q, combined with a high cost of new monbey due to the Volker Federal Reserve's scorched-earth policy to lick inflation. The S&Ls were borrowing high cost money short and investing low cost money long in fixed rate mortgages: banker’s nightmare.

When the Senate undertook damage control, Danny Wall was involved in drafting the new legislation as his boss, Jake Garn, was Chairman of the Committee. One common denominator, of all of these key players was a lack of knowledge or experience in the complex financial engineering in which they were engaged. The mixed government
structure was adversarial, superficial, and on a political schedule allowing untalented people to write laws by depending on the self-serving expertise of the lobbyists. Unfortunately there was no lobbying force for Democratic Capitalism anticipating the damage and providing useful counter-proposals.

The product of Wall’s drafting, coached by the U.S. League, was the Depository Institutions Deregulation and Monetary Control Act of 1980. This act phased out interest-rate controls and at the same time raised the FLSIC insurance coverage from $40,000 to $100,000. The coverage had been raised by Congress from $20,000 in 1974. The 5.5% interest cap had been extended by Congress to the thrifts in the 60s, on the interesting theory that capping deposit interest would help keep down mortgage costs.

It was a popular law, in favor of low-cost housing, probably used by every politician within reach during campaigns such as an example of his productivity and vision. It was a good concept if applied in a vacuum. The new law quietly removed the limitation on brokered deposits to 5% of total deposits. Brokered deposits were the device that investment bankers like Merrill Lynch later used to suck out all these low-return, but no-risk, savings accounts to move the money to the newly high risk S&L’s. Why not? It was insured.

The leap to $100,000 worth of deposit insurance was integrated at a late-night session on Capitol Hill, pushed by the chief Washington lobbyist of the U.S. League. It had no opposition and was later described as an afterthought. But it was typical of the sporadic, uncoordinated laws affecting the Savings and Loan industry. Until 1932, thrifts were regulated only at the state level. When the Federal Reserve was centralized in 1932, thrifts were given the option of being federally-chartered. In 1934, the first deposit insurance of $5,000 was passed for both banks and thrifts, with the reserve funded by assessments of members.

Not surprisingly, the 1980 legislation did not resolve the S&L dilemma, as a law to help attract funds could not work if the return on funds was not improved. In the first half of
19823, thrifts lost $3.3 billion, and cried for more government relief. This was the intention of the 1982 Garn-St. Germain Bill that President Reagan proudly announced. This bill attempted to deregulate the industry so it could now earn higher returns on the higher-cost deposits stimulated by the 1980 bill. It was an impressive laundry list:

! They could invest up to 40% of their assets in non-residential real-estate.

! They could offer market money funds free from withdrawal penalties or interest-rate regulation.

! In the same year Congress passed a resolution effectively committing the taxpayer to back up the FSLIC if it went broke.

! A single shareholder could own a thrift rather than 400 stockholders with a 25% individual maximum ownership.

! Land could be used for an asset in lieu of cash, helping developers with unsalable land.

! 100% financing could be done with no cash from borrower.

! Real estate loans were not limited to the location of the thrift.

! Accounting rules were stretched to include good will as part of the net worth, this premium paid for an acquisition over book has value only in the eye of the beholder. By 1986, it represented 40% of all thrift net worth, which was supposed to be the buffer against loss.

! New federal rules were so liberal that thrifts were converting from state charter to federal.

As a source of funds for state regulation, this last item sparked a liberalization competition where states such as California outdid the Federal with no limits on non-
residential loans. The only state that outdid California was Texas. The already liberal rules in the booming oil economy got a shot of adrenaline with the $100,000 deposit insurance. Texas bid the highest rates for brokered deposits and grew at three times the national average…”By 1987, 50% were run by managers who had entered the business after 1979 (over 80% were former real estate developers).” Danny Wall reappears later, fighting reform efforts as the crisis developed. In 1987, as a reward for loyalty and services rendered, he became Chairman of the FHLBB.

1983 was the beginning of Edwin Grey’s agony. He was well known and popular at the U.S. League of Savings Institutions, representing Great American First Savings Bank of San Diego as their P.R. man. His background was solid Ronald Reagan loyalist, as Grey had been his press secretary during his years as Governor, and he had worked a short time as Assistant to the President and Director of the White House Office of Policy and Development.

The November, 1982, League convention in New Orleans featured Ronald Reagan as keynote speaker. During that convention, Grey was asked to become Chairman of the Federal Home Loan Bank Board. He was sworn in on May 1, 1983 by his friend, Ed Meese, Attorney General. As described in “Inside Job,” this man, soon to become a pariah in an epic drama, expected to be a cheerleader for the industry for a couple of years and then go back to San Diego. His function was driven home his first day on the job when he received a phone call from Treasury Secretary Don Regan. “You’re going to be a team player, I take it,” Regan asked him. “Sure,” Grey answered. End of conversation.

Financial capitalism, soon to become speculative capitalism, was well represented. Don Regan was former Chairman of Merrill Lynch; retiring League Chairman Richard Pratt, a former Utah University professor, was headed to Merrill Lynch to be Chairman of their Capital Markets Group; John Heimann, Controller of Currency, was later Vice Chairman of Merrill’s Capital Markets Group. When the rush of money sucked out of low-paying savings accounts passed through deposit brokers like Merrill Lynch on their way to the
highest bidding thrift, they left as much as $150 million a year in Merrill fees.

When Grey became chief cheerleader, he had limited qualifications and was paid commensurately. If he had known what he was getting into, he probably wouldn’t have taken the job, or would have insisted on hazards duty pay. The 1980 legislation gave the thrifts an opportunity to pay better than competitive rates for deposits; the 1982 law gave the opportunity to invest this high-cost money seeking high-profit return.

Most importantly, with deposit insurance now backed by taxpayers if the FLSIC went broke, no one cared what the risk was. While going broke, troubled thrifts bid higher for deposits and kept effectively doubling the bet. Why not? The money was available. The deposit brokers, like Merrill Lynch, had advanced technology with national communication networks on line to computers to give daily information on where to place more bets. Package it at $99,999, the investors like the rate, the thrifts like the money, Merrill likes the fees, the politicians like “saving the S&Ls,” and everyone is a winner. Wrong!

Before Grey went into office, the missile was fired up and the countdown had begun, but the government was still busy with its uncoordinated design for disaster. Congress passed the Economic Recovery Act of 1981, making commercial real estate attractive by liberalizing taxation. This initiative from the Treasury Department of Don Regan would encourage new projects, many funded by thrifts. This misadventure helped the speculative craze in the “up” direction, but with the usual erratic government action, when the overbuilding problem gained visibility, a new law was passed.

The Tax Reform Act of 1986 pulled the plug on tax benefits and now produced a downward effect after the earlier upward one. This law lengthened the depreciation period from 19 to 31 years, “thus collapsing the present values of real-estate prices.” Not content with this blow, the reformers deprived present values of real-estate prices.” Not content with this blow, the reformers deprived passive investors of certain tax deductions on interest and depreciation, thus hiking the costs of investments. In case any profit were
left, the reform raised the capital-gains tax rate 20% to 28%.

While the missile was ready to fire, there were numerous warning signals. Study of the Penn Central Bank failure in 1981 provides lessons on high-risk, insured real-estate ventures. Government-insured deposits had recently broken the half-trillion level, up from $2.1 billion in 1940, $11.2 billion 1950, $55.8 billion in 1960, and $137.2 billion in 1970.

CATO, a Washington organization, wrote about thrifts in 1982, that “The ailing giant was on the brink with a total net worth of negative $70 billion,” pointing out the continuing abnormally of borrowing short to invest long. It predicted that the government could not substitute for market oversight in controlling the risk inherent in insuring deposits ten years later, after the predicted debacle, the government has yet to fully address the insuring of deposits without regard to risk. Worse than that, extrapolating the theory of insured deposits, it has created the “too big to fail” theory by rescuing the worst managed banks, such as Continental Illinois.

In Grey’s first year in office, he had to grapple with the failure of Manning Savings and Loan in Chicago. “The $117 million thrift had failed after growing rapidly, not by attracting local deposits but by using deposits from deposit brokers to invest in questionable real estate ventures. They had overdosed on brokered deposits.” This 1982 failure was the first warning of the damage done to the industry and ultimately to the taxpayer by eliminating the limit of 5% brokered deposits to total deposits. The limit had been established by the FHLBB in 1963, to shut the door on the thrifts’ bidding up the cost of this source of money, in turn stimulating risky investments trying to pay for this high-cost money and make a profit.

Grey knew the background of brokered deposits. He could see what had happened at Penn Central and Manning Savings, and he initiated action to eliminate FSLIC insurance protection for brokered deposits. This P.R. man from San Diego, this regular guy, this cheerleader, understood the impending disaster and took and took courageous action.
Courageous in that he would end up opposing the industry as well as Don Regan, the father of brokered deposits. But Grey made progress when Bill Isaac, Chairman of the FDIC, gave his support and the FHLBB approved the brokered-deposit limitation, to go into effect October 1, 1984. Grey’s arguments were supported by brokered deposits increasing from $3 billion at the end of 1981 to $29 billion at the end of 1983. His recommendation resulted in several years of personal abuse and frustration.

The industry, with its great lobbying strength, later highlighted by the activities of the “Keating Five,” thought they had installed a cheerleader as chairman of the FHLBB, but what they got was a public servant, identifying the industry’s hurtling toward financial disaster, and with a plan Congress started hearings on the proposed regulation, but it didn’t have much of a chance. Led by Danny Wall, Staff Director of the Senate Banking and Urban Affairs Committee, coached, funded, and entertained by the thrift lobby, “legislation was introduced that would have gutted Grey’s brokered-deposit regulation.

The California S&L Commissioner, Larry Taggart, warned a Washington banking law conference that cutting off the supply of 80% of the money flowing into the S&L, would do great damage as the only problem was occasional bad management. He didn’t discuss high-yield CDs sucking up savings accounts pumping it into thrifts that could only complete the equation by chasing higher-return, higher-risk projects.

The body blow to Grey’s solution came from a different direction. The First Atlantic Investment Corporation Securities Inc. (FAIL) of Miami and the Securities Industry Association sued in federal court to have Grey’s brokered-deposit regulation overturned. On June 20, 1984 FAIL won a victory, when Federal Judge Gerhard Gessell ruled that the brokered-deposit ban was illegal and that action for such a ban had to come from Congress.

Grey was under attack from many directions. The Washington jungle fighters were at work and at various times it was reported that he was fired, under FBI investigation, and messing up his expense accounts. The FBI cleared him on all charges, but he must have
learned how hard it is to try to play offense and defense at the same time. He later settled a $28,000 expense question with some embarrassment.

Grey was determined, despite setbacks, and used speeches during 1984 to warn of the impending disaster. He emphasized brokered deposits, risky lending, direct investments, and inaccurate appraisals, and reintroduced risk-based insurance. In January of 1985, he attacked the other end of the problem. If he could not turn the valve to show the pressure of money, he would try to curb its excessive risk. The new proposal would limit direct investments to 10% of thrifts, total assets and would limit growth to 25% a year. Some argue that growth at this rate will produce a rate of change beyond managements’ competence to control, but some thrifts were then growing at rates of 100 to 500%! Grey’s new regulation was scheduled to go into effect in March, 1985.

Congressional hearings were scheduled for late March, after 220 House members signed a resolution asking the Thrift Bank Board to delay implementation. Eventually, despite opposition and personal attacks, Grey got this new regulation. The league’s good thrifts became increasingly aware of what the crooks were doing to their industry. Senator Proxmire, Chairman of the Senate Banking Committee, provided steady support and, in time, St. Germain backed the bill.

The new rules were useful, and apparently Grey thought that 700 additional examiners were, too. Their inspection quickly showed a substantial number of thrifts requiring seizure, but such seizure would require funds to pay off the deposit-insurance obligation. By 1986, the FSLIC reserve had plummeted from $6 billion in two years to $2.4 billion.

In 1985, the Thrift Board was recommending a “recap” with as much as $25 billion in new funds to shut thrifts. This inevitably provoked opposition from both the good thrifts and the crooks. The good thrifts would have to fund the money, the crooks would have been put out of business, so both opposed. After two years of opposition, in April, 1987, the bank board sued Don Dixon and Vernon Savings for $540 million.
Dixon had been one of the early crooks, but Congressman Jim Wright had helped his Texas constituent fight off regulation. After the law suit, Wright, the Speaker of the house, gave his support. By then, the reduced version of shut-down money was $15 billion. In May, the Senate passed $7.5 billion and the House $5 billion. With such delay, costs were running $10 million a day supporting these “brain dead” thrifts. Congress finally passed a $10.8 billion recap bill in August of 1987.

In February, 1989, the Bush Administration, recognizing hundreds of these bankrupt thrifts, proposed legislation that was eventually passed in modified form in August of 1989. The Financial Institutions Reform Recovery and Enforcement Act of 1989 authorized an additional $50 billion of borrowing. The taxpayer was expected to cover 75%, the prudent and healthy thrifts the rest. “FIRREA” abolished the bank board and FSLIC. The FDIC, under Bill Siedman, integrated FSLIC.

Congress was now on a legislative roll, and mandated higher-risk-based net-worth standards such Grey advocated five years earlier. To show their constituents how serious Congress was about this problem, they put to work enough of the 19,000 staffers to produce a 393-page document detailing the new act. Nowhere could you find the words “We’re sorry,” but it did tell exactly “how net worth should be calculated; it cut back on the range of allowable investments by even well capitalized and well run thrifts; and, it required that thrifts increase the percentage of assets devoted to housing related activities to 70% up from the 60% level mandated two years earlier.

With this money and new people politically unencumbered by the sorry history of dissipation of taxpayer money, the government proved again that no matter how bad the problem was it could figure out how to fix it and make it worse. The Bush administration was very expert on the financing, as the new Resolution Financing Corporation bonds were included in government revenue, but the money spent cleaning up the mess was “off budget,” so the year’s net effect was a $14 billion reduction in the apparent deficit.

The FDIC moved quickly to close another 200 thrifts, those insolvent ones, which were daily wasting more taxpayer money. Bill Seidman, the head of FDOC, said, “The
amount of real estate that will be up for sale is likely to exceed $100 billion, so it is a huge task, the biggest liquidation in the history of the world.” Seidman set the tone for the indiscriminate speed intended in dumping this distressed merchandise. “Our basic policy is that every asset is for sale at the current appraised value. We don’t believe we are in the business of speculating on asset value.”

The bad thrifts had created a new art out of balance-sheet accounting. In a growing market, there is always a tendency to overvalue, that’s why there are reserve requirements. The crooks had many techniques, one of which was “flipping” real estate or trading it with other crooks at increasing fictional value for the cosmetic benefit of the balance sheet. They could quadruple values in a few hours.

The bubble broke, as the market was over-built and the empty offices could not be ignored any longer. In Texas, the break in oil prices was a contributing factor. With Seidman’s haste, the values plummeted as in any fire sale. Billions could have been saved with a longer term plan. Quickly the smart-money guys moved in, such as the Bass brothers from Texas, and the takeover artist, Ronald Perelman. The buyers of this heavily discounted merchandise were known as private investor groups, “PIGS.”

The best one-liner describing the government technique was that it “privatized the profits and socialized the losses. The new administration struggled to resolve the problem within the “no new taxes, read my lips” guidelines. The media covered the downward spiral with more attention than most exhibited five to six years earlier when Grey was struggling to head off disaster. That part of the media still searching for truth would do a service reviewing how well it studied Grey’s plans compared to how quickly printed attacks on him leaked by Keating’s attorneys.

October 31, 1988: *Business Week* “The S&L Mess and How to Fix It” points out that the famous Marshall Plan after World War II, did important rebuilding work for about $50 or $60 billion in 1988 dollars. What might $150 billion have done if invested in education and training instead of the thrift waste?

January 30, 1989: *FORTUNE* points out that profits from 2,000 healthy thrifts are barely enough to pay interest on clean up costs.

January 31, 1989: *Wall Street Journal*: “S&L mess isn’t all bad, at least for lawyers who were regulators.” It describes how a former Wall Street lawyer, who helped write deregulation law, was now helping a New York law firm, Freid, Frank, generate $12 million in billings. By 1988, the FSLIC had 200 in house attorneys but also spent $110 million in outside fees.

*Wall Street Journal* also featured “Wall Street firms battle for profitable role in thrift rescue. Shearson offering a no strings financial deal shocking Drexel, Bear Stearns, and Merrill.” Fees were as high as $20 million on a $200-million deal with five times the average underwriting commission on investment-grade corporate bonds. No wonder speculative capitalism has such priority. Why should one waste time trying to build and sell something when enormous fees can be made on the downside of the speculative curve as well as on the upside? The fees were part of the greatest pricing scam in the history of capitalism, a percentage of the deal with little reference to value added, services rendered, creativity or risk. The labor-value theory of both Smith and Marx was lost in the mists of time.

*Business Week* set the tone on January, 1989, “The smart money in S&L bailouts offer fat tax breaks for fat-cat investors.” It describes how the tax benefits will shelter other company profits.

February 20, 1989: *Business Week*, “Bush S&L plan full of good intentions and holes.” Locking-the-barn-door-after-the-horse-is-stolen mood imposed new rules such as the elimination of goodwill as capital; 1,300 out of 3,000 can’t meet the 6% tougher capital
requirement. In a poor economy, with the rush of punitive legislation, well run thrifts were being pushed over the brink into insolvency.

February 27, 1989: Robert Kuttner in Business Week observes that either market discipline or good regulation was needed but the situation was the worst of both worlds.

May 7, 1989: New York Times, “How many more big bailout bills will the taxpayer have to face before Congress finally understands that uncle Sam is a lousy banker?”

May 22, 1989: FORTUNE “This is a dirty business.” The Resolution Trust Corp. is the final resting place of $300-500 billion of assets, including $100 billion in disposable real estate.

October 27, 1989: Wall Street Journal, “The reality of life in modern America is that if you want to wreck something that works, let it fall into the hands of Congress.”

November 6, 1989: Business Week, “The El Dorado of Impaired Assets; Everything Must Go.” “The RTC’s risky sell off of $300 billion worth of assets from failed S&Ls has workout pros salivating.” It describes Wall Street’s plan to turn thrifts’ “trash into cash.”


February 5, 1990: Business Week, “The Thrift Mop-Up is Already a Mess.”

September 10, 1990: FORTUNE “S&Ls: Where did all those billions go?” This colorful article shows a Sherlock Holmes type tracking footprints. In the center, a chart shows the damage in 1990, as $147 billion, growing by 2030, with interest, to an astronomical $647 billion.

!First step: $25 billion is the estimated loss due to the original mismatch of
high-cost borrowing versus mandated low-fixed-rate mortgages.

Second step: $28 billion in losses on risky real estate projects pumped up by 1982 deregulation, funded by brokers deposits, stimulated by 1982 tax laws, then hurt by 1986 tax law.

Third step: $14 billion in excessive operating costs as the industry went into accelerated growth, fueled by the brokered deposits and protected by insurance.

Fourth step: $14 billion in premium prices paid to get brokered deposits, an extra half to three-quarters of a point. The worst thrifts paid the highest rate. Even if their situation was hopeless, they figured they would live well for a few more years.

Step five: $5 billion for cost of crooks. In September 1990, the justice department had charged more than 300 individuals and convicted 231. Later, accounting firms and prestigious law firms, like Kaye Scholer, were indicted. Considering the percentage of the total disaster, crooks like Charles Keating and politicians inevitability as the brokered deposits with insured risk guaranteed the entry of all types of high risk entrepreneurs and outright crooks. Why not? It was easier to buy a thrift than a casino in Atlantic City, and the skim opportunities were better.

Step six: $6 billion loss on more real estate investments, junk bonds, business and personal loans.

Step seven: $12 billion in government inefficiency in the sell-off, sometimes too fast, sometimes to slow.

Step eight: $43 billion in government delay, by far the largest single amount. According to Fortune “by keeping hundreds of losers open rather than shutting them down in 1983,
regulators ensured that S&Ls would continue to pay depositors interest they didn’t have, cloaking their inadequacy behind government approved accounting gimmicks.”  *Fortune* blames the regulations and ignores the stonewall tactics of the league lobby, Congress and executives. Underpaid, overmatched Grey had identified the problem and pushed his solution. Few listened.

March 14, 1994:  *Forbes’* Ellie Winninghoff writes about “Smart Buyers, Dumb Buyers.”

By forcing busted S&L’s to dump junk bonds in a panicked market, Congress cost the taxpayers billions of dollars and more or less guaranteed huge profits for well-heeled bargain hunters. Wall Street loved it. The investment houses were like pigs rolling in manure. They bought and put into inventory billions of dollars of face value in junk bonds paying 20, 30 on the dollar. When the market turned, in 1991, the big Wall Street houses made billions off their junk-bond holdings.

The morals of this messy situation are quite clear: a) when politicians try to fix things, they more often that not make them worse, and b) their bumbling actions often create financial opportunities that are hidden from most people but are there for people who know the ropes.

There is very little positive about this history. About 150 years of mistakes caused by politics’ overwhelming common sense, buy short-term *ad hoc* law not properly integrated with other actions of government, and by the presumption that complex, fast changing matters can be legislated and centrally administered by government. Politics prevailed from 1984, when Grey first initiated corrective action, until 1987 when incomplete action was taken. From a process point of view, it doesn’t matter whether the responsible politicians were effectively bought by the thrift lobby or uncomprehending of the loose monster. Integration is also critical. When Volker, at the Federal Reserve, undertook his campaign against inflation with a “the sky is the limit” attitude on interest rates, someone should have recognized the need to unshackle the thrift industry, allowing market-directed variable rates on both deposits and mortgages. The earlier resistance to variable-
rate mortgages was political, not reasonable.

The damage from erroneous law with central administration can be put into perspective by re-studying Alexis de Tocqueville’s delineation between central government as a policy maker and central government as an administrator. The forefathers of political freedom, Jefferson and Madison, and the great prophet of economic freedom, Adam Smith, emphasized that both freedoms could with minimum government. John Stuart Mill, in 1850, added the observation that good government can produce good ends by advice, encouragement, and guidelines to the private sector, not by legislation.

De Tocqueville’s early warning received empirical support from the failure of central administration in Russia and Eastern Europe. Additional proof can be found in the repeated failures in socialized South America, compared to the progress of the Asian “tiger” countries Taiwan, South Korea, Hong Kong, and Singapore. Some have called them market-oriented and authoritarian, but the central authority works on economic policy and tax incentives, not detailed administration.

Contemporary social philosophers, like Ludwig Von Mises, have covered the same subject in books like “Human Action” and “Bureaucracy.” His book on twentieth century government’s handling of the thrift industry. Hayek’s books, starting with “Road to Serfdom in 1944, emphasized the impossibility of trying to centrally administer any economy, as the variables of date, time, and attitude guarantee constant sufficiently to be within the capability of human competence.

“We Still Don’t Get It! Blame the Crooks, Not the Failure of Government.”

The U.S. culture is conditioned to central-government responsibility, with a decreasing ability to tell the truth about itself. Politicians of both parties blamed the S&L disaster on deregulation and lack of regulatory supervision. A survey in June, 1990, by the New York Times, reported that 49% of those polled blamed the S&L problem on bad management and fraud at the thrifts; 25% on lack of supervision, and 17% both.
Structural and process failure of government did not even get honorable mention, but the *Times* article did not say what the questions were. The epistemological failure starts with the media. A chronological search for root causes could include at least:

1800s – The states could have left the thrifts alone. Instead they layered on popular-sounding legislation trying to eliminate all risk, all hurt, an impossible goal, producing erratic legislation.

1800 Early 1900s – The government did not recognize the costs and risks of a separate infrastructure. They could have used tax laws to encourage banks to assimilate home mortgages. Similar tax incentives could have encouraged competition from companies and credit unions. Creative financial engineering could have given tax incentives to profit sharing/savings plans with opportunities to draw on funds for either home mortgages or major medical.

1932–1934 – Hoover federalized the thrifts but made it optional with state charter. When FDR reluctantly stopped bank runs with deposit insurance, a major mistake was made. Any insurance should have been risk-oriented, or, if government mandated, it would be privately provided. Privatization by definition would involve risk-based premiums and in the subsequent speculative craze, no insurance would be available for very high risk. This is the type of fail-safe system that the decentralized “market” discipline will provide, but not central government. Even if the variables could be programmed, the decisions are adversary, political, short-term, and superficial. For these reasons, it is not surprising that the government’s results are frequently wrong and the damage control even worse. The latter is faulty because the visibility of the problem now involves placing responsibility, in turn making the process even more political.

1960s – Lyndon Johnson’s “Guns and Butter” Program resulted in printing money and inflation. He used the usual warrior-state-leader’s technique of debasing currency to try to hide the cost of war. His erroneous view of both the function of government and its ability to redistribute wealth put much of the money into enervating support for the
disadvantaged and not into education and training. It accelerated a pattern of government that eroded the creation of wealth and was a direct cause of inflation. The Republicans, under Nixon, made it worse, continuing with an unfounded war, and welfare costs.

July, 1963 – FHLBB stops cut-throat competition for brokered deposits by imposing a limit of 5% of assets. A limited action, but a good brake, that would have prevented the speculative craze. Unfortunately, the inability to attract deposits resulted in eliminating the brake in 1980. It was not changed from 5 to 20 or even 40%. It was eliminated.

1966 – Congress extends the interest rates from commercial banks to thrifts (Regulation Q), presumably to try to provide low cost-mortgages. Later higher-paying CDs and money market funds sucked out billions of depositors’ money.

1970s – Volker, the determined inflation fighter, took action to reduce inflation but put the S&Ls into an impossible squeeze between high-cost money and government-mandated low-cost fixed-rate mortgages.

1970s – Industry lobbied for variable-rate mortgages. Congress was not interested. In the ‘70s, where other government action was causing inflation and then high interest rates, sensible deregulation would have been both on deposits and mortgages. If Congress worked on integrated plans, which it does not, tax relief could also have been provided for the first mortgage to minimize the impact of variable rate mortgages.

Late 1970s – FHLBB recommends risk-oriented reserve rules. This also would have minimized the problem. The industry successfully lobbied and prevented this proposal. Later the 5%-reserve requirement was reduced to 3% without reference to risk. After the problem became visible and political in 1988-89, in the midst of plummeting asset values, government reacted with a 6% requirement, pushing good thrifts over the newly defined insolvency line.

1978 – Congress passes “Right to Privacy Act.” Regulators later shutting thrifts for
criminal acts could not search for information on criminal action.

1980 – Lobbyist and Senate aides slipped in an increase of deposit insurance from $40,000 to $100,000 at a late hour in the course of passing the bill.

1982 – Congress passes another law allowing thrifts to invest up to 40% in non-residential, makes variable-rate mortgages phase out Regulation Q and pay interest on checking accounts. Some states outbid federal deregulation by eliminating any limit on investment.

1983-86 – FHLBB, under Grey, tried to minimize the disaster by eliminating insurance on brokered deposits, adding risk-oriented insurance, limiting direct investment to 10%, limiting growth to 25% and creating a liquidation fund as high as $25 billion. There was no action on any of these proposals until 1987, when criminal action was initiated against Vernon Savings and Don Dixon. Another influential Congressman had earlier observed that if Vernon Savings was being closed to embarrass Speaker Wright, then Grey should be pleased that the Speaker was concerned with the homeless, because, after the end of his term in June, 1987, Grey would be “sleeping on a grate.”

The political delays were caused by large amounts of lobbying money being spread around Congress. Democratic Capitalism and the average taxpayer were, as usual, silent and unrepresented. Inside Job provides a full view of the symbiotic relationship of politicians with the free-spending thrift lobby and the extreme spending of the crooks. The story of the politicians’ summoning the California regulators on the Lincoln Savings/Charles Keating scandal is particularly depressing. When it was clear that they couldn’t muscle the California regulators, who were threatening criminal action, the new Chairman, Danny Wall, moved the whole investigation to Washington, an unprecedented act in the 50-year history of the FHLBB, and a devastating blow to the morale of the regulators.

During the time that the S&L crisis was developing, the oversight was provided by the
FHLBB, whose Chairman was paid $79,000 a year. His field people made $14,000. He certainly never had access to President Reagan, who never mentioned S&L after his 1982 deregulation party. Grey also didn’t have access to the Secretary of the Treasury. The examiners were detail people, with little power, and easy to deflect.

The whole audit function could not have been weaker if it had been designed deliberately. To get another 700 examiners, the argument was that there were so few examiners that each had to cover forty-two thrifts. With current technology, an automated control system could be designed to work on a national network. With the “bells and whistles” automated on the exception principle, a small number of well paid, sophisticated auditors, with decisive power, could run an effective system at a fraction of the cost.

1996 was the 100th anniversary of the demise of the People’s Party. It should be resurrected to tell the people the S&L story. The Populist failed the people and the cost of that failure continues to affect both the economy and their sense of trust. The media fails the people by reporting on the exciting, not the profound. The university fails by not analyzing such egregious errors and recommending monetary programs relieved of short-term political mistakes.

From the beginning of this republic, finance capitalism has been able to lobby undemocratic privileges for the financial benefit of a few. From the beginning of this republic, politicians have passed poorly designed and executed laws. Despite these impediments there was enough growing freedom for the political/economic system to steadily improve the lives of most. Today U.S. citizens are being warned, the standard of living for most has stagnated, and millions have been effectively disenfranchised.

What has changed? Three things: The financial privileges are getting bigger, the political mistakes are getting bigger and the world is becoming more competitive. World competition now measures not only company performance, but also country performance. A country that does not follow policies supporting its job-growth economy is penalized.
by slower growth. The U.S. cannot afford the $1/2 trillion waste of the nation’s surplus in the S&L disaster. While most of the intellectual community continues to debate abstractions, this country is in decline because of bad laws and worse execution.
Chapter 9

Citizen Education for a Successful Democracy

To what extent should the enculturation of the young into the American democracy be the major function of schools? If a major purpose of schools is to teach the young their rights and responsibilities as citizens in a democracy, then what should the schools teach? And what must teachers know in order to teach these rights and responsibilities in effective and responsible ways?252

-Roger Sodon

Through my two decades of presiding over a university, I cannot recall a single serious faculty discussion of how undergraduate education could do a better job of preparing students as citizens. The results of that neglect are all too visible.253

-Derek Bok

The preface described my grandchildren developing their own capabilities in a cooperative environment not in their education but rather in team sports or musical groups. Each individual was motivated to work hard at their own development, to draw on others in this development, and to help others in their efforts. This simple arrangement produces superior results and provides fun and satisfaction.


253 Derek Bok, President Emeritus, Harvard University, at the College of Holy Cross, Worcester, MASS, Sesquicentennial Convocation, Sept. 17, 1993, Principal Address, reported in Holy Cross Crossroads, September/October 1993, pp. 8-9.
This arrangement of human affairs works well because it is based on the dual instincts of individual ambitions and social cooperation. It seems natural and obvious but is the polar opposite of a human history dominated by competition over territory or resources. As it works better and makes people happy, it can be the foundation of every human enterprise.

In a company it can maximize results while elevating people. As an economic system it can eliminate material scarcity while improving the quality of life. In a government it is the way to serve the general welfare through participatory democracy. In the world, it can build economic common purpose than can improve the standard of living of all and eliminate violence. It is he secret to social progress as in each generation there are more people reaching their potential having learned to function in a harmonious whole. More and better educated people add to each generation’s knowledge proving a ratchet effect to new knowledge and social progress.

This arrangement is both natural and rational. Natural because it is based on inate human desires, rational as it can be demonstrated to produce superior results. The necessary components are freedom and education.

Democracy depends on freedom and education; capitalism depends on freedom and education. The great American democratic experiment for two centuries, based on democracy and capitalism despite its imperfections, has allowed hundreds of millions to live better and happier. Inspired by this success and conditioned by the failure of non-free political-economic systems, the world is ready to move to democracy and capitalism, to free market economies.

This returns to Roger Soden’s query, as education is the critical component, who is going to teach the teachers about the latest refinements of democracy and capitalism? In a closed society the answer is the state, in an open society it cannot be the state. Who then? The citizen is ultimately responsible but this is circular as how can a poorly educated citizen recognize the problem and find the solution. The answer is the university with their mission to unify and elevate by using the simple arrangement of individual development in a harmonious whole.
This was the challenge by the eighteenth-century enlightenment summarized by Condorcet (Chapter 3). John Stuart Mill almost a century later questioned how well the challenge had been met: “How far the methods by which so many of the laws of the physical world have been numbered among truths irrevocably acquired and universally assented to, can be made instrumental to the formation of a similar body of received doctrine in moral and political science.”

Mill answered his own question by suggesting that the efforts of the university to build a knowledge base for improved organization of human affairs erred first by not identifying and validating elementary truths upon which a more complicated structure could be successfully added:

Students in politics thus attempted to study the pathology and therapeutics of the social body, before they had laid the necessary foundation in its physiology; to cure disease without understanding the laws of health. And the result was such as it must always be when persons, even of ability, attempt to deal with the complex questions of a science before its simpler and more elementary truths have been established.

The elementary truth for a successful free society is that each has the opportunity to develop to their own full potential as part of an interdependent group. The first mission of education then is to provide this opportunity for students to grow and relate. All other parts of the culture should support this mission of education. It should be the first requirement in universal education, not an accidental benefit of participating in team sports or musical groups.

How is the United States educational system doing in this first requirement? Failing.

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255 *ibid.*, p. 606.
There is excessive individualism at best, kids shooting kids at worst. From infancy, children need to learn to love not hate. Television and preschool education is the incubator of character. This citizen-in-training needs to start early to learn trust, and mutual respect. John Dewey summarized this early mission at the end of the nineteenth century:

The sympathetic coordination of individual purpose with that of others in common social endeavor, and in active mutual devotion to worthy universal ideals.\textsuperscript{256}

At the beginning of this century educators understood this elementary truth that education begins with individual effort, an interdependent association, common purpose, and shared ideals. At the end of the century interdependence, common purpose and shared ideals are challenged weakening the use of this elementary truth.

Retired Harvard President Bok observed in the quote at the beginning of the chapter that education students to be better citizens was not on the faculty’s agenda and “the results of that neglect are all too visible.” Experts in the science of teaching have knowledge and new technology available for the mission, but who is going to teach the teachers? The post-modern cult dominates many universities where the concepts of common purpose and shared ideals are regarded as anachronisms. It underscores the dilemma, if the university is the logical place to unite and elevate citizens in a free society what will the result be if many universities and professors regard these as quaint concepts from an innocent past?

Every child from infancy in a free society needs to know how to pursue the mission of life, liberty and the pursuit of happiness. They need to be trained to function in a harmonious whole. They need to learn that superior results, fun, and satisfaction are the products of any endeavor where people share a sense of common purpose. This

elementary truth should be the foundation of educational knowledge and it should be the mission of citizen education.

But in an open society how are citizens educated to a common ideology without it becoming unacceptable propaganda?

French intellectual Jean Francois Revel emphasized this distinction:

The teacher can either teach or indoctrinate. When the teaching is more important than the indoctrination, education fulfills its principal function in the best interests of those who receive it and in the interest of democracy. On the other hand, when indoctrination takes precedence, it becomes harmful, an abuse of childish innocence, and substitutes imposture for culture.\textsuperscript{257}

The answer is a government that provides the broad mission and funds and universities free to examine, test and promulgate the best of options, freely chosen. The university is then the locus for both curricula and pedagogy. John Dewey challenged the university to accept this vital role of a free society:

It is clear that our educational systems are in need of some kind of direction and systematization from expert sources. If the government does not furnish this, so much the greater the necessity for its being undertaken on a voluntary basis. It must be assumed with the authority of science, if without that of bureaucratic control. The universities are the natural centers of educational organization, unless the chaos of centrifugal force is to continue indefinitely. It is for them to gather together and focus the best of all that interest in the great variety of present practice, to test it scientifically, to work it out into shape for concrete use, and to issue it to

the public educational system with the imprimatur, not of governmental coercion, but of scientific verification. Organization on the basis of cooperation, of free and full interaction of the various parts of our educations system is a necessity.258

How would the first mission be funded to teach every child to love, not hate, to teach them that their individual ambitions are best accomplished in a cooperative society. Most citizens would be enthusiastic to sue their federal, sate and local taxpayer dollars to define the curricula and pedagogy to accomplish such a purpose.

Presently federal funding has great influence in universities, but for other purposes. Taxpayer dollars to assimilate, test and promulgate the most effective way to teach children to love note hate is not a significant part of this federal funding.

Peter Brinelow in Forbes described “academic politics” with the observation that “some of the bricks in the ivory tower are supplied by politicians. They are a mixed blessing.”

Brinelow did the scorekeeping on federal research grants directed to specific universities for political reasons. It was over $800 million in the early 1990s, dipped to under $400 million during the “Republican revolution” in 1996 and then grew back to $800 million in 1999.259

Children who are taught from infancy, first by television, the benefits of cooperation, common purpose, shared ideals would not later invade schools and kill kids. The Littleton, Colorado tragedy provoked the question, among others, of why the “jocks” harassed the “nerds”. Both had been conditioned to differences and violence. They had not been conditioned to understand and appreciate differences in any society. They had not been taught mutual respect and cooperation.


Two decades ago, a program was run in Lowell, Massachusetts in participatory democracy. Children learned that society is made up of people with different talents and interests but that society reached potential when each was given the opportunity to reach full potential in their particular talent. In their school society, the “jocks” participated by helping maintain their civil order. The “nerds” with skills on the calculator became respected because they were necessary to handle the financial aspects of their endeavor.

There are numerous tests in numerous places similar to Lowell that regularly validate that trust, mutual respect and cooperation produces superior results and is more fun.

Robert Owen, a pioneer democratic capitalist, learned that the training of cooperative workers began at an early age.

The argument for democratic capitalism is that individuals innovate and produce best in an environment of trust and respect.

Robert Owen at New Lanark in the early nineteenth century (Chapter 3, p. 21) learned how to improve his spinning mill’s results by better wages, shorter hours, better hosing and the encouragement of sobriety. In time, he recognized that the character he admired and sought in his workers was formed at a very early age.

Owen understood that for workers to reach their fullest individual development they had to first learn how to function in a harmonious whole. Although this instinct is natural to humans it had been suppressed by thousands of years of predatory domination. Owned understood to let it flourish in his New Lanark schools:

He brought together upwards of a hundred children, from one to six years of age, under two guardians. No attempt was made to teach them reading or writing not even their letter; nor had they any set lessons at all. They were trained to habits of order and cleanliness; they were taught to abstain from quarrels, to be kind to each other. They were amused with childish
games and with stories suited to their capacity. Two large, airy rooms were set apart, one for those under four years and done for those from four to six. This last from was furnished with paintings, chiefly of animals, and a few maps. It was also supplied with natural objects form the gardens, fields, and woods. These suggested themes for conversations, or brief, familiar lectures; but there was nothing formal, no tasks to be learned, no readings from books.\textsuperscript{260}

Most mill areas were filled with urban blight, the life expectancy was low, the children diseased, and crime prevalent. At New Lanark, out of three thousand children who had worked and studied there over a twelve-year period, only fourteen had died and not on has suffered criminal punishment.\textsuperscript{261} Owen had defined concepts, provided protocols, and proved that it all worked superbly.

Owen had found truths on the factory floor that American social philosopher John Dewey found in scholarly analysis. Dewey emphasized human duality and instructed his students: “Individuality cannot be opposed to association. It is through association that man has acquired his individuality and it is through association that he exercises it.”\textsuperscript{262}

Owen also saw that providing the child, ages 4-6, opportunities to follow his or her curiosity about natural events was a precursor to teaching the child how to think. Dewey later expressed it this way: “The native and unspoiled attitude of childhood, marked by ardent curiosity, fertile imagination, and love of experimental inquiry, is near, very near to the attitude of the scientific mind.”\textsuperscript{263} It was this capacity to think, Dewey believed that was a foundation for the successful democracy.


\textsuperscript{261} \textit{Ibid.}

\textsuperscript{262} \textit{John Dewey and American Democracy}, p. 44.

\textsuperscript{263} Dewey papers. “Lecture Notes Political Philosophy, 1892”, p. 38.
A Challenge to Universities

The improvements which, in modern times, have been made in several different branches of philosophy, have not, the greater part of them, been made in universities; though some no doubt have. The greater part of universities have not been very forward to adopt those improvements, after they were made and several of those learned societies have chosen to remain, for a long time, the sanctuaries in which exploded systems and obsolete prejudices found shelter and protection, after they had been hunted out of every other corner of the world.264

Adam Smith, 1776

In the first part of this chapter the responsibility of the government to fund and the university to teach children to love not hate was described. This lesson is the elementary truth upon which the superior economic system, democratic capitalism, is base, upon which participatory democracy depends, and upon which world economic common purpose can develop.

The university is failing to present this elementary truth. This section examines how well the university is teaching the means to the end of “life, liberty, and the pursuit of happiness” through the combination of democracy and capitalism. Is it possible that the elementary truth is integrated into the university’s presenting of democracy and capitalism? Are the concepts of cooperation, trust and mutual respect self-evident in this presentation?

Unfortunately, no. The university not only does not teach how to develop character necessary to a successful democracy, from infancy, most of the universities add to this failure with a distorted presentation of democracy and capitalism. This failure of both omission and commission is in four general categories:

• The combinations of capitalism and democracy that flows from the elementary truth of how people relate cooperatively is not presented for student examination.

• Energized by criticism of the excesses of other forms of capitalism the universities teach young reform minded students a contempt for commerce and a love of state. They teach them to be collectivists. They do not teach the protocols of governance necessary for participatory democracy, and an understanding of the distinction between central government policy and suffocation central administration.

• The university does not teach reform minded students the rudiments of economics and finance necessary to slow, then reverse the financialization of the economy. Lacking this knowledge, reform is not pursued to eliminate government errors and special privileges.

• The university does not properly equip citizens to make foreign policy a matter for political debate, not the prerogative of an imperial president. The United States will move successfully from the world’s super power to moral and economic leader only if citizens understand world politics and the ways to economic common purpose.

Part of the reason for failure is the academician’s contempt for commerce and instinctive love of the state, a legacy that goes back to Plato. An additional reason is the limitations of single discipline scholarship that thwarts the sense of context vital to an educated person, and prevents examination of how democracy and capitalism can be integrated in the most synergistic way.

The enlightenment challenge had been met, the end confirmed as attainable, and the means to end had been specified. Unfortunately, as Adam Smith lamented, academia had
not structured the process necessary to unify this knowledge for optimum governance of human affairs. Because of this default, the coherent system was neither assimilated nor promulgated by educational institutions. Instead, alternative systems were espoused and tried, with tragic results to society.

As the intellectual community had never organized the process to confirm the end and analyze the means, it now denies the end and contributes to confusion about the means. Many agree that the world is moving toward “free markets,” but education neither defines or refines it. As a consequence, there is a death struggle among forms of capitalism. Government leaders are not educated to design a monetary system capable of handling the needs of global capitalism, dominant speculation results. Business leaders are not educated to involve people and distribute surplus as the way to maximize profits.

This educational opportunity and obligation will note be met unless the intellectual community reexamines its fundamental contempt for capitalism and its abandonment of idealism in the light of how democratic capitalism can both eliminate material scarcity and elevate lives.

Such a reexamination is multidisciplinary by nature, a complex effort to assimilate information, much of it contradictory, and to analyze, prioritize, and synthesize that information into an integrated, coherent whole. The product, putting the human being into past and future context, is the original mission of a liberal-arts education. But academia has never had the capacity for multi-discipline examination and now the cultural conditioning of contempt for capitalism and the abandonment of idealism ahs institutionalized a large wall of resistance.

John Dewey understood the weakness of single-discipline study:

For one danger of higher education, from the point of broad human interests, is that with high specialization there is increasing likelihood of the center of scholarship getting removed from the mass of men, and the
things of daily life. Culture becomes tangential to life, not convergent.\textsuperscript{265}

To be coherent, the educational offering needs to include an understanding of the conflicts in capitalism, the abandonment of idealism by many, and the forms of collectivism with an elite still trying to micromanage complex affairs top-down. Students should have the opportunity to debate all of these propositions:

- That democratic capitalism is the only common ideology that can unite all in a nation and can unite nations. Democratic capitalism is based on a moral imperative. However, it can reach a larger audience as a pragmatic argument that freedom-based democratic governance benefits from the participation of all, and consequently is the most effective way to maximize surplus in a company or manage government or education.

- That global capitalism is being corrupted by finance capitalism’s domination of commerce. In the 1990s, the economies in Asia had been growing and improving the lives of millions. Their economic damage is a tragic case-study of a wrong turn for society led by the United States (Book I, Chapter 7)

- That society cannot sustain itself without a common ideology. Democratic capitalism can be that ideology, but it cannot succeed without the support of the intellectual community, many of whom now reject the concept of social progress.

- Acceptance of Marx’s advice that society is dependent on commerce and that social progress is possible only by moving to a superior form of commerce. Movement towards a superior form of commerce has always been in the direction of more freedom, moving from the slave

society of Athens, from the serfdom of the Middle Ages, from the wage-slavery of mercantilism, to the educated, independent, involved associates of the Information Age.

- Recognition that superior form of commerce was defined by Adam Smith, tested by Robert Owen, and refined by John Stuart Mill. It is democratic capitalism, where the participation of all in a harmonious environment maximizes surplus, it is an industrial philosophy and practice regularly validated today by thousands of democratic capitalist companies (Book I, Chapter 4).

- Recognition that the profit-sharing and stock-ownership features of democratic capitalism can distribute wealth broadly, motivating the associates while energizing the economy (Chapter 7).

- Understanding that global capitalism is not a monolithic enterprise run by predatory and greedy capitalists. It often is, and can be, the democratic economic force that eliminates scarcity and the moral force that uplifts all society. It can be a source of power diffusion, not concentration.

- Because the predatory forces of war and imperialism have lost economic logic, the goal of world peace and plenty is attainable in the twenty-first century.

- Acceptance that the violent events of the twentieth century did not invalidate the goals of human governance through a rational order, rather the persistent violence has been caused by government errors by leaders poorly trained in universities.
• That, despite the failure of communism and socialism, collectivists ignore the evidence and still try to micro-manage complex societies, suffocating participatory democracy, wasting needed funding, and failing on their social mission.

• Recognizing that the optimism of the Enlightenment is still appropriate. People can organize society to attain full potential when the means is to free individuals for full development as part of a harmonious whole.

This educational offering of collectivism is combined with a limited examination of democratic capitalism. Young students with the greatest sensitivity to the human condition and the greatest desire for a contributory career, are the most damaged. At that beautiful moment when students sense a unity among people and feel a desire to make it a better world, they are deflected to systems that do not work, and they have no opportunity to inspect the one system that does work based on these opposite views:

• Mercantilism is the cruel economic mechanism. Democratic capitalism both maximizes surplus and improves the quality of life.

• There is an inherent tension between ultra capitalism and democracy, but, there is an inherent symbiosis between democratic capitalism and democracy.

• Ultra capitalism’s mission is to maximize profits and stock price, democratic capitalism’s ultimate mission is the feed the world, unite in economic common purpose, and stop war.

• Ultra capitalism treats the employee as a cost commodity to maximize surplus; democratic capitalism elevates the associates to maximize surplus.
• Maldistribution of wealth is inherent in ultra capitalism; democratic capitalism through profit-sharing and ownership distributes wealth broadly.

Some students become bureaucrats, educators, community leaders, and then they pass on the same cultural conditioning to the next generation, meanwhile treating capitalism as the enemy of social progress. The bureaucrats so trained are suspicious and adversarial with an instinct to police and punish industry. Generic capitalism is assumed guilty without a trial. Mercantilists and speculative capitalists regularly provide greedy examples to refresh this view. Captains of industry who pay themselves millions of dollars a year have no sensitivity to how their excesses help sustain public contempt.

Lacking common ideology, the United States will eventually go into decline. Ironically, for most citizens the common ideology has not changed: It is the hope for a better life for themselves and their kids. What has changed is the strength of the corruptions and the academic disinterest in examining that capitalism which captures the power of participatory democracy with the energy of capitalism.

There is an evolving technology that can revolutionize education in the sense that each individual can be presented with the opportunity for continuing self-development. The same delivery technology can sensitize people how to live in a harmonious whole. Yes, people can be sensitized to love, not hate, if their mental bombardment, starting with TV at the earliest age, includes the benefits of social cooperation.

Public Education Can be Reformed by the Principles of Democratic Governance

No part of American life that could be improved more dramatically than a conversion of public education from the present top-down, command-and-control system to the elementary principles of participation and cooperation. Instead, disenchantment with public-school education provokes debate on national standards, charter schools, school
choice, vouchers, and trashing the teachers’ unions. The common denominator is running away from the problem.

The simple mission of developing both sides of the child’s personality, individual skills and capacity to contribute to a harmonious whole, is well done by many teachers. The *de facto* mission, however, for the key person, the principal, is not now development of both sides of the students, but keeping parents away from the superintendent, boosting tests scores, and getting reports in on time.

The structure is worse than common-and-control. In many cases, an ill-informed interpretation of decentralization resulted in “decentralization” to school boards which then become involved in administrative details. The result, in most cases, is the worst of both worlds, a principal with a confusion of direction and little freedom to release the vitality of both teachers and students.

In every effort to free the system to release the latent energy of people there has to be a key leadership level. In education the chief “emancipator” should be the principal. The end is participation and contribution from teachers and students but the means is the principal with the requisite authority and responsibility for results. Authority and responsibility can be passed on to the teachers but the principal is key to accountable performance to the community and key to holding each teacher to accountable performance. This form of organization is regularly validated by certain principals who assume the prerequisite authority and free the teachers to educate students far beyond other schools in their immediate environment.

There are so many positives in education: Most teachers are good people attracted to the opportunity to contribute, to make a difference. There are also many experts in the science of teaching and new delivery systems that can make education a continuous process from cradle to grave.

What is lacking is a clear mission and funding from the federal government to the
universities to examine, test and present the best ways for very young people to learn trust, mutual respect and cooperation. This fundamental needs to be followed by a mission and funding that challenges the university to finally assume its role as the scientific assimilator, tester and promulgator of knowledge about the best organization of human affairs.

This is a country based on political and economic freedom, democracy and capitalism. But, which democracy? That which tends to anarchy, that which tends to suffocating central administration, or the one that depends on the participation of educated citizens?

Which capitalism? The one that maximizes profits, concentrates wealth and demeans people or the one that maximizes profits, distributes wealth broadly and elevates people?

The university that can fulfill this responsibility and give the world its best ever chance in the twenty-first century is not the university that has abandoned idealism. It is the university that is excited by the potential of people and society and is prepared to assume the role as the locus of knowledge on how each individual and society in general can reach full potential.
Chapter 10

ERISA
How Government Blew the Opportunity to Invest Your Pension $
Greedy people on Wall Street and CEOs contributed to this corruption of capitalism but 
the root cause is bad design by your government. They did not structure the plan using 
tax policies and regulation in order to accomplish the stated mission. In 2006 your 
government passed a pension reform act that addressed none of these basic questions but 
tried to put band aids on the government insurance of pensions leaving the usual question 
of how long it will be before the mounting damage is passed onto the taxpayer. You will 
be doubly hurt by your government, a badly damaged pension and your taxes to pay for 
the bail out.

You need to determine how much of the trillions of dollars that should have made your 
retirement comfortable is in fact invested in economic growth or how much of it is still 
sloshing around Wall Street providing substantial annual consumption for you money 
managers. You the people are responsible for deciding how your retirement money is 
invested. Those now making the decisions for you are financially motivated for their own 
short-term gain, not to maximize the amount of money available to you on retirement. 
Because of this, you need to understand the conflict between democratic capitalism and 
ultra capitalism and why the former will maximize your retirement income, and the latter 
can destroy your savings. You need to learn how to reform the economic system by 
moving from ultra-capitalism to democratic capitalism.

Democratic capitalism produces more wealth, broadly distributed, through the 
participation of wage earners in forms of ownership. The work culture is one of trust and 
cooperation. Ultra-capitalism is a combination of modern mercantilism in which the wage 
earner is treated as a disposable cost commodity with a finance capitalism that is 
dominant over rather than supportive of economic freedom. The work culture is one of 
fear and intimidation.

Your study has critical social implications because the economic system that will provide 
you the greatest amount of money in retirement is, at the same time, the economic system 
that will maximize domestic and world economic growth, benefiting an increasing 
number of participants and providing tax revenues to help the rest.
To assist you in your study and discussion are references in this article to books including my book *Democratic Capitalism, The Way To a World of Peace and Plenty*. At the end of the article there is a glossary of terms, an understanding of which is necessary in your study.

You will find that democratic capitalism was well defined by Adam Smith in 1776 but that his conditions for success have never been observed. It is understanding these conditions and application of your political power for reform that will bring democratic capitalism to full potential and provide you and your family with a comfortable retirement.

Congress passed ERISA in 1974 to protect your pensions. It was a potentially dramatic moment in the history of capitalism because much as $100 billion a year was mandated for investment. Unprecedented amounts of patient capital would be invested in order to provide retirement income many decades in the future, along with a “capital wage” from dividends, averaging 6% at that time, that could be spent or saved to the further benefit of the economic growth.

Where would it go and how would it get there? The possibilities were exciting: stronger economic growth by companies issuing stock for investment in facilities and new product development and public investment in education, urban transit, research in new energy sources, and environmental needs.

Corporate America initiated the short-term earnings pressure by the way they measured performance by their money managers. The analysts at the beginning of the bull market were usually young low paid MBAs. With all of the attention on quarterly earnings against prediction they became rock stars and many moved up into millions of dollars a year compensation. In most Board meetings the first featured event was review of how these outside observers described the company’s fortunes.

Directors and executives of public companies were personally threatened by ERISA and rushed to insulate themselves from responsibility for investment. They did this with

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layers of advisors outside the company. Company pension committees then reviewed the performance of the money managers quarterly and then fired those whose performance for the year was not competitive with other managers. This was the genesis of the perversion of patient capital to short term that changed the nature of capitalism in America. The discipline to invest surplus for long-term benefit is the essence of capitalism and the results of which cannot be measured in less than three years. The shift to short-term measurement eventually provoked cost cutting as the quick way to improve earnings.

Corporate America gave the money to outside managers and measured then on quarterly earnings per share and fired them on annual results that were less than their competitors. This same short-term measurement was applied to corporate performance and began the shift the economy away from “stakeholder” capitalism to “shareholder” capitalism. The former meaning the long-term obligation to customers, shareholders, employees, suppliers, and the community; the latter meaning only immediate profits for the owners of stock.

This new capitalism succeeded because management so motivated can produce quick profits simply by stopping long-term investment in new products and facilities. They fire people by the thousands, “downsizing” was the expression. The media and the Business Schools celebrated this “American Model” as though they had found the long sought “new mode of production.” There were a lot of riches being visibly enjoyed by a few.

The $100 billion a year was not invested it was given to wall Street with the assumption of investment. The investment bankers would handle the bonds and the stock market would move the money coming into the market into new growth stock. Wasn’t that their function? This simple dynamic, however, had a few important conditions to be understood and observed by the designers of ERISA. For the free market to reach full potential money must be neutral, that is, without influence on the commercial process. This, in turn, required that asset inflation in either stocks or real estate must be controlled by tax policies, bank and margin requirements. The obligation of government to control currency and credit for the general welfare meant that the tendency towards excessive
liquidity, too much money, would have to be anticipated and controlled. Too much money always gravitates to speculation.

Too bad! None of this was done and most of the money flowed into the stock market and not enough of it flowed out in new stock for growth. The money had no where to go but up and the longest bull market in history began. The pension money flowing into the stock market soon dominated the economy with enormous rewards or punishment for a few cents change in quarterly earnings per share. Instead of the peoples’ money democratizing capitalism, it was perverted into a new mercantilism in which firing people was the way to produce quarterly earnings. Stocks that had been held for six years on average were sold in less than a year. Dividends shrank from 6% to less than 1% in the bull market. Despite the greater volume of transactions, fees for handling the money went higher. Mutual fund fees reached ten times that of index funds that produced the same or better results. Profits from financial services exploded from 4% of total corporate profits to over 40%.

In this environment, CEOs’ overriding consideration was building up and protecting the short-term price of the stock. Shortfall of a few cents a share in quarterly earnings per share could wipe hundreds of millions, even billions, of dollars off market value. A high stock price also made acquisitions possible, and a low one made takeover more likely. They “smoothed earnings” by dipping into inventory or bad-debt reserves; slipped into “creative accounting” to prevent a miss against quarterly targets; and finally some plunged criminally into faking earnings. CEOs trapped in this dynamic hoped that the shortfall was temporary and that good times coming would correct the books. When this did not happen, they were hooked on faking earnings.

Once CEOs were trained like Pavlov’s dog the Wall Street agenda was easily implemented. Wall Street did not like dividends because they did not make money on dividends and preferred that companies keep the cash and use it for stock buybacks or as an attraction for a deal. Wall Street hates dilution so those companies thinking about using the stock market for its original purpose of raising cash for investment decided not to sacrifice stock price by dilution. On the all-important earnings-per-share upon which
the price of the stock was based any addition of total stock would increase the divisor and arithmetically reduce the earnings per share, e.p.s.

This short-term profit-pressure not only cut existing programs but also limited the amount going into new investment. The expectation that ERISA money would flow through the stock market into investment in the job-growth economy was incorrect. Some of it was invested but most of it went into driving the values of stock up and up with much of it being peeled off by those handling the money. Many of the apparent investments in new equity issued were deals with the same short-term motivation to make lots of money at the beginning of the deal with little risk.

The wage earner at the time ERISA was designed should have expected a long-term secure double-digit return on their pension investments, one-half from dividends and the other half from appreciation. The expectation that dividends would continue to provide about one-half of the total return was also a victim of the short-term pressure. Tax laws encouraged savings in retirement funds like 401 (k) by allowing them in pre tax dollars and tax laws allowed deferral of taxes until retirement but that provided the money manager with a built in lock on the money. Tax-free dividends for the people would have provided persistent pressure to distribute surplus in dividends not in stock buybacks or deals but that did not happen and dividends during the Bubble economy shrunk in absolute amounts and in percentage of profits paid out. After the Bubble burst dividends recovered some but in late 2006 are only returning 2% and more money is still going into stock buy backs to reduce the total shares in the divisor and arithmetically improve the e.p.s.

The Congressional designers of ERISA believed in the free market in general terms but did not understand these few conditions needed for the free market to spread wealth:

- Capitalism succeeds by a discipline to invest surplus capital for long-term gain, instead of short-term consumption. In your study learn how much of the trillions of dollars of pension savings in the past thirty years went into consumption by finance capitalists instead of investment for the benefit of the wage earner.
- Economic freedom needs neutral money, a medium of exchange without influence on the commercial process. Neutral money must be enough, but not too much, patient, low-cost, and non-volatile.

- Peace was Smith’s first condition for success of economic freedom because nothing consumes more resources and destroys social cohesion more than war.

The following are the few rules that we would have included if we had been part of the design of ERISA. The mission presumably was to direct the money into investments that would provide the maximum amount of money for your retirement.

Public companies should be measured and held accountable to a three year running average of sales growth, profits, and cash flow against management predictions.

*It would be helpful in your investment decision to have a goal that balanced return and security with the emphasis on security. If you feel that a 10-12% safe return is the goal then a good start would be 6% dividends, the long-term average. If these dividends were tax-free there would be persistent pressure on companies to make dividends the highest priority next to reinvestment in growth. With half of the return in dividends the goal for a modest long-term corporate profit growth of 5-7% is consistent with increasing world competition.*

Tax-free dividends for low-and-middle income wage earners

*Tax-free dividends would give the wage earner that long sought “capital wage” that could be spent or saved for the benefit of the economy. The tax free feature would insure pressure on companies to again distribute the surplus in growth investment and dividends. Although the wage earner might spend some or all of the dividends for a time the gross amount diverted from stock buy backs and non-strategic acquisitions is so large that the final pension can still represent a 10% return.*

Speculation with borrowed money should be limited.
Our committee should discuss what neutral money is and how it can be provided. We will learn that there never has been neutral money because our government has never controlled asset inflation in stocks and real estate and in fact denies that it can be done. It can be done with tax policies, margin and bank reserve requirements and must be done to protect your retirement savings. Too much money, “excessive liquidity” always gravitates to speculation or high-risk projects.

The rules are few and seemingly simple but require functional understanding of the many variables in the economic equation. They are reviewed in the following with regular reference to how they have impacted your retirement savings. Deeper study is encouraged by references to books.

At the time of ERISA most pensions were defined benefit where the company was responsible for paying a certain amount each month in retirement. Companies said that it was their money because they had to pay a specific benefit on retirement. For this reason they were able to take performance over estimate into current profits. In the quarter century before the market crashed the estimate used on what the pension money would earn was steadily increased from a conservative 6% to 11% or more. Historically half of a double-digit return was dividends but they were being steadily reduced as part of the return. At the time of ERISA the stock market valued earnings at about 7 times, that is a dollar of earnings per share meant a stock price of $7. This was low as the long-term average was 15 times. As most of the hydraulic pressure went, not into new equity for growth but rather into pushing up the value of stocks by the end of the century earnings were valued at about 30 times. That same dollar of earnings was now worth $30 on the market. Extraordinary amounts of personal wealth was produced by this phenomena.

As the pension portfolio grew in value and the return estimates became more aggressive companies were able to describe their pension plans assets as “over funded” and many declared a funding “holiday.” The motivation was to improve short-term earnings. After the market went down many of these plans were in fact under funded. Steel, autos, and airlines with the greatest concentration of defined benefit plans were hit hard and could not pay the pensions in contradiction to the original mission of ERISA. Their obligations
were dumped on the PBGIC government insurance that was quickly exhausted with further cost to be dumped on the taxpayer.

During this time retirement savings shifted significantly from defined benefit plans, with an assured amount to be paid each month of retirement, to defined contribution in which the company put a certain amount into the plan but the individual was responsible for the “investment” decisions. In addition 401(k) plans became popular because the individual was able to save from pre-tax dollars and most companies made some level of match with the individual’s contribution.

During the same quarter century there was a dramatic shift in the distribution of corporate surplus. There are four places the surplus can be distributed; reinvestment in growth, dividends, stock buybacks and deals. Stock buy-backs took cash out of the company to buy stock in the market theoretically improving the earnings per share because there were fewer shares to divide into the earnings. Surplus used in acquisitions looked like investment but most of the money went to the deal makers and in fact the acquired company in many cases borrowed money to pay dividends and fees to the acquirers.

There was about $1 trillion dollars spent on stock buybacks and non-strategic acquisition during the quarter century that could have been invested in growth programs, maintenance, and facility replacement. It is now clear that major companies sacrificed vital investments in their prime facilities. We now have CEOs of Long Island Lighting explaining away thousands of suffering people without power as some type of act of God. We have the CEO of BP Oil explaining how their transmission pipes in Alaska were so eroded that they had to shut the line down adding to price volatility in gasoline

Corporate raiders showed the way by taking advantage of the easy credit amplified by the flow of pension money to attack companies with a premium offer over the stock price and then fire people and strip benefits to pay for the acquisition. Takeovers almost always increased the price of the stock and for that short-term reason gained the support of the money managers motivated to improve their standing in measurements such as the Becker Median. This was an extraordinary perversion of capitalism: the very people responsible for the future value of the peoples’ investment were financially motivated by
the system to chose short-term results that cut back on long-term investment!

ERISA money turned into easy credit that drove the bull market and funded adventures from LTCM to Enron. Global companies practiced wage arbitrage moving quickly into the lowest wage opportunity with no thought of wages high enough for reciprocal purchases without which free trade does not work. The Southeast Asian countries had their economic momentum reversed by hot money and currency speculation. Muslim leaders called America “economic imperialists.” Russia tried to move to this form of capitalism with “shock therapy” with disastrous results.

With easy credit and favorable tax policies deals proliferated on Wall Street and a crucial change was made in how they priced services. Instead of hourly-based advisory annual fees they now priced on a percentage of the deal. As deals proliferated and became bigger finance capitalists were the first to be comfortable with annual compensation in the $50 million to $100 million range. With the encouragement of the finance capitalists and money managers CEOs were then encouraged to participate in the feast with millions of stock options and increasing compensation from a growing smorgasbord of plans. The practice of Board Compensation Committee to review the internal logic of compensation was abandoned for comparison only to a peer group of other overpaid CEOs.

During the 1980s and 1990s everyone seemed to be enjoying enormous wealth. Hidden was the reality that the big increases in productivity were going to the top 1% and not to the wage earner. Inequalities of wealth reached record levels. The Business Schools and financial press adopted this new “shareholder capitalism” as the sought for new mode of production. Managers who tried to hang on to long-term building plans were derided as “entrenched management,” and support went to the raiders. Well known people warned of the developing dangers; Warren Buffett persistently recommended long-term investment, famous speculator George Soros warned that instabilities in the international monetary system threatened both the economy and social cohesion; famous M&A attorney Marty Lipton warned that we were sacrificing long-term growth for short-term earnings.

A major reason that capitalism was corrupted by ERISA was a lack of control of asset
inflation. This was not new, however, as the government has never prevented asset inflation and that has caused every recession including the crash of ’29 and the Great Depression. The government has fought price inflation vigorously with dedication to keeping enough people out of work to prevent it.\(^{267}\) This is a policy that favors the wealthy and that is why it is a priority. A little bit of inflation helps the debtors who repay with fewer dollars and conversely hurts the creditor class.

Asset inflation in stocks and real estate has done more damage to the people in repetitive business cycles. They began in the first Washington administration when Alexander Hamilton made good on his promise to get the wealthy and powerful involved in the new government by giving them non-democratic privileges, the opportunity to borrow large amounts of money to speculate. This has been the prime reason that wealth is concentrated and capitalism functions at a fraction of potential. When Alan Greenspan was chairman of the FED he testified before Congress that there was nothing the government could have done to prevent asset inflation in the Bubble Economy. The tools to prevent asset inflation should be obvious, they include bedsides interest rates, bank reserves, margin requirements and taxes. The urgency to control asset inflation and the tools to do it were presented in a paper in April 2006 by the Central Bankers Club BIS in Basel, Switzerland, titled “Is Price Stability Enough?”\(^{268}\) At the same time China is increasing band reserve requirements to cool their asset inflation.\(^{269}\)

ERISA was not the only bad design of government. When Paul Volker became Chairman of the Fed in 1979 he was peppered by the European Central bankers because of the extreme price inflation in America a product of Johnson’s “Guns and Butter” program. Volker conducted a scorched earth policy to control price inflation taking interest rates up to 20%. He succeeded and at the same time destroyed the S&L industry who were in the impossible bind of borrowing high cost money short and investing in low returns long. He also bankrupted several South American countries who were trying to build their economies. How our bankers got away with floating rate interest loans is another story.

\(^{267}\) Phillips Curve and NAIU pp.
\(^{268}\) BIS #
\(^{269}\) 7.5% to 8.0% in and then to 8.5% in?
Countries struggling to improve the lives of their people should never get blindsided by the cost of their loans going up by several multiples.

The damage from Johnson’s “Guns and Butter” was long and wide spread as will the damage from the cost of the Iraq war. Without debating the merits of either war should we not consider a Constitutional Amendment that requires all wars to be self supported by immediate taxes sufficient to cover the cost of war. Politicians of the Warrior state know that they can count citizens tend rushing to support their president when he declares war. It would be better if citizens examined the circumstance more carefully as they would if taxes were to be increased in that year to pay for the war.

Volker’s scorched earth price inflation fighting destroyed the S&L and then Congress made it worse. They began with the wrong mission: “save the S&LS” when the original mission was” low cost mortgages” This is typical of Congress to not even get the mission straight. The S&L, another case study for students of capitalism and democracy, is examined in chapter ?

Glossary:

**Derivatives:**

A value based on an underlying instrument such as stocks or currency. They did not exist in most forms until 1980 and now $4 trillion a day is traded in the world’s electronic casino. This is about one-half of America’s total commercial activity, GDP, for the whole year. Former Chairman of the FED lauds them as they add liquidity and provide a discipline. But who needs more liquidity, we have more than enough and I am not sure that quickly pulling the value of remote currencies back into their norm has social value. Carol Loomis of *Fortune* called them “Alligators in the Swamp” in a 1994 article and her friend Warren Buffett more recently called them “time bombs” for the holders and for the economy. As more of your money is now going into hedge funds and derivatives you should study and decide on the proper relationship of risk and reward.
Distribution of Surplus:

Companies can use their surplus in four ways: reinvestment in growth, dividends, stock buybacks, and deals. The first two can have a direct and positive effect on economic growth and the ultimate retirement savings and for that reason have a social connotation. Present governance gives full authority to the CEO to decide on distribution. This should be a matter for full Board attention as it is crucial to both company’s, nations and world growth.

Earnings per share: Total after tax profits divided by the number of shares outstanding. Profit is not the same as cash surplus as it includes non-cash calculations like depreciation and amortization. A cut back on investment in new equipment, for example, could make depreciation greater than expenditures and thus an addition to cash and surplus.

Hedge funds: At one time an investment opportunity for those who could put in a million dollars but now becoming a favorite of money managers with your retirement savings. They are many things to many people but in general they are unregulated investment pools that tie up money for longer periods of time and provide almost no disclosure. They are enormously profitable as they charge fees double mutual funds and take 20% of the profits. Watch this one carefully because of the obvious motivation to maximize profits in an enterprise with heavy use of derivatives that allow subjective judgment of future value. Beauty is truly in he eye of the beholder. When Enron “a hedge fund on top of a gas line” needed to improve quarterly earnings the traders were asked to “crank the dials” which meant go back to future estimates of profit and squeeze more out.

Study the LTCM experience in 1998. They were a very successful hedge fund that claimed that they made money with a “market neutral” approach, that is they bet enough
on stocks and derivatives going up and down and for the reason were not vulnerable to
the market direction. There is great pressure on hedge funds for performance and as more
get into the act it gets harder to make money on anomalies in currency for example. For
this reason LTCM “went directional” on Russian bonds just in time to get clobbered
when they defaulted.

Ownership

Can vary from full ownership through ESOP plans, to stock purchase through profit
sharing plans, to pension savings. Superior performance requires the coupling of the
financial motivation with the work culture of trust and cooperation.
Chapter 11

Enlightenment Two

The Integration of Knowledge for Social Progress

The 18th century

Inspired by Isaac Newton’s scientific identification of order in the universe, some of the budding social scientists of the Enlightenment searched for the best order in human affairs. Their goal was infinite human progress; the means was more wealth, broadly distributed, and the prevalence of law—rather than violence—among nations. Voltaire and the French philosopes emphasized the humanistic aspects, Adam Smith articulated the economic structure, and Immanuel Kant foresaw the political-ethical agenda.270 Francis Bacon’s experimental method combining reason and empirical verification was useful to specify the means and validate the ideal. Underlying the effort was a democratic belief in the worth and potential of each human individual.

Enlightenment thinkers in America, founders of the Republic, aimed at designing a political structure that would reflect the will and wisdom of educated citizens to displace the egregious mistakes of the powerful few. The Marquis de Condorcet, a French revolutionary, integrated Enlightenment knowledge as a social program to benefit generations to come, predicting that new freedoms would have their best opportunity in America, “that happy land where freedom had only recently kindled the torch of genius.”271

Most of the world, however, was not ready to shift to economic common purpose. George III fumbled his way into the American Revolution; Louis XVI precipitated the French Revolution and lost his head; Condorcet died in prison during the Reign of Terror. The forces of business-as-usual continued their self-serving policies of nationalism,

271 Ibid., p. 432, see pp. 62-73.
imperialism, militarism, mercantilism, and the big mistakes made by hereditary monarchs and the entrenched oligarchies of the wealthy. The seeds of an enlightened economic order based on the common welfare of the people had been planted, but the harvest of a democratic capitalism was far in the future.

*The Mid-19th century*

John Stuart Mill and Karl Marx confirmed that Smith’s theory that economic freedom would spread wealth naturally. It had been validated in practice on the small scale, but they had to point out that the system was functioning at but a fraction of its potential because wealth was still too concentrated. Each proposed changes in the work culture: Trust and cooperation would motivate workers to add more wealth, and a fair share of the results from improved performance would distribute wealth more broadly.\(^{272}\)

In two books, *Theory of Moral Sentiments* and *Wealth of Nations*, Smith had integrated the instinct for social cooperation with individual ambition to drive the free-market system, concluding that “little else is required to carry a state to the highest degree of opulence from the lowest barbarism but peace, easy taxes, and a tolerable administration of justice, all the rest being brought about by the natural course of things.”\(^{273}\)

Marx, in his great work, *Capital*, correctly criticized unevolved capitalism, but his critique of what was wrong is less important than his statement of what is right: Social progress depends upon development of a superior economic system that is assimilated by the culture, to be followed by a modification of the political structure in support of that approach to improved economic life. Because improvement of the human condition depends on the efficacy of the economic system, it is intellectually myopic and politically impractical to urge civil, social, and political rights ahead of economic freedom.

Mill (name your favorite writings of Mill, as we do Smith’s and Marx’s) integrated the energy of participatory workers with the motivations of private property and competition; he proposed that material benefit is maximized by an improvement in the

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\(^{273}\) Cited in *ibid.*, p. 171.
quality of life of the workers fortunate to work in a moral environment.\footnote{Ibid., p. 49.}

The intellectual community of the late-19th century did not, however, assimilate this integration of knowledge for human betterment. Consequently, neither the schools nor the churches educated the citizens to integrate growing democracy with the work place, either to reform the structures at home towards economic freedom or unite in economic common purpose abroad. The word “capitalism” came into use as a pejorative term implying wealth and privilege, greed and disrespect for the laboring class. Political leaders, having been failed by their teachers, continued in the traditional paths of nationalism, imperialism, mercantilism, militarism, and the mistaken abuse of power and wealth.

\textit{The 20th Century}

The economic genie was, nevertheless, out of the bottle! Throughout the 20th century, economic freedom continued to confirm its capacity to improve lives in many, many corporate environments, not only in democratic societies but also in authoritarian countries, as well. China and India lifted a half-billion people out of extreme poverty in a decade, and Southeast Asia was not far behind. The collectivist alternatives that were tried under Communism all failed, and when a Communist country such as China did begin to achieve success, it was through communistic capitalism. The Marshall Plan after WW II and, then, the European Union confirmed that economic common purpose could help to stop the violence. The Information Age made the world more productive, smaller, and more interdependent. Electronic advances came to the aid of communication, education, and human community in the most enlightened burst of democratic technology since Gutenburg.

\textit{The Early 21st Century}

Despite this positive trend, early in the 21st century the world was still full of violence,
misery, and fear. The root causes had become worse because of a failure of American leadership. Our “city on a hill” had hidden its Founders’ lamp of liberty under the bushel-basket of fascist militarism that supported, and was supported by, a corporate elite. Wealth was concentrated in record amounts at home. The economic progress of emerging nations suffered reversal under the impact of bad advice and worse greed from the American economic system dominated by finance capitalism.\footnote{Ibid., pp. 278-291.}

After the demise of communism, the world was moving towards economic common purpose; the global gyro was holding the balance between peace and plenty. America should have been the natural leader of this extraordinary opportunity; instead, it hardened into a jingoistic nationalism, a greedy imperialism, and a paranoid militarism as the power-adoring few committed every kind of egregious mistake in judgment and performance. The will and wisdom of the people was not sought, only manipulated; the world’s gyro was gyrating crazily between war and violence. And yet the people could not find their voice to protest: The intellectual community had never assimilated the integration of knowledge that could supply an enlightened starting point for economic and political reform. Consequently, most citizens were helpless before the concentration of wealth and power at home, and they did not know how to prioritize economic common purpose abroad in a winning political and commercial foreign policy.

\textit{What We Need from Our Universities}

Reform of the economic system is the starting point for a better America and a better world, but it cannot happen without an epiphany in higher education. Our universities must accept their responsibility to educate citizens in democracy and capitalism, and to train persons in the media to interpret national and international events in light of the demands of democratic capitalism so that they may thereby continue educating the voting public. The failure of higher education to perform this public duty has been documented by university presidents and deans, among them Derek Bok, president emeritus and interim president of Harvard University:
Through my two decades of presiding over a university, I cannot recall a single serious faculty discussion of how undergraduate education could do a better job of preparing students as citizens. The results of that neglect are all too visible.\textsuperscript{276}

Bok subsequently got hundreds of university presidents to endorse this view.

Francis Bacon long ago had cautioned: “It is not possible to run the course right when the goal itself has not been rightly placed.”\textsuperscript{277} A Baconian clear sense of the public mission of academia is now sadly missing, as typified by the opinion of Stanley Fish, dean emeritus of the University of Chicago, who challenged Bok:

The task of educating students to be better citizens would deform [higher education by replacing] the true task of academic work: the search for truth and the dissemination of it through teaching.\textsuperscript{278}

Does the abstract search for truth require a moral anarchy? Do universities have neither public duty or nor ethical focus? Is not, rather, the failure consistently and scientifically to apply abstract truth and pure knowledge to appropriate human questions both academically acceptable and ever theoretical? No professor’s academic freedom has been violated when he or she is asked to investigate the topic, and then teach freely from her or his professionally specialized point of view on the question: What is the best way to organize and conduct human life? Socrates died trying to answer the question. Plato wrote a book about it. Aristotle surveyed and catalogued all the best answers to it.

Perhaps we can excuse Rawls’s loss of nerve for the noble endeavor of organizing human affairs rationally as reaction to the failure of alternative political systems. Perhaps his intellectual fatigue resulted from the failure to perfect society through his own elite design, and this led Rawls to a false conclusion: “It did not work;

\textsuperscript{276} Derek Bok, \textit{Give me a proper bibliographical entry.}

\textsuperscript{277} Reference needed—and NOT to a secondary source!

\textsuperscript{278} Stanley Fish, \textit{give me a proper bibliographical entry, The New York Times, etc.} Dean Fish, subsequently a Law professor in Florida, amplified his definition of academic freedom to say that it is the right to teach anything that a professor may choose, so long as it is not a form of “indoctrination.” \textit{Give me a proper bibliographical entry, The New York Times, July 23, 2006: 13—no indication of a section in the paper?}
If I were a university professor (which I am not), I would lecture on Smith, Marx, Mill, and some others to say that the alternative that Rawls was seeking did not work because it started at the political end of the question, not at the economic end. The emergence of a better society depends upon the development of a superior economic system. Those who declare defeat and walk off the field leave government policy undefended before the predations of two fierce beasts of prey: namely, the finance capitalists who spend huge amounts to protect their exploitive system, and the military-industrial complex that sucks up vast sums in its great march towards nuclear catastrophe. A government thus dominated has neither the will nor funds enough to effect a betterment of society for the general welfare.

*Contra* Rawls, I cite Edward Wilson, Professor of Biology at Harvard, winner of both Nobel and Pulitzer prizes, who wrote scientifically and in the spirit of the Enlightenment about the unification of knowledge for human betterment:

> I believe that the Enlightenment thinkers of the seventeenth and eighteenth centuries got it mostly right the first time. The assumptions they made of a lawful material world, the intrinsic unity of knowledge, and the potential of indefinite human progress are the ones we still take most readily to our hearts.\(^{279}\)

Wilson identified the lack of integration in scholarship, along with an underprepared media, as a serious impediment to the unification of knowledge requisite to the rational organization of human affairs:

> The root cause of the problem: ... the overspecialization of the educated elite. Public intellectuals, and trailing close behind them the media professionals, have been trained almost without exception in the social sciences and humanities. They consider human nature to be their province and have difficulty conceiving

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\(^{279}\) Edward O. Wilson, *Consilience*
the relevance of the natural sciences to social behavior and policy.280

One effect of the knowledge explosion of the 20th century is that even the smartest among us can no longer be “a Renaissance man,” a person who is reputedly a master of many fields. Not only the well-educated but also the hard-working are compelled by professional necessity to overspecialize in what it takes to be the best at what one does. Medical doctors, for example, study for long years to become high-paid technicians of human plumbing, but they do this at the expense of no equivalent learning in the humanities and social sciences or even in a field as closely allied to their own as, say, psychology, with a focus on the healing powers of the mind, or even nutrition, the source of bodily health.

At the opposite extreme, a Journalism major in college learns how to write so as to please a publisher or editor and to communicate with an 8th-grade readership or viewership, but people in the media know better than to pitch their writing and news reporting to a level of higher literacy than that, lest they lose their audience and seem elitist to the general reading and watching public who are more interested in entertainment than in facts. When, for example, news reporters are confronted with the latest collapse of some Southeastern Asian country, it is far easier for them to offer simplistic analyses: blame religious conflict or indict some authoritarian leader, than it is to dig deeper into the real, economic causes of the unhappiness, and America’s own complicity in predatory international finance that abetted yet one more human disaster.

And the list of examples goes on: Did you ever try to talk to a mathematician? Theologians speak a language all their own, part Greek, part Latin, mostly nonsense. Can you get your computer guru to rise above geekdom long enough even to use human language?

There is so much to know in our world of competing knowledges that the intellectuals and professors are usually no better off than their confused and unwilling undergrads. University curricula are specialized and fragmented, and each professor or department

280 Ibid., p. ???.

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chair is zealous to defend his or her intellectual turf in faculty battles over enrollment levels and grant money. The occupational hazard of having to learn provincially and with professional exclusivity then results in a failure to integrate knowledge for the better of the human condition. The humanists and historians listen to mostly to other humanists and historians; the scientists are the only ones who can understand other scientists; the psychologists listen to other psychologists, and the sociologists listen to other sociologists, but they rarely listen to each other; no one listens to the economists because no one in the other disciplines has ever studied economics enough to be able to understand an expert in the field, and, besides, economists are boring when they talk. Intra-disciplinary research teams are much in vogue, but genuine inter-disciplinary research efforts are rare. When, God forbid, anyone should step outside his or her field of expertise to attempt to make interdisciplinary meaning and articulate a logical relationship among disciplines, the opposing overspecialized experts will, as often as not, ridicule the effort. Philosophers of physics talk glibly of their TOEs (Theory of Everything), but hardly any other professional intellectual is ready to address that task anywhere in between quantum mechanics below or astrophysics above. Most people, therefore, shyly default before highly complex questions and say, “It’s not my field.” The search for cohesive, integrated truth about the human condition goes begging. The respective faculties aggressively and rightly protect their academic freedom, but freedom from what and for what?

Applying this complaint against over-specialization to problems of democracy and capitalism, one finds that the universities do not teach an integration of these two all-important aspects of American and global political-economic life. Most philosophers, professors of literature, and history teachers speak the word “capitalism” as if it were a distasteful four-letter epithet—never mind that these same academics are relying heavily on TIAA-Cref for their retirement packages! Programmatic Liberals on the faculty used to praise Marx beyond all reason, although this excess has become less fashionable since “the fall of the Wall,” but in so doing, these same Liberals and their overly idealistic students, said to be motivated by compassion for the subjugated masses, turned a blind eye to the hundreds of millions that were murdered in the name of achieving a “classless society.” Dean Fish may deplore “indoctrination” all he likes, but generations of socially
sensitive students have been indoctrinated to an anti-capitalist attitude by their professors. Business majors, by contrast, enthusiastically take the course, “How to become a millionaire by the time you’re 30,” but courses in Business Ethics are viewed as wimpy and largely irrelevant.

There is, nevertheless, a way forward that our universities might take. Let us give heed to Bacon and listen to Wilson. Bacon criticized the scholasticism of his time because it was artificially intellectual and insufficiently rooted in fact or grounded in an abiding concern for the human condition:

The primary notions of things which the mind readily and passively imbibes, stores up and accumulates, are false, confused, and over-hastily abstracted from the facts ... whence it follows that the entire fabric of human reason which we employ in the inquisition of nature, is badly put together and built up, like some magnificent structure without any foundation. 281

Following Philosopher Bacon’s advice, let us use our intellects to recover our academic idealism in the quest for the best possible way to organize and uphold human life. And let us end the university skirmish in an honorable truce by entertaining Biologist Wilson’s peace proposal:

There is only one way to unite the great branches of learning and end the culture wars. It is to view the boundary between the scientific and literary cultures not as a territorial line but as a broad and mostly unexplored terrain awaiting cooperative entry from both sides. The misunderstandings arise from ignorance of the terrain, not from a fundamental difference in mentality. 282

While the university professors fiddle, the world burns. As we blunder along our well-worn way towards more folly and greater violence and everlasting fear, the reform-minded intellectual community has been satisfied with promoting political solutions that

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281 Proper footnote.
282 Give me a proper reference.
do not work well even at home, much less in other societies. Instead, they ought to have been examining how to refine capitalism and apply the principles of democracy in the realm of finance not only in America but in other cultures as well. Democratic capitalism as a concept, an historical development, a functioning system is rarely offered for student examination, whereas the ultracapitalism that fosters an environment of anxiety and intimidation, and maximizes short-term profits by suppressing wages and benefits, is ever before the students’ eyes. The students are not taught the simple and effective ways to reform and democratize capitalism because their teachers cannot teach what they themselves have never learned.

Democratic Capitalism and the Integration of Knowledge for Human Betterment

In agreement with Karl Marx, I propose that the starting point for the integration of knowledge insofar as it touches “the common welfare” (U.S. Constitution) is the realization that social progress depends upon the development of a superior economic system. I call broadly upon the professorship for a revision of the curriculum to include an application of Baconian empiricism and the scientific methods employed in the hard sciences to our truth-seeking processes in politics and economics. Historians on the faculty must contribute to this multidisciplinary cooperative with a careful study of the Enlightenment as summarized by Condorcet. Economists and philosophers must engage in cross-discipline discourse on Smith and Mill and Marx and others to determine whether and how they were working towards this same integration of knowledge for the good of all. Philosophers, historians, economists, and geopoliticians must read Kant together and then discuss ways to reform the United Nations, the World Bank, the International Monetary Fund, and the other agencies of globalism. Professors from the School of Business and the Law School must make common cause with their colleagues in the other faculties to learn what needs reforming and how to reform it, and to learn how to integrate democracy and capitalism, and, in so doing, how to strengthen both.

Along the way, a number of specific topics will arise that require the collaborative effort of multidisciplinary specialists: For example, students need to study the mistakes made by the few and the harm caused to the many. Teachers of history, foreign affairs, and
macroeconomics, then, must engage future voters in a unit of study on Woodrow Wilson and his ignorance of economic freedom at the 1919 Peace talks that made WW II inevitable. Following that, the next unit might appropriately be on Herbert Hoover and his three mistakes in the supply of money, taxes, and tariffs that exported the overdue stock market Crash of ’29 into the Great Depression.  

Experts in English economic history must educate our students and our fellow voters about the roots of economic freedom with particular concentration on Smith’s conditions for economic success. Democratic power will not counteract the lobby power of finance capitalists until citizens understand, as Smith did, that neutral money means a supply, cost, and volatility that does not affect the commercial process, and that control of currency and credit for the general welfare means limits on speculation with borrowed money. Voters armed with that knowledge would make some changes in Washington by way of the ballot box.

Professors of the humanities, of religion, and of ethics must grapple with democratic capitalism as the means to improve the human condition, but they need to collaborate in this with professors of business, management, and marketing who will be interested in democratic capitalism because it maximizes profits. Democratic capitalism is, I affirm, an inherently moral system that can eliminate material scarcity and unite people in economic common purpose. Does an economic system function better because it is moral? Can the moral economic system be a model for other elements of the culture? Is it true that performance improves in every human association when trust and cooperation define the work environment? The radical theoretical propositions implicit in these questions ought to be exciting to any philosopher or ethicist. The radical political implications in them ought to be exciting to any professor of political theory and practice with an eye on educating the next generation of citizen-voters.

The quest for human values, together with the front-loading of academic activity with ethical agendas just itching to be “indoctrinated,” is not so lacking in universities, these days, as Dean Fish may fantasize. Black Studies, Women’s Studies, Poverty Studies,

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283 Carey, op. cit., p. 444.
Hispanic Studies, Gay Studies, and some others are hotbeds of indoctrination, not to mention old favorites like Philosophy 101 and Ethics 102. Why not a Department of Democratic Capitalism Studies!

The discomfort that some academicians sense in “values studies” derives from the war between science and religion and the chasm between reason and faith—a distinction in our post-Enlightenment mind as important as the separation of church and state is in the body politic. A century ago, religious dogma dominated most universities and chapel attendance was required. Freedom from that kind of indoctrination has been a hard-fought revolution. At the same time, the need for human values, and the urgent political, social, and moral issues demanding our attention with every broadcast of the Evening News, are more pressing, more complex, and more existentially a matter of life and death than ever before.

Democratic Capitalism: A Set of Universal Human Values

In the clash of moral opinions, no one set of organized ethical solutions is all-inclusive enough to answer all of our problems; therefore, our search for values must be as cross-cultural and interdisciplinary as our university studies need to be.

What, then, has our experience taught us to do? The great religions of history have taught us to be kind, generous, and forgiving towards one another, and biologists and anthropologists tell us that altruism may well be inherent within our species, a characteristic, indeed, that fits us for survival. We do not have to be told that living in peace with one another would be better than living at war: We just know it in our genes; and more than that, we are rational. The Enlightenment taught us to employ reason and science to specify both the ideal and the means of our humane endeavor. In our global environment, even the least-informed isolationist among us now knows—at least in principle—that “we” cannot be happy while the rest of the world festers in poverty and disease and misery and violence. Our ideal state, then, is—and must be—one of peace and prosperity.

Ever to be achieving that state, we need a value system, an economic system, and an
educational system that enables us to bridge the secular and the religious, that makes sense to all disciplines and to all fields of study, that can function in any culture and within any political structure, that stretches the horizon of the ideal by transforming the mistakes of history into hope for the future, and that is premissed on an economic system superior to all the others that have prevailed in history before us.

Democratic capitalism is a set of human values that responds to all of the above. Democratized capitalism is a way of making a living far superior to the slave economy of ancient Athens in which Plato and Aristotle lived. Their political-economic environment, and their privileged status within it, left them with an elitist view towards business and industry, an elitist view that generations of philosophers and professors have imbibed to their own harm. A distaste for the world of work and secular productivity that characterizes much philosophical Idealism and contributes to a breach between soul and body is unhealthful and unhelpful, and it ought not to be indoctrinated in our children at school.

Democratic capitalism is also far superior to the wage-slavery imposed on the working classes by the oligarchies of history, from the royals to the robber barons, from mercantilists to ultracapitalists, those finance capitalists whose business is making money on money, and who treat employees as dispensable, cost-saving devices that can be downsized as a means of upping stock prices.

Democratic capitalism is an inherently moral economic system that works best when the work environment is one of trust and cooperation. The inexorable pressure of competition on companies and countries forces people to work together. The Information Revolution—the new Industrial Revolution—in which we now function, requires that workers be educated, self-reliant, intelligently responsive, and collaborative. Businesses that fail to foster these characteristics among the staff will tend to fail, but businesses that do not treat their people honorably, that do not include educated and intelligent people in planning and guidance of the enterprise, that do not fairly and generously share the wealth with self-reliant and cooperative associates, will lose those people to other, more democratically capitalistic—and therefore more competitive—corporations.
Democratic capitalism is an economic system that has demonstrated its capacity to improve lives, to elevate masses of poor people into the middle class, and—given the chance—to function adequately even under authoritarian regimes. And now that so many others have rubbed the lamp of that democratic-capitalist genie, young people living in even totalitarian countries can view the good life on TV and communicate about freedoms via the internet; in time, their natural yearning for liberty will motivate them to change their governments to allow the peace and prosperity that others have to flourish in their own countries.

The demonstrated historical process is this: When people begin to work and earn in a way that is free, whether they yet enjoy full social, civil, and political rights or not, they thereby achieve an ever greater measure of their human potential. They begin to demand a greater field of play, more room to work, more freedoms in which to live their lives. As the people are thus uplifted by the success of their economic activity, authoritarian governments either eventually fall before the in-coming tide of freedom or float gradually upwards on that tide to allow greater economic freedoms, then greater political freedom, and then full civil and social rights. Economic freedom works best with full democratic freedoms, but even without them, it still works.

Democratic capitalism’s greatest enemies are also great impediments to social progress: the concentration of wealth, perennial violence among nations and peoples, and privileges enjoyed by the few at the expense of the many. This axis of interrelated evils can be eliminated but only through understanding gained by way of integrated knowledge and by integrating the power of democracy and the energy of capitalism when they run in tandem.

I propose, therefore, “Enlightenment Two,” a multi-disciplinary project of intellectual inquiry and international citizen education designed to reform our economic systems, to build and distribute wealth more broadly, to reform domestic governance and foreign policy so that they will support and protect the superior economic system of democratic capitalism both at home and around the world. I believe that this endeavor will lead to global economic common purpose, that it will give trust and cooperation a chance, and
that the ever-widening achievement of this goal will do more than any other single thing to end wars, abate violence, and relieve fear. As the world’s standard of living goes up, the violence will go down.