Ludwig von Mises: Capital Supply And American Prosperity[1]

I

One of the amazing phenomena of the present election campaign is the way in which speakers and writers refer to the state of business and to the economic condition of the nation. They praise the administration for the prosperity and for the high standard of living of the average citizen "You never had it so good," they say, and, "Don't let them take it away."

It is implied that the increase in the quantity and the improvement in the quality of products available for consumption are achievements of a paternal government. The incomes of the individual citizens are viewed as handouts graciously bestowed upon them by a benevolent bureaucracy. The American government is considered as better than that of Italy or of India because it passes into the hands of the citizens more and better products than they do.

It is hardly possible to misrepresent in a more thorough way the fundamental facts of economics. The average standard of living is in this country higher than in any other country of the world, not because the American statesmen and politicians are superior to the foreign statesmen and politicians, but because the per-head quota of capital invested is in America higher than in other countries. Average output per man-hour is in this country higher than in other countries, whether England or India, because the American plants are equipped with more efficient tools and machines. Capital is more plentiful in America than it is in other countries because up to now the institutions and laws of the United States put fewer obstacles in the way of big-scale capital accumulation than did those foreign countries.

It is not true that the economic backwardness of foreign countries is to be imputed to technological ignorance on the part of their peoples. Modern technology is by and large no esoteric doctrine. It is taught at many technological universities in this country as well as abroad. It is described in many excellent textbooks and articles of scientific magazines. Hundreds of aliens are every year graduated from American technological institutes. There are in every part of the earth many experts perfectly conversant with the most recent developments of industrial technique. It is not a lack of the "know how" that prevents foreign countries from fully adopting American methods of manufacturing but the insufficiency of capital available.

II

The climate of opinion in which capitalism could thrive was characterized by the moral approbation of the individual citizen's eagerness to provide for his own and his family's future. Thrift was appreciated as a virtue no less beneficial to the individual saver himself than to all other people. If people do not consume their whole incomes, the non-consumed surplus can be invested, it increases the amount of capital goods available and thereby makes it possible to embark upon projects which could not be executed before. Progressive capital accumulation results in perpetual economic betterment. All aspects of every citizen's life are favorably affected. The continuous tendency toward an expansion of business activities opens an ample field for the display of the energies of the rising generation. Looking backward upon his youth and the

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[1] Ludwig von Mises delivered this address before the University Club of Milwaukee on October 13, 1952. [Original publisher's note: This address was made in 1952. It was a prophetic address and still is; more will understand this now (in 1979) than twenty-eight years ago (in 1952). The implied prophecy is: If the United States continues to hamper capital accumulation by erosive and expropriational taxes, larger and larger shares of the incomes of people and corporations will be siphoned off into government waste and welfare programs, and our growth will be slowed, then stagnated, and eventually we shall sink into poverty. Socialists, communists, preachers, ecologists, union leaders, teachers, demagogues — seething with envy and covetousness will shunt us into "the decline and fall of the United States." It may turn out to be greater than what is described in Gibbon's *The Decline and Fall of the Roman Empire*.]

conditions in his parent's home, the average man cannot help realizing that there is progress toward a more satisfactory standard of living.

Such were the conditions in all countries on the eve of the First World War. Conditions were certainly not everywhere the same. There were the countries of western capitalism on the one hand, and on the other hand the backward nations which were slow and reluctant in adopting the ideas and the methods of modern progressive business. But these backward nations were amply benefited by the investment of capital provided by the capitalists of the advanced nations. Foreign capital built their railroads and factories and developed their natural resources.

The spectacle that the world offers today is very different. As it was forty years ago, the world is divided into two camps. There is, on the one hand, the capitalist orbit, considerably shrunk when compared with its size in 1914. It includes today the United States and Canada and some of the small nations of Western Europe. The much greater part of the earth's population lives in countries strictly rejecting the methods of private property, initiative and enterprise. These countries are either stagnating or faced with a progressive deterioration of their economic conditions.

III

Let us illustrate this difference by contrasting, as typical of each of the two groups, conditions in this country and those in India.

In the United States, capitalist big business almost every year supplies the masses with some novelties: either improved articles to replace similar articles used long since or things which had been altogether unknown before. The latter — as for instance, television sets or nylon hosiery — are commonly called luxuries, as people previously lived rather contented and happy without them. The average common man enjoys a standard of living which, only fifty years ago, his parents or grandparents would have considered as fabulous. His home is equipped with gadgets and facilities which the well-to-do of earlier ages would have envied. His wife and his daughters dress elegantly and apply cosmetics. His children, well fed and cared for, have the benefit of a high school education, many also of a college education. If one observes him and his family on their weekend outings, one must admit that he looks prosperous.

There are, of course, also Americans whose material conditions appear unsatisfactory when compared with those of the great majority of the nation. Some authors of novels and plays would have us believe that their gloomy descriptions of the lot of this unfortunate minority is representative of the fate of the common man under capitalism. They are mistaken. The plight of these wretched Americans is rather representative of conditions as they prevailed everywhere in the pre-capitalistic ages and still prevail in the countries which were either not at all or only superficially touched by capitalism. What is wrong with these people is that they have not yet been integrated into the frame of capitalist production. Their penury is a remnant of the past. The progressive accumulation of new capital and the expansion of big-scale production will eradicate it by the same methods by means of which it has already improved the standard of living of the immense majority, viz., by raising the per-head quota of capital invested and thereby the marginal productivity of labor.

Now let us look at India. Nature has endowed its territory with valuable resources, perhaps more richly than the soil of the United States. On the other hand, climatic conditions make it possible for man to subsist on a lighter diet and to do without many things which in the rough winter of the greater part of the United States are indispensable. Nonetheless, the masses of India are on the verge of starvation, shabbily dressed, crammed into primitive huts, dirty, illiterate. From year to year things are getting worse; for population figures are increasing while the total amount of capital invested does not increase or, even more likely, decreases. At any rate, there is a progressive drop in the per-head quota of capital invested.

In the middle of the eighteenth century conditions in England were hardly more propitious than they are today in India. The traditional system of production was not fit to provide for the needs of an increasing population. The number of people for whom there was no room left in the rigid system of paternalism and government tutelage of business grew rapidly. Although at that time England's population was not much more than fifteen percent of what it is today, there were several million destitute poor. Neither the ruling aristocracy nor these paupers themselves had any idea about what could be done to improve the material conditions of the masses.

The great change that within a few decades made England the world's wealthiest and most powerful nation was prepared for by a small group of philosophers and economists. They demolished entirely the pseudo-philosophy that hitherto had been instrumental in shaping the economic policies of the nations. They exploded the old fables:

1. that it is unfair and unjust to outdo a competitor by producing better and cheaper goods;
2. that it is iniquitous to deviate from traditional methods of production;
3. that labor-saving machines bring about unemployment and are therefore an evil;
4. that it is one of the tasks of civil government to prevent efficient businessmen from getting rich and to protect the less efficient against the competition of the more efficient; and
5. that to restrict the freedom and the initiative of entrepreneurs by government compulsion or by coercion on the pan of other powers is an appropriate means to promote a nation's well-being.

In short: these authors expounded the doctrine of free trade and laissez faire. They paved the way for a policy that no longer obstructed the businessman's effort to improve and to expand his operations.

What begot modern industrialization and the unprecedented improvement in material conditions that it brought about was neither capital previously accumulated nor previously assembled technological knowledge. In England, as well as in the other western countries that followed it on the path of capitalism, the early pioneers of capitalism started with scanty capital and scanty technological experience. At the outset of industrialization was the philosophy of private enterprise and initiative, and the practical application of this ideology made the capital swell and the technological know-how advance and ripen.

One must stress this point because its neglect misleads the statesmen of all backward nations in their plans for economic improvement. They think that industrialization means machines and textbooks of technology. In fact, it means economic freedom that creates both capital and technological knowledge.

Let us look again at India. India lacks capital because it never adopted the pro-capitalist philosophy of the West and therefore did not remove the traditional institutional obstacles to free enterprise and big-scale accumulation. Capitalism came to India as an alien imported ideology that never took root in the minds of the people. Foreign, mostly British, capital built railroads and factories. The natives looked askance not only upon the activities of the alien capitalists but no less upon those of their countrymen who cooperated in the capitalist ventures. Today the situation is this: thanks to new methods of therapeutics, developed by the capitalist nations and imported to India by the British, the average length of life has been prolonged and the population is rapidly increasing. As the foreign capitalists have either already been virtually expropriated or have to face expropriation in the near future, there can no longer be any question of new investment of foreign capital. On the other hand, the accumulation of domestic capital is prevented by the manifest hostility of the government apparatus and the ruling party.

The Indian government talks a lot about industrialization. But what it really has in mind is nationalization of already existing privately owned industries. For the sake of argument, we may neglect referring to the fact that this will probably result in a progressive decumulation of the capital invested in these industries as was the case in most of the countries that have experimented with nationalization. At any rate, nationalization as such does not add anything to the already prevailing extent of investment. Mr. Nehru admits that his government does not have the capital required for the establishment of new state-owned industries or for the expansion of such industries already existing. Thus, he solemnly declares that his government will give to private industries "encouragement in every way." And he explains in what this encouragement will consist: we will promise them, he says, "that we would not touch them for at least ten years, maybe more." He adds: "We do not know when we shall nationalize them."[2] But the businessmen know very well that new investments will be nationalized as soon as they begin to yield returns.

IV

I have dwelt so long upon the affairs of India because they are representative of what is going on today almost in all parts of Asia and Africa, in great parts of Latin America and even in many European countries. In all these countries the population is increasing. In all these countries foreign investments are expropriated, either openly or surreptitiously by means of foreign exchange control or discriminatory taxation. At the same time, their domestic policies do their best to discourage the formation of domestic capital. There is much poverty in the world today; and the governments, in this regard in full agreement with public opinion, perpetuate and aggravate this poverty by their policies.

As these people see it, their economic troubles were in some unspecified way caused by the capitalist countries of the West. This notion included, until a few years ago, also the advanced nations of Western Europe, especially also the United Kingdom. With recent economic changes, the number of nations to which it refers has been more and more restricted; today it means practically only the United States. The inhabitants of all those countries in which the average income is considerably lower than in this country look upon the United States with the same feelings of envy and hatred with which within the capitalist countries those voting the ticket of the various communist, socialist, and interventionist parties look upon the entrepreneurs of their own nation. The same slogans that are employed in our domestic antagonisms — such as Wall Street, big business, monopolies, merchants of death — are resorted to in speeches and articles by the anti-American politicians when they are attacking what is called in Latin America, Yankeeism, and in the other hemisphere, Americanism. In these effusions there is little difference between the most chauvinistic nationalists and the most enthusiastic adepts of Marxian internationalism, between the self-styled conservatives eager to preserve traditional religious faith and political institutions, and the revolutionaries aiming at the violent overthrow of all that exists.

The popularity of these ideas is by no means an effect of the inflammatory propaganda of the Soviets. It is just the other way round. The communist lies and calumnies get their persuasiveness, whatever it may be, from the fact that they agree with the sociopolitical doctrines taught at most of the universities and held by the most influential politicians and writers.

The same ideas dominate the minds in this country and determine the attitude of statesmen with regard to all the problems concerned. People are ashamed of the fact that American capital developed the natural resources in many countries which lacked both the capital and the trained specialists required. When various foreign governments expropriated American investments or repudiated loans granted by the American saver, the public either remained indifferent or even sympathized with the expropriators. With the ideas underlying the programs of the most influential political groups and taught at most of the educational institutions, no other reaction could be expected.

Four years ago there assembled in Amsterdam the World Council of Churches, an organization of one-hundred-and-fifty-odd denominations. We read in the report drafted by this ecumenical body the following statement: "Justice demands that the inhabitants of Asia and Africa should have the benefits of more machine production." This implies that the technological backwardness of these nations has been caused by an injustice committed by some individuals, groups of individuals or nations. The culprits are not specified. But it is understood that the indictment refers to the capitalists and businessmen of the shrinking number of capitalist countries, practically to the United States and Canada. Such is the opinion of very judicious conservative churchmen acting in full awareness of their responsibilities.

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[2] Cf. Jawaharlar Nehru, *Independence and After, A Collection of Speeches*, 1946–1949. New York 1950, page 192.

The same doctrine is at the bottom of the foreign aid and the Point Four policies of the United States. It is implied that the American taxpayers have the moral obligation to provide capital for nations that have expropriated foreign investments and are preventing the accumulation of domestic capital by various schemes.

There is no use indulging in wishful thinking. Under the present state of international law, foreign investments are unsafe and at the mercy of each sovereign nation's government. It is generally agreed that every sovereign government has the right to decree a fictitious parity of its inflated currency as against dollars or gold and to try to enforce this arbitrarily fixed spurious parity by foreign exchange control, that is, by virtually expropriating foreign investors. As far as some foreign governments still abstain from such confiscations, they do so because they hope to talk foreigners into more investments and thus to be later in a position to expropriate more.

In the ranks of those nations that do all that can be done to prevent their industries from getting badly needed capital, we find today also Great Britain, once the cradle of free enterprise and before 1914 the world's richest or second richest country. In exuberant and entirely undeserved praise of the late Lord Keynes, a Harvard professor found in his hero but one weakness. Keynes, he said, "always exalted what was at any moment truth and wisdom for England into truth and wisdom for all times and places."[3] I heartily disagree. Just at the moment in which it must have become manifest to every judicious observer that England's economic distress was caused by an insufficient supply of capital, Keynes enounced his notorious doctrine of the alleged dangers of saving and passionately recommended more spending. Keynes tried to provide a belated and spurious justification of a policy that Great Britain had adopted in defiance of the teachings of all its great economists. The essence of Keynesianism is its complete failure to conceive the role that saving and capital accumulation play in the improvement of economic conditions.

V

The main problem for this country is: will the United States follow the course of the economic policies adopted by almost all foreign nations, even by many of those which had been foremost in the evolution of capitalism? Up to now in this country the amount of savings and formation of new capital still exceeds the amount of dissaving and decumulation of capital. Will this last?

To answer such a question one must look upon the ideas about economic matters held by public opinion. The question is: do the American voters know that the unprecedented improvement in their standard of living that the last hundred years brought was the result of the steady rise in the per-head quota of capital invested? Do they realize that every measure leading to capital decumulation jeopardizes their prosperity? Are they aware of the conditions that make their wage rates tower above those of other countries?

If we pass in review the speeches of political leaders, the editorials of newspapers, and textbooks of economics and finance, we cannot help discovering that very little attention, if at all, is paid to the problems of capital equipment. Most people take it simply for granted that some mysterious factor is operative that makes the nation richer from year to year. Government economists have computed a rate of yearly increase in the national income for the past fifty years and blithely assume that in the future the same rate will prevail. They discuss problems of taxation without even mentioning the fact that our present tax system collects large funds, which would have been saved by the taxpayer, and employs them for current expenditure.

A typical instance of this mode of dealing (or rather, non-dealing) with the problem of America's capital supply may be cited. A few days ago the American Academy of Political and Social Science published a new volume of its Annals, entirely devoted to the investigation of vital issues of the nation. The title of the volume is: Meaning of the 1952 Presidential Election. To this symposium Professor Harold M. Groves of the University of Wisconsin contributed an article, "Are Taxes Too High?" The author comes out "with a largely negative answer." From our point of view, the most interesting feature of the article is the fact that it reaches this conclusion without even

[3] Cf. J. Schumpeter, *Keynes, the Economist* (in *The New Economics*, ed. by S. E. Harris, New York 1947, page 85.)

mentioning the effects which taxes on income, corporations, excess profits, and estates have upon the maintenance and formation of capital. What economists have said about these problems either remained unknown to the author or he does not consider it worthy of an answer.

One does not misrepresent the economic ideas determining the course of American policies if one blames them for not being conscious of the role the supply of new capital plays in improving and expanding production. An instructive example has been provided by the conflict between the government and business concerning the adequacy of depreciation quotas under inflationary conditions. In all the agitated debates concerning profits, taxes, and the height of wage rates, the capital supply is hardly mentioned, if at all. In comparing American wage rates and standards of living with those of foreign countries, most authors and politicians fail to stress the differences in the per-head quotas of capital invested.

In the latest forty years American taxation more and more adopted methods which considerably slowed down the pace of capital accumulation. If it continues along this line, it will one day reach the point at which no further increase in capital will be possible, or even decumulation will set in. There is only one way open to stop this evolution in time and to spare this country the fate of England and France. One must substitute sound economic ideas for fables and illusions.

VI

Up to this point I have employed the terms capital shortage and scarcity of capital without further explication and definition. This was quite sufficient as long as I dealt primarily with the conditions of countries whose capital supply appears as inadequate when compared with the supply in more advanced countries, especially in the economically most advanced country, the United States. But in examining American problems, a more searching interpretation of terms is required.

Strictly speaking, capital has always been scarce and will always be. The available supply of capital goods can never become so abundant that all projects, the execution of which could improve the material well-being of people, could be undertaken. If it were otherwise, mankind would live in the Garden of Eden and would not have to bother at all about production. Whatever the state of the capital supply may be, in this real world of ours there will always be business projects that cannot be launched because the capital they would require is employed for other enterprises, the products of which are more urgently asked for by the consumers. In every branch of industry there are limits beyond which the investment of additional capital does not pay. It does not pay because the capital goods concerned can find employment in the production of goods which are in the eyes of the buying public more valuable. If, other things being equal, the supply of capital increases, projects which hitherto could not be undertaken become profitable and are started. There is never a lack of investment opportunities. If there is lack of opportunities for profitable investment, the reason is that all the capital goods available have already been invested in profitable projects.

In speaking of the capital shortage of a country that is poorer than other countries, one does not refer to this phenomenon of the general and perpetual shortage of capital. One merely compares the state of affairs in this individual country with that of other countries in which capital is more abundant. Looking upon India one may say: here are a number of artisans producing with a total capital of ten thousand dollars products with the market value of, let us say, one million dollars. In an American factory with a capital equipment of one million dollars, the same number of workers turn out products with the market value of 500 times as many dollars. Indian businessmen unfortunately lack the capital to make such investments. The consequence is that productivity per man is lower in India than in America, that the total amount of goods available for consumption is smaller, and that the average Indian is poor when compared with the average American.

There is, especially under inflationary conditions, no reliable standard available that could be applied in measuring the degree of the scarcity of capital. Where it is impossible to compare a country's conditions with those of countries in which the supply of capital is more plentiful, as is the case with this country, only comparisons with the hypothetical size of the capital supply (as it would have been if certain things had not happened) are possible. There is in such a country no phenomenon that would present itself as capital scarcity so clearly and manifestly as the capital scarcity presents itself today to the people of India. All that can be said is: if in our nation people had saved more in the past, some improvements in technological methods (and lateral expansion of production by duplication of equipment of the kind already in existence for which the capital required is lacking) would have been feasible.

VII

It is not easy to explain this state of affairs to people misled by the passionate anti-capitalistic agitation. As the self-styled intellectuals see it, the capitalist system and the greed of the businessmen are to blame for the fact that the total sum of products turned out for consumption is not greater than it actually is. The only way to do away with poverty they know is to take away — by means of progressive taxation — as much as possible from the well-to-do. In their eyes the wealth of the rich is the cause of the poverty of the poor. In accordance with this idea the fiscal policies of all nations and especially also of the United States were in the last decades directed toward confiscating ever-increasing portions of the wealth and income of the higher brackets. The greater part of the funds thus collected would have been employed by the taxpayers for saving and additional capital accumulation. Their investment would have increased productivity per man-hour and would in this way have provided more goods for consumption. It would have raised the average standard of living of the common man. If the government spends them for current expenditure, they are dissipated and capital accumulation is concomitantly slowed down.

Whatever one may think about the reasonableness of this policy of soaking the rich, it is impossible to deny the fact that it has already reached its limits. In Great Britain the Socialist Chancellor of the Exchequer had to admit a few years ago that even total confiscation of all that has still been left to people with higher incomes would add only a quite negligible sum to internal revenue and that there can no longer be any question of improving the lot of the indigent by taking it away from the rich.

In this country a total confiscation of incomes above twenty-five thousand dollars would at best yield much less than one billion dollars, a very small sum indeed when compared with the size of our present budget and the probable deficit. The main principle of the financial policies of the self-styled progressives has been pursued to the point at which it defeats itself and its absurdity becomes manifest. The progressives are at their wit's end. Henceforth, if they want to expand public expenditure further, they will have to tax more heavily precisely those classes of voters for whose support they have hitherto canvassed by placing the main burden upon the shoulders of the minority of wealthier people. (A very embarrassing dilemma indeed for the next Congress.)

But it is exactly the perplexity of this situation that offers a favorable opportunity for the substitution of sound economic principles for the pernicious errors that prevailed in the last decades. Now is the time to explain to the voters the causes of American prosperity on the one hand, and of the plight of the backward nations on the other hand. They must learn that what makes American wage rates much higher than those in other countries is the size of capital invested and that any further improvement of their standard of living depends on a sufficient accumulation of additional capital. Today only the businessmen worry about the provision of new capital for the expansion and improvement of their plants. The rest of the people are indifferent with regard to this issue, not knowing that their well-being and that of their children is at stake. What is needed is to make the importance of these problems understood by everybody. No party platform is to be considered as satisfactory that does not contain the following point: as the prosperity of the nation and the height of wage rates depend on a continual increase in the capital invested in its plants, mines and farms, it is one of the foremost tasks of good government to remove all obstacles that hinder the accumulation and investment of new capital.