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# Henry Hazlitt: Economics in One Lesson Study Guide

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# HENRY HAZLITT: ECONOMICS IN ONE LESSON
# STUDY GUIDE, 2008
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## CHAPTER ONE: THE LESSON

**Outline**

A. SOURCES OF ECONOMIC FALLACIES
  1. **Special Pleading of Selfish Interests**
    a. Interest Groups
    b. Public Relations "Flacks:" the "best hired minds"
  2. **Fallacy of Overlooking Secondary Consequences**
    a. Bad economist focuses on the immediate good and the direct consequences of a proposed course of action
    b. Good economist looks beyond the immediate and examines the longer and indirect consequences of a given policy
  3. Self-Indulgent Economists
    a. "There are men regarded today as brilliant economists, who deprecate saving and recommend squandering on a national scale as the way of economic salvation" [In Keynesian economics, this is known as "**priming the pump,**" *i.e.*, stimulating the economy to "jump start" it: *e.g.*, the 2008 Wall Street "bail out"]
    b. **John Maynard Keynes**: "In the long run we are all dead."
    c. The tragedy is that we are "already suffering the long-run consequences of the long-run consequences of the remote or recent past."
    d. "Today is already the tomorrow which the bad economist yesterday urged us to ignore."
  4. The Lesson
    a. The **art of economics** consists in looking not merely at the immediate but at the longer effects of any act or policy; it consists in tracing the consequences of that policy not merely for one group but for all groups."

B. NINE-TENTHS OF ECONOMIC FALLACIES RESULT FROM IGNORING THIS LESSON
  1. Most Common Error Focuses on the Immediate Consequences for a Particular Group
  2. The Opposite Error Focuses on the Long-Run Consequences for All Groups
    a. Error Often Made by **Classical Economists**: "Callousness toward the fate of groups that were immediately hurt by policies or developments which proved to be beneficial on net balance and in the long run."
  3. Central Sophism of the "New Economics"
    a. They fall into the ancient errors associated with **mercantilism**

C. DEMAGOGUES AND BAD ECONOMISTS PRESENT ONLY HALF-TRUTHS
  1. The Answer: Correcting the Half-Truth with the Other Half

**Review**

sources of economic fallacies art of economics error of classical economists
mercantilism and the "new economists"

## CHAPTER TWO: THE BROKEN WINDOW

**Study Questions**

1. Who benefits from the broken window? Who suffers loss from it? Is the community better off as a result?

**Review**

broken window fallacy

# CHAPTER THREE: THE BLESSINGS OF DESTRUCTION

**Study Questions**

1. What is meant by asserting that there is an "accumulated" or "backed-up" demand?" [The Clinton Administration talked about "a peace dividend" following the end of the Cold War].

2. What does Hazlitt mean when he says that this variation on the broken window fallacy confuses **need** with **demand**? What does **effective economic demand** require?

3. What is another fallacy? In what sense is the printing of money "the world's biggest industry?" [The fall of oil prices during the current economic recession also illustrates the fallacy of such thinking because the price mechanism itself is in disarray and the prices of this particular commodity have actually been falling, even though relative food costs have been rising in most places]. Wartime and peacetime **inflation** (usually related to printing extra money) create the illusion of economic growth.

4. "The inability to produce automobiles, radios, and refrigerators during the war did bring about a cumulative post-war demand *for those particular products*. To most people this seemed like an increase in total demand, as it partly was *in terms of dollars of lower purchasing power*. But what mainly took place was a *diversion* of demand to these particular products from others. . . . The war, in short, changed the post-war *direction* of effort; it changed the balance of industries; it changed the structure of industry."

5. What do you believe accounts for the stimulation of energies following a war? Mere inflation does not create greater demand. What happens to buying or purchasing power when productive power is wiped out?

6. "Plants and equipment cannot be replaced by an individual (or a socialist government) unless he or it has acquired or can acquire the savings, the capital accumulation, to make the replacement. But war destroys accumulated capital." What are some of the possible **offsetting factors** that may eventually yield a net increase in overall **productivity**?

**Review**

| | | |
|---|---|---|
| effective economic demand | inflation | offsetting factors |

# CHAPTER TWENTY-THREE: THE MIRAGE OF INFLATION

**Study Questions**

1. Scan Parts 1-3. The "pump-priming" fallacy of Keynesian is addressed in Part 4: "In our own day the most persistent argument put forward for **inflation** is that it will 'get the wheels of industry turning.'" Unfortunately, the current global financial crisis is lending some respectability once

again to Keynesian economists. The particular magician's trick that inflation has been designed to accomplish is this: Inflation (which changes the **relationships of prices and costs**) is designed to "encourage a resumption of output at the points where idle resources [land, labor, and/or capital] exist, by restoring a workable relationship between prices and costs of production." [NOTE: By definition, inflation drives up prices so that, presumably, they better reflect actual costs. This deception is designed to reduce the hoarding of any sort of resource and create the illusion of growth and prosperity. Resources may be withheld until there is a greater return on investment. Inflation appears to promise a greater return.

2. NOTE: The historical context of this discussion is this: Labor unions became politically powerful through their ability to get political protection for their efforts to raise wages for their members through **collective bargaining**. This is a system put in place during the New Deal in which the government gave unions, such as the AFL, the CIO, the Teamsters, and others, monopoly power to coerce business owners into raising wages. Of course, this means that the extra costs to the owners have to be made up elsewhere, usually in the form of higher prices. The result is that industries become less competitive in the global marketplace. Sometimes, they become less productive, too. This is also one reason that unions want to be able supervise and otherwise control the outcome of elections that may be mandated to determine whether a company or an industry is to be unionized. The government is used as "muscle" to enable the union to get established. From the union standpoint, the desired result is a **closed shop**: workers must join the union and pay union dues. Even in the absence of a closed shop arrangement, non-members may be required to pay equivalent amount to the dues into a "fair share" fund.

3. "It should be immediately clear that this [change in the relationship of prices and costs] could be brought about more directly and honestly by a reduction in unworkable wage rates. But the more sophisticated proponents of inflation believe this is now politically impossible [*i.e.*, labor unions have political clout and use it to protect their vested interests]. . . . [W]hat they are themselves proposing, stated in bald terms, is to *deceive* labor by reducing *real* wages (that is, wage rates in terms of purchasing power) through an increase in prices." But, of course, labor unions come back and index their wage demands to the consumer price (cost-of-living) index.

4. Why does Hazlitt call inflation "the opium of the people?" Is its purpose to confuse the situation of planned economies? Why does Hazlitt call inflation a form of taxation (and a flat tax at that!)? What does inflation encourage and what does it discourage? Writing so soon following the Second World War gives Hazlitt a better historical grasp of where inflation and similar policies might lead: "Its inexcusable injustices drive men toward desperate remedies. It leads men to demand totalitarian controls. It ends invariably in bitter disillusion and collapse."

**Review**

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|---|---|---|
| inflation | relationships of prices and costs | collective bargaining |
| reduction of real wages | inflation as a form of taxation | |

# CHAPTER TWENTY-FOUR: THE ASSAULT ON SAVING

**Study Questions**

1. Why do "savings" exceed "investment" only by the amounts that are actually **hoarded** in cash? What usually accounts for a rise in hoarding? Hazlitt comments on the effects of "cheap money" policies (*i.e.*, inflationary policies). What accounts for "a psychopathic fear of 'excessive' interest rates? What happens if interest rates are kept artificially low?

2. What are some fallacies concerning capital? How should we distinguish consumers' durable goods from capital proper? Why is a "surplus" of capital not going to be a problem?

**Review**

| | | |
|---|---|---|
| hoarding | cheap money policies | artificially low interest rates |
| capital proper | | |

# CHAPTER TWENTY-FIVE: THE LESSON RESTATED

**Study Questions**

1. The answer to economic questions is “already contained in the formulation of the problem.” But algebra should remind us that “inevitable implications are not necessarily obvious implications.” Figuring out these implications (following the inductive factual research that must be made) is the **deductive** side of economics.

2. Who is the “Forgotten Man” of **William Graham Sumner**? How did the New Deal wrongly apply this phrase? NOTE: The New Deal’s use of the phrase is an example of what Bastiat called **false philanthropy**. Furthermore, the use of inflation to by-pass or “short-circuit” what Hazlitt calls **unworkable wages** in chapter 23 is a consequence of what Bastiat calls **stupid greed** through coercive price setting. The spilling of vast quantities of milk, the plowing under of crops, and the mass destruction of farm animals served the same purpose.

3. Why is the fundamental economic fallacy almost inevitably a result of the **division of labor**? Why does any producer have an interest in **scarcity** wherever there is an elaborate and minute division of labor? Is the solution to the loss of income or work to artificially reduce supplies? What does Hazlitt mean by the “insane doctrine of wealth through scarcity?”

**Review**

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|---|---|---|
| deduction | Forgotten Man | William Graham Sumner |
| false philanthropy | stupid greed | division of labor |
| wealth through scarcity | | |