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# Lord Peter Bauer: From Subsistence to Exchange: Study Guide

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**LORD PETER BAUER: FROM SUBSISTENCE TO  
EXCHANGE AND OTHER ESSAYS:  
STUDY GUIDE, 2006-2011  
Steven Alan Samson**

**I. FROM SUBSISTENCE TO EXCHANGE**

**Outline**

- A. INTRODUCTION (3)
  - 1. **Internal Trade** Today Is Not Regarded as an Engine of Growth [obverse of the vicious circle of poverty idea, pp. 6, 16]
  - 2. The Case Was Different Two Centuries Ago
- B. INTERNAL TRADE AS AN ENGINE OF GROWTH (3-4)
  - 1. The **Level of Human Capital** Was Raised in the 17-18C
  - 2. Trading Activities Are Productive in Emerging Countries Today
- C. NEGLECT OF TRADING ACTIVITY (4-7)
  - 1. Trading Activities Get Little Attention
    - a. Mistaken attitude
  - 2. First-Hand Observation Would Have Shown the Error
    - a. Keith Hancock
    - b. Allan McPhee
    - c. Transformation of West Africa in two generations
  - 3. This Neglect Still Persists in Mainstream Literature
    - a. Gerald M. Meier
  - 4. What Would Be Different if It Had Been Properly Appreciated
    - a. The “**international demonstration effect**” (holding that the availability of Western goods encourages consumption at the expense of savings and investment) would have been rejected
    - b. Third World regions with the most **Western commercial contacts** were the most advanced
    - c. The concept of “**incentive goods**” had dropped from the literature
  - 5. Another Error: The “**Vicious Circle of Poverty**”
    - a. Belied by massive aggregate investments in agriculture
      - (1) Cash crops
    - b. Bauer’s Refutation
      - (1) Money is the result, not the precondition, of economic achievement
    - c. This idea is a major lapse in modern development economics
    - d. Influenced drastic policies of **resource mobilization**
  - 6. Other Persistent Lapses
    - a. Alleged **dollar shortage**
    - b. Disregard of price (supply and demand)
    - c. Disregard of trading
  - 7. Emphasis on So-Called **Imperfections of the Market**
- D. FROM MISFORTUNE TO DISASTER (7-8)
  - 1. Wider Exchange Is Indispensable for a Society’s Advance from Extreme Poverty
  - 2. Major Hazards Accompany a Low Level of Attainment
  - 3. Misery and Forced Collectivization in Ethiopia, Sudan, and Elsewhere in Africa
    - a. Enforced reversion to subsistence conditions
    - b. Hazards of a subsistence economy seem more acceptable than the hazards of an exchange economy [due to the influence of ideology]

4. Trading Activity Is Required for an Advance from Subsistence Production
  - a. Purchases and credit
5. Spread of New Ideas and Modes of Behavior
- E. SMALL-SCALE OPERATIONS (8-11)
  1. Trading Activities Are More Labor-Intensive in the Third World
  2. Small-scale, isolated operations
    - a. Lack of storage facilities and substantial cash reserves
  3. Example of **Nigerian Groundnuts**
    - a. Shipping
    - b. Imports, such as matches
  4. Sales of Produce and Purchase of Consumer Goods in Small Quantities Is Not Wasteful
  5. Collecting/Bulking of Produce and Breaking Bulk/Distribution of Merchandise Involves Much Self-Employed Labor
    - a. Absence of officially-imposed obstacles
    - b. Price of self-employed labor is low
    - c. Multiplicity of small-scale traders in part represents the substitution of cheaper labor for more expensive labor
  6. Business in Used Containers Uses Labor and Conserves Capital
    - a. Trader supplies marketing services and, often, credit
      - (1) Process of bulk-breaking in the financial market
  7. Large Number of Intermediaries (Middlemen)
    - a. Supply price is low
    - b. Option of bypassing a redundant intermediary
  8. Choice May be Restricted by the Terms of Loans
  9. No Clear Distinction between Farmers and Traders or Moneylenders
  10. Traders May Become Manufacturers
- F. NONMONETARY INVESTMENT (11-12)
  1. **Capital Formation**
  2. These Forms of Investment Are Often Ignored [cf. Bastiat's "What Is Visible and What Is Invisible"]
    - a. Their quantitative and qualitative importance
    - b. Productivity of these investments, which are made by people with a direct interest in the returns [cf. The Parable of the Talents]
  3. Adverse Consequences of Ignoring Capital Formation
    - a. Taxation and other policies often reduce the farmer's proceeds or increase his costs
  4. Consequences of this Neglect
    - a. Neglect of direct agricultural investment [Grameen Bank fills this void]
    - b. False assumptions
    - c. It precludes the framing of policy designed to maximize productive saving and investment
  5. Statistics
- G. THE SCOPE AND EFFECTIVENESS OF ECONOMICS
  1. Major Shortcomings: A Summary
    - a. Serious practical consequences
    - b. Need to recognize that cultural and political factors may be influenced by changes in economic variables

## Review

internal trade	rise in level of human capital	transformation of West Africa
critique of international demonstration effect		impact of Western commercial contacts
incentive goods	vicious circle of poverty	resource mobilization
alleged dollar shortage	intermediaries	capital formation

## II. DISREGARD OF REALITY

### Outline

- A. INTRODUCTION (15)
  - 1. Hegel's Owl of Minerva
- B. HIGH HOPES AND EMERGING DOUBTS (15)
  - 1. Economists' Exaggerated Self-Esteem
    - a. John Maynard Keynes
    - b. Neglected impact of religious and military leaders
  - 2. Milton Friedman: Economists Suggest Policy Options
  - 3. Disregard of Evident Reality
- C. UNEXPECTED TRANSGRESSIONS (16-18) [cf. What Is Seen, and What Is Unseen]
  - 1. First Example: Economists on the 1940s-Early1950s **Dollar Problem**
    - a. An apparently indefinitely persistent and inescapable worldwide shortage
    - b. Dollar glut in the late 1950s
      - (1) Reality: Quantities supplied and demanded depend upon price
      - (2) This discussion stopped with the end of the shortage
    - c. This episode was a serious transgression by economists
  - 2. Second Example: The **Vicious Circle of Poverty**, or the Idea of Self-Perpetuating Stagnation and Poverty
    - a. This was the signature tune of foreign aid advocates in the 1950s
    - b. Reality: All developed countries were once undeveloped
    - c. If this thesis were valid, mankind would still be in the Stone Age at best
  - 3. Winds of Fashion [Eph. 4:14: "Every Wind of Doctrine"]
  - 4. Examples of Retrogression Given in the Above Two Examples
    - a. No such pre-WWII assumptions
  - 5. Meanwhile, Major Advances in Economics Have Taken Place
    - a. **International trade theory** [which refutes the vicious circle of poverty]
    - b. **Theory of foreign exchanges** [which refutes the dollar shortage]
  - 6. Dissenters [Bauer Must Be Included in Their Ranks]
    - a. Obstacle: **A voice needs an echo** [cf. Mills' utilitarian case for liberty]
    - b. Reality: Dissent was crowded out by articulate groups in the academy and media [Regnant orthodoxies with retrograde views hold the strongest hand until the façade of their invincibility crumbles: cf. Thomas Kuhn's scientific revolutions]
    - c. **Collateral**: Illustration: Keynes vs. Hayek, Round Two  
<http://www.pbs.org/newshour/rundown/2011/04/keynes-vs-hayek-round-two.html>
  - 7. These Episodes Prepared Bauer to Question Received Opinion
  - 8. Third Example: Argument That Third World Poverty Is the Result of Western Neglect or Exploitation
    - a. Reality: The most backward countries are those with the fewest commercial contacts with the West
    - b. The most advanced have the **most extensive and diversified contacts**
  - 9. Persistence of These Myths
- D. ADVANCES IN ECONOMICS (18)
  - 1. Advances in Knowledge Are What Is Expected from Any Academic Discipline
    - a. Price theory, including the recognition of transaction costs
    - b. Nature of the firm, including the economics of vertical integration
    - c. Social cost [Coase, critiqued by Rothbard]
    - d. Theory of international trade and theory of foreign exchanges
    - e. Diffusion and use of knowledge [cf. Hayek and Sowell]
    - f. Economics of property rights [cf. De Soto]

- g. Economics of political and bureaucratic processes [cf. public choice theory]
- 2. Retrogression Stems from the Disregard of Reality
- E. THE EMPEROR INVERTED (18-21)
  - 1. Mathematization of Economics
    - a. Its usefulness in understanding elasticity and feedback effects
    - b. Various critics point out its major limitations
      - (1) Norbert Wiener
  - 2. Uses of **Econometric Methods**  
 [An example of an econometric (cliometric) study is Robert Fogel and Stanley Engerman's controversial 1974 work on slavery entitled *Time on the Cross*]
    - a. Research has been skewed to variables that are amenable to formal analysis [*i.e.*, whatever cannot be measured or weighed doesn't exist, as J. B. Watson put it]
    - b. What is quantifiable is confused with the significant
    - c. This has led to inappropriate claims being made for these methods
    - d. Other forms of reasoning are smothered
  - 3. Consequences
    - a. Burgeoning of incompetent or inappropriate econometric studies
    - b. Dismissal of studies based on direct observation or sampling as anecdotal
    - c. Result: Atrophy of close observation
  - 4. Traditional Methods Are Disappearing [everything driven down to the "least common denominator"]
  - 5. Differences between Physics and Economics
    - a. Difficult to discern uniformities in economics
    - b. Imprecise concepts [what Paul Valéry called "the vagueness of vague things"]
    - c. Such fuzziness limits the informative use of mathematical methods
  - 6. Economics Needs to Incorporate Practices from Historical Scholarship
  - 7. Objective Reasoning Is Just as Possible in Economics as in the Natural Sciences
  - 8. Mathematical Methods Often Provide an Effective Façade to Conceal Empty Formalism
    - a. New clothes without an emperor within them
  - 9. Indifference to Reality
- F. THE WIDER SCENE (22)
  - 1. Baffling Divorce from Reality [Some Ideologies Prefer Obfuscation]
  - 2. Symptoms
  - 3. Arguments Can Be Assessed Logically But Not Why People Accept Them
  - 4. Self-Interest May Be a Factor [Collective Self-Interest Even More So]
  - 5. The Existence of Special Interest Groups Cannot Account for Some Anomalies
    - a. *E.g.*, hostility to the West and the West's supine response to it
    - b. Such a response by the West would have been unthinkable before WWII
- G. AMPUTATION OF THE TIME PERSPECTIVE (22-24)  
 [NOTE: "Since Machiavelli, a dimension has been amputated from man's political existence. The operation was a success; but there are stitches and scars, inevitably. . . . Those riddles we find in Machiavelli, those ambiguities and ironies—they mark the points where, the soul having been cut away, we are troubled with the illusion that 'something' is still there." Quoted in Wilfred M. McClay, "The Enduring Irving Kristol," *First Things*, 215 (August/September 2011): 31]
  - 1. Mixed Motives: Confusion between Advancement of Knowledge and Promotion of Policy
    - a. Policy-inspired transgressions against reality
    - b. **Facts reshaped to fit objectives**
  - 2. Ignorance of the Past
    - a. **Ernst Gombrich** (art historian), 1950: Amputation of the time dimension

- b. Background must be ascertained
          - (1) *E.g.*, cash crop exporting countries
          - (2) Causes of inequality
  - 3. Effects of the Disruption of Sustained Observation
    - a. Future shock
  - 4. Resulting Neglect of Antecedents and Processes
    - a. Habits of thoughts in social sciences based on misleading analogies
  - 5. Result: **Loss of Collective Memory** and the **Manipulation of History**
- H. COLLECTIVE GUILT (24-25)
  - 1. Consequences of the Widely Articulated **Feeling of Guilt in the West**
    - a. What It Helps Explain
      - (1) Unfounded notions about Western responsibility for Third World backwardness and the allegedly damaging effects of commercial contacts
      - (2) Spineless conduct of the West toward African despots
      - (3) West's readiness to sponsor international forums that embarrass and undermine the West
    - b. Hostility toward South Africa
  - 2. Readiness to Give Aid
    - a. Guilt-ridden people hope to assuage their feelings by giving away (tax-payers') money without questioning the results
  - 3. Novelty of Guilt Today
    - a. Materially, the West Has Never Had It So Good, Nor Ever Felt So Bad about It
      - (1) Failure of material prosperity to bring about expected happiness
    - b. Confusion of Charity with Tendentious Self-Flagellation
    - c. Blaming the West for Inequalities
  - 4. Repudiation of Western Society [cf. Roger Scruton's "Culture of Repudiation"]
  - 5. **Social Determinism**
    - a. Participation in **Collective Guilt** Has Taken the Place of **Personal Responsibility**
      - (1) [An alleged American propensity for violence was blamed for the Kennedy assassination – cf. "vast right-wing conspiracy"]
    - b. Conspiracy-mindedness
  - 6. Summary
    - a. Kenneth Clark: indispensability of confidence and continuity
- I. MISUSE OF LANGUAGE (25-26)
  - 1. Disregard of Reality Promotes Erosion of Language
    - a. Result: Cultural disintegration
  - 2. People Have No Say in So-called Democracies or People's Republics
  - 3. Specious Aggregates, Such as the "Third World"
  - 4. Growth of Specialization
    - a. Fatalistic suppression of the critical faculties by those who can do nothing
  - 5. Information Glut and the Atrophy of Reflection
  - 6. Decline of Tradition Religious Belief
    - a. Result: Diffusion of credulity

[NOTE: G. K. Chesterton wrote: "When people stop believing in God, they don't believe in nothing – they believe in anything"].
- J. NEED TO RESTATE THE OBVIOUS (26-27)
  - 1. Malevolent Forces Undermine Our Mental and Moral Faculties
  - 2. Indifference to Reality Has Undermined Standards in Parts of Economics
  - 3. José Ortega y Gasset: Absence of Standards Is the Essence of Barbarism (*Revolt of the Masses*)
  - 4. Western Poise and Self-Assurance in the International Arena Has Been Undermined

5. Blaise Pascal: Source of Moral Conduct Is Clear Thinking
6. George Orwell: First Duty of Intelligent Men Is to Restate the Obvious

## Review

dollar problem	vicious circle of poverty	blaming Western oppression
most backward societies	mathematization of economics	econometric methods
atrophy of close observation	traditional methods	façade for empty formalism
ignorance of the past	Ernst Gombrich	rewriting of history
social determinism	collective guilt	personal responsibility eroded

Robert Michels' Iron Law of Oligarchy: "Who says organization, says oligarchy." The Wikipedia article on the Iron Law of Oligarchy asserts: "Any large organization, Michels pointed out, has to create a bureaucracy in order to maintain its efficiency as it becomes larger—many decisions have to be made daily that cannot be made by large numbers of disorganized people. For the organization to function effectively, centralization has to occur and power will end up in the hands of a few. Those few—the oligarchy—will use all means necessary to preserve and further increase their power."

Jerry Pournelle's Iron Law of Bureaucracy states that in any bureaucratic organization there will be two kinds of people: those who work to further the actual goals of the organization, and those who work for the organization itself. Examples in education would be teachers who work and sacrifice to teach children, vs. union representative who work to protect any teacher including the most incompetent. The Iron Law states that in all cases, the second type of person will always gain control of the organization, and will always write the rules under which the organization functions.

<http://www.jerrypournelle.com/archives2/archives2mail/mail408.html#Iron>

## V. FOREIGN AID: ABIDING ISSUES

### Outline

- A. THESIS (41)
  1. Foreign Aid Has Adverse Effects on Factors Behind Economic Progress
- B. THE AXIOMATIC APPROACH TO AID (41-42)
  1. Post-WWII **Origins of Foreign Aid** (Development Aid)
    - a. Grants or soft loans to relatively poor countries
  2. Its Subsequent Expansion
    - a. Original goal: self-sustaining growth
    - b. It is currently a regular component of Western budgets
  3. Transfer from the West
    - a. **Rio Conference**: Larger transfers contemplated
    - b. Likewise the UN Poverty Summit
  4. Wide Extension of the Scope of Intergovernmental Subsidies
  5. Misuse of the Word "Aid:" Promotes an Unquestioning Attitude
    - a. It disarms criticisms, obscures realities, and prejudices results
  6. Most **Official Aid** Goes to Governments, Not to the Destitute People
  7. **Effects of Foreign Aid**
    - a. It brought the Third World into existence
    - b. It is a source of the North-South conflict

- c. It promotes the politicization of life
  - 8. Unquestioning Attitude Prevails in Public Discussions of This Policy
- C. SOME CONSPICUOUS ANOMALIES (42-43)
  - 1. Britain Continued to Supply Aid to Argentina during the Falkland Islands War
  - 2. Western Aid to Iraq Facilitated the Build-up of Its Military Arsenal
  - 3. Aid Continues to Governments That Embarrass and Thwart the Donors
- D. AID WITHOUT STRINGS? (43-44)
  - 1. Aid Is Increased Despite Policies That **Harm** the Subjects of the Recipients
    - a. Persecution
    - b. Suppression of trade
    - c. Restrictions
    - d. Confiscations
    - e. Nationalization
    - f. Subsidized import substitutions
    - g. Economic controls
  - 2. Criteria for the Aid
    - a. Geared largely to the per capita incomes of recipient countries
    - b. This does nothing to discourage policies of impoverishment
  - 3. **Persecutions and Expulsions**
    - a. Resulting impoverishment makes recipients eligible for more aid
  - 4. Armaments Expenditures
    - a. Third World governments accounted for 1/5 of spending on armaments, 1981
  - 5. Paradox of Import Restrictions by Donors against Exports from Recipients
- E. ARGUMENTS AND JUSTIFICATIONS (44-47)
  - 1. The Case for Foreign Aid Has Come to Be Regarded as Self-Evident:
    - Assumptions**
    - a. Aid is needed in order to emerge from poverty
    - b. Aid is needed to improve the condition of the destitute
  - 2. Central Theme: **Vicious Circle of Poverty** and Stagnation
    - a. The facts refute this notion
    - b. The fact of development also refutes it
  - 3. Success Stories
  - 4. Model Behind the Vicious Circle of Poverty Hypothesis
    - a. Central idea: low income is the problem
  - 5. The Volume of Investible Funds Is Not a Critical Independent Variable
    - a. **Simon Kuznets:** Capital formation was a minor factor in the West's development
    - b. Poor people can generate or secure sufficient **funds for progress**
      - (1) If motivated to improve their material condition
      - (1) If not inhibited by government policy or lack of public security
  - 6. Replacement of Subsistence Production by Market Production
    - a. This process is accompanied by certain kinds of **capital formation** that are often overlooked in the statistics
    - b. These categories of capital formation are indispensable yet usually do not require monetary savings or investments
  - 7. **Capital:** The Result, Not the Precondition, of Successful Economic Performance
    - a. **Economic performance** depends on personal, cultural, and political factors
    - b. Key factors: people, culture, and political arrangements
  - 8. Commercial Lending Is Virtually a Requirement for Doing Business in Africa
    - a. Traders in turn lend to smaller traders [trickle-down economics]
    - b. Responsibility and **productivity** are the keys
  - 9. The Definition and Protection of **Property Rights** Make External Commercial Funds Available
  - 10. **Objections to Development Aid:** It Is Unnecessary and Promotes **Dependency**



- a. Development aid can cause a vicious circle
  - b. External subventions (subsidies) are insufficient for economic advancement
11. **Corollaries of the Vicious Circle Argument**
- a. Third World poverty inhibits government spending on education
    - (1) Reality: Aid-dependent governments spend lavishly on **prestige projects** and armaments while **neglecting education**
  - b. Poverty inhibits population control programs
    - (1) Reality: There is already widespread knowledge of contraception
12. Notion of the Vicious Circle Reflects Unwarranted Condescension
- F. **WHAT CAN SUBSIDIES ACHIEVE? (47-49)**
- External Donations: Unnecessary, Insufficient, and a Retardant to Economic Advance
1. External Subsidies Raise the Rate of Exchange and **Impair Foreign Trade Competitiveness**
    - a. Overall productivity of resources is the usual result of an inflow of private capital
    - b. This is less likely with official subsidies because these are rarely expected to produce a positive real return
  2. Encouragement of Beggary and Blackmail
  3. Subsidies Go to Governments
    - a. Strengthening of the power of government
    - b. Aid as an enabler of destructive practices [cf. co-dependency]
    - c. Disastrous **politicization of life** [cf. Minogue, *Politics*, ch. 13]
  4. Gains and Losses of Political Struggles: Increased Stakes
    - a. Politicization **diverts attention and resources** from productive economic activity
  5. Subsidies Enable Governments to Restrict the Flow of Foreign Commercial Capital
  6. Adverse Effects Compounded by Preferential Treatment of Governments That Promote Birth Control
    - a. Poverty in the Third World is not caused by population pressures
  7. Robert McNamara Compares Population Pressure with Nuclear War [Al Gore makes a similar invidious comparison with regard to global warning]
  8. Misdirected Obsession with Numbers
    - a. Some of the poorest countries are sparsely populated
    - b. Some of the most densely populated countries are highly prosperous
- G. A DOUBLE ASYMMETRY (49)
1. Evidence in Favor of External Subsidies Is Inconclusive
    - a. They are more likely to inhibit economic advance
  2. The Maximum Contribution of Subsidies Is Very Limited
    - a. It is too small to affect national income
  3. **Double Asymmetry**
    - a. Adverse effects far outweigh favorable ones
    - b. Relative volume of subsidies: too small to benefit, but large enough to harm
  4. The Heart of the Problem: Relationship of Subsidies to Government Receipts
    - a. It is the relationship of subsidies to **government receipts** and **foreign exchange earnings** that is relevant to major adverse repercussions
    - b. The Reason: Subsidies are far larger relative to tax receipts and foreign exchange earnings than to national income
    - c. See Rogers, Simon, and Ami Sedghi.  
[Sub-Saharan Africa in Data: From Infant Mortality to Government Debt](#)
- H. AID AND POVERTY (50-51)
1. Chief Argument in Favor of Aid: To Help the Neediest
    - a. But this is a low priority for governments
  2. No Machinery for State Relief in Most of the Third World

- a. Aid may conflict with political priorities
  - (1) e.g., Sri Lanka and Sudan
- 3. Examples of Recipient Government Policies
  - a. Enforced population transfers
  - b. Suppression of trade
  - c. Collectivization
  - d. Civil war
  - e. Result: precarious subsistence production
- 4. Much of the Aid Rewards Policies of Impoverishment or Immiseration
  - a. Here is a real vicious circle
- 5. Aid Can Alleviate Acute Shortages
  - a. Subsidies avert total collapse
  - b. Subsidies conceal the worst effects of destructive policies
- 6. Post-Communist Governments
  - a. Obstacles to reform
  - b. Subsidies for limited periods should be linked to reformist policies
- I. REFORM OF AID (51-52)
  - 1. Official Subsidies Should Be Terminated or Curtailed
    - a. Difficulties due to powerful and articulate interest groups
    - b. Implementation of reforms could bring transfers closer to proclaimed objectives
  - 2. Most Important Single Reform: A Radical Change in Criteria of Allocation
    - a. Restriction to governments that promote economic progress and general welfare
  - 3. The Futility of Linking Further Aid to Market-Oriented Policies
    - a. Unlikely to be implemented in practice
    - b. Consequences of excessive state control
    - c. Cosmetic changes
  - 4. Official Subsidies Should Be **Bilateral** Rather Than Multilateral
  - 5. Subsidies Ought to Be “**Untied**”
    - a. De-linkage from domestic interests [which makes aid disguised subsidies to them]
  - 6. Straight-Forward Grants Rather Than Subsidized Loans [Which Are Also Subsidies to Domestic Interests]
    - a. Otherwise, it is difficult to determine which palms are being greased
  - 7. These Proposals Are Unlikely to Be Implemented
  - 8. There Is Little Prospect for Substantial Reform

## Review

origins of foreign aid	Rio Conference	official aid
effects of foreign aid	anomalies	harm to recipients
persecutions and expulsions	assumptions behind foreign aid	vicious circle of poverty
Simon Kuznets	capital formation	capital
economic performance	property rights	objections to development aid
dependency	corollaries of the vicious circle argument	
what subsidies achieve	perils of politicization	double asymmetry
chief argument for aid	no machinery for state relief	enforced population transfers
subsistence production	aid can alleviate acute shortages	
bilateral subsidies	de-linking aid from domestic interests	

## VI. WESTERN GUILT AND THIRD WORLD POVERTY

### Study Questions

1. **Allegation That the West Is Responsible for Third World Poverty** Summarize the views of Paul A. Baran and Peter Townsend. What do the **poorest countries** have in common? How does Bauer refute the assertions of each? What are some of the errors of the Cambridge pamphlet? How does Bauer answer **Ronald J. Sider**, Oxfam, Cyril Connolly [BTW, many Third World countries are poorer now than they were before *independence*], **Kwame Nkrumah**, and Julius Nyerere? (53-57)
2. **Spread of Material Progress** What has been the **principal agent** of material progress in the Third World? Illustrate how the spread of material progress from more to less advanced regions is a commonplace of history. Where did the idea of material progress originate, according to J. B. Bury and Christopher Dawson? How was **Malaya** transformed between the 1890s and 1930s? What accounts for it? What did **late 19C Black Africa** lack? How did cocoa production in West Africa become a staple of world trade by the 1950s? What evidence does Bauer produce in arguing that the slave trade did not cause economic backwardness? Why does he say that guilt is a prerogative of the West? (57-60)
3. **The Charge That Western Prosperity Is the Result of Exploitation** Who profits from promoting the misconception that western prosperity is a result of **exploitation**? Identify at least three **sources** of this idea. What is the principal assumption behind it? Why does Bauer claim that colonialism was not the cause of poverty in Afghanistan, Tibet, Nepal, Liberia, and Ethiopia? Was colonialism the cause of prosperity in such wealthy countries as Switzerland, Norway, Canada, Australia, and New Zealand? How has the charge against colonialism been expanded in recent years? Why? (73-76)

### Outline

- A. ALLEGATION THAT THE WEST IS RESPONSIBLE FOR THIRD WORLD POVERTY (53-57)
- B. SPREAD OF MATERIAL PROGRESS (57-60)
- C. THE CHARGE THAT WESTERN PROSPERITY IS THE RESULT OF EXPLOITATION (61-63)
- D. ALLEGATION THAT THE WEST MANIPULATES INTERNATIONAL TRADE TO THE DETRIMENT OF THE THIRD WORLD (63-68)  
Alleged **Unfavorable Terms of Trade** Is a Major Theme in Demands for a New International Economic Order (NIEO)
  1. Rebuttal: The Poorest Areas of the Third World Have No External Trade
    - a. People benefit from the widening of opportunities which external trade represents
  2. Other Objections to This Charge
    - a. The terms of trade vary from one country to another throughout the Third World
    - b. Changes in the terms of trade have little to do with a country's welfare without reference to changes in the cost of production of exports
    - c. Unfavorable terms of trade are meaningless except by reference to a base period
    - d. This decline must end at some point before reaching zero
    - e. The West is unable to prescribe international prices
  3. The Share of a Country in Total World Trade Is by Itself No Index of Prosperity or Welfare
    - a. The British and American shares of world trade have declined since the

- 1950s
    - b. The Third World's share has increased compared with earlier times
  - 4. External Debts of the Third World
    - a. The cost of soft loans has diminished greatly
    - b. **Balance of payments deficits** of Third World countries do not mean they are being exploited or impoverished by the West
      - 1) They occur when governments live beyond their means and pursue **inflationary policies**
  - 5. Decline of Particular Economic Activities
    - a. The decline of one activity, such as the Indian textile industry, should not be confused with the decline of the economy as a whole
    - b. Cheap imports extend the choice and economic opportunities of people in poor countries
    - c. If they were not accompanied by the expansion of other activities, the population would be unable to pay for the imports
  - 6. West Blamed for a Third World Brain Drain
    - a. The training of many of the emigrants was financed by the West
      - 1) Formal education is not an indispensable instrument of emergence from personal poverty or economic backwardness
    - b. The more serious problems are the **enforced exodus** or outright expulsion of many enterprising and skilled people [see Landes and Sowell]
  - 7. Ethnic Discrimination Allegedly Has Damaged the Third World
    - a. In fact, the countries in which such discrimination has occurred were those where material progress was initiated or promoted by contact with the West
    - b. Such discrimination, where it occurred, was negligible compared with the massive and sometimes brutal persecution of ethnic and tribal groups by the governments of many Asian and African states
  - 8. External Commercial Relations Act as Channels for the Flow of Human and Financial Resources as Well as New Ideas, Methods, and Crops
    - a. The material advantages from external contacts are greater than ever
  - 9. Many Third World Governments and Their Allies Benefit from **State Economic Controls** [Remember Bastiat's Idea of "Legal Plunder"], Particularly Restrictions on External Commerce
    - a. Economic controls strengthen control over their subjects
    - b. The controls are rationalized by allegations that the West had forced imports upon them
    - c. This merely reveals a barely disguised condescension towards the ordinary people there
  - 10. The Disparagement of External Contacts Is Relatively Recent
- E. ALLEGATION THAT THE MERE DAY-TO-DAY ACTIVITIES OF THE PEOPLES OF THE WEST ALSO HARM THE THIRD WORLD (68-70)
  - 1. **International Demonstration Effect:** Cheap Consumer Goods Are Said to Obstruct Development by Encouraging Spending at the Expense of Saving
    - a. This ignores the role of external contacts as an instrument of development
    - b. Paying for the new consumer goods usually requires improved economic performance
  - 2. **Alleged Cultural Dependence**
    - a. In fact, western goods have been accepted selectively and not indiscriminately
    - b. The accusation that the West also damages the Third World through its patent laws has the opposite implication
    - c. Both the provision of Western goods and also the alleged withholding of them are said to be damaging

3. The **Allegedly Lavish Consumption** Habits of the West Have Plundered the Environment
    - a. The implication is that the West has caused famine elsewhere
  4. **Famines** Occur in Backward Regions with Practically No External Commerce
    - a. The absence of external trading links variously reflects the policies of rulers who are hostile to traders and even to private property [not to mention to various ethnic and tribal groups that are targeted for elimination]
    - b. Attempts to support populations with Western donations would inhibit the development of viable agriculture
  5. Rebuttal: Western Consumption Is More Than Paid for by Western Production
    - a. It not only finances domestic consumption but also provides the capital for domestic and foreign investment as well as **foreign aid**
    - b. The gap between production in the West and in the Third World is even greater than the gap in consumption
- F. WAYS THE WEST **HAS** CONTRIBUTED TO THIRD WORLD POVERTY (70-71)
1. Politicizing Economic Life in the Third World
    - a. The chief exponents of Western guilt have blamed colonial governments and Western influence for not promoting such policies sooner
  2. Western Contacts Have Helped Bring about a Sharp Decline in Mortality
    - a. This is a factor behind the recent rapid population growth
- G. ALLEGATIONS THAT EXTERNAL CONTACTS DAMAGE THE THIRD WORLD ARE PLAINLY CONDESCENDING (71-72)
1. They imply that Third World people do not know what is good for them, nor even what they want
    - a. Image of the Third World as a uniform stagnant mass
  2. Exponents of Western Guilt [cf. Scruton's Culture of Repudiation] Further Patronize the Third World by Suggesting That Its Economic Fortunes Are Determined by the West
  3. The Brutalities of Rulers Are Excused

## Review

poorest countries	British colonialism	Ronald J. Sider
Kwame Nkrumah	contact with the West	transformation of Malaya
late 19C Black Africa	sources of the exploitation charge	
unfavorable terms of trade charge	balance of payments deficits	
beneficiaries of state economic controls	how the West allegedly damages Third World	
international demonstration effect	Western foreign investment and aid	
west's contribution to Third World poverty	condescension	

## IX. HONG KONG

### Outline

This was originally published in 1980

- A. LIBERAL ECONOMICS LESSON: PROSPECTS FOR SUCCESS (109-10)
  1. Scarcity of Resources in Anonymous Asian Country
  2. Standard View: Low Expectations
  3. MIT View: Vicious Circle of Poverty
  4. **Gunnar Myrdal** (Swedish Socialist and Economist)
    - a. Emphasized need for **comprehensive planning**
  5. Pearson Report [Lester Pearson Was a Liberal PM in Canada]
  6. **UNCTAD: General Principle Fourteen**

7. Academic Consensus ["Settled Science"]
- B. THE EXPERIENCE OF HONG KONG (110)
  1. Phenomenal Progress Since the 1940s
  2. Rapid Rise of Income and Real wages
  3. Other Successes: A Supporting Cast (South Korea, Taiwan, Singapore)
- C. ALVIN RABUSHKA'S MONOGRAPH (110-13)
  1. 140 Year History
  2. **Policies**
    - a. Fiscal conservatism
    - b. Low taxation
    - c. Market prices for government services
    - d. Liberal immigration policy
    - e. Unrestricted movement of capital
    - f. Minimal intervention into commercial life
  3. Absence of Special Incentives
  4. Lack of Natural Resources and Colonial Rule Encouraged Non-Intervention and Fiscal Conservatism
    - a. Open economy
  5. **Drawbacks of Government Assistance**
    - a. Diversion of resources from more productive uses
    - b. Wasteful results of subsidies made more apparent in an open economy like Hong Kong's
  6. Absence of Natural Resources Assists Material Progress by **Discouraging Wasteful Policies**
    - a. "Sustained **budget deficits** financed by **credit creation** . . . tend to bring about wasteful spending" [cf. U.S. debt ceiling crisis]
    - b. British colonial accounting system prevented sustained budget deficits
    - c. Absence of election promises "reduced the **prizes of political activity** and therefore interest in organising pressure groups"
    - d. Result: Fiscal conservatism
    - e. Role of the wish to attract foreign capital, *etc.*
  7. Adaptability
    - a. Hong Kong's prosperity despite restrictions placed on exports
  8. Exceptions to Hong Kong's Use of Market Prices for Government Services
    - a. Cash subsidies to the poor
    - b. Compulsory primary education
  9. **External Pressures** towards a More Full-Fledged Welfare State
    - a. Attempts to reduce competition from Hong Kong by **inflating costs** [This dynamic can also be seen domestically within the United States]
      - (1) Foreign aid may be manipulated serve domestic interests
    - b. **Resentment** by supporters of state-controlled economies over the rise in living standards in market-controlled economies
    - c. Ambitious administrators, discontented intellectuals, and aspiring politician hope for greater scope in a more politicized society
    - d. Gov. Sir Murray McLehose
    - e. Threat of western trade barriers, labor legislation, *etc.*
  10. Rabushka's Admiration for Hong Kong
  11. Crucial Factor: Limited Government
    - a. This economic philosophy offers little scope for ambitious literati
- D. LESSONS OF HONG KONG (103-05)
  1. Decisive Role of **Personal Aptitudes, Mores, and Political Arrangements**
    - a. Access to markets is less fundamental
    - b. Physical or financial resources are much less important
  2. Vicious Circle of Poverty Idea Confuses Poverty with Its Causes
  3. Natural Resources Can Produce Windfalls without Lasting Progress
    - a. [cf. the silver mines of Potosi that helped bankrupt Spain]

4. Success without Natural Resources (Venice, the Low Countries, Switzerland, Japan) vs. Backwardness Amidst Natural Abundance
  - a. Alexis de Tocqueville on the English character
5. Population Increase Is Not an Obstacle to Progress
6. Economic Performance Owes Little to Formal Education
  - a. This fact is disturbing to professional educationists
7. Hong Kong Refutes Various Staples of the Development Literature
  - a. Self-perpetuating poverty
  - b. Inevitability of balance of payments difficulties
  - c. Indispensability of comprehensive planning and foreign aid
  - d. There is an organized perpetuation of these fables
8. What the Hong Kong Experience Shows
  - a. Planning teams and advisory groups are unnecessary
  - b. "Hong Kong has succeeded in defiance of the best professional opinion."
9. Hong Kong's **Unpopularity with Aid Lobbies** [cf. Natural Propensity toward Scapegoating]
  - a. Bad press
  - b. Hong Kong compares favorably with the rest of Asia
  - c. Socialism's favorable press
  - d. Disapproval of any deviation from western market norms
10. UNCTAD: Principle Fourteen
  - a. Its patent untruth
11. Personal Freedom Is Not a Function of Independence
  - a. Hong Kong is a dictatorship with high personal freedom
  - b. An unelected government is quite capable of being more limited than an elected one [cf. Kuehnelt-Leddihn on the confusion between liberty and equality]

## Review

Gunnar Myrdal	comprehensive planning	UNCTAD: Principle Fourteen
Hong Kong's policies	wasteful policies discouraged	drawbacks of assistance
budget deficits and credit creation		inflating costs
resentment of supporters of state-controlled economies		personal aptitudes, etc.
lessons of Hong Kong	Hong Kong's unpopularity with aid lobbies	

## X. EFFECTIVE INFLUENCE ON OPINION: THE SHENOY *Dirigistes* MEMORIAL LECTURE

### Study Questions

1. What made B. R. Shenoy a hero and a saint? (116)
2. What did the Government Planning Commission produce in 1956? What were some of its goals? What concerns did Shenoy raise? What was the case made by mainstream development economists and the international aid community (including the Ford Foundation) for comprehensive planning? How did they react to Shenoy's **Note of Dissent**? (116-119)
3. What were some of Shenoy's specific objections? (119-20)
4. How did the orthodoxy in India and the West ignore both the basic tenets of economics and of simple empirical evidence? (120)

5. What do you suppose was the effect on production of the neglect of price (which was set by state buying monopolies) by the Second Indian Five Year Plan and the World Bank report on Nigeria? (120-22)
6. *Dirigistes* are proponents of central planning rather than market-oriented solutions. What are the dangers of relying upon external economic advice? (122)
7. How is it that Shenoy has had greater long-run influence? (122-24)

### Review

India's Second Five-Year Plan    Shenoy's Note of Dissent    payment difficulties of LDCs  
price-less economics                      *dirigistes*

## XII. EGALITARIANISM: A DELICATE DILEMMA

### Review

- A.[I] CENTRAL DILEMMA FOR EGALITARIANS (139)
  1. State Action to Remove Economic Differences Entails Extensive Coercion
- B.[II] SOCIAL PROBLEMS (139-40)
  1. Extensive Concern with Economic Differences
  2. Appeal of Egalitarianism
  3. Quantification
    - a. Limitations of statistics
  4. Various Paths to Income Equality: Some Ironic
- C.[III] MORAL AND POLITICAL CASE FOR EGALITARIAN POLICIES (140-42)
  1. **Self-Perpetuating Movement** for More Egalitarianism Once the Case for It Is Taken for Granted
    - a. If the results are deemed unsatisfactory, it is assumed that more extensive efforts are required
    - b. If the policies are deemed to have failed, it is concluded they were not drastic enough
  2. "Exercise of State Authority Implies of Power between Ruler and Subjects"
    - a. Enforced removal of economic differences that result from voluntary arrangements intensifies the inequality of coercive power [*Dirigistes* place little faith in what Hayek calls "spontaneous order"]
  3. Someone Else's Possession of Wealth Does Not Restrict Our **Choices** [The Chief Problem Is Envy-Arousal]
    - a. Wealth normally results from activities that extend the choices of others
    - b. Samuel Johnson's saying is echoed by John Wesley's threefold exhortation: Earn all you can, save all you can, give all you can
  4. Readiness to Utilize Economic Opportunities Generates Economic Differences
    - a. Especially at times of rapid social, economic, and technical change
  5. The Main Dilemma [or Actual Harm] of Egalitarian Ideology
    - a. Assumption that a **malevolent force** has perverted the course of events [combining Marx's economic determinism with a devil theory of history]
    - b. Discrepancy between assumption and reality
  6. Social Justice Equated with Substantially Equal Incomes
    - a. This interpretation is anomalous because it assumes that incomes are not earned but extracted [It is an expression of the sort of class consciousness discussed in chapter 11]
  7. Disregard of Reality: Misconception That Incomes of the Relatively Prosperous



- 8. Are Secured Generally at the Expense of the Rest of the Community  
Lamentable Consequences of This Misconception
    - a. Maltreatment and **destruction of productive groups**, including ethnic and religious minorities
      - (1) Inadequacy of wealth by itself to confer power or ensure survival [cf. René Girard on the scapegoating of the rich and powerful]
    - b. Question of fair shares
  - 9. Incomes Are Earned Rather Than Distributed to Recipients
  - 10. "Redistribution" Is a Misleading Term
    - a. It is really expropriation of resources from producers [cf. the story of Naboth's Vineyard, 1 Kings 21]
- D.(IV) DENIAL THAT SUCCESS REFLECTS MERIT (142-43)
- 1. Resentment [Born of Envy]
  - 2. R. H. Tawney: **Equality of Opportunity**
    - a. Intractable Problem: How should unequals be treated?
  - 3. Inequality of Advantages [cf. the Term "Differently Abled"]
    - a. **Attempts to offset advantages** by taxation, etc., conflict with other criteria of equality [cf. John Rawls's idea of "justice as fairness" and his "veil of ignorance" thought experiment]
  - 4. Open Society
    - a. Its incompatibility with substantial equality
    - b. Success of some communities in the face of adverse official discrimination
  - 5. Sinister Consequences of the Belief in Equality
  - 6. Doctrine of the Natural Equality of Men
- E.(V) THE COSTS AND CONSEQUENCES OF EGALITARIANISM (143-44)
- 1. Usual View of the Principal Cost of Egalitarian Policies
    - a. It is thought to be a reduction of efficiency and material progress
      - (1) This is expressed as a **trade-off** between equality and efficiency
      - (2) Such formulations recognize that economic activity is not a **zero-sum game**
  - 2. Dilemma That Bauer Emphasizes: Surrender of Freedom to Achieve This Goal
  - 3. If People's Circumstances and Capacities Were Essentially the Same, Incomes Would be Largely Equal in an Open Society [Of Course, They Are Not]
    - a. Political action to reduce real differences require an extension of state power that is incompatible with a free society
  - 4. Consequences of the Persistence of Income Differences
    - a. Misleading idea of **redistributive taxation**
      - (1) Confiscation of income of producers for the benefit of others, including politicians and bureaucrats [cf. Bastiat's legal plunder]
  - 5. Imposition of Specific Disabilities
    - a. Talents regarded as common property [cf. England's prevention of emigration of craftsmen; Rousseau's general will]
    - b. Quotas
  - 6. Extension of Coercive Power in an Open Society
  - 7. Politicization of Life
    - a. Attention of ambitious people are diverted from economic activity to gaming the system [cf. R. J. Rushdoony's idea of the gambler state]
  - 8. Consequences: Question of Who Controls the Government Has Become a Matter of Overriding Importance
    - a. [cf. Bastiat on suffrage and universal plunder]
    - b. **Ferocity of political struggle** in many Third World countries, not to mention the United States
- F.(VI) APTITUDES AND MOTIVATIONS (145-46)
- 1. The Question of Why People Are Poor Is Fundamental for Sensible Remedial Action

2. Large-Scale Penalization of Productive Groups
    - a. **Guilt-manipulation** of the productive [cf. David Chilton's *Productive Christians in an Age of Guilt-Manipulators*]
  3. The "Right" of Support without Stigma
    - a. Negative income tax
    - b. Why specific welfare services may still be required
      - (1) e.g., the prevalence of health and dental decay among the children of unskilled workers with television sets
  4. International Wealth Transfers
    - a. Many recipients are paupers who prescribe the political conduct of the donors
- G.(VII) CONFLICTING OBJECTIVES (146)
1. Egalitarian Measures Often Benefit Primarily the Middle Classes
    - a. [In fact, many were so designed deliberately in order to gain political support; the [il]logic of class warfare takes many strange shapes]
  2. **Determinism**
    - a. Poverty is seen as a **condition**
    - b. Prosperity viewed as a result of **conduct**
    - c. *QED* (according to this illogic): The poor are passive but virtuous [victims] while the rich are active but wicked [villains]
- H.(VIII) GENERAL THEORIES OF HISTORY (146-48)
1. Successive Stages of History
    - a. **Extension of state power** is justified as **progressive**
  2. But Such Stages Are Not Distinct and Definable
  3. The Personification of Collectivities
    - a. [This is a holdover from animism]
    - b. This familiar practice obscures the fact of decisions being made
  4. Reality: The Variability of Events and Consequences
  5. The Inadequacy of Economic Determinism as an Explanation
    - a. Its appeal is not diminished by its obvious shortcomings
    - b. Opposite conclusions can be drawn from the same premises [e.g., Marxists correlate capitalism with war while classical liberals correlate it with peace]
  6. Ideologues Typically Regard It as Their Duty to Hurry up the Historically Inevitable [and Serve as History's Vanguard or Midwife]
    - a. This is a claim made on behalf of alleged **laws of history**
    - b. Spurious moral or intellectual justification for coercion
    - c. Underpinning of the Marxist-Leninist position at popular, academic, and political levels

## Review

egalitarianism	self-perpetuating movement	choices
malevolent forces blamed	destruction of productive groups	
R. H. Tawney	equality of opportunity	attempts to offset advantages
trade-offs	zero-sum game	redistributive taxation
ferocity of political struggle	guilt-manipulation	determinism
extension of state power	laws of history	spurious justification