the GROWTH Objective

"MAN IS A CREATURE who lives not upon bread alone, but principally by catchwords," wrote Stevenson three-quarters of a century ago. Economic debate is a running record of the correctness of his statement. One catchword after another takes the popular fancy, is bandied about as if it were the final expression of truth, becomes the slogan for a variety of debatable proposals, is gradually subjected to the cold light of analysis, loses its glamor, and passes into the discard, to be followed by another magic phrase.

Among the catchwords in greatest favor at the moment is "economic growth." Like other catchwords, it expresses or implies an objective which is obviously desirable in itself. It is harmful only to the extent that it comes to be regarded as describing a new and epoch-making discovery that supersedes old rules and principles, and hence is used to justify specific measures that violate these rules and principles.

From *The Guaranty Survey*, March 1959. Albert C. Wilcox, editor.

What Economic Growth Means

Economic growth is usually discussed in terms of what the Department of Commerce calls the gross national product, the total estimated money value of all goods and services produced in the United States within a specified period. Unfortunately, money is the only common denominator available to measure the wide variety of goods and services produced. Money, however, is a very imperfect unit of measurement because the value or purchasing power of money changes as prices rise and fall. Variations in the gross national product, therefore, reflect two sets of changes: changes in the amounts of goods and services produced and changes in the prices of these goods and services.

To overcome this difficulty, the Department of Commerce estimates the gross national product not only at current prices but also in terms of a hypothetical dollar of constant purchasing power. This is the so-called real national product, a sort of aggregate of what may be roughly thought of as the physical volume of output, although no physical unit of measurement is or can be used, and although physical volume has no literal meaning when applied to the output of services.

The real national product, despite its admitted vagueness and imperfections, is generally accepted as a useful concept and a fairly good measure of over-all production, and the increase in this product from one time period to another is what is usually meant by economic growth.

Thus defined, economic growth is an objective with which few people could quarrel. It means more useful things to serve the needs and desires of the people. It is what men have always striven for in their individual lives and what economists have always pointed to as the greatest hope for material progress in the future. It is an idea, an aspiration, and a reality as old as human history. Despite the immense obstacles placed in its way by ignorance, superstition, physical violence, and political interference, it has been interrupted only temporarily, because it is a product of human nature and normal human behavior.

Growth in a Free Society

In a free society protected against violence and fraud, economic growth is an automatic process. It takes place as a result of the desire of individuals to better the material condition of themselves and their families. In this endeavor, people save, invest, devise new and better tools, invent new products and new processes, and employ other people in order to operate more efficiently and on a larger scale. In this respect, individual proprietors and corporations behave in essentially the same way. Under the spur of competition and the profit motive, they strive constantly to produce more and better products at a lower cost. The result is economic growth.

For centuries during and after the Middle Ages, this natural process was retarded, and at times halted completely, by the extreme insecurity of life and property and by tight political restrictions on economic activities. When the system of state prohibitions and state-protected monopolies now known as mercantilism gave way to a regime of relatively free enterprise about two hundred years ago, the Western world entered upon a period of unprecedented economic growth. Within decades, the material conditions of life changed more than they had done in centuries of feudalism and mercantilism. This almost explosive progress is still going on, and it still owes its vitality to the same individual initiative, the same desire for personal self-betterment, the same freedom from paralyzing controls that actuated it from the beginning.

Many Complicating Factors

Economic growth in our complex modern society, while automatic in the sense of being self-generating, is not completely smooth and uninterrupted. It requires balance among many interrelated and interacting forces. As saving and investment increase, the supply of productive equipment must increase accordingly, and the same is true of the relation between consumption and the supply of consumer goods. Prospective markets cannot be gauged with perfect accuracy, nor can prospective costs. Industry must become familiarized with new processes and consumers with new products. Workers must find and learn new jobs. There is a constant need for readjustments and the correction of errors, and these corrections take time. For all these reasons, total output can never equal theoretical capacity. One hundred per cent employment of human and material resources is an impractical dream.

How fast can economic growth occur in practice? Between 1929 and 1957, both of which were years of generally good business, the real national product increased at an average rate of slightly less than 3 per cent a year. This company's index of business activity, which reflects a long-term rate of growth approximating that of the real national product, rose at about 3.6 per cent a year during the postwar period 1947-57. It is questionable, however, whether such a high rate can be maintained over a longer term, as the postwar years were to some extent a "catching-up" period following the long depression of the 1930's and the war-induced shortages of the early 1940's. Experience so far suggests that 3 per cent is about as high an annual rate of growth as can be reasonably expected over a long period, although any such answer must, of course, remain subject to revision in the light of future developments.

Danger of Arbitrary Goals

The essential point is that experience must be the guide. No arbitrary rate can be postulated and treated as a national objective. This is where the sloganeers of "economic growth" are treading on dangerous ground. To them, economic growth is not merely a natural and desirable occurrence; it is a program. They would set up a goal based upon theoretical calculations rather than practical experience, and in striving to achieve this goal they would make use of fiscal policy, monetary policy, and various forms of centralized planning.

The most popular objective among the "economic growth" enthusiasts seems to be a growth rate of 5 per cent a year, apparently because this is approximately the average rate for the early postwar years when industrial reconversion from war to peace and the great upsurge in prices were over. This is below the wartime rate of 10 per cent or more achieved under obviously abnormal and highly inflationary conditions, but it is substantially above the 3 per cent rate based on actual long-term experience. The 3 per cent rate is rejected by the "5 percenters" as inadequate because the long span of years on which it is based included some periods of recession – with the clear implication that such periods can and should be avoided in the future.

Blueprint for Inflation

How would recessions be avoided, according to the 5 per cent school? Principally by making the 5 per cent growth rate a national objective and shaping fiscal, monetary, and business policies around it. To begin with, federal spending would be deliberately increased at that rate. This rise in federal spending, reinforced by appropriate tax, monetary, price, wage, and profit policies, would cause other types of expenditure to increase accordingly. The increase in total expenditure would be matched by equivalent increases to output, incomes, and governmental revenue so that there would be no price inflation, no Treasury deficits, no increases in tax rates, and no rise in the ratio between governmental and private spending. The only difference would be that economic growth would proceed steadily at the 5 per cent rate, instead of varying from year to year and averaging out at about 3 per cent, as in the past.

This program is so full of gratuitous and unrealistic assumptions that it would be difficult to know where to begin the list. Its weaknesses might be summarized by the statement that it assumes the feasibility of an arbitrary rate of growth at variance with the testimony of experience, and assumes further that this rate could be achieved by inflationary methods that would stimulate without inflating and without causing a "boom-and-bust" cycle.

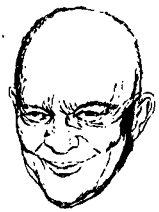
Actually, the rate of economic growth in a free society is determined by the same factors that cause it, namely, the relative propensity of individuals and business firms to spend, save, and invest. It is the net resultant of a complex set of powerful forces. It cannot be predetermined, and any plan to increase it by fiscal manipulations is simply a blueprint for inflation.

Uninterrupted Boom Impossible

It is easy to understand why theorists become impatient when they contemplate the gap between actual output and full capacity, and why they are prone to devise schemes for closing this gap. Yet it is significant that businessmen are seldom found among proponents or adherents of such schemes. Businessmen know by experience that economic freedom includes the freedom to make mistakes and that only in a society where mistakes are never made can output continuously match full capacity. Economic regimentation offers no solution, because dictators also make mistakes, and their mistakes not only are on a larger scale but also are beyond the discipline of free markets, the great automatic correctors of mistakes. Dictators' mistakes may not cause unemployment in the usual sense, but they are sure to cause hidden unemployment in the sense of misdirected utilization of resources.

The desirability of economic growth is not subject to question, and if the United States can achieve a long-term annual growth rate of 5 per cent or even more, so much the better. But when economic growth becomes a slogan for proposals aimed at uninterrupted business boom, it becomes a menace to economic stability and economic freedom as well. • • •

HISTORY is with him



TO DATE, no one has accused President Eisenhower of being a deep student of history, but apparently he has delivered himself of a comment which is backed by the weight of a great deal of history. He is credited by *Life* magazine with having said at one of his National Security Council conferences, "Damn it, when are you going to learn that national security and a sound economy are the same thing?"

From *The Indianapolis Star*, March 10, 1959.