

A DISASTER IN VIRTUALLY EVERY RESPECT

By JAMES R. LOTHIAN

THE PONTIFICAL COUNCIL for Justice and Peace (PCJP) issued a white paper on the world economy in October, “Towards Reforming the International Financial and Monetary Systems in the Context of Global Public Authority”, that within days of its release provoked a firestorm of criticism. And deservedly so.

The document is a disaster in virtually every

respect. It is a mixture of empirical assertions, half-baked economic theorising, dubious moral theology and tendentious textual exegesis. It is also quite unevenly written, with the rambling style, off-kilter transitions and subordinate clauses seeming to appear from nowhere that smack of a work by committee. Its bottom line is a call for a world political body—dubbed in rather Orwellian fashion by the document’s

authors “the Authority”.

The desirability of such a body the authors assert is “obvious if we consider the fact that the agenda of questions to be dealt with globally is becoming ever longer”. Here they catalogue “peace and security; disarmament and arms control; promotion and protection of fundamental human rights; management of the economy and development policies; management of the migratory flows and food security, and protection of the environment”.

“In all these areas”, they go on to say, “the growing interdependence between states and regions of the world becomes more and more obvious as well as the need for answers that are not just sectorial and isolated, but systematic and integrated, rich in solidarity and subsidiarity and geared to the universal common good.”

Two Expressed Concerns

What should this world political body be? According to the Pontifical Council: “[It] should have a realistic structure and be set up gradually. It should be favourable to the existence of efficient and effective monetary and financial systems; that is, free and stable markets overseen by a suitable legal framework, well functioning in support of sustainable development and social progress of all, and inspired by the values of charity and truth.”

Underlying the Pontifical Council’s proposal are two sets of expressed concerns: the economic dislocations stemming from the recent financial crisis and a supposedly widening income gap between rich and poor countries. The culprit in both instances, according to the PCJP, is the market economy, or what they term “economic liberalism”. Their putative solution is intervention of various sorts by the Authority.

“Economic liberalism”, the PCJP write, “is ... a form of ‘economic apriorism’ that purports to derive laws for how markets function from theory.” This is, true at least to some extent, but beside the point. Any scientific theory has a strong *a priori* element to it. But if a particular theory survives over a long period of time, which the theory supporting the superiority of a market economy has done, it gets amended as new empirical evidence comes to light.

The PJCP, however, go on to suggest that there is in fact no empirical evidence to support the superiority of a market economy. They write: “An economic system of thought that sets down *a priori* the laws of market functioning and economic development, without measuring them against reality, runs the risk of becoming an instrument subordinated to the interests of the countries that effectively enjoy a position of economic and financial advantage.”

The PJCP are wrong, both in the small and in the large. Ample empirical evidence derived from studies of regulated industries, exists showing that in most

instances regulation does more harm than good. Political failure, in effect, trumps the market failure—real or imagined—that gave rise to the government intervention.

On a country-wide level, the PCJP are also wrong. An absence of distorting government intervention and the pursuit of other good policies like price stability and the opening up of international trade—coupled with good institutions, the enforcement of private property being key—enable growth. They provide the incentives to entrepreneurs to engage in the activities that reduce costs, raise the rate of return to investment and thus foster faster economic growth. With increased economic growth, in turn, comes a reduction in poverty.

The increased growth in China and India that followed economic liberalisation in both countries in the 1980s is a major case in point. On one set of estimates, the result has been a reduction in China since 1981 of 600 million out of 1.3 billion people living in extreme poverty, defined as those earning less than one dollar per day. In India, the comparable figure is a reduction of 300 million out of 1.1 billion people living in abject poverty.

Advantageous to Society

Two centuries ago, Adam Smith stated the theoretical case for a market economy very clearly in his *Wealth of Nations*. In a particularly telling passage Smith wrote:

Every individual is continually exerting himself to find out the most advantageous employment for whatever capital he can command. It is his own advantage, indeed, and not that of the society, which he has in view. But the study of his own advantage naturally, or rather necessarily, leads him to prefer that employment which is most advantageous to the society.

Nobelist George J. Stigler called Smith’s analysis here an “an overwhelmingly important triumph”. Smith, Stigler says, “put into the centre of economics the systematic analysis of the behaviour of individuals pursuing their self-interests under conditions of competition. ... [His] proposition that resources seek their most profitable uses, so that in equilibrium the rates of return to a resource in various uses will be equal, is still the most important substantive proposition in all of economics.”

Economists give two reasons supporting this proposition. The first is based on information. In a market-centred economy the action takes place between individual producers and consumers. Those producers have the detailed day-to-day knowledge of the markets in which they operate that a government regulator or government planner cannot possibly have. Prices, therefore, reflect relative values more

closely than prices set by the regulator's or planner's dictate.

The second has to do with human behaviour more generally. Adam Smith justified his proposition using his famous—and often foolishly derided—metaphor of the “invisible hand”:

As every individual, therefore, endeavours as much as he can both to employ his capital in the support of domestic industry, and so to direct that industry that its produce may be of the greatest value; every individual necessarily labours to render the annual revenue of the society as great as he can. He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it. By preferring the support of domestic to that of foreign industry, he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention.

The underlying notion here is that markets provide a way of constructively harnessing individual self-interest so that society at large benefits.

The idea certainly did not originate with Smith, as the following quote from the late-scholastic priest

and theologian Tomás de Mercado, O.P. (c. 1500-1575) indicates:

We cannot find a person who does not favor his own interests or who does not prefer to furnish his own home rather than that of the republic. We can see that privately owned property flourishes, while city- and council-owned property suffers from inadequate care and worse management. ... If universal love will not induce people to take care of things, private interest will. Hence, privately owned goods will multiply. Had they remained in common possession, the opposite would be true.

The contrast between the views of Smith and Mercado and the views of PCJP could not be starker. Smith and Mercado inhabit the Christian world in which original sin and concupiscence are realities. The PCJP authors inhabit a very different world. It is the world of Rosseau, or going back farther in time, Pelagius.

I can think of no more thoughtless—and indeed pernicious—scheme than the PCJP's call to set up a world “Authority” with both political and economic power.