

# IDEAS ON LIBERTY

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## Canute's Courtiers Were Wrong

Shortly after the northeast blackout a *New York Times* headline blared: "Under Deregulation, Montana Power Price Soars." The story explained that "Montana residents used to pay some of the lowest rates for power in the Northwest, but now, some lawmakers lament, they pay among the region's highest. What happened? Mainly deregulation."

The story went on: "Montana Power executives argued six years ago that state residents would benefit from paying competitive rates for electricity and natural gas. As market rates have gone up, though, the residents have had to bear the cost, critics of deregulation say."

Although the article acknowledged that "So far Montana has not experienced the kind of supply problems that plagued California in recent years," the strong impression was left that rising prices are a grave indictment of deregulation.

The historic blackout again demonstrated that the word "deregulation" is subject to as many interpretations as a Rorschach inkblot. California is said to have embraced deregulation, but this is true only if the word means something other than the removal of regulation. In Montana, legislation was passed in 1997 to allow a choice of retail electricity providers. Retail prices were frozen for two years, and electricity co-ops, which serve half the state's homes, were allowed to opt out of the new arrangement.



All but two did so. When the price freeze expired, prices rose, which has upset customers. An organization of single mothers even sued the state in federal court, claiming the legislation is unconstitutional because, the *Missoulian* reported, it "caused or will cause huge power rate increases that deprive the women of the basic necessities of life." (A district court judge dismissed the suit.)

Rather than dwell here on the misleading use of the word "deregulation," let us focus on the proposition that rising retail prices per se indicate that that something is amiss. This belief rests on a usually unspoken, but nevertheless consequential premise that prices ultimately are arbitrary and can be controlled by government with impunity.

This in turn is part of a deeper fallacy: the proposition that economic laws do not exist and that the belief that they do is a superstition limiting man's collective power to arrange his social life. It's an old misconception, a throwback to pre-economics. As Ludwig von Mises wrote in *Epistemological Problems of Economics*,

When men realized that the phenomena of the market conform to laws, they began to develop catallactics and the theory of exchange, which constitutes the heart of economics. . . . The development of economics . . . did more to transform human thinking than any other scientific theory before or since. Up to that time it had been believed that no bounds other than those drawn by the laws of nature circumscribed the path of acting man.

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It was not known that there is still something more that sets a limit to political power beyond which it cannot go. Now it was learned that in the social realm too *there is something operative which power and force are unable to alter* and to which they must adjust themselves if they hope to achieve success, in precisely the same way as they must take into account the laws of nature. [Emphasis added.]<sup>1</sup>

Thus economics—the identification of the regularities that constitute the market process—stood in the way of the sheer will of the ruler. He could command, but if he contravened the laws of economics he could not bring about the results he wished. “Thus,” Israel Kirzner wrote, “the idea that there exist in society ‘laws’ which operate regardless of the will of the rulers was a genuinely revolutionary idea.”<sup>2</sup> And, Mises added, “Whoever wished to combat liberal economic policy was compelled to challenge the character of economics as a science. Enemies arose against it for political reasons.”<sup>3</sup>

## “A Prodigiously Ingenious Mechanism”

The German Historical School of the late nineteenth century was one of those opponents of liberalism that rejected economics. It held that only specific historical episodes could be described, and that no universal laws regarding human action existed. Carl Menger, founder of the Austrian school, defended economics against the historicists. Mises did the most to systematize the “science of human action” (which he called “praxeology”) and to free it from its earlier tentative empirical mooring. But one can find hints of the Misesian approach in the writings of Frédéric Bastiat and others. Bastiat saw spontaneous regularity all around. “We should be shutting our eyes to the facts if we refused to recognize that society cannot present such complicated combinations in which civil and criminal law play so little

part without being subject to a prodigiously ingenious mechanism. This mechanism is the object of study of political economy.”<sup>4</sup>

What does this theorizing mean? It means that regardless of motives, if the government puts a ceiling on prices, there will be unsatisfied demand—shortages (other things being equal). If the government puts a floor under prices, there will be unsold goods—surpluses (again, other things equal). If a minimum wage is legislated, there will be surplus labor—unemployment. It’s the law.

The story of the control of electricity prices is classic. For the last few decades, the demand for electricity has been rising. Think about how many new uses people have for electricity: computers, modems, VCRs, DVD players, cordless telephones, video-games, and more. But while this demand was rising, regulators often thwarted the industry’s ability to meet that demand with greater supply. Meanwhile, retail prices were strictly controlled by the authorities.

Prices are signals. They communicate vital information about the state of resources, goods, and services. Changes in those signals indicate changes in prevailing conditions—and stimulate remedial action: conservation by consumers and new supplies and alternative products from entrepreneurs. The idea that anything good can come from distorting or squelching those signals is astounding in its lack of wisdom. It’s equivalent to believing that a person with a fever can be helped by placing his thermometer in ice water. Yet that is the policy that has often been followed with electricity (and so many other things).

The would-be regulators may not want to hear it, but King Canute the Great’s courtiers were wrong. He couldn’t really “command the tides of the sea to go back.” □

1. Ludwig von Mises, *Epistemological Problems of Economics* (New York: New York University Press, 1976 [1960]), p. 3.

2. Israel M. Kirzner, *Ludwig von Mises* (Wilmington, Del.: ISI Books, 2001), p. 72.

3. Mises, p. 4.

4. Frédéric Bastiat, *Economic Harmonies* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1996 [1870]), p. 5.

# Grutter v. Bollinger: A Constitutional Embarrassment

by George C. Leef

**A**ll animals are created equal—but some are more equal than others.” So goes the crucial line in George Orwell’s classic *Animal Farm*. The Supreme Court’s recent decision in *Grutter v. Bollinger* makes one think of that line, since it gives constitutional approval to the policies used at many colleges and universities that group applicants by race and treat certain groups as “more equal than others.” Racial preferences can’t be used too overtly, the Court said, but they are acceptable, and if one takes the rhetoric of the decision seriously, it would seem that the nation would be in a terrible state if colleges and universities didn’t use them.

*Grutter* has been wildly cheered by most of the higher education community and social interventionists generally. By “social interventionists,” I refer to those who believe that virtually every aspect of society can be improved by the application of their wisdom, whether it’s the housing market, health care, preparation for retirement, or anything else. Social interventionists are never content to leave processes alone if they can take over and direct them. When it comes to universities, student admissions can’t just be left up

to a simple rule like “admit the academically best students possible.” Instead, social interventionists delight in trying to engineer a student body that is “diverse” and have convinced themselves that doing so is both noble and immensely beneficial.

## The Problem of Government Education

I would not care in the least if any private college or university wanted to use racial preferences to assemble a student body that it regarded as having the ideal mix of people. They should be free to discriminate on the basis of race—or religion, musical tastes, family background, political views, acceptance of vegetarianism, or anything else—if they want to. The trouble occurs when government-funded institutions adopt such preferences. We can blissfully ignore the choices of private institutions that can neither tax nor control us. When dealing with government, however, people cannot escape its power and are entitled to expect that they will not be treated differently from others, or compelled to support institutions that do.

This is one of the vast number of controversies that would never arise if government did not undertake activities that go outside

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