

Part V

Some General Observations Relevant to Trading in Futures

Some Economic Myths of our Times

by
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First, let me commend the Chicago Mercantile Exchange for holding this conference. This conference as an effort to improve the functioning of the market for the most important of all agricultural commodities, cattle; to assist in the process of price discovery; and to make possible the shifting of risk from those who wish to avoid it to those who elect to bear it.

This is a major undertaking, and a constructive one. The thing I like about this approach is that it is progressive. We who believe in the market economy believe that there must be innovation and change if the market is to be at its best. Insurance was such an innovation. The official grading of commodities was another. Futures trading was another, and the adaptation of this institution to additional commodities is yet another.

But, let me speak this word of warning: When you have successfully worked out the technical details of futures trading in live cattle, there will remain another great unsolved problem, which is the lack of public understanding. And if they don't understand it, how will they accept or support it? A.G. Osgood, vice president of the Harris Trust and Savings Bank, facetiously defines futures trading as "buying and selling what you never had and did not pay for at more than it cost." How will the people understand such an operation? Of today's voting public, only about 10% have had as much as one formal course in economics. Imagine the mathematical competence of the population if only 10% of the people have ever studied arithmetic!

The esoteric aspects of market operations may not have been particularly troublesome in years past, when we were, in effect,

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governed by those we called "the wise, the rich and the well-born." But we now live in what has been called "the age of the Common Man." If the common man doesn't understand the market, he is not likely to defend or support it. He may, in fact, tear it down, and replace it with centralized decision-making, as he already has in one-third of the world. Your chairman has mentioned the fact that I formerly served as economic advisor in the federal government. While in that post, I was impressed with the generally low level of economic literacy in the country, and with the handicaps thereby imposed on the functioning of the economic system. I drew up a list of economic myths, deeply and widely held erroneous beliefs which jeopardize the functioning of a free economy. Some of these I wish to share with you. Here are two:

- (1) The myth that if someone gains, someone loses.
- (2) The myth of heroes and villains.

But before I comment on these individual myths, let me say a word about economic mythology in general. Economics is a mystery to many. Stand on a busy street corner some weekday morning and watch the people streaming by, each occupied with with his own affairs. Where are they bound? What are they about? How did they get their present jobs? Who had the forethought to produce the goods with which their needs might be met? Pick out one of them and ask yourself, "What is his probable income? Why not more? Why that much?"

Or go into a modern supermarket. Here are some 5,000 food items on display, each marked with a price. What forces led to the production of all of these items? Why does some particular cut of meat sell at \$1.05 per pound? Why not \$.90 or \$1.25? December cattle futures at the Chicago Mercantile Exchange were recently quoted at \$27.50. Why that price? Why not more, or less? The census lists some 1,800 different occupations in the United States, including 264,000 stenographers, 330,000 plumbers and 38,000 airline pilots. How did we happen to get approximately the right number of people to fill these jobs? Ask these questions of the people themselves, and you would get a variety of answers, partly based on things wholly personal, and partly based on economic mythology. That there might be undergird-

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ing principles — economic laws — which explain and coordinate this multiplicity of activities would be a novel thought to many. The whole process, marvelously integrated and interdependent as it is, seems without unifying principle.

If someone were to ask, "Why do people behave as they do?" he would be told, "They do what they themselves have chosen," a reply that leaves much unexplained. How does 200-million people, operate without central direction, make the proper choices? How would you explain the voluntary system, with each person freely choosing his own job and making his own decisions? The principles which support it are not understood. To many people, economics is beyond comprehension.

People do not like to be without comprehension. They like to understand things, to have some belief which permits an observed event to take on meaning. This craving finds outlet in the myths which people create to explain their condition, or their hopes, or the events they see about them. The belief does not necessarily have to be true, some fragment of truth will suffice. There is not ordinarily a disposition to place the myth to the test. To do so would be to risk the security of mind which the myth provides, which is the very purpose of its being. The motive which leads to the propagation of a myth is not the scientific quest for fact; it is a subconscious desire for a personally acceptable answer to the question, "Why?"

Thus, there arise fragmentary and inconsistent explanations for observed events. I shall deal with two of these economic myths.

The myth that probably causes the most difficulty in the field of public policy is this: the belief that if two people engage in a transaction and one of them is seen to gain thereby, it must follow that the other has lost. One man's gain is felt to be another man's loss. This myth is extended to encompass whole groups. Economics is looked on as a game of dice: "No greater value is carried away than is brought in." To put it concretely: Members of the Chicago Mercantile Exchange deal in farm commodities. The myth has it that if members of the exchange are seen to make money, they must have made it at the expense of the farmers. This is the myth. It needs the best analysis we can give it.

Consider two common characterizations of the exchange pro-

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cess. In the first one, the average citizen drives past the suburban home of some wealthy businessman, notes the huge lawn, the lovely landscaping and the late-model car parked in the driveway. "Nobody," says he to himself "could get that much money without taking it away from somebody else!"

In the second characterization, this same citizen buys a pair of shoes at a drygoods store owned by the same businessman. "Thank you!" he says, as he receives his shoes. "Thank you!" says the clerk as he rings up the money. Is this exchange of "thank you's" a mere matter of form? Or does it express something intuitively or even subconsciously felt by these two people? In any case, buyer and seller have cause to be pleased with this voluntary transaction, and to thank each other. Each received an item of greater value *to him* than the value of the item with which he parted. The buyer preferred the shoes to the money; for the seller the reverse was true. So both gained by the exchange.

Which of these two characterizations is the more accurate, the citizen's allegation that he has been exploited, or his courteous acknowledgement of a service rendered? Is the exchange process mutually advantageous? Or is it a matter of exploitation? The myth says that trade is exploitation — exploitation of the weaker by the stronger, of the smaller by the larger, of the poorer by the more wealthy.

Once this myth is embraced, many things follow. All profits become evil, all business is viewed as a scramble to take something away from somebody else, and all wealth is thought to have been accumulated by exploitation. Any nation which really accepts this myth will either confiscate or closely regulate its private property. It will inject government deeply into the marketing and pricing process, and will substitute centralized decision-making for the operation of free markets. The fact that the United States has gone so far in this direction is evidence that the myth is widely held. The danger to a free society bred by this myth is subtle and great.

It is clear that as specialization and trade take place, the total volume of wealth increases. With widespread trading, the net worth of the country is rising. The gross evidence is contrary to the myth. Experience shows that when people are free

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to exchange goods, they invariably do so. If, as the myth would have it, one party or the other is victimized in the process, then it would be most extraordinary that the total population would so consistently lay itself open to injury. Nothing that I have said denies the fact that exploitation *does* sometimes exist, that on certain occasions someone's gain is someone else's loss. This is the fragment of truth which keeps the myth alive.

The great myths of literature are liberally supplied with heroes and villains. In fact, the essence of mythology is the personification of events. When the volcano erupted, Vulcan was at work; when the waves rose, Poseidon was troubled; if events were against man, it was because some God had thwarted him.

One of the great myths of economics is the personification of hopes and problems; the explanation of events in terms of individual acts. This myth has immense appeal:

- (1.) It simplifies complex matters.
- (2.) It permits instantaneous appraisal of current proposals.
- (3.) It provides outlet for the human desire to extoll virtue and to castigate villainy.

The utility of instant identification will be attested by anyone who has watched a television program. The audience wants to know who to pull for, and whom to be against; our stylized Westerns readily accommodate this wish. Heroes wear white hats or ride white horses. Villains are identified by scowl or speech. One can switch on the set in the middle of a program and be current as to the plot in a moment. So with the economic myth. Should the citizen favor some proposal? This is not a difficult matter. He identified his hero, and notes where the hero stands on the question; if the hero is for it, the citizen feels safe in supporting it. More likely, the citizen decides what he himself is for and attaches the hero's label to any public figure who concurs.

Heroes and villains can be individual persons, political parties, vocational group or causes. They come in various sizes and categories. Among individual heroes there is the elder-statesman type, the man of action, the rough-hewn man of the people, the man of principle, and many others. For villains, one can take his choice. There is the pawn of the vested interest, the unscrupulous

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man, the expedient man, and the man who is simply uninformed. Men in public life become type-casted in one or another of these categories, tabbed and labeled for instant recognition. The man who accidentally acquires a hero's billing is fortunate indeed; the man who has the misfortune to be cast as a villain can spend the rest of his life trying to detach the label.

How accurate are these labels? Not very accurate, obviously. Most men and most organized groups are too complex to be accurately tabbed as villainous or heroic. There must be enough authenticity in the labeling process to make the whole operation credible. This need not be very much.

What caused the Great Depression? The myth says that Herbert Hoover was responsible, though a search of the literature of the 1930's turned up 43 different explanations, put forward by responsible people, for that complex event.

Why does the farm population keep declining? The myth says that farms are being liquidated by the Secretary of Agriculture, and this despite the documented fact that the technological revolution is responsible.

What causes wages to rise: The myth delegates sole responsibility to the labor unions, despite the fact that the trend began long before there were any unions and despite the fact that wages rise in non-union industries as well as in organized plants.

Who is for fiscal responsibility? The Republicans, says the myth, though the Grand Old Party can count some great spenders among its number. Who is for the common man? The Democrats, says the myth, despite the fact that a large sector of the party represents the privileged part of the society.

Who are the heroes saluted by those now called liberals? Among others, the myths lists Jefferson, Jackson, and Franklin Roosevelt. Certainly Jefferson would be ill at ease with the programs now offered under the liberal label. Who are the heroes recognized by those now called conservatives? Hamilton, Lincoln, and Robert Taft are among them, though Lincoln certainly frightened some of the conservatives of his time.

Certain causes come to be identified in economic mythology as heroic. The fight against monopoly is such a cause. The fight against inflation is another. The fight for labor is yet another.

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Another is the fight for pure food, as witnessed by the "cranberry crisis" of 1959, when the Department of Health, Education, and Welfare prohibited the sale of berries containing such infinitesimal quantities of herbicide that a person would have to consume 13 tons in order to experience injury.

Some causes become identified in economic mythology as villainous. The desire of farmers to employ seasonal workers younger than the legal minimum age is such a villainous cause, despite the willingness and the ability of young people to engage in such labor. Importation of labor from Mexico is also villainous. And, make no mistake about it, trading on the commodity exchanges is identified (by some people) as contrary to the public interest.

Sometimes a cause will shift from one category to another. Protecting American industry from foreign imports was once heroic, but is now villainous. The cause of agriculture was once heroic, but the city man, with his far greater number of votes, finds the merit of his cause increasing relative to that of his country cousin.

Of course there are some authentic heroes and some genuine villains, and these are often discovered. The country's leaders do indeed make decisions which have far-reaching consequences, for good and ill. It is appropriate for the people to try to take the measure of their leaders, and to appraise their acts. The problem comes with oversimplification, to which the leader himself is often a part. He tries to receive credit for more than he really does. It is a matter of poetic justice, perhaps, that he also, then, be charged with responsibility for more than his share of the things that go wrong.

Demythologizing economics is a difficult task. A professor may spend a full class period with 30 students analyzing some particular piece of economic life with all its complexities and interrelationships. But that night some political figure, in a five-minute telecast for a nationwide audience, will explain the whole thing simply and understandably in terms of heroes and villains.

In the myth of heroes and villains, we have an unfair basis for judging individuals; a method by which the public engages in self-delusion on a grand scale, and a threat to marketing insti-

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tutions like the Mercantile Exchange.

How should we, who are concerned with the proper functioning of the market economy, deal with these myths? Must we accept them and live with them? Has our interdependent society become so complex that economic understanding is impossible? I say, "NO!" Economic education *is* necessary. I quote Thomas Jefferson: "I know of no safe depository of the ultimate powers of society but the people themselves; and if we think them not enlightened enough to exercise their control with a wholesome discretion, the remedy is not to take it from them, but to inform their discretion by education." Abraham Lincoln said, "Let the people know the facts and the country will be saved."

Our defense of the market system must be intelligent and progressive, not archaic or reactionary. The central objective should be freedom. The word freedom is here used in the constitutional sense — a concept which so limits the freedom of each as to maximize the freedom of all. A serious error comes from considering freedom to be synonymous with license, the total absence of restraint. A better concept of freedom is that it be closely tied to responsibility. The plain citizen puts it simply: "Your freedom ends where my rights begin." The more responsibility is self imposed, the less restraint will have to be supplied from outside. Certainly, it is within the province of government to prescribe the general conditions under which access to the market is to be available — conditions related to health, public safety, the national security, patent rights, and the like. But arbitrary exclusion from the market does not fit the criterion.

To argue for free access to the market is to contemplate an active, but not a dominant role for government. This role is to improve the functioning of the exchange system, to place a floor over the pit of disaster, to help the individual equip himself better for his task as a decision-maker, and to see that the market functions as an enlightened institution.

Many who believe in the market system allow themselves to be backed into a corner and forced to defend an institution which is not at all what they advocate. They unintentionally take on the defense, not of the free market, but a caricature thereof. They are maneuvered into defending the free market, not as

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it is or as it could be, but as it once was or as its adversaries contend it should be.

What is here advocated is a market free from manipulation, free from misrepresentation, free from gross ignorance, and free from senseless gyration as well as free from government domination. It means the kind of market that intelligent people are capable of creating in the modern day.

Advocacy of access to the market need not and should not be a doctrinaire position which renounces all of the enlightened marketing institutions that have developed since the turn of the century, though adversaries of the free market try to force defenders into such a position.

If the advantages of the market are to be retained, the myth which makes the market synonymous with exploitation will have to be dispelled. If the abuses of the market are to be avoided, the market must be a more enlightened institution. In any case, economic education must occur. The market system at least deserves to be understood before it is condemned, and presently, it is being condemned without proper understanding.

Students of biology learn that there are three distinct circumstances within which different species exist together. There is the parasitic relationship, as when the mistletoe attaches itself to the oak and lives by exploiting its host. There is the competitive relationship, as when corn and weeds compete with each other for moisture and sunlight. There is the symbiotic relationship, by which two species help each other, as do the bee and the clover.

Failure to understand these relationships has led man to drive to the point of extinction certain species which were wrongly felt to be harmful. We now discover that relationships thought to be parasitic are not so in fact and that the number of symbiotic relationships is far greater than we thought to be true.

Likewise, the myth that the tradesman is parasitic has placed in jeopardy an institution which holds immense possibilities for improving levels of living. The need is to dispell this myth and make the market an even more effective instrument.

If the Chicago Mercantile Exchange is to be successful in the trading of live cattle, the technical details of such trading will

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have to be worked out, as perhaps they have already been, and the market will have to perform in a constructive fashion as perhaps it is already doing. That will be necessary. But it will not be sufficient. In the long run, whether cattle trading succeeds, or whether the Mercantile Exchange continues to exist, or whether the market economy survives will depend on the public understanding and acceptance of these institutions. The myths that jeopardize the market will have to be dispelled. At stake is the economic system itself. The big job is education.

Other Economic writers have taken pains to prove "That if someone gains in a transaction, someone must lose." The readers may refer to the book which inspired the Technocrats of the thirties entitled, The Engineers and the Price System" by Thorstein Veblen, or to Bakken's "Theory of Markets and Marketing" in which the author categorically states, "In a true market transaction one man's gain is another man's loss." This basic precept is elucidated in chapter 10 of his book. A number of other writers would take sharp exception to Paarlberg's thesis. Editors note

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