

How FDR Prolonged the Great Depression

by Jim Powell

President Franklin Delano Roosevelt's stock has long been overvalued. Now there are signs that his public image bubble is ready to burst and his lofty reputation is headed for a crash.

The 1950s through the 1990s were the glory years for FDR hagiographers such as James MacGregor Burns, Arthur M. Schlesinger Jr., Frank Freidel, William Leuchtenberg, Ted Morgan, and Kenneth S. Davis, who embraced the view that the Great Depression proved the failure of free-market capitalism, the greatness of FDR, and the need for continuing government intervention in the economy. That view continues to be heard, of course, as it was in *Freedom: A History of US* by Joy Hakim, whose children's history books have sold some 4 million copies. "The first hundred days of [FDR's] presidency are famous for their accomplishments," she gushes.

There is one small problem with this view: its central premise is wholly false. The New Deal failed to get America out of the Great Depression. If anything, it made matters worse. Throughout the New Deal era, the median annual unemployment rate was 17.2 percent. At no point during the 1930s did unemployment go below 14 percent. Although there was episodic recovery, the 1937 peak for per capita output was lower than the previous peak in 1929. And the 1937 peak was followed by a crash. As Milton Friedman and Anna J. Schwartz have observed, that was "the only occasion in our record when one deep depression followed immediately on the heels of another."

The Great Depression was the most impor-

Cato senior fellow Jim Powell's book, FDR's Folly, How Franklin D. Roosevelt and His New Deal Prolonged the Great Depression, will be published in September by Crown Forum.



At a Capitol Hill dinner on Social Security reform attended by more than a dozen members of Congress, José Piñera makes a point about the urgency of giving workers private accounts to Rep. Jennifer Dunn (R-Wash.) and her fiancé, Keith Thomson.

tant economic event in American history, ushering in the biggest peacetime expansion of federal power. Accordingly, more and more economists have focused on the New Deal's bottom line—the actual effects of New Deal policies—rather than on the good intentions of New Deal personalities.

The first crack in the conventional wisdom appeared with the publication in 1963 of Friedman and Schwartz's *Monetary History of the United States*, which showed that the principal culprits responsible for the Great Depression were Federal Reserve officials who presided over the contraction of the money supply by a third between 1929 and 1933. Erratic Fed policies contributed to prolonging the Great Depression. It was a government failure, not a market failure.

Since then, dozens of journal articles and several academic books have reported the effects of one New Deal policy after another, and the findings are overwhelmingly negative. The New Deal prolonged

Continued on page 15

In This Issue



Debating campaign finance, p. 6

Boaz on history	2
School choice conference	3
Recent events	4
Educational Freedom and Urban America	8
New Social Security studies	12
Is there a coffee crisis?	12
Avoiding Korean War II	13
Upcoming events	13
Socialism goes high-tech	14
Libertarian ideas on the air	18
Wedding bells	19
To be governed . . .	20

The Importance of History



Why so much interest in history at the Cato Institute? The lead article in this publication examines whether Franklin Roosevelt's New Deal got America out of the Great Depression. A few issues back, Michael Chapman looked at FDR's cousin Theodore and declared him "no friend of the Constitution." Recently Cato has hosted authors Anne Applebaum talking about the Gulag and Thomas Fleming discussing Woodrow Wilson and World War I.

Why all this history? Why not just stick to current policy issues? There are three reasons.

First, we study topics such as the Gulag for the same reason that there's a Holocaust Memorial Museum on the Mall in Washington: to remind ourselves, Never again. Never again must such things happen. (Though Applebaum writes, sadly, "This book was not written 'so that it will not happen again,' as the cliché would have it. This book was written because it almost certainly will happen again.")

Second, as the American Founders understood, the study of history is our best guide to the present and the future. In his great "liberty or death" speech, Patrick Henry proclaimed: "I have but one lamp by which my feet are guided, and that is the lamp of experience. I know of no way of judging the future but by the past." The authors of the *Federalist Papers* wrote of history as "the oracle of truth" and "the least fallible guide of human opinions." The American revolutionaries were close students of the ancient republics and the history of England. They traced their own demands to the "ancient and undoubted rights of Englishmen" and beyond that to the common law, Magna Carta, and the popular assemblies of the early English peoples. The first publication of the Declaration of Independence in book form in 1776 combined the document with lengthy excerpts from the influential *Historical Essay on the English Constitution*. As historian H. Trevor Colbourn wrote, "The history made by the American Revolutionaries was in part the product of the history they read."

The Founders understood that freedom is best defended when a philosophical claim is supported by a historical claim. From their study of history they learned of the ancient rights of Englishmen, the importance of individual virtue in preserving freedom, and the dangers of power and thus the necessity of constraining and dividing it. Consider Hamilton's warning in *Federalist 75* about the powers of the president in foreign affairs, a warning of particular relevance today: "The history of human conduct does not warrant that exalted opinion of human virtue which would make it wise in a nation to commit interests of so delicate and momentous a kind,

as those which concern its intercourse with the rest of the world, to the sole disposal of a magistrate created and circumstanced as would be a President of the United States." (I copied that text from www.speaker.house.gov, where it is accompanied by a picture of Speaker Dennis Hastert; I hope he has read the essay.)

History helps us to understand the development of our civilization, including the ideas that shape it. Often the ideas that we now regard as universal principles arose in response to particular circumstances. Magna Carta and similar medieval charters reflect the struggle to constrain the power of kings. From such guarantees of specific liberties, eventually liberty developed. The rights guaranteed in the Bill of Rights reflected particular historical experiences: with religious wars, censorship, confiscation of property, the Star Chamber, and the constant tendency of government to seek more power.

Third, people get much of their understanding of government and policy from history. The way we view the Constitution, the industrial revolution, the robber barons, the New Deal, and other historical events shapes our view of the present. Far too often these days our public institutions such as schools and universities

fail to give students a proper appreciation for the great achievement of the Founders in creating a society in which government is constrained by law. Instead, we get revisionist accounts of Washington and Jefferson and hagiographic treatment of the Roosevelts, all of it accompanied by calls for more power to be entrusted to Washington.

American students need to learn about the greatness of America. But that requires an understanding of what makes a nation great. Is America great because we put a man on the moon or defeated Saddam Hussein? Or is America

great because it's the country that has offered more freedom to more people to pursue their own happiness than any other nation on earth?

Some people think that a great nation must be governed by great men wielding great power. History suggests otherwise. Right after he wrote, "Power tends to corrupt and absolute power corrupts absolutely," the historian Lord Acton went on to say, "Great men are almost always bad men." And great men with great powers are no substitute for our Constitution. The truly great men are the ones who have fought for liberty, who have walked away from power, who have helped to bring power under the rule of law. Limited government is a great achievement, a recent achievement in the sweep of history, and history teaches us that it can be lost. Appreciating where it came from and how rare and fragile it is will help us to preserve it.

“The truly great men are the ones who have fought for liberty, who have walked away from power.”

—David Boaz

Speakers assess urban education half a century after *Brown v. Board*

Inner Cities Need School Choice

Politicians can afford to be ambivalent about school choice. Many live in affluent neighborhoods where the public schools are relatively good. Those who don't can usually afford to ship their children off to prestigious private academies—and often they do just that. For low-income parents whose children are trapped in failing inner-city schools, however, the issue of educational freedom is not merely academic. On May 15, the Cato Institute's Center for Educational Freedom spon-

sored a daylong conference, "Educational Freedom and Urban America: *Brown v. Board* after Half a Century," to examine the promise of school choice for urban families.

Former Milwaukee school superintendent Howard Fuller, founder of the Black Alliance for Educational Options, opened the conference with a rousing keynote speech in which he cast the fight for school choice in all its forms as a struggle for social justice. Blasting as hypocrites those who oppose choice while keeping their own children out of public schools, Fuller noted that "there's nothing new about choice. People with money in America have always had choice." Fully equal participation in American democracy, he argued, requires that all parents have the power over their children's education that comes only with choice. Fuller also stressed that people who worry that vouchers and other forms of choice will harm "public education" have conflated the established system of government schools with its purpose: the provision of education to the public.

The luncheon address was given by pastor and former congressman Rev. Floyd Flake (D-N.Y.). Flake confirmed his sup-



At Cato's conference on urban education and school choice, Barbara Mickens describes the frustration she felt as a Washington, D.C., parent until the Washington Scholarship Fund enabled her children to attend private school.

port for vouchers but also argued that in the near term it is necessary to look at ways to improve the state-run system. He directed heavy criticism at the special education system, which he said has too often been used as a dumping ground for children that schools simply fail to educate.

Continued on page 11



Cato analyst Casey Lartigue and Phyllis Berry Myers, president of the Center for New Black Leadership, were among the speakers at "Educational Freedom and Urban America" on May 15.

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Capitol Hill forums on Medicare, the Patriot Act, Iraq war, and privatization

World Poverty Falling Dramatically

◆**April 2:** The Declaration of Independence is justly celebrated as an inspiring rhetorical work and a historical document of the first importance. Less appreciated, however, is its role as a lens through which the supreme law of the land, as articulated in the Constitution, has been interpreted. Scott Douglas Gerber, editor of *The Declaration of Independence: Origins and Impact*, strove to remedy that deficiency at a Cato Book Forum, “**The Legal Significance of the Declaration of Independence.**” Gerber surveyed the Declaration’s influence on Abraham Lincoln and the jurisprudence of Clarence Thomas and explained how even the apparently strictly structural or formal features of the Constitution’s vision of government



have been seen as inextricably linked to the natural law embodied in the Declaration. Cato’s vice president for legal affairs Roger Pilon elaborated on the moral ideas that informed the Declaration and contrasted a jurisprudence grounded in natural law with the doctrine of a “living constitution.”

◆**April 3:** The last two decades, during which global trade and interconnectedness have grown at an astonishing rate, have seen an equally dramatic decline in global poverty. Yet even the encouraging statistics gathered by the World Bank may understate the extent of the gains made by the world’s poor. Former World Bank economist Surjit S. Bhalla explained why at a Cato Book Forum on his book *Imagine There’s No Country: Poverty, Inequality, and Growth in the Era of Globalization*. Bhalla used national accounts data to supplement and correct the notoriously inaccurate survey data used by the bank and found that poverty had fallen precipitously, from 44 percent in 1980 to 13 percent at the end of 2002. The United Nations’ goal of reducing the world poverty rate to 15 percent by 2015, Bhalla concluded, has already been met and exceeded. He also noted that while global inequality trends are less encouraging if one compares countries, weighing China and Madagascar equally despite the vast difference in their populations, similarly impressive reductions in inequality appear when individuals are compared instead. Brookings Institution vice president Carol Graham sup-

plemented Bhalla’s remarks with findings from some of her own research.

◆**April 10:** Since the terrorist attacks of September 11, 2001, Samuel Huntington’s phrase “the clash of civilizations” has leapt from the lips of many pundits. But do we really face an irreconcilable conflict between the respective cultures of Islam and the West? Pakistani physicist Pervez Hoodbhoy, author of *Islam and Science: Religious Orthodoxy and the Battle for Rationality*, examined the roots of terrorism at a Cato Forum that asked, “**Is Islam Inherently Anti-American?**” He concluded that the conflict has more to do with foreign policy than with religion or civilization. Hoodbhoy criticized the tendency of Arab rulers to use the United States as a scapegoat but had equally harsh words for shortsighted American policies that had hastened the fall of secular Arab rulers and brought together “the finest of fanatics from around the globe” in Afghanistan to fight the Soviet Union.

◆**April 14:** Scholars looked at the problems with the so-called Patriot Act at the Cato Hill Briefing, “**What’s Up with the Patriot Act? Concerns about the Legislative Response to 9/11 and the Prospect of a Patriot II.**” Timothy Lynch, director of Cato’s Project on Criminal Justice, offered a framework for thinking about security policy and warned against the assumption that more security always requires the sacrifice of freedom. Often, he suggested, intelligence agencies do not need new powers; they need to use their existing powers more wisely. Jim Dempsey of the Center for Democracy and Technology sketched the legislative history of the Patriot Act and described some of its more disturbing provisions. New powers granted to law enforcement agencies—powers typically not limited to investigations of terrorism—include the ability to search a house without notifying the owner, to collect information about Web browsing and e-mail without evidence of wrongdoing, to obtain authorization for “roving wiretaps” without specifying either the person or the location to be monitored, and to compel businesses to disclose records without meaningful judicial oversight.



Raghuram Rajan discusses the need for free financial markets in the developing world at an April 24 Book Forum. (top)

David Boaz welcomes Rep. Jim DeMint (R-S.C.) and Sen. Lindsey Graham (R-S.C.) to a Capitol Hill dinner on April 8 at which José Piñera discussed Social Security reform with more than a dozen members of Congress.

◆ **April 15:** The Second Amendment is not an especially cryptic bit of text. One can debate precisely what sort of weapons are covered by “the right to keep and bear Arms,” but if it means anything, it must surely mean that peaceful citizens can keep handguns in their own homes for self-defense. Surely—unless you live in Washington, D.C., where even this most basic exercise of Second Amendment rights is illegal. At the Cato Hill Briefing, “**You Can Fight City Hall: Ending the District of Columbia’s Gun Ban,**” legal scholars Gene Healy and Robert Levy discussed an independent lawsuit they have filed on behalf of six District of Columbia residents who seek to overturn the status quo. Levy outlined the history of the Second Amendment and the precedents that have grown up around it, and Healy focused more narrowly on the case at hand, explaining the legal strategy they planned to pursue. Attorney Alan Gura, lead counsel in the case, was on hand to take part in the question and answer period.

◆ **April 16:** American legend Buzz Aldrin, who made history as one of the first men to walk on the moon in 1969, shared his vision of the future of space technology with the audience at a Cato Book Forum on the collection *Space: The Free-Market Frontier*, to which Aldrin contributed an essay. Courtney Stadd, chief of staff at the National Aeronautics and Space Administration, spoke on the state of his agency. The book’s editor Edward L. Hudgins and James Muncy of PoliSpace outlined the exciting possibilities opened up by a shift from the view of space as a government program to one of space as one more frontier to be explored and developed by private enterprise.

◆ **April 22:** Few institutions shape modern life as powerfully as the business firm. At a Cato Book Forum, *Economist* reporter Adrian Wooldridge, coauthor of *The Company: A Short History of a Revolutionary Idea*, presented a compressed history of the corporation. Wooldridge detailed how the original free-market advocates, classical liberals such as Adam Smith and A. V. Dicey, denounced the chartered joint stock company as a creature of the state. He also highlighted transformations in the corporate

Astronaut Buzz Aldrin highlights a Cato Book Forum on April 16 for *Space: The Free-Market Frontier*, to which Aldrin contributed a chapter.



Jacob Sullum, author of *Saying Yes: In Defense of Drug Use*, and Sally Satel, author of *P.C., M.D.*, offer different perspectives on drug use and abuse at a May 29 Book Forum.

Cato defense scholars Charles Peña and Chris Preble advocate a quick exit from the Persian Gulf at a May 2 Hill Briefing.



form, describing the transition from the industrial giants of early 20th century to the dynamic companies familiar today, merging and fragmenting with dizzying rapidity. Daniel Yergin, coauthor of *The Commanding Heights*, provided a dual perspective on the book as both a founder of a company and a writer on global markets.

◆ **April 23:** During his campaign, George W. Bush talked about “transforming” the armed forces and “skipping a generation” of military technology, but is there any evidence that those things are happening? Two

panels of experts took up that question at a half-day Cato Institute Conference, “**Defense Transformation: Moving Forward or Stuck in the Past?**” On the first panel, which examined post-Cold War military spending, Baker Spring of the Heritage Foundation defended continued high spending, arguing that it generated “indirect economic benefits” and stressing that social entitlements were the faster growing part of the budget. Less sanguine about current spending trends were Chris Hellman of the Center for Defense Information,

Continued on page 6

EVENTS *Continued from page 5*

Steven Kosiak of the Center for Strategic and Budgetary Assessments, and Cato's Charles Peña, each of whom noted that, despite all the talk of transformation, the only old system to actually be mothballed was the Crusader artillery system. Peña calculated that if the military restructured its forces and scrapped antiquated commitments, it could fulfill its functions with \$200 billion, or half its projected budget. Daniel Goure of the Lexington Institute and Dave McIntyre of the ANSER Institute for Homeland Security opened the panel on transformation's progress with the assertion that it was moving along at an acceptable pace. Former Cato military analyst Ivan Eland acknowledged some progress but argued that progress was blocked by an "iron triangle" formed by the military establishment, legislators, and defense contractors. Michael Vlahos of Johns Hopkins University's Applied Physics Laboratory took a different approach, analyzing defense transformation as a rhetorical tool, part of the propagandistic narrative of American dominance.

◆**April 24:** International financial markets are undoubtedly the least well understood and the most maligned part of global capitalism. Indonesian leader Mahathir Mohamad famously blamed his country's economic

troubles in the late 1990s on a conspiracy of ruthless financiers, and a cottage industry in criticism of the supposed "Washington consensus" on market openness has sprung up. At a Cato Book Forum, University of Chicago finance professor Raghuram G. Rajan, coauthor of *Saving Capitalism from the Capitalists: Unleashing the Power of Financial Markets to Create Wealth and Spread Opportunity*, made the case for the invaluable role of those markets in providing a "Goldilocks government, a government that's just right," which is to say, a government active enough to provide a stable framework for markets without squelching them with burdensome regulation. When capital markets are global, he observed, local elites who were previously concerned with using state power to capture domestic markets instead pressure governments to institute reforms that will allow them to compete internationally. The International Monetary Fund's Kenneth Rogoff and Cato's Brink Lindsey both praised the book, though Lindsey questioned the inclusion of antitrust policy in the conception of a "just right" government, warning that a "bigness is badness" mentality could frustrate development.

◆**April 25:** Social Security's long-term fiscal trouble has been much discussed, but far less attention has been paid to the ballooning share of GDP absorbed by the *other* major federal program for the elderly—Medicare. At a briefing on Capitol Hill, "Will Medicare Ever Graduate from Reform School?" Cato director of health policy studies Tom Miller looked at the structural problems with the status quo and the reasons why the "market in name only" reforms that have been proposed will fail to remedy them. Miller outlined his ideal reform—transition to a truly market-based, defined-contribution system—as well as several politically more likely reform scenarios.

◆**May 2:** At a Cato Hill Briefing, "After Victory: A Strategy for Exiting the Persian Gulf," Charles Peña documented the competing points of view within the Bush administration on the merits of democracy in Iraq. Peña warned that skeptics in the region and around the world are likely to question American motives if U.S. actions are seen

as stifling Iraqi self-government. Christopher Preble, Cato's director of foreign policy studies, followed with a discussion of U.S. troop deployments in Iraq and the Middle East. The collapse of the Hussein regime, Preble showed, provides a golden opportunity for a substantial reduction of the U.S. military presence that has cost American taxpayers hundreds of billions of dollars over the past decade.

◆**May 7:** At a Book Forum, *The Real Environmental Crisis: Why Poverty, Not Affluence, Is the Environment's Number One Enemy*, author Jack M. Hollander, professor emeritus of energy and resources at the University of California, argued that poverty-related environmental problems dwarf those that obsess most of the environmental community. Alleviating poverty would accordingly do more to improve environmental quality than would enactment of the various national and international policy agendas of the environmentalist establishment. Moreover, those broader Green agendas are generally counterproductive in that they make more difficult the process of wealth creation in the Third World that is so vital to achieving environmental improvement.

◆**May 8:** Minneapolis talk radio personality Jason Lewis, "Minnesota's Mr. Right," was the luncheon speaker at a *Cato Policy Perspectives 2003* seminar in Minneapolis. Clint Bolick, author of *Voucher Wars*, keynoteed, and Tom Palmer and Jerry Taylor discussed Cato's work.

◆**May 12:** A few days after the special three-judge panel of the U.S. District Court of the District of Columbia handed down its long-awaited opinion in the McCain-Feingold case, Cato's Center for Constitutional Studies and the Federalist Society sponsored a Policy Forum, "The Campaign Finance Decision: What Does It Mean and Where Do We Go from Here?" on the startling 1,600 page decision—the product of a divided court and confusing, multiple opinions. James L. Swanson, editor in chief of the *Cato Supreme Court Review*, criticized the court for failing to affirm Madisonian first principles of limited government and noted



Cato Sponsor Joe Lund welcomes Tom Palmer to Minneapolis for a seminar featuring talk show host Jason Lewis and *Voucher Wars* author Clint Bolick.

principles of limited government and noted that the First Amendment is not a policy option but an imperative. Kenneth W. Starr and Jan W. Baran, who, as counsel for Sen. Mitch McConnell, challenged this regime of speech regulation, discussed the main holdings of the decision, its impact on soft money and issue ads, and what the Supreme Court might do. Randolph D. Moss and Trevor Potter, counsel to the congressional sponsors of the legislation, defended the law as a reasonable regulation of political speech that would give citizens confidence in democracy and diminish corruption. The Supreme Court will hear the case on September 8.

◆ **May 15:** An all-day conference, “*Educational Freedom and Urban America: Brown v. Board after Half a Century*,” looked at education in America’s cities as we approach the 50th anniversary of the *Brown v. Board of Education* decision. Speakers included former representative Floyd Flake (D-N.Y.), former Milwaukee school superintendent Howard Fuller, Paul Peterson of Harvard’s Program on Education Policy and Governance, Andrew Coulson of the Mackinac Center, Emily Feistritz of the National Center for Education Information, and Cato education analysts David Salisbury and Casey Lartigue.

◆ **May 16:** The Bush administration is pursuing a number of reforms to overhaul the federal bureaucracy. At a Cato Hill Briefing, “**Government Reform: Competitive Sourcing, Privatization, and Other Options**,” the leader of the White House’s competitive outsourcing initiative, Angela Styles, discussed past progress and future plans to allow private contractors to bid for up to one-quarter of all federal work. Styles was optimistic that these efforts to accelerate contracting would provide Americans with a government that costs less and provides better services. The Reason Foundation’s Geoffrey Segal argued that broader privatization is needed to move commercial activities fully into the private sector. Cato’s Chris Edwards argued that many functions, such as postal services and air traffic control, should be privatized to reduce taxpayer costs and improve efficiency. He also argued that the coming entitlement spending crisis

An overflow crowd of diplomats and scholars turned out to hear French economist Pierre Garelo discuss the roots of French anti-Americanism at a roundtable luncheon on April 28.



Cato chairman William Niskanen watches as Brooke Oberwetter prepares to drive in the tying run to help the Cato Running Dogs defeat the Heritage Foundation in softball on June 18.

should make widespread program termination a top priority for the administration and Congress.

◆ **May 21:** At a Policy Forum, “**Ashcroft’s U-Turn: Suing Big Tobacco for a Quarter Trillion Bucks**,” Cato’s Robert Levy argued that the Justice Department’s case against the tobacco industry is baseless—driven by politics, not law. Matthew Myers of the Campaign for Tobacco-Free Kids insisted that the lawsuit is a necessary remedy for the industry’s fraudulent and dangerous marketing practices. Attorneys Kenneth Bass, representing the industry, and William B. Schultz, supporting the government, debated whether cigarette companies have behaved in a manner that would justify the use of RICO, an act originally designed as a weapon against organized crime.

◆ **May 27:** At a Policy Forum, “**Public Health and Private Rights: Communicable Diseases, Panic Attacks, and the Constitution**,” three scholars discussed new challenges to public health protection. Lawrence O. Gostin of Georgetown University Law Center and Johns Hopkins University, the principal author of the controversial Model Emer-

gency Health Powers Act, argued that state public health laws are antiquated and that state officials need additional powers to effectively deal with infectious diseases. George J. Annas of the Boston University School of Public Health said preparedness was vital but maintained that mass quarantines are doomed to fail because even communist dictatorships cannot enforce them effectively. Jonathan Turley of George Washington University Law School argued that existing laws provide the government with ample authority to deal with health-related emergencies. According to Turley, the proposals that would confer additional powers on the government represent a serious threat to civil liberties.

◆ **May 29:** At a Book Forum, *Saying Yes: In Defense of Drug Use*, Jacob Sullum of *Reason* magazine displayed more than a century’s worth of anti-drug propaganda related to tobacco, alcohol, marijuana, and other drugs and argued that most drug users use drugs responsibly. Sally Satel, a senior fellow at the American Enterprise Institute who also has a psychiatric practice focusing on drug treatment, argued that Sullum underestimated the social costs of

Educational Freedom and Urban America

On May 15 the Cato Institute's Center for Educational Freedom held a conference titled "Educational Freedom and Urban America: Brown v. Board after Half a Century." Among the speakers were Howard Fuller, director of the Institute for the Transformation of Learning at Marquette University, former superintendent of the Milwaukee Public Schools, and founder of the Black Alliance for Educational Options; Casey Lartigue, a Cato policy analyst; and Andrew Coulson, author of *Market Education: The Unknown History*. Excerpts from their remarks follow.

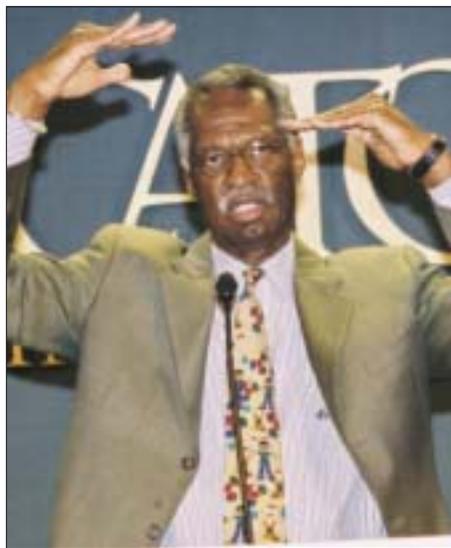
Howard Fuller: We black Americans are at a strange point in our history. Because of the gains made in the 1960s, 1970s, and 1980s—and some in the 1990s—more opportunities have opened up for us. DuBois's talented tenth has never been more in evidence. We have black people at all levels of the political structure of this country. We have black millionaires. We influence the cultural direction of this country with our music and the way we dress. We have young men making millions of dollars for bouncing a ball, or hitting a ball, or tackling somebody who's got a ball—and then getting millions more hawking T-shirts and sweat-shirts and athletic shoes. And we've got young men killing each other for those shoes.

There's a dichotomy between black folks who've made it and the masses of our people who know another kind of reality. When I travel around this country and see what is happening to our children, I know that far too many of them are dying physically and mentally. It's clear to me that we've got to have a multifaceted strategy to save our children. And all of us who are honest know that education alone cannot do it. But what's equally clear is that education will be the cornerstone of any broad strategy that we develop and pursue.

In many areas of this country, the District of Columbia being one, poor African-American children are being precluded from being effective participants in our democracy because we are failing to educate them. Too many of our children are being told, even in 2003, that "my check is gonna come whether you learn or not."

I believe that Mortimer Adler was right when he said that there are no unteachable children; there are adults who have not figured out how to teach them. Too many of our children are being forced to stay in schools that do not work for them and, frankly, didn't work for their parents. They and their families lack the power to influence the educational institutions that continue to not serve them well.

Our mission at the Black Alliance for Educational Options is to actively support parental choice, empower families, and increase educational options for black children. We support means-tested vouchers, homeschooling, charter schools, contract schools, black independent schools, and



Howard Fuller: "We have to ask why people do not want low-income parents to have choice. The hypocrisy on this is phenomenal."

other public and private choices. We do not support the destruction of public education. One of the reasons that people continue to run that bogus line is that they do not make a distinction between public education, which is a concept, and the system that *delivers* public education. The *system that delivers* public education, as we've structured it in America, is not public education. Public education is the concept that it is in our interest to educate all our children. What makes public education public is that it serves the public's interests. Is it available to everyone? Is it something we

can all access? I would humbly argue that a school district that continues to push children out, that continues for whatever reason to be unable to teach our children to read and write, that graduates children who can't read and write is not in the public's interest. What we therefore have to do is to commit to a *purpose*, not institutional arrangements.

You can have a lot of different delivery systems; that's clear in higher education. People have no problem with students taking Pell Grants to religious or nonreligious schools. All you hear is, "Give me my Pell Grant." People have no problems with G.I. Bill money being taken public or private. Nobody said that was destroying public education.

Say that you have on the corner a school that everybody knows has never educated anybody's kids, but it's a "public" school. You've got another school four blocks away that is able, for whatever reason, to educate the children that can't be educated in the other one, but that school is, oh my God, a religious school. I would argue that it is in the *public's interest* to put the children where they can be educated.

There was a time when it was "progressive" to fight the bureaucracy. There was a time when some of us carried signs that said, "Power to the people." What is interesting is that some of the folks who used to rail against the bureaucracy now *are* the bureaucracy. The discussion is no longer about empowering the people to fight the bureaucracy. Now we're supposed to believe that magically, because they're now in charge, the people's interests are going to be met. I believe the people's interests are going to be met only when the people are empowered to fight for their interests.

We have to ask why people do not want low-income parents to have choice. The hypocrisy on this is phenomenal. We have teachers teaching in schools that they would never put their own children in and then demanding that somebody else's children stay there. We have public school teachers putting their own children in private schools. We have leaders in Congress pontificating. But *where's your child?* The argument always comes down to: "If we let these poor par-

“Too many of our children are being told, even in 2003, that ‘my check is gonna come whether you learn or not.’”

ents out, it will destroy the system.” I have a question: is it about the system, or is it about the parents and the children?

Over the last 14 years, I’ve heard all of the objections. One that I find interesting is that we don’t know about choice because it’s new. There’s nothing new about choice. People with money in America have always had choice. If you have money and the public schools do not work for your children, you’re going to do one of two things. You’re going to move to a community where the public schools do work, or you’re going to put your kids in a private school.

I understand that our position is controversial. But social change is always controversial. It transfers power to people who never had it and takes power from others who’ve had it. How can that not be controversial? But you know what? We think it is the right thing to do, and we are willing to fight forever on this point. We understand that the race goes, not to the swift, but to those who can endure until the end.

Casey Lartigue: Last December I published a paper about schools in the District of Columbia. I tried to track what’s going on with the system because it seemed strange that there was so much resistance to trying something different with a system that has so much trouble—so many kids dropping out and performing at such low levels. Now, I think you could say we’ve got, to quote President Bush, a “coalition of the willing,” with the school board president as well as the mayor coming out and saying that they would like to try something different, and choice is on the table.

In my paper, which will appear in a book next year, I start out with a very simple question: how much is being spent on D.C. public schools? The Census Bureau says the amount spent per student is \$15,122, all costs included. The lowest figure, \$8,500, comes from Parents United for D.C. Public Schools. In between those two figures are the National Education Association that says it’s \$13,500 per student and the U.S. Department of Education that says it’s \$11,000 per student. The Census Bureau has a different report that says that it’s actually \$10,800 for “operating costs.” Then if you ask the D.C. public schools them-

selves, they say that it’s \$10,477 per student. There’s so little agreement about the amount spent that I don’t think anyone, including people in the system, can tell you how much is really being spent.

Per pupil spending is interesting, but in the end the issue comes down to what the kids are learning. If you send someone to the store to buy something, you’re interested in both how much you spend and what the person brings you. It’s the same thing in education. We’re spending all this money; do we have kids staying in these schools for a decade or more and coming back with an education? So I took a look at the outputs of the system. I looked at SAT scores, the Stanford 9 scores, and a



Casey Lartigue: “We’re spending all this money; do we have kids staying in these schools for a decade or more and coming back with an education?”

review of the worst performing schools. People who cite scores are criticized by other people who say that the reason scores have declined is that the number of test takers has increased. So I decided to look beyond just the last two years. It turns out that sometimes the scores go down when the number of test takers increases, and sometimes they go up when the number of test takers increases. If you have a broader scope, you can see that there is no real pattern to this. Some people have been saying that the loss of students to charter schools explains the drop in test scores

within the last two years. But then they make the contradictory claim that scores have declined because charter school students are not doing very well. I don’t know which claim is true, but it seems that those people somehow find a way to hold both of those thoughts in their heads at the same time. Just so you know, last year in D.C. the average SAT score was 796 without charter schools; it was 799 with charter schools.

In addition to looking at scores across the school system, I’m also trying to look at education in different parts of the city. D.C. is both a highly educated city and a city with people who can hardly read. It has the highest percentage of residents with a college diploma—39 percent—and yet 37 percent of the residents in the city read at the 3rd grade level or below, so there’s a very serious gap. In Ward 3, which has the highest income in the city, 79 percent of the residents have a college degree. They are 10 times more likely to have a college diploma than someone who lives in Ward 8, the poorest ward. So we can guess which part of the city would benefit the most if there were some kind of choice.

Andrew Coulson: I’d like to start by addressing a point that came up earlier. Someone said that there are only so many private school seats available; maybe it’s 1,200 or something like that in D.C., so a voucher program would give us 1,200 extra children enrolled in private schools and that’s it. That’s not the way markets work in general, and it’s not the way markets work in education. In Chile they introduced something very much like a school voucher program in 1982, and at that time about 20 percent of students were enrolled in private schools. Over the next 10 years the percentage went to about 40 percent, and now it stands around 45 percent. So nearly half of all students in Chile are now enrolled in private schools as a result of subsidization, and the rate of enrollment is continuing to grow. In Zanzibar, an archipelago off Tanzania where there’s not a lot of disposable income, there was incredible growth in private schooling, at the primary level in particular, between 1994 and 1999.

Continued on page 10

“If we pass something that’s called ‘school choice’ and it doesn’t work, we’ll destroy the futures of a lot of children. We have to care about the details.”

POLICY FORUM *Continued from page 9*

Up until 1994, private primary education was illegal in Tanzania. Since it was legalized, it’s been growing at a rate of 51.6 percent per year. So the number of children enrolled in private schools in Zanzibar is doubling every two years. Lack of places in private schools is not an issue at all.

Something I’d like to talk about in light of the discussion today is the potential for a Pyrrhic victory by the school choice movement. All of us in this room are in favor of school choice in one form or another, and we’ve been spending a lot of time trying to make choice available to more families. We’re actually getting close to succeeding now: school choice laws are being passed; one was passed in Colorado recently, and the winds are changing in D.C.

But what if we pass a school choice program just to pass a school choice program and it doesn’t work? That’s a very real possibility; we could have a Pyrrhic victory on our hands and do a disservice, not merely to the children who would immediately be going to those schools, but to children for decades to come. If we pass something that’s called “school choice” and it doesn’t work, we’ll destroy the futures of a lot of children. We have to care about the details. It’s not enough to just say “school choice”; we have to talk about the policy details.

You can’t look at a variety of different large-scale school choice programs in the United States. There isn’t a single state, there isn’t even a single city, where the majority of parents have ready access to a competitive education marketplace. Tuition vouchers and tax credits help a tiny fraction of students. Even charter schools serve only about 1.5 percent of students nationwide. So you have to look outside the modern United States if you want to compare large-scale choice programs with government school systems. In the late 1990s I did just that by looking at historical cases: I looked at ancient Greek schools, medieval Islamic schools, and schools on up through the Enlightenment and the 19th century in England, the United States, and Canada.

I found that systems that had five particular features tended to outperform ones

that didn’t have all five of these features. The features were *choice* and some direct *financial responsibility* for parents and *freedom, competition,* and the *profit motive* for schools. Now, that’s a very controversial finding, and before jumping ahead and making policy it’s a good idea to test it in some way. I have been trying to do that by seeing if evidence from the developing world gives rise to the same findings. The interesting thing about the developing world—countries like India, Pakistan, Chile, Indonesia, and Colombia—is that private schooling makes up a much larger segment of the marketplace than it does in the developed world. There’s also a lot more variation in



Andrew Coulson: “Systems that had five features tended to outperform ones that didn’t have all five. The features were choice and some direct financial responsibility for parents and freedom, competition, and the profit motive for schools.”

what it means to be a private school in those countries—or what it means to be a public school, for that matter. Sometimes private schools are totally fee charging, sometimes they’re partially subsidized, and still other times they’re fully subsidized by the state and heavily regulated. Public schools sometimes charge fees, and their level of autonomy varies greatly, not only from country to country, but even within a country.

Evidence from the developing world suggests a pattern that’s similar, but not exactly identical, to the one that emerges from the historical evidence. If you try to

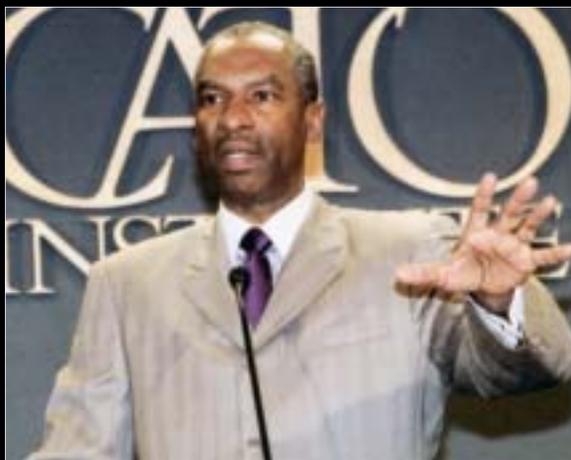
isolate the five most important factors in the effectiveness of the best school systems in the developing world, you find that schools should be minimally regulated, privately owned, forced to compete to attract students, freely chosen by parents, and at least partially paid for by parents. Schools with those characteristics show superior academic achievement, higher efficiency, improved facilities maintenance and school atmosphere, greater responsiveness to parental demand, and faster enrollment growth. Enrollment growth is a huge issue in the developing world because so many children still have no access to schooling at all.

The most important similarity between the findings from the developing world and the findings from the historical evidence is that having parents pay directly some of the cost of their children’s education is crucial. It makes all the difference in the world if schools are at least partially paid for by parents instead of being fully funded by the state. That presents us with a problem. Obviously, we want to ensure universal access to schools regardless of family income. How do we reconcile that with the need for some parental copayment? Fortunately, some of the evidence from the developing world is pretty detailed.

There’s a fantastic study of some 68,000 schools in Indonesia, where there’s huge variation in how much of any given school’s funding comes from the central government and how much comes from parents. It varies not only within the private sector but also within the public sector. The biggest change in the efficiency of a school comes when parents go from paying nothing toward the cost of that school’s operation to paying something. As parents pay more of the total cost, the efficiency of the school goes up, but the rate of the increase gets smaller. So programs in which parents make some small copayment toward the cost of their children’s education do better than programs that make education free and universal.

What policies could we adopt in urban America and America at large to bring the benefits of competitive market systems to all children? If we expand the scope of

Continued on page 17



Speakers at the conference “Educational Freedom and Urban America” included Cesar Chavez Public Charter High School principal Irasema Salcido; Rev. Floyd Flake, former member of Congress and senior pastor of

New York’s Allen African Methodist Episcopal Church; and Paul E. Peterson, director of the Program on Education Policy and Governance at Harvard University.

CATO CONFERENCE *Continued from page 3*

Flake also argued that many educational problems had their origins in the breakdown of family structures and suggested that real academic progress would require greater engagement of parents in the educational process.

The first of the day’s three panel discussions focused on problems with the current quasi-monopoly of government schools. Cato analyst Casey Lartigue cited statistics from the Washington, D.C., public school system, outlining a long history of underperformance, despite relatively high per pupil expenditures. Lawrence Patrick III, president of the Black Alliance for Educational Options, attributed the great disparities in public school quality to the legacy of racist laws that had been explicitly intended to deny African Americans access to education, arguing that choice could help to undo the effects of past discrimination. A slightly different perspective was provided by National Center for Education Information president C. Emily Feistritz, who discussed choice, not between schools, but between alternative forms of teacher certification.

A counterpoint to the grim portrait

painted by the first panel was provided by the second, which examined several islands of success in the ocean of urban school failure. Drawing on findings from his own extensive research, Paul E. Peterson of Harvard University’s Program on Education Policy and Governance reported that private schools spend far less of their budgets on administrative overhead, have much lower levels of violence and drug activity, communicate more with parents, and show greater success at closing gaps in test scores between white and black students. Parent Barbara Mickens, whose children attend parochial school through the Washington Scholarship Fund, gave a more personal account; she described the frustration she felt as she watched her children fall behind in the public system. Principal Irasema Salcido of the Cesar Chavez Public Charter High School for Public Policy recounted the challenges she has faced in creating a culture of achievement at her unique institution.

The conference closed with a look to the future of choice and urban education. David Bositis of the Joint Center for Political and Economic Studies examined public attitudes

toward school choice and the problems of political coalition building that stand in the way of reform. Andrew Coulson, author of *Market Education: The Unknown History*, extracted lessons from his survey of competitive education markets in the developing world, suggesting that some parental copayment was a key feature of successful school choice programs. His analysis dovetailed with that of American Enterprise Institute scholar Frederick Hess, who touted the value of what he provocatively termed “mean choice.” Reformers have thus far attempted to assuage the fears of opponents by offering vouchers as a supplement to government schools, Hess said, but he argued that true competition means that government schools that fail to adapt must ultimately be shut down. Cato’s David Salisbury noted that, while examples of robust and widespread choice-based reform were hard to come by in the United States, reforms based on greater regulation or increased funding were abject failures.

The full conference can be viewed online at www.cato.org/events/urbaned. A book of conference papers will be published in May 2004, the 50th anniversary of the *Brown v. Board of Education* decision. ■

Is welfare reform a success?

Drug Critics Threaten Medical Progress

According to populist politicians, pharmaceutical companies are the modern equivalent of the mustache-twirling villain of silent film fame, cackling as he makes a tidy profit from the suffering of the poor. Cato scholar Doug Bandow provides a rare defense of the much-reviled drug manufacturers in “Demonizing Drugmakers: The Political Assault on the Pharmaceutical Industry”



Doug Bandow

(Policy Analysis no. 475). High drug prices, he writes, are commensurate with the high costs of research and development—and of compliance with the burdensome and time-consuming Food and Drug Administration approval process. The enormous benefits provided by new drugs developed in recent decades, argues Bandow, were made possible by inherently risky research investments that require the lure of significant profits. Instead of undermining that vital incentive through price controls, Bandow advises a combination of private charity for both foreign and domestic patients and the creation of a drug benefit as part of comprehensive Medicare reform that would move the system to a defined-contribution model.

◆ Social Security: It's Even Worse Than You Thought

In March the Social Security trustees released their yearly report on the health of the system. Social Security analyst Andrew Biggs, who has since become associate commissioner for retirement policy at the Social Security Administration, examines their findings in “Failing by a Wide Margin: Methods and Findings in the 2003 Social Security Trustees Report” (Cato Briefing Paper no. 82). The small bit of “good news”—the trustees now project that the program will be insolvent in 2042 instead of 2041—is more than outweighed by the dire portrait the report paints of the longer term. As Biggs explains, this year's report is the first to look beyond the 75-year horizon to capture the full present value of the system's total expected shortfall, a whopping \$11.9 trillion. That's about

\$7 trillion more than is revealed in a 75-year analysis, a deficit that would require an increase in payroll taxes of almost 4.5 percent to cover. Biggs also looks at the trustees' stochastic analysis of different possible outcomes, which reveals a mere 2.5 percent probability that Social Security will remain solvent through 2075 in the absence of reform. The message, Biggs writes, is clear: “action is needed on Social Security, and the sooner action is taken the easier and cheaper it will be.”

◆ Have Your Pension and Eat It, Too

In the two decades during which the Cato Institute has promoted Social Security reform, the radical idea of allowing workers to decide how best to invest their own money has gone from a fringe notion to a subject of serious legislative debate. But, as Cato's Andrew Biggs notes in “Large Accounts and Small Cash Deficits: Increasing Personal Account Size within a Fiscally Responsible Social Security Reform Framework” (Social Security Paper no. 30), that heartening progress means that reformers must begin to offer detailed proposals. Those who are most eager to empower workers will want to allow a larger proportion of payroll taxes to be diverted to private accounts, and those who are primarily concerned with the system's impending insolvency may prefer smaller accounts in order to avoid running up large deficits now. Biggs finds that both types of reformers can get what they want under a modified version of one of the plans developed by the President's Commission to Strengthen Social Security.



Andrew Biggs

children into poverty. As Cato scholar Michael Tanner observes in “Welfare Reform: Less Than Meets the Eye” (Policy Analysis no. 472), neither prophecy came to pass. Reform, he notes, has indeed been a limited success: poverty and welfare rolls are down, and even former welfare recipients whose income hasn't risen in the move from welfare to work report that they're more satisfied with their lives now. But in other realms, reform has fallen short: states have done their best to undermine time limits and work requirements, out-of-wedlock birth rates remain high, and a welter of other forms of government assistance means that even those who've left welfare are far from being fully self-sufficient. Tanner concludes that we are bumping up against the limits of what can be achieved through tinkering with the welfare system. The next step, he says, must be to focus on improving economic growth and phasing out benefits that create an incentive for dependency in the first place.

◆ **Coffee Talk**

Opponents of globalization are fond of attacking companies like Starbucks as illustrations of all that's wrong with free global markets. Isn't it unjust, they ask, that Third World farmers make only pennies growing the beans for some yuppie's \$5 latte? Brink Lindsey, director of Cato's Center for Trade Policy Studies, examines that critique in “Grounds for Complaint? Understanding the ‘Coffee Crisis’” (Trade Briefing Paper no. 16). Low coffee bean prices, he concludes, are a sign, not of market failure, but of market success, primarily in the form of the increasing productivity of coffee growers. It is nonsensical, argues Lindsey, to blame coffee retailers for improvements in Brazilian agricultural methods or for the low costs of production in Vietnam, which recently emerged as a coffee-growing powerhouse. Ameri-



Michael Tanner



Brink Lindsey

◆ **The Limits of Welfare Reform**

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 was supposed to utterly transform the welfare system. Some observers held that it would break the dependency trap into which so many recipients had fallen, promoting self-sufficiency and individual initiative. Others said that it would rend the social fabric like a buzz saw, driving a million

can café patrons, meanwhile, are paying for packaging, labor, and the overhead of ambiance, not primarily for coffee beans. Attempts to counteract falling coffee bean prices through quotas or “fair trade” price inflation only distort market signals, delaying necessary adaptations in developing world agricultural sectors and thus exacerbating the problem.

◆ **Seoul Suckers**

For half a century, since the end of the Korean War, the United States has maintained a heavy troop presence in South Korea, shouldering much of the burden of defending the country from its unstable neighbor to the north. In “Bring the Troops Home: Ending the Obsolete Korean Commitment” (Policy Analysis no. 474), Cato senior fellow Doug Bandow argues that the time has come to rethink the U.S. relationship with South Korea and withdraw the 37,000 American troops stationed there. Now that the Cold War has come to an end, writes Bandow, there is no need for the United States to supplement the military of a nation with many friends in the region and enormous technological and economic superiority over North Korea. He notes that the U.S. military presence on the peninsula is not only unnecessary but a liability because it engenders anti-American sentiment.

The revelation that communist North Korea may have developed nuclear weapons makes the issue more urgent. Some pundits have since written of the need for “regime change” there, and administration officials have refused to rule out military action. In “Wrong War, Wrong Place, Wrong Time: Why Military Action Should Not Be Used to Resolve the North Korean Nuclear Crisis” (Foreign Policy Briefing no. 76), Bandow warns that the reckless use of force would gamble with the lives of millions of South Koreans as well as those of the American troops stationed in South Korea. Instead of risking a second, potentially nuclear Korean War, Bandow recommends cooperating with regional allies to contain North Korea and prevent the sale of nuclear materials by means of multilateral diplomacy backed by the threat of a blockade, with military action considered only as a last resort to prevent the transfer of nuclear arms to terrorists.

◆ **Twelve Irrelevant Men**

To prevent abuse of the criminal justice system, the Framers of the Constitution provided not only for trial by jury but also for grand juries to act as a filter on criminal indictments. But in “A Grand Façade: How the Grand Jury Was Captured by Government” (Policy Analysis no. 476), Timothy Lynch, director of Cato’s Project on Criminal Justice, and attorneys W. Thomas Dillard and Stephen R. Johnson argue that the grand jury has increasingly become an empty formality at best and, at worst, a means by which overzealous prosecutors can bypass constitutional rights. Convened behind closed doors without a judge or opposing counsel present, grand juries typically act as little more than puppets of state prosecutors, the authors write. Those prosecutors can then use the grand jury’s subpoena powers to do an end run around the Fourth Amendment requirement that warrants be obtained for police searches or the Fifth Amendment ban on compulsory examination of the accused. As first steps toward reform, the authors recommend increasing judicial review of the dissemination of subpoenaed evidence and guaranteeing grand jury witnesses the right to have a lawyer present.



Timothy Lynch

◆ **Missile Defense: Defend America**

Proponents of a missile defense system justify it as a means of protecting the United States from ballistic missile attacks by rogue states. But, as Cato’s director of defense policy studies Charles Peña observes in “Missile Defense: Defending America or Building Empire?” (Foreign Policy Briefing no. 77), rogue states lack the capability to strike the United States with such weapons and will not acquire it in the foreseeable future. The true motive for developing an ambitious missile defense system, Peña argues, is to



Charles Peña

protect forward-deployed U.S. troops around the world, enabling future interventions. Peña warns that this would, with some justification, raise concerns of American overreach, needlessly antagonizing other nations. If the United States is to develop any form of missile defense system, he writes, it should be a limited, land-based system designed exclusively to protect the homeland. ■

Cato Calendar

Constitution Day

Washington • Cato Institute
September 17, 2003

Cato City Seminar

Chicago • Ritz-Carlton
October 9, 2003

**Cato University Fall Seminar
Arguing for Liberty: How to Defend
Individual Rights and Limited Government**

Quebec City • Chateau Frontenac
October 23–26, 2003

Speakers include Tom G. Palmer, Don Boudreaux, Karol Boudreaux, Monte Solberg, Gene Healy, and Robert Sirico.

Cato City Seminar

Dallas • Four Seasons Las Colinas
October 29, 2003

Cato City Seminar

Houston • Four Seasons
October 30, 2003

Cato City Seminar

New York • Waldorf-Astoria
November 7, 2003

**The Future of the Euro
21st Annual Monetary Conference
Cosponsored with The Economist
Washington • Renaissance Hotel
November 20, 2003**

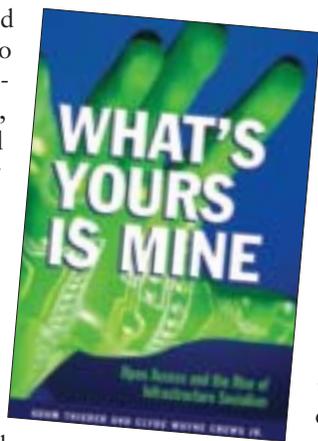
Speakers include Alan Greenspan, James M. Buchanan, Vito Tanzi, José Piñera, Anna J. Schwartz, Laurence J. Kotlikoff, and Václav Klaus.

For more information, visit www.cato.org

Infrastructure socialism moves to cyberspace

“Open Access” or Forced Access?

We’ve been told for years that the introduction of competition to many industries that are allegedly “natural monopolies” can be accomplished only by forcing those who produce valuable infrastructure (railroad tracks, telephone wires, optical cable, or even computer operating systems) to allow everyone to have access to them. Now companies such as Microsoft, Disney, and Ebay are petitioning the Federal Communications Commission to adopt rules that would guarantee them access to the wires owned by cable and telephone companies.



In *What's Yours Is Mine: Open Access and the Rise of Infrastructure Socialism*, Adam Thierer and Wayne Crews show that the effect of such requirements has been to distort incentives and transform competitive and innovative businesses into “lazy public utilities.”

They suggest that, instead of forcing investors to make the fruits of their investments open to their competitors, legislators “could eliminate artificial, government-created barriers to genuine competition like electricity franchises that outlaw competition against the incumbent.” Instead of looking for ways to eliminate politically created barriers to real competition, policymakers (unsurprisingly) have often preferred to confiscate the exclu-

sive property of investors. In addition to generating the many perverse incentives documented in *What's Yours Is Mine*, such approaches undermine the institutions of property and contract generally.

Advocates of such policies call them “open access.” Thierer and Crews suggest that the more honest term is “forced access,” and they show that forced access is a taking of property created by others. They also offer extensive case studies of electricity, telephone networks, cable television, and software. Ironically, Microsoft Corp. was the victim of demands by competitors for access to its operating system a few years before it became an advocate of “open access” to cable and phone lines.

What's Yours Is Mine is available in paperback for \$12.95. It can be purchased at bookstores, at www.catostore.org, or by calling 800-767-1241. ■

News Notes

Against the Dead Hand Wins Fisher Award

The Cato Institute received the 13th annual Sir Antony Fisher International Memorial Award for publishing Brink Lindsey’s book *Against the Dead Hand: The Uncertain Struggle for Global Capitalism*. The award, for the publication that best “enhanced public understanding of the free society,” was presented at the Atlas Economic Research Foundation’s third annual Liberty Forum in April. Past winners of the award have included *The Mystery of Capital* by Hernando de Soto, *The Excuse Factory* by Walter Olson, *Simple Rules for a Complex World* by Richard Epstein, and *In Defense of Global Capitalism* by Johan Norberg (published by the Swedish institute Timbro; Cato will publish an American edition in September). Previous Cato winners include *The Economic Consequences of Immigration* by Julian Simon, *Patient Power* by John Goodman and Gerald Musgrave, and *Perpetuating Poverty*, edited by Doug Bandow and Ian Vásquez.



Two Cato books have been published in foreign languages recently. *Libertarianism: A Primer* by David Boaz was published in Czech by the Liberalni Institute as *Liberalismus: V Teorii a Politice*. *Global Fortune: The Stumble and Rise of World Capitalism*, edited by Ian Vásquez, was published in Turkish by Liberte Yayinlari as *Kapitalizm ve Küresel Refah*. Polish, Serbian, and Russian editions of *Libertarianism: A Primer* are also in the works.

For foreign rights to any of Cato’s books, contact Amy Mitchell at amitchell@cato.org.

The Cato Institute’s Spanish-language website, elcato.org, celebrated its fifth birthday on May 29. It was launched in 1998 by Luis Figueroa and the Project on Global Economic Liberty. Since then, José Piñera Jr., Fernando Alessandri, Constantino Díaz-Durán, and Juan Carlos Hidalgo have served as the editors of elcato.org under the direction of Ian Vásquez. The site now receives an average of about 80,000 visits per month, making it the leading classical liberal/libertarian website in the Hispanic world.

“The New Deal failed to get America out of the Great Depression. If anything, it made matters worse.”

THE NEW DEAL *Continued from page 1*

the Great Depression by doubling taxes, making it more expensive for employers to hire people, making it harder for entrepreneurs to raise capital, demonizing employers, destroying food, promoting cartels, breaking up the strongest banks, forcing up the cost of living, channeling welfare spending away from the poorest people, and enacting labor laws that hit poor African Americans especially hard.

Reports of those findings had been accumulating in the shadows, largely ignored until 1999, when Stanford University historian David M. Kennedy won a Pulitzer Prize for *Freedom from Fear: The American People in Depression and War*, a popular work drawing on some of that research. “Whatever it was,” he wrote, the New Deal “was not a recovery program, or at any rate not an effective one.”

My new book, *FDR’s Folly, How Franklin D. Roosevelt and His New Deal Prolonged the Great Depression*, is the first work to focus on the entire range of findings. It won’t be the last such book, however, since critical analyses of the New Deal continue to appear.

New Deal Attack on Employers

FDR made it more expensive for employers to hire people, ensuring that fewer people would be employed. The National Industrial Recovery Act of 1933 established the National Recovery Administration, which authorized some 700 cartels with codes mandating above-market wages.

By giving its imprimatur to labor union monopolies, violent strikes, and surging wage rates in mass production industries, the 1935 National Labor Relations Act, commonly known as the Wagner Act, contributed to layoffs. Over the course of three months in 1937–38, General Motors dismissed a quarter of its employees, and overall U.S. car production dropped almost 50 percent. Economists Richard K. Vedder and Lowell E. Gallaway, in their 1997 study *Out of Work*, estimated that by 1940 unemployment was eight points higher than it would have been in the absence of higher payroll costs imposed by New Deal policies.

Taxes more than doubled during the Great Depression, and the federal take rose from

\$1.6 billion in 1933 to \$5.3 billion in 1940. Federal taxes as a percentage of the gross national product jumped from 3.5 percent in 1933 to 6.9 percent in 1940. Ordinary people were directly hit with higher liquor taxes and Social Security payroll taxes. FDR increased the tax burden with higher personal income taxes, higher corporate income taxes, higher excise taxes, higher estate taxes, and higher gift taxes. He introduced the undistributed profits tax. Those taxes reduced the amount of money employers had to finance growth and jobs.

In their 1998 study, *The Great Depression*, economists Thomas E. Hall and J. David Ferguson wrote that “antibusiness tax laws would certainly have had a negative impact on employment. In addition, the uncertainty experienced by the business community as a result of the frequent tax law changes (1932, 1934, 1935, 1936) must have been enormous. Since firms’ investment decisions very much depend on being able to plan, an increase in uncertainty tends to reduce investment expenditures . . . investment as a proportion of output was at low levels.”

New Deal securities laws further depressed employment by making it harder for employers to raise capital. The 1933 Securities Act required detailed financial reports from issuers of new securities. Economic historian Lester V. Chandler of Princeton University has described the effect of the new rules this way: “The regulations on new security issues were burdensome, especially in the early stages before lawyers, financiers, and corporate officers became accustomed to them, understood procedures, and worked out routines. Compliance was time-consuming and expensive. Also, businessmen were fearful of the civil and criminal penalties that they might inadvertently incur.”

The first empirical investigation of the effects of the Securities and Exchange Commission, established in 1934, was conducted by future Nobel laureate George J. Stigler. His work showed that fewer companies raised capital in the stock market after the SEC was established than before, and that rates of return on new stocks issued in the 1920s (the pre-SEC stock boom) were not significantly lower than rates of return on new stocks issued in the 1950s (the first

boom after the Great Depression). New Dealers had claimed that the Great Depression was brought on by stock market abuses and fraud. But, if that were true, pre-SEC rates of return would have been depressed, and the SEC would have improved rates of return. Analyzing data on industrial company stocks issued between 1926 and 1939, economist Gregg A. Jarrell confirmed Stigler’s findings. What, then, was the point of making it more difficult for employers to raise capital and hire people?

In 1938 FDR authorized an unprecedented antitrust crusade against big employers. The Department of Justice hired some 300 lawyers to file about 150 antitrust lawsuits. Often they were filed not just against a single company but against an entire industry. There were lawsuits against the milk, oil, tobacco, shoe machinery, tire, fertilizer, railroad, pharmaceuticals, school supplies, billboards, fire insurance, liquor, typewriter, and movie industries, among others. But the antitrust crusade was a flop. The government won few cases, and some dragged on as long as 13 years. FDR’s antitrust crusade disrupted an already depressed economy, making it harder for employers to recover and provide more jobs. G. Warren Nutter and Henry Adler Einhorn’s 1969 study, *Enterprise Monopoly in the United States*, was one of several showing that there wasn’t any evidence of increasing private-sector monopoly during the 1930s. The whole antitrust crusade was based on an illusion.

As if all that weren’t bad enough, FDR demonized employers with poisonous rhetoric. In accepting the 1936 Democratic presidential nomination, FDR lashed out against “economic royalists . . . the privileged princes of these new economic dynasties, thirsting for power. . . . They created a new despotism . . . this new industrial dictatorship. . . . We seek to take away their power.” Is it any wonder that so many people concluded that America wasn’t a safe place to invest?

Breaking Up the Strongest Banks

FDR’s major banking “reform,” the second Glass-Steagall Act, broke up the strongest banks, including J.P. Morgan & Company—universal banks that engaged in both

Continued on page 16

“African Americans were major victims of the National Recovery Administration.”

THE NEW DEAL *Continued from page 15*

commercial banking (deposits and loans) and investment banking (securities underwriting), because New Dealers imagined that securities underwriting was a factor in all the bank failures.

In 1986 Eugene N. White reported that during the 1920s, before the passage of the Glass-Steagall Act, banks that engaged in both deposits and loans and securities underwriting were less likely to fail than were investment banks that didn't engage in securities underwriting. White further reported that, between 1930 and 1933, 26.3 percent of all national banks failed, compared with only 7.6 percent of banks that engaged in securities underwriting. The reason for the greater safety of universal banks, White suggested, was diversification.

University of Chicago economists Randall Kroszner and Raghuram Rajan gathered data on securities issues during the 1920s and compared the performance of issues underwritten by universal banks and those issued by investment banks. They found that 40 percent more of the bonds issued by *investment* banks—the kind of banks approved by New Dealers—went into default.

FDR didn't do anything about a major cause of 90 percent of the bank failures, namely, state and federal unit banking laws, which limited banks to a single office, thus preventing them from diversifying their loan portfolios and their source of funds. Unit banks were highly vulnerable to failure when local business conditions were bad, because all their loans were to local people, many of whom were in default, and all their deposits came from local people who were withdrawing their money. Canada, which permitted nationwide branch banking, didn't have a single bank failure during the Great Depression.

FDR signed the Banking Act of 1935, which centralized power at the Fed. Allen H. Meltzer makes clear in his recent *History of the Federal Reserve* that the seven governors of the Fed almost always had to interpret conflicting information, and they were human beings prone to error. Centralizing power meant their errors would harm, not just a city or a region, but the entire United States.

The first bad call came in July 1936, just five and a half months after the new Fed began to operate. It increased the reserve requirement for banks by 50 percent, which meant a higher proportion of a bank's money had to stay in the vault, rather than be lent and reinvested. On January 30, 1937, the Fed increased bank reserve requirements another 33.3 percent. Those bad calls triggered a contraction of the money supply, which was one of the most important factors bringing on the depression of 1938—the third most severe since World War I. Real GNP declined 18 percent, and industrial production was down 32 percent.

What about FDR's federal deposit insurance reform? It didn't stop bank failures. Since depositors no longer worried about losing their money, though, there weren't any more serious bank panics. Deposit insurance transferred the cost of bank failures from depositors to taxpayers, undermining incentives for depositors to steer clear of risky banks. The full consequences of federal deposit insurance became apparent in the 1980s, when savings-and-loan bailouts cost taxpayers \$519 billion.

Punishing Discounters, Destroying Food

National Recovery Administration cartels forced prices for goods and services above market levels, making everybody poorer. The “little people” fared worst. In April 1934, 49-year-old immigrant Jacob Maged of Jersey City was fined and jailed for three months after charging 35 cents to press a suit, rather than the 40 cents mandated by the National Recovery Administration's dry cleaning code.

The Agricultural Adjustment Acts (1933, 1938) forced up farm prices, which meant higher food prices for millions of Americans. Under the AAAs, Secretary of Agriculture and future vice president Henry Wallace had farmers plow under some 10 million acres of cultivated land, destroying wheat, corn, and other crops. Hog farmers were paid to slaughter some 6 million shoats (young pigs). That was the sort of thing John Steinbeck protested in *The Grapes of Wrath*.

The SEC enforced price fixing on Wall Street—the high commissions that investors paid to buy or sell securities. Real reform—deregulation, competition, and discount

prices—didn't come to Wall Street until 1975.

The Robinson-Patman Act, amending the Clayton Antitrust Act in 1936, made it illegal for A&P, King Kullen (“World's Greatest Price Wrecker”), and other chain stores to share discounts on volume purchases with consumers. FDR struck another blow against consumers by signing the Miller-Tydings Retail Price Maintenance Act in 1937. That act amended the Sherman Act to let manufacturers fix the retail prices of branded merchandise and stop chain stores from offering great discount prices.

In 1938 FDR signed into law the Civil Aeronautics Act, which enabled the federal government to enforce an airline cartel. For 40 years, not a single license was issued for a new interstate airline, and consumers were hit with high fixed fares.

The New Deal Made African Americans Worse Off

African Americans were major victims of the National Recovery Administration. The labor codes, drafted by craft unions that excluded African Americans, specified above-market wages, which effectively outlawed price competition in labor markets. Since large numbers of black workers were unskilled, their best hope was to work at a lower rate and get on-the-job experience that would increase their skills and their ability to compete. “Because of the NRA, wages in the South's largest industry, textiles, increased by almost 70 percent in five months,” reported George Mason University law professor David E. Bernstein. “Employers responded to such massive wage increases by investing in mechanization and dismissing their unskilled workers.” Some 500,000 black workers were estimated to have lost their jobs because of the National Recovery Administration's minimum wage codes.

Black workers were big losers under the National Labor Relations Act, hailed as the “Magna Carta” of compulsory unionism. “To the extent that the Wagner Act raised wages and labor standards beyond market levels,” wrote Bernstein, “it had the same effect as a minimum wage law in eliminating marginal African American jobs.”

Black farmers were left high and dry when their land was flooded by the Tennessee Val-

Continued on page 17



Cato president Edward H. Crane and adjunct scholar Walter E. Williams received honorary doctorates at Francisco Marroquin University in Guatemala on May 10.

Ed Crane receives the Adam Smith Award, “given to recognize an individual who has made a sustained and lasting contribution to the perpetuation of the ideals of a free market economy,” from the Association of Private Enterprise Education at its annual conference on April 6. APEE vice president Jane S. Shaw presents the award.



THE NEW DEAL *Continued from page 16*

ley Authority. According to economist John Moore, TVA dams “permanently flood a total of about 730,000 acres . . . an area which is approximately as large as the state of Rhode Island.” A reported 15,654 people were forced from their homes to make way for dams. Farm owners received cash settlements for their condemned property, but the thousands of black tenant farmers got nothing.

The AAAs reduced farm acreage and gave millions of dollars to big farmers, but the 600,000 black sharecroppers got nothing. In a 2001 National Bureau of Economic Research study, Price V. Fishback, William C. Horrance, and Shawn Kantor reported that “income inequality was exacerbated as the landowners’ incomes increased and the incomes of the much larger group of tenants, croppers and workers declined.”

What about all the New Deal relief programs? The bulk of that money was skewed away from the South, which was the poorest region. Historian Leonard Arrington estimates that, on average, a person living in the West received 60 percent more New Deal money than a person living in the South. Historian Don Reading found there was less New Deal spending in the

states that had higher percentages of black residents, higher percentages of tenant farmers, and lower per person incomes.

Economic historian Gavin Wright of Stanford concluded that less New Deal welfare spending went to the southern states that gave FDR big winning margins (over 67 percent) in 1932, presumably because FDR was sure to win those states again. More New Deal spending went to western states where FDR had won less than 60 percent of the vote in 1932, to help ensure victory in 1936.

Warren Harding Beats FDR as Anti-Depression Fighter

The Great Depression wasn’t written in the stars. After all, the severe depression of 1920 was over in about a year. The president then was Warren G. Harding, who succeeded where FDR failed. Harding cut federal spending, cut taxes, and went back to his card games. Harding’s slogan “less government in business” turns out to have been a vastly better guide than FDR’s disastrous “New Deal.” Everybody, especially the poorest among us, is better served when private property is secure, the currency is stable, markets are open, people are free to make their own bargains, government burdens are lifted, and it’s safe to invest for the future. ■

POLICY FORUM *Continued from page 10*

programs like the Children’s Scholarship Fund, and do that by making large-scale tax credits available for both businesses and individuals who donate to those funds, we could easily raise tens of millions of dollars in very short order. Pennsylvania found that out: the state has a tax credit for businesses that donate to a scholarship fund. Businesses give money to the scholarship fund, and the fund subsidizes the education of low-income children. There is a \$20 million cap on the amount of money that can be collected under this program from businesses, and the cap’s usually hit in the first two weeks of eligibility each year. If Pennsylvania got rid of that cap, businesses would donate more money.

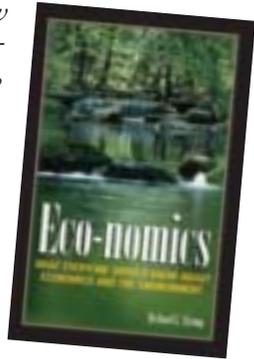
The flexibility that such funds offer and the level of hands-on interaction with the recipients are tremendous benefits in and of themselves. That flexibility would allow a progressive need-based system of financial assistance. The lowest income families would either be fully subsidized or pay only a very small copayment; the subsidy would decrease as incomes rose, and the wealthiest families would not receive any subsidy. ■

A Short Book on a Big Topic

What do you give to a friend who thinks only regulation protects the environment? From now on, the answer is easy: *Eco-nomics: What Everyone Should Know about Economics and the Environment* by Richard L. Stroup, just published by the Cato Institute. In 86 pages—a couple of hours' reading—Stroup explains how to understand tradeoffs, how property rights replace conflict with cooperation, how regulation works and doesn't work, and how to make environmental policy choices.

In clear, straightforward language, Stroup addresses the questions that everyone should

ask about how to protect the environment and how to make markets work. *Eco-nomics* has drawn praise from environmentalists and economists alike. David



Simpson, senior fellow at Resources for the Future, writes: "Rick Stroup's volume is thin but weighty. He packages essential insights in readable, concise prose. Whether or not they end up accepting Stroup's prescriptions, environmental advocates of all stripes ought to consider them carefully. Far too much effort has been wasted on ineffective and inefficient approaches to environmental improvement. Environmental-

ists and public decisionmakers ought to at least wrestle with the same questions Stroup does before deciding on a course of action. He has given them an enlightening and provocative template for doing so."

Richard L. Stroup is a professor of economics at Montana State University and a senior associate at PERC—the Center for Free Market Environmentalism. He is coauthor of a primer on economics, *What Everyone Should Know about Economics and Prosperity*, and of a leading college textbook, *Economics: Private and Public Choice*. Stroup is an adjunct scholar of the Cato Institute.

Eco-nomics is available in paperback only for \$9.95. It can be purchased in bookstores, at www.catostore.org, or by calling 800-767-1241. ■

Corporate Crime Examined in *Regulation*

One argument for U.S. military intervention abroad is that it helps to protect American economic interests. In the cover story of the Spring 2003 issue of *Regulation*, Eugene Gholz of the University of Kentucky and Daryl Press of Dartmouth College take a close look at that argument. They conclude that "the forward deployment of the American military to police the most economically vibrant parts of the world is a poor investment. . . . If the war on terrorism requires more U.S. military effort in the future, the resources now committed to defend Europe, Japan, and South Korea—both troops and dollars—would be freed up to combat al-Qaeda or other attackers."

Two articles look at regulatory responses to corporate crime. Stephen M. Bainbridge of UCLA School of Law deplors "The Creeping Federalization of Corporate Law" in the Sarbanes-Oxley Act and elsewhere. Adam C. Pritchard of the University of Michigan Law School argues that securities exchanges can police market abuses if they're allowed the authority to do so.

Other articles look at the benefits of biotechnology, the high costs of funeral regulation, federal highway policy, and the

continued misunderstanding of California's energy crisis. And Penn Jillette provides his inimitable take on war, regulation, Las Vegas, and much else in "The Final Word."

José Piñera's essay "Latin America: A Way Out" highlights the new issue of *Cato Journal* (vol. 22, no. 3). He offers a more optimistic view of Latin America's future than did Mario Vargas Llosa in his essay "Why Does Latin America Fail?" in the January–February 2003 issue of *Cato Policy Report*.

Benjamin Powell of George Mason University takes a look at one of the great economic successes of recent years, Ireland. In "Economic Freedom and Growth: The Case of the Celtic Tiger," he argues that a series

of sound economic policies created remarkable growth from 1987 to 2000. Those policies included reduced inflation, free trade, spending cuts, and tax reduction. Ireland now has lower taxes and a higher per capita GDP than England and Germany.

Ben Craig and Owen Humpage of the Federal Reserve offer a skeptical analysis of the "strong dollar policy." Abdiweli M. Ali and Hodan Said Isse examine the determinants of corruption. Other essays and book reviews address globalization, mercantilism, adoption, trade sanctions, and conflict reduction.

Regulation and *Cato Journal* are available at newsstands and at www.cato.org.

Captions for p. 19

Dean Stansel was an intern and later fiscal policy analyst for Cato. **Robin Hulsey** was assistant director of public affairs. After leaving Cato in 1998, they lived in Richmond and now live in Clovis, New Mexico, where Dean teaches economics at Eastern New Mexico University and Robin is expecting their first child.

Lucas Mast was a research assistant in Cato's telecommunications department in 2000–2001, and **Anita Stevens** was intern coordinator. They both now work for Clarium Capital Management in San Francisco.

Tim Lynch was a young lawyer at Cato in 1992, when **Lee Ooi** arrived as an intern from the George Mason University master's program. Tim is now director of Cato's Project on Criminal Justice, Lee is director of economic analysis at White and Case, a Washington law firm, and they are the parents of three-year-old Seamus.

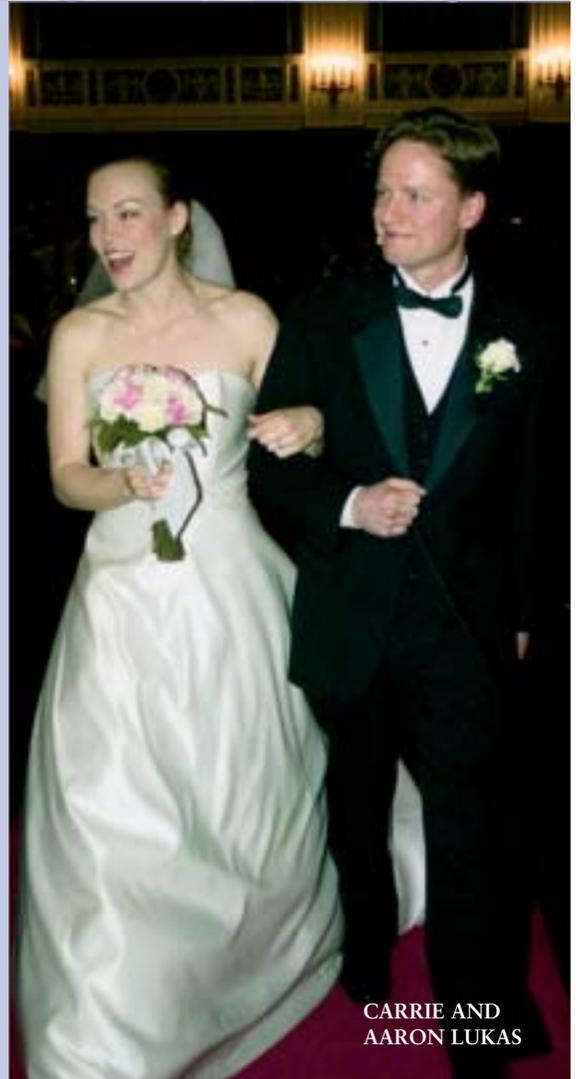
Solveig Singleton was Cato's director of information studies in the late 1990s, when **Ananda Gupta** served as an intern. Solveig is now a senior policy analyst at the Competitive Enterprise Institute, and Ananda is a fledgling game designer. They are attended by Darcy Olsen and Shankar Gupta.

WEDDING BELLS

ROBIN AND DEAN STANSEL



Former Cato employees Carrie Lips and Aaron Lukas were married on Saturday, April 12, and held their reception in the Cato Wintergarden. Aaron, now the speechwriter for U.S. Trade Representative Robert Zoellick, was an intern, founding webmaster, and trade policy analyst at Cato. Carrie, now a staff member of the Select Committee on Homeland Security headed by Rep. Christopher Cox, was a Social Security analyst at Cato. In honor of their wedding, we acknowledge some other couples who met while they worked at the Cato Institute.



CARRIE AND AARON LUKAS



LUCAS AND ANITA MAST



TIM AND LEE LYNCH



ANANDA GUPTA AND SOLVEIG SINGLETON

◆ **Stop them before they legislate again**

Atlanta Democrat Rep. John Noel was so upset that he could not get sweet tea at a restaurant that he and four co-sponsors filed a bill that would make it a misdemeanor “of a high and aggravated nature” not to offer sweet tea in any restaurant that serves iced tea.

The punishment for such an egregious offense? As many as 12 months in jail.

—*Rome (Georgia) News-Tribune*, April 7, 2003

A San Francisco law went over the line when it actually outlawed the act of addressing someone by a gender pronoun they did not prefer. The ordinance actually considered it a form of harassment to call a “he” a “he” instead of a “she” if “he” thinks he’s a “she.”

—Michael Alvear in the *Washington Blade*, April 11, 2003

Walking will become the official exercise of the Free State if Gov. Robert L. Ehrlich Jr. (R) signs a bill passed by the Maryland General Assembly. Del. William A. Bronrott (D-Montgomery), sponsor of the bill, credits a Montgomery County third-grade class with the idea.

—*Washington Post*, April 15, 2003

◆ **Or maybe the fundamental problem is that the government isn’t trustworthy**

Right now, however, the [Chinese] government is trying to recover from a series of admissions that officials had covered up the extent of the disease in Beijing and around the country.

“The fundamental problem here is

that people don’t have faith in the government,” said Kang Xiaoguang, a leading social scientist.

—*Washington Post*, April 29, 2003

◆ **Ow, ow, ow!**

House committee chairmen have signed off on a plan, endorsed by Majority Leader Tom DeLay, to cut 1 percent from their respective budgets by eliminating waste, fraud, and abuse.

—*Washington Times*, May 15, 2003

◆ **You can’t make this stuff up**

Position available: Interpreter, must be fluent in Klingon.

The language created for “Star Trek” is one of about 55 used by the Oregon Department of Human Services, which treats mental patients in Multnomah County [which includes Portland].

“There are some cases where we’ve had mental-health patients where this was all they would speak,” said the department’s Franna Hathaway.

Officials say that obligates them to respond with a Klingon-English interpreter.

—*New York Post*, May 12, 2003

◆ **Or you can just keep on lying and denying until your term ends**

As a media strategist who has worked for both Bill and Hillary Clinton during rough times (and good ones) . . . I also have a lot of sympathy for Arthur Sulzberger Jr. and Howell Raines, or anyone else caught in the maelstrom of a scandal . . .

What should a newspaper or network do when faced with a scandal?

First, remember some of the cliches you

reach for when trouble hits the politicians you report on: “The coverup is worse than the crime.” “Everything that can be known will be known, so get it out fast.” They’re cliches, and they’re true.

—Mandy Grunwald in the *Washington Post*, June 8, 2003

◆ **Global warming, global cooling, anyway it’s capitalism’s fault**

On a chilly and sodden afternoon last week, Christina Vrachnos braced herself against the wind on Madison Avenue, and cast her eyes toward the skies. “Is it global warming?” she wailed. “What is it? What have we done to deserve this wretched weather?”

Ms. Vrachnos, who works in the marketing department of a financial publishing company, had suited up to brave temperatures that had dipped into the low 50’s.

—*New York Times*, June 8, 2003

◆ **Wacky French ideas**

Let us dream about some ideas to improve [the United Nations charter’s] structure and behavior in order to obtain a viable and more credible United Nations:

Establish a permanent military force at the sole disposal of the secretary general. This force would be completed by civil observers who could suspend unfair and illegitimate election returns or constitutional changes.

Complete budget financing by a tax on speculative movements of capital.

—Andre Lewin, chairman of the French United Nations Association, in the *New York Times*, March 15, 2003

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