# Milton Friedman 1912-2006: “Free market” architect of social reaction

**By Nick Beams**
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In his afterword to the second edition of *Capital* in 1873, Karl Marx noted that the scientific character of bourgeois economics had come to an end about 1830. At that point the class tensions generated by the development of the capitalist mode of production itself made further advances impossible. “In place of disinterested inquirers there now stepped forward hired prize-fighters; in place of genuine scientific research, the bad conscience and evil intent of apologetics.”

The economist Milton Friedman, who died last Thursday aged 94, will be remembered in years to come as one of the classic representatives of this tendency. Indeed his own career, culminating in his rise to the position of intellectual godfather of the “free market” over the past four decades, is a graphic example of the very processes to which Marx had pointed.

In the post-war boom, now looked back on as a kind of “golden age” for capitalism, at least in the major economies, Friedman was very much on the margins of bourgeois economics. When this writer begun a university study of economics in the latter half of the 1960s Friedman, and the free market Chicago School in which he was a central figure, were regarded as eccentrics, if not oddities. This was the heyday of Keynesianism, based on the notion that regulation of “effective demand” by government policies—increased spending in times of recession, cutbacks in periods of economic growth and expansion—could prevent the re-emergence of the kind of crisis that had devastated world capitalism in the 1930s.

All that was about to change. The breakdown of the post-war economic boom in the early 1970s, bringing deep recession as well as rapid inflation and high unemployment, saw the collapse of the Keynesian prescriptions. Under the Keynesian program, inflation was regarded as the antidote to unemployment. Now the two were taking place in combination—giving rise to the phenomenon of “stagflation”.

The boom’s demise was not the product of the “failure” of Keynesianism. Rather it was caused by the re-emergence of deep-seated contradictions within the capitalism economy. This meant that the bourgeoisie in the major capitalist countries could no longer continue with the program of class compromise based on concessions to the working class—the pursuit of full employment and the provision of social welfare measures that had characterised the boom—but had to undertake a sharp turn.

Friedman provided the ideological justification for the new orientation: the denunciation of government intervention as the cause of the crisis and insistence on a return to the principles of the “free market” which had been so discredited in the 1930s. Less than a decade after the collapse of the boom, Friedman’s “eccentric” theories had become the new orthodoxy and Keynesianism the new heresy.

In October 1976, the Swedish Academy in Stockholm, sensing the shift in the winds, awarded Friedman the Nobel Prize for economics. One month before, in a major speech to the British Labour Party conference, prime minister James Callaghan summed up what was to become the new conventional wisdom and its implications for government policy.

“We used to think that you could spend your way out of a recession and increase employment by cutting taxes and boosting government spending. I tell you in all candour that that option no longer exists, and in so far as it ever did exist, it only worked on each occasion since the war by injecting a bigger dose of inflation into the economy, followed by a higher level of unemployment as the next step.”

Milton Friedman was born in Brooklyn, New York, the fourth son of immigrants from central Europe. He later wrote that while the family income was “small and highly uncertain” and financial crisis was a constant companion, there was always enough to eat, and the family atmosphere was warm and supportive.

After graduating from high school before his sixteenth birthday, Friedman won a scholarship to study at Rutgers University, New Jersey. He initially planned to become an actuary and studied mathematics, but his interest in economics grew under the impact of the Great Depression. Graduating in both mathematics and economics in 1932, he gained a masters degree from the University of Chicago 12 months later. Friedman initially obtained a government job at the National Resources Committee—a creation of Roosevelt’s New Deal—and then joined the National Bureau of Economic Research. When the war began he was involved in the development of federal tax policy and is credited with developing the federal withholding tax, which forms the basis of the pay-as-you-go system.

After receiving his doctorate from Colombia University in 1946, Friedman returned to University of Chicago to teach economic theory. He remained there until his retirement in 1976, the head of what had become known as the Chicago School of economics, based on the free market and an insistence on the importance of the quantity of money in determining the business cycle.

Friedman was active in Republican policy circles. In 1964 he served as an informal adviser to the presidential candidate and standard-bearer for the Republican right wing, Barry Goldwater, and was an adviser to both Richard Nixon in 1968 and Ronald Reagan in 1980. When Reagan won office, Friedman served as a member of his Economic Policy Advisory Board and in 1988 received the Presidential Medal for Freedom. In 2002, President George W. Bush honoured him for “lifetime achievements” and hailed him as a “hero of freedom” at a White House function on the occasion of his 90th birthday.

Friedman’s work on economic theory was guided by an adherence to what is known as the quantity theory of money. Friedman used this theory, which has a long history going back to the English philosopher David Hume, to formulate his opposition to the Keynesian perspective of demand management and government intervention. According to Friedman, if too much money were created by the monetary authorities, prices would increase—inflation, he insisted was always a monetary phenomenon. The task of government, he claimed, was not to regulate the economy through spending, but to ensure a sufficient expansion of the

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money supply to account for natural economic growth, and allow the market to solve the problems of unemployment and recession.

However if the Keynesians were to be refuted, Friedman saw that it was essential that the battle take place on their ground, with historical and statistical analyses. This was the background to his major theoretical work *A Monetary History of the United States 1867-1960*, written jointly with Anna Schwartz and published in 1963. Through an examination of economic history, Friedman and Schwartz sought to reveal the crucial role of the supply of money in determining the level of economic activity and, in doing so, to establish the necessary guidelines for future policy.

In its statement announcing the awarding of the Nobel prize to Friedman, the Swedish academy placed special emphasis on this work. "Most outstanding," the citation read, "is, perhaps, his original and energetically pursued study of the strategic role played by the policy of the Federal Reserve System in sparking off the 1929 crisis, and in deepening and prolonging the depression that followed."

But it is through an examination of the 1930s depression—the most important economic event of the twentieth century—that the theoretical bankruptcy of Friedman's work stands most clearly revealed. According to Friedman, what would have been a normal recession in 1929-30 was transformed into an economic disaster by a series of policy mistakes made by the Federal Reserve, the body responsible for regulating the money supply.

In the first instance, he maintained, the Federal Reserve had wrongly started to tighten monetary policy in the spring of 1928, continuing until the stock market crash of October 1929 under conditions that were not conducive to tighter money—the economy had only just started to move out of the previous business cycle trough in 1927, commodity prices were falling and there was no sign of inflation. The Federal Reserve, however, considered it necessary to rein in the speculative use of credit on the stock market.

In Friedman's view, however, the most significant impact of the Federal Reserve's policies was not in sparking the depression but in bringing about the collapse of 1931-32. As banks were going into liquidation, the Federal Reserve, instead of expanding credit and stabilising the financial system, cut the money supply and exacerbated the crisis. Altogether, he and Schwartz found that the money supply in the US contracted by one third between 1929 and 1933. As critics of Friedman have pointed out, this fall was as much a product of the contraction in economic activity as an active cause.

Notwithstanding such objections, Friedman's analysis served important political purposes—it transferred attention from the failures of capitalism and its free market to the role of governments. As Friedman expounded in an interview with Radio Australia in July 1998, the Great Depression was not a "result of the failure of the market system as was widely interpreted" but was "instead a consequence of a very serious government failure, in particular a failure in the monetary authorities to do what they'd initially been set up to do" and prevent banking panics.

The obvious question then was: why did the Federal Reserve fail to prevent a collapse? According to Friedman, the board of the New York Federal reserve was wracked by a series of conflicts following the death of its powerful governor Benjamin Strong. These prevented the implementation of correct policy.

"The fact that bad monetary policy was carried out," he explained in a television interview for the PBS series the "First Measured Century", "was, in part, the result of a real accident, which was that the dominant figure in the Federal Reserve System, Benjamin Strong ... had died in 1928. It is my considered opinion that if he had lived two or three more years, you might very well not have had a Great Depression."

Such were the absurd lengths to which Friedman was prepared to go in order to prevent any critical examination of the role of capitalism and the "free market" in bringing about the greatest economic collapse in history. What was perhaps even more absurd was that his analysis was taken seriously in academic circles, which launched a search to discover Strong's real views and whether he would have acted differently.

Friedman's ascendancy to the ranks of "leading economist" had little to do with the intellectual and scientific value of his work. Rather, it was the result of his continuing efforts to extol the virtues of the free market and private property in opposition to the prevailing orthodoxy. Consequently, when the post-war compromise ended, and new prize-fighters were required, he was installed as chief propagandist for a new, socially regressive era based on the unfettered accumulation of wealth by a tiny minority ... all in the name of human "freedom".

The basis of Friedman's ideology was the conception that human freedom was inseparable from the unfettered operation of the market and the system of private property. Moreover, the market was not a particular social formation arising at a definite point in the history of human society but had a timeless quality. Just as the ruling classes in feudal times had the priests on hand to assure them that their place in the hierarchy was God-given, so Friedman assured the ruling classes of the present day that the social system which showered wealth and privileges upon them was rooted in the very nature of human social organisation itself.

In his book *Capitalism and Freedom*, published in 1962, he wrote: "Historical evidence speaks with a single voice on the relation between political freedom and the free market." Expanding on this theme in a lecture delivered in 1991, he went on to identify the market with all forms of human social interaction.

"A free private market," he wrote, "is a mechanism for achieving voluntary co-operation among people. It applies to any human activity, not simply to economic transactions. We are speaking a language. Where did that language come from? Did some government construct the language and instruct people to use it? Was there some commission that developed the rules of grammar? No, the language we speak developed through a free private market."

Friedman's attempt to turn the development of language, and by implication every human activity, into a market phenomenon collapses upon even the most preliminary analysis. The free market presupposes the existence of separate individuals who exchange the products of their private labour. In language, however, people do not exchange their private creations. In order to understand and in turn be understood, the individual must learn the language that has already been developed by socialised humanity. Friedman's assertion makes about as much sense as would a claim that individual elements engage in a "market transaction" when they "exchange" electrons to form a compound.

If Friedman's free market dogmas had no scientific content, they were nonetheless extremely valuable in the service of definite class interests, as the experience of Chile was to graphically demonstrate.

In 1975, following the overthrow of the elected Allende government in a military coup on September 11, 1973, the head of the junta, Augusto Pinochet, called on Friedman and his "Chicago boys"—economists trained under his tutelage—to reorganise the Chilean economy.

Under the direct guidance of Friedman and his followers, Pinochet set out to implement a "free market" program based on deregulation of the economy and privatization. He abolished the minimum wage, rescinded trade union rights, privatised the pension system, state industries and banks, and lowered taxes on incomes and profits.

The result was a social disaster for the mass of the Chilean population. Unemployment rose from just over 9 percent in 1974 to almost 19 percent in 1975. Output fell by 12.9 percent in the same period—a contraction comparable to that experienced by the United States in the 1930s.

After 1977, the Chilean economy enjoyed something of a recovery, with the growth rate reaching 8 percent. Ronald Reagan proclaimed Chile as a "model" for Third World development, while Friedman claimed that the "Chile experiment" was "comparable to the economic miracle of

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post-war Germany." In 1982 he heaped praise on the dictator Pinochet whom, he declared, "has supported a fully free-market economy as a matter of principle. Chile is an economic miracle."

But the recovery was short-lived. In 1983 the economy was devastated, with unemployment rising, at one point, to 34.6 percent. Manufacturing production contracted by 28 percent. Between 1982 and 1983, gross domestic product contracted by 19 percent. Rather than bringing freedom, the free market resulted in the accumulation of vast wealth at one pole and poverty and misery at the other. In 1970, 20 percent of Chile's population had lived in poverty. By 1990, the last year of the military dictatorship, this had doubled to 40 percent. At the same time, real wages had declined by more than 40 percent. The wealthy, however, were getting wealthier. In 1970 the top one-fifth of the population controlled 45 percent of the wealth compared to 7.6 percent by the bottom one-fifth. By 1989, the proportions were 55 percent and 4.4 percent respectively.

The Chilean experience was no isolated event. It was simply the first demonstration of the fact that, far from bringing human freedom, the unleashing of the capitalist free market could only take place through the organized violence of the state.

In the United States, the monetarist free market program implemented during the Reagan administration was accompanied by the destruction of the trade unions, starting with the smashing of the air traffic controllers' union, PATCO, in 1981. As Federal Reserve Board chairman Paul Volcker was later to remark: "The most important single action of the administration in helping the anti-inflation fight was defeating the air traffic controllers' strike."

Likewise in Britain, the Thatcherite economic counter-revolution, based on the ideas of Friedman and one of his most influential mentors, Friedrich Hayek, led directly to the smashing of the miners' union through a massive intervention by the police and other state forces in the year-long strike of 1984-85.

Elsewhere the same processes were at work—notably in Australia, where the program of privatization, deregulation and the free market saw state-organised suppression of the workers' movement, all carried out by the Hawke-Keating Labor governments between 1983 and 1996.

As Friedman went to his grave, the plaudits filled the air. Bush hailed him as "a revolutionary thinker and extraordinary economist whose work helped advance human dignity and human freedom." Margaret Thatcher praised his revival of the "economics of liberty" and described him as an "intellectual freedom fighter". US treasury secretary Henry Paulson said he would always be counted "among the greatest economists." The *New York Times* obituary described Friedman as a "giant of economics" for whom criticism of his actions in Chile was "just a bump in the road." Australian prime minister John Howard called him "a towering figure of world economic theory" while an editorial in Rupert Murdoch's newspaper the *Australian* called him "liberty's champion".

And so it went on. Nothing, it seems, gratifies the rich and powerful so much as the justification of their elevated position in terms of freedom and liberty. In the coming period, however, under changed social conditions and in different political circumstances, the name Milton Friedman will evoke a very different response.

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