

about save more, buy more wisely, or what not, is a bunch of nonsense. That is not the way in which we have produced inflation. We have produced inflation as citizens by instructing the Congress to vote more expenditures and not to vote more taxes. We have produced inflation as citizens by demanding from the government that they have a full employment policy and therefore bring pressure on the Federal Reserve to validate it. When and as the political climate changes, our representatives in government will do what we ask them to do.

**QUESTION:** Do you think the social fibre could withstand this?

**MR. FRIEDMAN:** Of course, that depends on how severe it is. Obviously I'm not going to make any predictions on what would happen if we went through another 1929-33 but that is not what is called for. That's not in the cards at all. The kind of unemployment, the kind of slow growth you have to go through is something which is far less severe. The country could stand it. There would be no great pressure. On the contrary, I personally believe that the kind of inflation we've been having does vastly more harm to the social fabric than the corrective measures would do if they were taken gradually and reasonably. Right now you have a country being divided into two classes: the class of those people who have been benefiting from inflation and the class of those people who have been hurting by inflation. A great many people have benefited from inflation. Half the population of the United States owns their own homes. A greater part of those have mortgages. The greater part of those mortgages were taken out at low interest rates and have essentially been paid back by inflation. Every home owner has had a great capital gain as a result of inflation. And that has tended to produce a divisiveness within the society between them and the poor suckers who have been putting their money in savings and loan associations and have been financing the mortgages and have been taken to the cleaners. I believe that a period of relatively slow growth, of

higher unemployment running somewhere like 6½%, 7% for awhile would not be very damaging to the social fabric at all. That is what is called for. Not a Great Depression. A Great Depression like 1929-33 occurs only when you have a real monetary collapse, and there's no reason why we should have that.

you're saying, and what is true, is that anybody who bases his judgments about the character of the world or the character of events solely on what he hears in the TV news at night or what he reads in the paper in the morning does not have a very firm foundation on which to make his judgment.

**QUESTION:** Could you tell us the three steps you would positively take to combat inflation?

**MR. FRIEDMAN:** There's only one step that will effectively combat inflation. I don't have to give you three steps; I'll just give you one. That is, keep the quantity of money growing slowly. I'll be glad to give numerical values. What we have to do is to keep the quantity of money (M1) growing at something like 3% or 4% per year for the next two or three years. And by the end of two or three years, that would bring inflation down to something like 1% or 2% a year. It's easy enough to specify that. That doesn't mean it's easy to do. The real problem is not how to stop inflation, but how to make the measures needed to stop inflation politically acceptable. Because following that policy will have some consequences. It will have side effects, and some of those side effects will not be pleasant. We cannot stop inflation without going through a period of slow economic growth and high unemployment. Once we've stopped inflation, we can have high employment, we can have high growth, but we cannot go from a high rate of inflation to a low rate of inflation without going through such a temporary period. I hasten to add that we cannot continue on a high rate of inflation without going through one too. The great defect in most public discussions of this issue is the implicit assumption that there is some way to avoid these costs. You go to your physician and he says, "You've got appendicitis; you must have your appendix taken out," and you say, "If I have my appendix taken out, I'll be in bed two weeks." He says, "That's right," and you say, "Gee, I don't want to bear that cost." Well then, if you're a sensible man you'll ask, "What happens if I don't have it taken out?" He'll say, "Well, you'll

probably be in a permanent bed for a longer time.” That is the situation with this country. We are sick. Fundamentally, this is a very strong country economically, but we’re sick. We have the inflation disease. If we don’t tend to it, if we let it go, we’re also going to have unemployment, we’re going to have controls, we’re going to have a great many unpleasant things. If we stop it, we’re going to have a great many unpleasant things for a time. That’s the choice we’re faced with. That’s why I keep saying the problem of stopping inflation is political, not economic. The problem is having the political will to take these measures.

**QUESTION:** What do you see in the politics of today that leads you to say that someone will stand up and say this will stop?

**MR. FRIEDMAN:** Conventional political wisdom has it that inflation is less damaging politically than unemployment. That’s a heritage of the Great Depression. That wisdom is changing. The political situation is very different today than it was five or ten years ago, and it will still be different ten years from now. We know very well that Mr. Wilson in Britain lost his position in the first place some years back because of inflation, not because of unemployment. Mr. Heath succeeded him and lost his position because of inflation, as well. Mr. Tanaka in Japan is at an all time political low because of inflation. Mr. Allende in Chile lost his life because of inflation. The conventional wisdom is changing. As people have more experience with inflation and as the memory of the Great Depression fades farther back, in the future the political liability which unemployment incurs gets less relative to the political liability which inflation incurs. So when we’ll change is when the public at large is sufficiently aroused about the problems of inflation that it makes it politically advantageous to do something effective about it. Fundamentally, this is a representative government. There is a fundamental sense in which the people who produce inflation are the public. Not in the economic sense. That’s why all this business

major source of inflation. The major source of inflation, this time as every time, has been that the government has spent too much and printed too much.

**QUESTION:** Why should a free trader deal with a nation that places a surtax or boosts a duty?

**MR. FRIEDMAN:** Well, I believe that two wrongs don't make a right. In the case of a communist collectivist country in which the government does the trading, my feeling is, I don't want, as a government, to subsidize them whatsoever. Indeed, if they are regarded as a present danger, I may want to restrict trade in weapons, or things like that. But we're not talking about that for the moment. With respect to the rest, it seems to me you have to make the best deal you can with them, provided you get paid cash on the barrel-head. Let us turn from that to the common market, which has been trying to erect a wall around its agriculture. They are hurting themselves by that wall. There's a strong temptation to say, "Well, we can't have free trade if they don't have free trade. If they put up barriers, we have to put up compensatory barriers." But it turns out when you analyze it, that by putting up these additional barriers, we hurt ourselves as well. We are best off if neither they nor we have barriers. If they have barriers, we are next best off if we don't have any. And we are worst off if we both have.

**QUESTION:** What should we do with India and Bangladesh who are without gold to pay for commodities?

**MR. FRIEDMAN:** In the first place, charity is an individual matter and not a governmental matter. More honor to those people who in their private capacity contribute of their own funds to help out the people of Bangladesh and the people of India who are poor. I have long been opposed to foreign aid on our part to those countries. I have been in India; I have studied the situation in India. I am

myself personally convinced, and I wrote to this effect more than ten years ago, that our foreign aid has done India tremendous damage, that India would be far better off than she is, if we had never given her a penny of governmental foreign aid. The reason is that our foreign aid doesn't go to the Indian people. It goes to the Indian government. The effect of our foreign aid is to strengthen the Indian government against the people. The reason why India is in the terrible and tragic situation that it is now is because it is misgoverned and because free markets are not permitted to prevail. India has tremendous potential. India could be an economic miracle, but it isn't because of the strait-jacket of governmental control coming down from New Delhi. And we have contributed to that strait-jacket by subsidizing the government and its policy. I think that foreign aid for charitable reasons is not an appropriate governmental function. It's a private function. If I want to give charity, I should give charity where I want to give it out of my own resources. I am not being charitable when I take from your pocket to give a third person. I have said for many years that I am in favor of an eleventh amendment to the Bill of Rights. And that eleventh amendment should be that everybody shall be free to do good — at his own expense.

**QUESTION:** Should we be listening more to news media as authentic and honest sources of news?

**MR. FRIEDMAN:** Well, obviously you must express your own judgment about what you think is authentic and what you think is honest. Obviously, you cannot automatically assume that just because you read it in the newspapers it is true. I suppose your own experiences have shown you that that isn't the case. I think you are pointing to a very real thing and a thing that does occur. One of the problems is a tendency for hysteria to take the place of thought and analysis. Right now the oil crisis is a great crisis. A year ago it was a meat crisis. Next year it will be something else, and nobody remembers what happened to the last crisis. So I think what

concerned with credit and the rate of interest. The other view is that it's concerned with money and the quantity of money. So far as money and the quantity of money are concerned, the rate of growth of the quantity of money was at a fairly rapid rate until about June of this past year. Since June, the quantity of money has grown hardly at all. In that sense, monetary policy has been tight. It has shifted from a rate of growth in the quantity of money (M1) of about 7% a year to a rate of growth of nearly zero in the past four or five months. From the point of view of interest rates, interest rates have been higher for a much longer period of time. Indeed, interest rates have been coming down, and the short term interest rates have been coming down in the past two months or so. If you judge tightness or ease in monetary policy by interest rates, you have to say that monetary policy was extremely tight beginning a year or more ago when interest rates started to go up. There is still a difference of opinion among economists about whether to use interest rates or the quantity of money as a criterion of tightness. But that difference of opinion is less now than it was a few years ago and is declining. An increasing fraction of economists agree that the relevant thing to look at is the quantity of money and not the interest rate. In fact, high interest rates are almost always a sign of easy money, not of tight money, because interest rates are high when you have inflation, and you have inflation when you increase the quantity of money too rapidly. Thus high interest rates are a sign that money *has been* easy.

**QUESTION:** Would you care to predict the price of gold at 10:00 a.m. on the Fourth of July, 1976?

**MR. FRIEDMAN:** Yes, I shall be glad to do that. It will be three times the price of soybeans, provided you let me pick the unit in which I'm going to measure the price of soybeans.

**QUESTION:** Does the size of our agricultural production have any impact on the inflation rate at all?

MR. FRIEDMAN: Very little. There is a great deal of confusion between relative prices and the absolute level of prices. Many people talk about a rise in a particular price as inflationary. People are kind of schizophrenic about this. I have yet to see any headline in the newspaper: "Decline in the cost of computer service is deflationary." Have you seen that headline? The cost of these hand-held computers has come down in the past two years from about \$100 to \$20. I take it that we should suppose that that produces deflation, but nobody points to it. There's assymetry in reaction, and this is your point. Inflation has to do with the average level of all prices. Let's suppose that food prices go up. This means that people have to spend somewhat more on food. This means they have less to spend on other things. Up to that point there is no reason why the average price level should be affected. But, let's suppose that the rise in the price of food occurs because of a short crop. Well, then there is a little reason for the general price level to be affected, because a short crop means that people's total real income is a little less than it was before. There are fewer goods to buy matched against the same dollar income, and therefore there is a reason for the price level to be a little higher on that account. Let me illustrate that more exactly with oil. Everybody has pointed to oil as a source of inflation. The reason why everybody has pointed to it is because everybody likes to find excuses. I have yet to hear the Central Banker or the Secretary of the Treasury in this country or any other country stand up on the podium, and beat his chest and say, "I produced the inflation." I haven't found that man yet and you haven't either and you won't. Now, he says that it's the Arab oil people who produce the inflation. Let's look at the magnitudes. There's no doubt that the Arab oil cartel by reducing the production of oil has produced a shift of real income from us to them. We are poorer. By how much? By 195%. That alone would justify a 1% percentage point rise in the price index number. To that extent you could argue it is a source of inflation. But both the rise in the price of food and the rise in the price of oil have not been the



That's what has happened time and again with these rapid bubbles. I suspect that's what is going to happen again. So during the next six or nine months, there will probably be a decline in the rate of inflation to something like 6%.

There are already some signs in the declining prices of sensitive commodities and in various other indicators. When that occurs, everybody will breathe a sigh of relief and say, "Oh boy, we've got inflation on the run."

We will have things like Olsen's article in yesterday's *Wall Street Journal*, the headline of which was "Inflation Has Been Whipped." He was giving essentially the same analysis as I am but he was drawing from it the conclusion that inflation has been whipped, which was a wrong conclusion.

REMEMBER, inflation was going at the rate of 4½% in August, 1971, when President Nixon felt impelled by political pressure to impose wage and price controls in order to stop inflation. People get accustomed to things, and when they discover it's 6% instead of 12%, everybody will be joyful, although it's an intolerable rate of inflation for the long run. The real lesson to be drawn is that that's when we have to keep on drawing in the belt in order to get the rate of inflation down to a level we can really live with. But that won't be the reaction. The reaction will be that we're going to have to do something about the unemployment which will undoubtedly accompany the continued slowdown, recession, sidewise movement, or whatever you want to call it, in which the economy is engaged. So there will be enormous pressure from Congress, from the public, from everybody, to do something about unemployment. There will be a pressure for more and more government spending, there will be a pressure for the Federal Reserve Board to open the monetary gates and turn the printing presses faster.

If that occurs, as it has before, initially it won't keep inflation from staying down at 6% because it takes time before monetary expansion has an effect on inflation. It will start an expansion, and we'll start overcoming the recession. Employment will

start going up, but then by early or late '76 we'll be off to the races again. Inflation will start to heat up again. And that's the point at which there will be great pressure to put on price and wage controls. "We've been having such good success holding down inflation," people will say, "we can't let it get away from us now."

The first step has been taken, namely the establishment of the Council on Wage and Price Stability. The Director of it is an excellent man, an alumnus of The University of Chicago, a former member of the faculty of the Department of Economics of The University of Chicago, who does not believe in wage and price controls. But we have seen before, how people who do not believe in wage and price controls may nonetheless be forced by their political masters to impose it. And that, I am afraid, is the scenario in store for us.

Where that will ultimately end, who knows? The only reason for hope is that we don't know where it will end. If we were sure, I'm afraid what we would be sure of would be that it would end in disaster. But somehow or other, historically we have been very bad predictors about how those forces work themselves out. All I can say is that as of the moment it looks as if we're in for another roller coaster ride down to something like a 6% rate of inflation, and back up to something like a 15 to 20% rate of inflation. We don't have to do that. It's perfectly easy to stop inflation, if we really had the will to do it, but we don't have that will. That, at the moment, is what I'm afraid we're in for. Thank you.

**QUESTION:** Why is there a great divergence of opinion among distinguished economists over the last six months on the tightness of money supply?

**MR. FRIEDMAN:** There is no great divergence of opinion among economists as to the tightness of the money supply. There is a great divergence of opinion about how to define the tightness, about what to look at. There are, and have been for 150 years, two views about monetary policy. One view is that it's

always involve restricting free markets and restricting free men.

The most important of these false cures for inflation, is, of course, price and wage controls. It is a false cure because as everybody here knows it doesn't work and never has worked. It's interesting to note why it's introduced. People always ask the following question: "How come the government officials in Washington or in England or in France are so stupid? You say that price and wage controls have not worked in 2000 years. Yet here are all these smart officials. They know the history as well as you do. Why do they impose price and wage controls?"

The answer to that puzzle is very simple. Price and wage controls are always imposed by a government that wants to produce inflation but wants to give the public the impression that it's doing something against inflation.

Of course, government officials are not so stupid as to think that controls are going to work. They know the history of price and wage controls. They know that whenever they are imposed, they seem to be successful for a time, because they suppress inflation, but then pressure builds up and prices explode. That's what's happened every time.

But if you are a political official you tend to have a very short time horizon. You're looking forward at most to the next election, and you hope that maybe the price and wage controls will repress inflation long enough. At the same time you want to produce inflation. You are trying, somehow or other, to expand government spending or print more money in order to produce an appearance of prosperity, or to eliminate unemployment, or to produce euphoria before the next election, or more simply you're trying to do what the people want. What the public wants is for the government to spend, and also for the government not to tax. Well, if you're going to spend on the one hand and if you're not going to impose explicit taxes on the other, you're going to have to impose the hidden tax of inflation.

Fundamentally, that is the reason you have inflation, because the public at large has asked for

inflation. At the moment President Ford says — and I'm sure he is sincere — that he is completely opposed to price and wage controls. And yet, as a realist, I believe that there is at least a 50/50 chance that within two years we will have price and wage controls.

**THIS IS NOT** something I welcome. I'm not telling you what I'd like to have happen; I'm trying to be realistic and tell you what is in fact likely to be in store. Currently the index number shows the rate of inflation running at something like 11% to 12% a year. I think the chances are very great that within the next six to nine months that rate of inflation is going to come down very drastically, not because of the new economic program that President Ford has proposed, but because of what's already in the pipeline, because of the fact that this 11% or 12% is something of a bubble. The basic monetary and fiscal expansion of the past five or six years, which has been highly inflationary, has not been that inflationary and does not justify an 11% or 12% rate of price rise. You have an 11% or 12% price rise partly because of the unveiling of some of the price increases that were repressed by price controls, partly because enterprises have been making precautionary price increases in fear of future price controls, partly because of the widespread inflationary expectations which lead people to get out of money into goods. All of those are temporary .

The basic underlying monetary expansion of the past three or four years would justify something like a 6% or 7% per year price increase. That's the basic built-in inflation in our system. As these temporary phenomena disappear, we're going to come back down to that.

Historically, bubble inflations have broken as fast as they have risen. Take the most obvious example of the Korean War inflation. I've forgotten the exact number, but I think the rate of rise of wholesale prices came from something over 20% to roughly zero in six months.



dom of choice about how to spend their money.

That's what all of us should have been saying in the newspapers at the time. That's what you people should have been asserting: "Don't hurt the consumer by this measure. We want freedom of markets, because it's in the interest of the consumer."

Now free markets are on the defensive. They are on defensive here; they are on the defensive all over the world. Why? They are on the defensive not because they haven't worked, but because they have worked. It's precisely because every time political authorities have tried to do without them, they have gotten into trouble. The only way political authorities have found to pay for their mistakes is to try to take advantage of the free market by interfering with it and by controlling it.

The long-term trend has clearly been toward greater governmental control. I've cited the figure of 40% as the percentage of our national income being spent by government. That number was 10% in 1929. It's gone up from 10% to 40%. If you want to look forward to the future, I will predict one thing with absolute certainty. That will not happen again. The percentage cannot go up to 160% in the next 40 years.

But the trend is still going on. It's 40% in this country; it's 55% in Great Britain. We're about 15 years behind Great Britain, and we're heading in that direction. The increase in government spending relative to the total has been accompanied by an increase of government interventions of all kinds, most recently, price and wage controls, which were abolished temporarily, the establishment of a commission that these markets are going to be subjected to, and so on.

**I WANT** to leave the long-term trend, about which you are aware, and talk about the short-term situation. Let's look forward and see what's coming in the next few years. Public Enemy Number 1 is supposed to be inflation. And it is. Inflation is a serious and very important problem. From the short term point of view, the worst thing about inflation is the false cures which governments adopt and which







which in the political world would not, in fact, be enacted.

I don't say this for the moment in criticism of anybody. I'm very much disappointed in the program. I hoped it would be more than that. I can understand why President Ford came out with this particular program. Maybe he was right to do so. I'm not making a political point. Maybe I'm all wrong about the character of the program, but surely the view I'm expressing, that this program is not an effective program suited to the needs of the time, is not a wholly foolish view, and you might expect that in the ordinary course of events there would be at least a few people who would hold that view. Have you heard one stand up and say that? You have heard one business leader after another stand up and say, "Well this is a statesman-like, decent, attractive program. It has some possibilities. We will cooperate with it." Why have you heard no businessmen stand up and attack it? Because a businessman would be foolish to do it. He would be false to his duty. He would be violating the interests of his stockholders if he stood up and talked like that. Because there are too many legal and extra-legal ways in which the government could crack down on his corporation.

**Do WE HAVE** free speech on TV? Not a bit of it. Why is TV so bland? Of course it's slanted, but that's a slant that appeals to the powers that be in Washington. But it's bland. Why? Because government gives, and government takes away, licenses. And every TV station operates under the threat that its license might be taken away.

If, by accident, the television camera had been invented in the 19th century and the printing press in the 20th century, we would have no free press today. We would have a free TV in that case, but we would not have a free press.

We do have something of a free press, but even there we have some limits. We have something of a free press because of the accident that the press grew up at a time when there were free markets, and the press was not subject to control. You did not have to



So I believe that you cannot really say that free men make free markets. They may or may not. But you can say with great certainty that free markets make free men and that controlled markets destroy free men.

This is more than symbolism; it is reality. If you look at our historical record you will see that very clearly. It's interesting to contrast the tycoons of industry of the 19th and the 20th century. The tycoons of industry of the 19th century, at a time when we had truly free markets and almost no governmental intervention, were men of independent mind and independent thought who were willing to stand up and say what they thought and what they believed. They were willing to express their opinions on affairs, wherever the chips might fall. The tycoons of the 20th century are people who have learned how to get around Washington. The criterion of success is that you know how to butter up the right people in Washington and get the right governmental regulation, or laws, or interpretations .

**IF YOU WANT** to see the effect of the absence of free markets on free men, I ask you to contemplate the state of free speech in the United States today. How many people in the United States today enjoy freedom of speech in the literal sense, that they feel free to get up and say what they believe, honestly and freely without fear of the consequences? I believe that only those of us who happen to hold tenured positions in private universities are today pretty fully assured of freedom of speech.

If you are the president of a great corporation, would you really feel free to get out and express your frank opinions? Let's take a simple case. Here is a program designed to fight inflation that President Ford came out with recently. I have yet to hear a single major business leader in this country stand up and say that almost the whole of that program is hogwash. Which it is. It's not a program to stop inflation. It's a program which is a collection of goodies, mostly intended to provide benefits to special interest groups with some items tacked on which can be given the label of "anti-inflation" and







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# Free Markets for Free Men

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