



## **Filthy Lucre: Economics for People Who Hate Capitalism**

*Joseph Heath*

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"Economics is haunted by more fallacies than any other study known to man." -- Henry Hazlitt, *Economics in One Lesson* (1946)

Every day economic claims are used by the media or in conversation to support social and political positions. Those on the left tend to distrust economists, seeing them as friends of the right. There is something to this, since professional economists are almost all keen supporters of the free market. Yet while factions on the right naturally embrace economists, they also tend to overestimate the effect of their support on free-market policies. The result is widespread confusion. In fact, virtually all commonly held beliefs about economics--whether espoused by political activists, politicians, journalists or taxpayers--are just plain wrong.

Professor Joseph Heath wants to raise our economic literacy and empower us with new ideas. In *Economics Without Illusions*, he draws on everyday examples to skewer the six favourite economic fallacies of the right, followed by impaling the six favourite fallacies of the left. Heath leaves no sacred cows untipped as he breaks down complex arguments and shows how the world really works. The popularity of such books as *Freakonomics* and *Predictably Irrational* demonstrates that people want a better understanding of the financial forces that affect them. Highly readable, cogently argued and certain to raise ire along all points of the socio-political spectrum, *Economics Without Illusions* offers readers the economic literacy they need to genuinely understand and critique the pros and cons of capitalism.

## **Filthy Lucre: Economics for People Who Hate Capitalism Details**

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# From Reader Review Filthy Lucre: Economics for People Who Hate Capitalism for online ebook

## Trevor says

It was the subtitle of this book that got me in – ‘Economics for those who hate capitalism’. I’ve been reading a few books lately that have been economics for those who love capitalism and I was hoping that this would take to task some of the fundamental assumptions of free market economics and present some way forward for people who are sick of seeing obscene amounts of social product go into increasingly fewer hands while large numbers of the world’s population have nothing or, if they are particularly lucky, next to nothing.

That wasn’t quite how this book turned out. I don’t want to say that the title and sub-title are false advertising, the problems with the book being a bit more subtle than that, but the book wasn’t what I was hoping for.

There are effectively twelve chapters and an epilogue to this book. The first six are responses to rightwing fallacies – such as: it is all about incentives or it’s all about personal responsibility or that the government’s role in the free market is always negative. He then has six chapters on leftwing fallacies – such as, calls for equal pay miss the point, just prices aren’t possible and that perennial favourite of all egalitarian types, his countering of the idea that profits are always bad.

I don’t want to give you the wrong idea here; there were parts of this book I really liked. He starts off by talking about *Blade Runner* and how shocking that film seemed when it first appeared (another film I have always meant to watch). This was perhaps my favourite part of the book and the bit I’m most likely to remember from it. His point was that the film was set in the future and yet there are still advertisements. This is the opposite of what most science fiction up until then had taught us to expect the future to be like – fiction had assumed that in the future we would no longer need money; the future would not have profits, the future would be a kind of vision splendid of a communist utopia where people would be beyond the nonsense of competition, wages and other such things. *Blade Runner* presented a ‘dystopia’ where the future looked frighteningly like the present day, only more so. In fact, the shortest glimpse at the horror that is commercial television is perhaps enough to prove that the future vision of *Blade Runner* has proven to be much more accurate a depiction of our future than say *Star Trek*.

One of the core notions behind this book is that free markets are the most efficient way to organise production – naturally with some provisos (most notably around ‘externalities’, which we really need to come back to if I can remember). The problem with planned economies (say in the former Soviet Union and Eastern Block countries) from an economic view point (so, therefore leaving aside the other problems with freedom, democracy and such these societies had) was that economies are insanely complicated things. The problems with planning, as free market types never stop getting their kicks from pointing out, is that there are simply too many things to take into consideration for any centralised plan to accommodate. You can virtually be assured that the thing that you forgot or overlooked will suddenly be the essential detail that sinks your plan. That none of the books I’ve read then goes on to explain how businesses (multinational corporations, for example) with economies larger than most countries are then able work around and overcome these ‘planning problems’ (surely they have a centralised plan too...) is just one of the little mysteries of Capitalism I’ve never quite grasped.

Is there a solution to the dead hand of the socialist planned economy? Well, the solution isn’t actually to have no plan, but to completely decentralise economic planning by giving control over to the market itself.

The problem with socialist planned economies wasn't so much with the idea of planning per se, but with centralised planning. It is at about this point that people start to go on about bureaucrats in ivory castles (though the people in charge of say IBM are never referred to as either bureaucrats or living in ivory castles for some very strange reason). Capitalism's advantage here is taken to be the free market, where, because of self-interest, all of the agents in the economy act locally and this means globally we end up living in the best of all possible worlds.

Given this glorious vision of the free market we then get the string of rightwing myths such as, all government interference in the market is invariably bad and counter-productive (ending up hurting those who it was supposed to assist). Rent control laws are a favourite whipping boy here. The point being that the market is supposed to automatically respond to a shortage of housing by putting rents up – this then attracts investment and thereby increases the amount and quality of housing stock available and then makes everyone happy – smiling faces all around. The essential piece in this puzzle is the initial increase in the cost of rent – but then governments (read: evil do-gooders) come along and think they are helping the poor by controlling the increase in rents (read, stopping rents going up the economically appropriate level). This creates disincentives for people to invest in the supply of rental accommodation and therefore makes the problem the policy was seeking to address all the worse.

Where I found this book most interesting was where it sought to explain how to combat the 'red in tooth and claw' aspects of capitalism without undermining the efficiency of market capitalism. He does not, for example, accept that there is a huge pair of scales with efficiency written on one side and equality on the other and that more of one invariably leads to less of the other. He doesn't accept that markets can be left entirely to their own devices. As it seems with most things today, it is all about reframing the debate.

He makes the point that Capitalism would have been impossible without insurance, for example. Without government guarantees over bank deposits and the ability to militate against runs on banks and the subsequent losses these runs would create, the consequences to investment would be catastrophic. So, he argues, the rightwing arguments against other forms of insurance, like say health care insurance and unemployment insurance, ring hollow given that they are more than happy to accept these forms of insurance that are organised by governments and benefit them in ways it would be difficult for capitalism to exist without.

Insurance becomes, then, a very important concept in this book and the main weapon to be used by those who hate some of the consequences of free markets. In a sense, this same logic works for finding market ways to add externalities to the economy. Externalities are an interesting example of market failure; the environment being a classic example. When you drive your car you pay for the petrol you use, but that doesn't cover all of the negative effects of your driving. You don't pay for the noise pollution or air pollution you help to create, nor the cancers you cause and so on. Externalities are examples of market failures and finding ways to fix them is an important role for government. Given our conservative party here in Australia has spent the last few weeks tearing itself apart on exactly this question (how to create an emissions trading scheme to work into the market some of the costs of our current high carbon diet) getting rightwing people to accept that the market isn't always and invariably perfect is a real problem and one that is likely to cost us dearly into the future.

All the same, other negative aspects of free markets mentioned in this book are just accepted as being inevitable and people are advised just to get used to them. Profits are good. Inequity in pay is good. Globalisation is good. Or, if not actually good, then the best that can be expected. As a case in point, let's look at the Economics 101 view of foreign trade and discover why all trade is always good.

The first point is that leftwing types often see trade as being something that is forced on poor countries by rich countries and is always in the best interests of the rich countries with the poor countries invariably being ripped off. The argument against this grossly negative view is that a country will only agree to trade if they can see they will derive some benefit from the transaction. Therefore, the fundamental assumption ought to be that trade is mutually beneficial, otherwise, why would the two sides enter into it?

Trade makes sense on the basis of relative efficiency. If the US can make 100 televisions and 200 washing machines in an hour and Australia can make 5 televisions but 100 washing machines in an hour it might be best for Australia to stop making televisions altogether – but it might also make sense for the US to stop making washing machines and direct all of its investment toward making televisions and just buy washing machines from Australians – even if we are less efficient at making both products. This is because the US is so much more efficient at making televisions and only somewhat more efficient than Australia at making washing machines. Getting both sides to make what they are most efficient at making means that both sides will be better off.

The ‘myth’ of trade is that it kills local industries, whereas, in reality, it kills off only those that can’t compete with foreign companies and redirects investment towards economic activity where the country has better skills and is therefore better able to compete. In fact, the whole competition idea with foreign markets is shown in the book to be a bit of a myth in itself, as when you trade people will only trade with you if you have something they want to trade for. I thought this reading of global economics was interesting (as I’ve found it interesting in other books I’ve read recently too) even if a little Pollyannaish.

That trade is seen as an unequivocal good seems to overstate the benefits while ignoring complications – something the left seem to be constantly accused of and ridiculed for doing in these books. With so many countries in debt up to their eyeballs, the US and Australia just two such countries, and with creditor nations like China prepared to lend well beyond our ability to repay (in the expectation we will keep buying their products), the simple balance of international trade discussed in most such books on economics seems optimistic at best.

The fact that about the only thing the US is able to trade on the international market is weapons also makes the appraisal of trade as unequivocal good also ring hollow. Our encouraging (via subsidies and other benefits) of third world countries to plant cash crops such as coffee, bananas, cocoa beans and the like and then our forcing them to sell these to us at low prices (often due to a glut on the market caused due to our initial investment which was done precisely to bring down the price of these commodities) all so we can sell the leaders of these countries guns to keep their local populations under control just doesn’t seem like something we should be very proud of.

There is also a section criticising Marx’s theory of surplus value, and this is the second time recently I have read something that implies that Marx said that the problem with capitalism is that workers are not given enough to ‘buy back the product’ of their labour. Both authors have then gone on to show how stupid Marx was for coming up with such ideas. The problem is Marx didn’t say anything like that at all. It is true that Marx saw that the cost of labour was less than the value that could be gained from deploying labour (and in many ways that is self-evident – otherwise why would a capitalist buy the labour in the first place?), but Marx’s solution wasn’t to give the surplus back to the worker – his problem with capitalism was that virtually all of the surplus went to the capitalist.

This is an interesting book, and yet another in a line of books I’ve been reading lately to give myself an education in economics – but I think I do need to read a book now that actually gives a leftwing view of these matters, at least, more than in just the title.

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### Suhrob says

There is a chance that one could rate a book like this high just because one agrees with it. I do agree with vast majority that is said here, but even if I try to account for this bias I still think it is an incredibly worthwhile read and arguably there is genuine attempt to be balanced (there are 6 fallacies both for left and right). Don't get turned off by the sensationalist title, this is a well thought through, reasonable discussion. Heath might suffer a bit of hindsight smugness, some points might be discutable, but I think it is even worth a second read (something I almost never do!).

Also a big plus for me is that the essentially the whole book is argued from the neo-classical standpoint i.e. not using the currently popular behaviourist approach (with a small exception of a discussing hyperbolic discounting and dynamical preference inconsistency). Heath even explicitly states his reservation to behavioral economics in the appendix (via the charity principle). I am much more open to the behavioral approach (if done carefully), but I think the first line of attack on most of these fallacies can (and should) be done from the more classical standpoint.

This concludes the review. Now the part where I unsolicitedly vent my frustration by using snippets from the book (aka Give me rampant intellectualism as a coping mechanism!)

*Meanwhile, other departments (like philosophy) find themselves turning away job applicants literally by the hundreds. The wage rate, which should be sending a signal to the effect that “the world does not need more philosophers,” is sending the opposite message. As a result, society must rely upon unemployment, rather than low wages, to deter entry into the field. Because of this, something of a “lottery economy” develops, where some people win big and most wind up with nothing.*

Oh yes, that does make me feel better! Fret no more, there are solutions too:

*With other sorts of employment, on the other hand—anything that is advertised as “pampering”—the waste of someone else’s time constitutes a significant element of that which is being consumed. This is why there are fewer maids than there once were but more massage therapists. The more expensive the other person’s time is, the greater the sense of luxury produced through the act of wasting it.*

May I interest you in our Feng Shui interior designers with PhDs? They study Dark Energy... you don't want that nasty stuff to flow through your appartement, clogging up your chakras, do you?

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### Craig says

A very simplified overview of the field of economics. With critiques of both left and right wing economic policies and theories. A fascinating and humorous introduction for a chap like myself who knows virtually nothing about economics. I'll probably read it again some day to remind myself.

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## **Ian "Marvin" Graye says**

### **A Contribution to the Critique of Political Economy**

What we now call Economics was once, at the time of Marx, called Political Economy.

One of the major achievements of this book is to reveal just how much political philosophy sits behind Economics, and vice versa.

The book is written from the perspective of the Left. Well, a Left.

It reflects a reasonable level of economic literacy. It acknowledges past errors on the part of both the author and the Left, and seeks to remedy them. In the words of one of the titles of the book, it seeks to remove illusions and debunk myths.

I approached the book with several motives and biases. Would it be consistent with my existing values? If not, would it help me to understand, reconsider or change them? If it was consistent, would it help other people to understand and/or embrace such values? Would it persuade or enhance the thinking of people on the Left? Would it persuade or enhance the thinking of people on the Right?

### **Some Critical Criteria**

The book isn't so much concerned with the comparative assessment of two or more economic systems (e.g., Capitalism and Democratic Socialism).

It's more concerned with the basis upon which today's version of Capitalism can be justified or criticised and, if it needs to be finessed to accommodate various political objectives, what are the economic consequences of such attempts to finesse it.

It made me ask, by what standards should we measure and assess the success or efficiency of any particular type of Economy?

I'd start off by suggesting two socio-economic goals:

- 100% employment (for those who want it); and
- a minimum subsistence wage.

### **Six Things I Like about this Book**

#1 The basic concept of the book is the debunking of six Right Wing myths and six Left Wing myths about Capitalism.

#2 The book recognises that Capitalism in some form or other is here to stay, that it isn't about to collapse because of internal contradictions, and that the prospects of a permanent revolution (whether Communist or Anarchist) are infinitesimal.

#3 The express goal of the book is to improve the arguments of the Left.

#4 The book recognises the importance of Economics to Politics.

#5 It seeks to find a common ground between the Left and the Right based on solid Economics.

#6 It wants to make Left-oriented socio-economic programs more economically effective and efficient (and therefore acceptable to traditional supporters of the Right).

### **Six Things I Don't Like about this Book**

#1 It's been published under two separate titles: "Economics Without Illusions" and "Filthy Lucre". The latter signals a skepticism about Capitalism and reduces the potential audience for the ideas in the book.

#2 It's been published under two separate sub-titles: "Debunking the Myths of Modern Capitalism" and "Economics for Those Who Hate Capitalism".

#3 There's a fair amount of subjectivity in the essays. Statements or theories with which Heath disagrees are described as obviously erroneous, mistaken or fallacious.

#4 Each essay is quite diverse and could have been broken into several separate essays. The six plus six format started to dictate the method of exposition, to its detriment.

#5 The lack of sub-headings detracted from the clarity and direction of a fairly difficult, technical and abstract subject matter.

#6 I question the book's ability to persuade a dyed in the wool Capitalist. To some extent, the book preaches to the converted, if indeed it can change the mindset of modern Left-wing, Anarchist or Green supporters.

### **12 Observations about Capitalism**

Below are some personal thoughts on Capitalism prompted by a reading of the book.

#### **#1 Selfishness or "Greed is Good"**

Capitalism opposes State intervention in the market. One way or another, it believes that the market can operate effectively for the common good without regulation by the State.

The market consists of individual people or entities acting, working, consuming, producing, trading or exchanging in their own interests. All of the participants act selfishly, arguably greedily, although they don't have to act solely this way.

Capitalism as a political philosophy isn't concerned about the selfishness or greed of the individual participant. It believes that across the economy as a whole the net result of individual selfishness or greed benefits society in the most effective and efficient way.

There is an averaging process at work. As long as on average it works, Capitalism is good for society. The net effect of all of this selfishness is the common good.

It doesn't matter that 20%, 40% or 50% suffer for the benefit of the rest. Any individual suffering is collateral damage that is justified by the common good. The suffering of the minority is justified by the

benefit of the mean (i.e., the average). The mean, alright. It's but a short journey to a destination where 80% suffer for the benefit of 20%.

Thus, the battle between Capitalism and Socialism is a battle between averaging and equalisation.

Capitalism describes the achievement of the common good by the market as the work of an invisible, almost divine, hand. The outcome is good and wise, even though it wasn't deliberately planned. In fact, planning is viewed as counter-productive and futile. The divine hand can achieve a better outcome than an office full of public servants and computer simulations.

Heath actually concedes that:

*"Historically...the way that Capitalism simulates socialist planning has been far more successful than any actual socialist system. The primary reason is that 'socialist planners' cannot be trusted to make the hard decisions that socialist planners are supposed to make."*

Any attempt to plan a different outcome is regarded as more deleterious to society as a whole.

## #2 Human Nature

Capitalism believes that selfishness is natural and legitimate.

Adam Smith wrote that, when a man acts in his own interest, "*he frequently promotes [the interest] of society more effectually than when he really intends to promote it.*"

At this level, there is a trust in human nature, a desire not to interfere in its natural processes.

On the other hand, when attempts are made to change how the market or Capitalism operate, the Capitalist argument is that human nature becomes a negative. There is a moral hazard that human beings will attempt to exploit the State-imposed system for their own advantage. They will be lazy, unmotivated and deceitful. It doesn't matter that the same humans, the same human nature, the same character traits occur under laissez-faire Capitalism, as long as the average is for the common good. There is no recognition that the human nature of the few might make no material negative difference to the common good. If 10% abuse the welfare system, does it undermine the effectiveness of the 90%?

We are asked to accept human nature in producers, but not in consumers.

## #3 The Market

The blind faith in the market and the invisible hand falls down when it comes to competitive behavior.

Selfishness means that no business wants to lose market share to a competitor, none wants to make a loss, none wants to be wound up.

As a result, the natural tendency of a business or of human nature is to be defensive. People lie, cheat, defraud, exploit, undercut, overcharge, misrepresent, overpromise and underdeliver. They abuse positions of power, they abuse monopolies, they form cartels, they collude, they conspire against the public.

These consequences of human nature under Capitalism, which are denied by its advocates, have to be

countered by legislative initiatives of the State. The market has to be forced to be honest.

The human nature of Capitalists cannot be trusted to run the market honestly or effectively. The market cannot operate legitimately or perfectly in the absence of the State.

The market, left to its own devices, will not only prejudice consumers, but other competitors.

The very failure of the market invites and legitimates the intervention of the State. If Capitalists were as virtuous as their apologists proclaim, there would be no need for the State.

The market has nobody to blame but the human nature of participants in the market.

One problem with State intervention is getting it right. The nature and extent of the intervention should be no more than is necessary to honour the promise of a perfect market.

#### **#4 The Goal of Full Employment**

The primary goal of Capitalism is not necessarily to employ people. That is a by-product of what Capitalism does. If it could better achieve its primary goal (making more capital) without employing people, then it would and does do so (e.g., by the use of machines).

Thus, if we assess Capitalism by whether it achieves full employment (one of my socio-economic criteria), then we are judging it by an outcome rather than a goal. It shouldn't really surprise us that it will never get a mark of 100% in this test.

#### **#5 The Effect of Competition on Prices**

In the same way, I don't think that it is necessarily a goal of Capitalism to reduce prices payable by consumers. This is an outcome of one aspect of competition.

The natural tendency of Capitalism (built into the human nature of a capitalist) is to charge whatever price you can get away with, whatever people are prepared to pay.

Thus, an unrestricted monopoly will inflate its prices, unless some restraint is imposed by the market or the State or people simply refuse to buy their product.

The more there is effective competition, the greater the commercial pressure to reduce prices (or differentiate in terms of quality).

The more we save money on some products (through lower prices), the more we have to spend on additional products.

We still spend the same amount of money, only we spend it on a greater diversity of products and capitalists. As a result, a greater diversity of people are employed in the process. However, because the amount of money being spent remains the same, the wages of each employee across the diversity of employers might be reduced.

#### **#6 The Effect of Competition on Wages**

One aspect of pricing is the relative abundance or scarcity of the input. The more scarce it is, the higher the price.

People who want work are theoretically abundant. Because full employment is not a goal, people and employees are treated like any other input. The abundance of potential employees reduces wages.

Unemployment is Capitalism's way of reminding us that we are abundant. It can maintain that it can't employ us all. If we all want a job, then we will all have to drop our wages. In a sense, the same amount of money has been allocated to the same total wages bill. We can either have unemployment and higher wages, or full employment and lower wages.

If the goal of Capitalism was full employment, it would go about things in a different way.

Heath tells an apocryphal story about an engineer who witnessed Chinese workers building a dam with picks and shovels. He asked why they didn't use equipment. The response was that this would destroy many jobs. The engineer said:

*"I thought you were interested in building a dam. If it's more jobs you want, why don't you have your men use spoons instead of shovels?"*

## #7 The Price of Goods and Services

Prices are determined by an attempt to recover the cost of inputs and a projected profit.

Let's say that a corporation wishes to sell its entire inventory for \$100M.

The composition of this total price might be:

- \$25M rent, infrastructure and capital costs;
- \$25M material input;
- \$25M labour; and
- \$25M projected profit.

Thus, the aim is to make a 25% profit.

The problem is that the strategy will always come under pressure when the corporation encounters competition. If it doesn't drop its prices, it incurs the risk that it won't meet its sales projections. If this happens, it mightn't meet its profit projections.

The question is what happens if the shareholders and management don't want the shareholders' dividends (their profit share) to drop? If it is to remain constant, then one of the other three inputs in our determination of the price has to be reduced.

Of the three inputs, two are supplied by other Capitalists, one is supplied by the workforce. There is often less bargaining power with the other Capitalists. They want to maintain their pricing, and might even have entered into medium-to-long term supply contracts (property leases, loan agreements, supply agreements that

guarantee the price of their goods or services).

Thus, Capitalists insulate themselves from the risks, and the burden of cost-cutting falls to workers. You either have to reduce your individual wages or some of you will lose your jobs.

## **#8 Minimum Wages**

Capitalists can deal with this challenge far more easily by dropping wages or sacking staff, because employees negotiate their wages and working conditions on an individual basis. They have little bargaining power with the corporation. They certainly don't have the same bargaining power that other Capitalists have.

One way they try to increase their bargaining power is to leverage their collective power through membership of a trade union. However, Capitalism despises this challenge to their bargaining power.

The other way to get a fair wage is for the State to legislate a minimum wage. This works against the logic of Capitalism's desire to let market competition determine relative wages. However, in a way, it achieves the same level of insulation as the input of other Capitalists into the price mechanism have achieved.

Naturally, Capitalists argue that, if there is a minimum wage, they won't be able to employ as many people. Therefore, a minimum wage will result in greater unemployment.

Remember that the goal of Capitalism is not necessarily to achieve full employment. The problem of unemployment is somebody else's problem.

Of course, one other response to a minimum wage would be to reduce the proportion of one of the other inputs into price to compensate. A one percent increase in wages could be offset by a one percent reduction in profit. However, this is out of the question. It interferes with the primary goal of Capitalism, which is to generate more capital from the capital we already have.

## **#9 Unemployment**

Whose problem, exactly, is unemployment? Whose fault is it? Is it the fault of the employee that there aren't enough jobs to go around? Are you a useless piece of shit because Ayn Rand's Objectivist acolytes want to throw you on the scrap heap?

The Social Welfare State deals with the issue by providing unemployment benefits. Perhaps this involves an element of empathy, altruism and charity that is bad for Capitalism or society as a whole.

However, the benefits all get spent on rent, groceries and other essentials, which are provided by Capitalism. Thus, the benefit is effectively a safety net for business. It just keeps the money flowing in the system.

Of course, the benefits are funded out of the taxes we all (including corporations) pay. Thus, collectively, we bear the financial burden of Capitalism's failure to provide full employment.

Once again, the State remedies a failure of Capitalism (even though Capitalism declines responsibility for full employment).

## **#10 Production as a Joint Venture**

Of the three inputs into price, two are external (often on contract), and only one (employees) is internal, even though they might be engaged on employment contracts.

Because they are internal to the corporation, most management still views the relationship as a master/servant relationship. There is rarely a sense in which the relationship is a joint venture aimed at jointly succeeding in the market.

Marx justified much of his theory of the internal contradictions of Capitalism and the inevitability of Revolution and Communism on the exploitation and alienation of workers that occurred/occurs under Capitalism.

I think this could be ameliorated, if the relationship was seen more as a joint venture, and the input of an employee given the same respect as the input of another Capitalist.

## #11 Profit

Many people on the Left regard profit with suspicion. They think it is a form of theft. Before property can be theft, there must be profit, which Marx regarded as the surplus value created by labour.

There has been much recent criticism of Marx's theory of surplus value. However, it wasn't unique to Marx at the time he espoused it, and all of its advocates have had to make room for greater understanding of pricing.

I think that profit is the product of all of the inputs mentioned in the price mix, even if the root cause of much Capital might have been somebody's personal effort or labour. The thing is that, once capital exists, it wants to multiply. Capital wants to make more capital. It takes money to make money.

I don't dispute the legitimacy of profit. I do, however, advocate different ways of sharing it around. It's perfectly acceptable for capital to earn an appropriate return of investment. Let's say that is 20%. That 20% then becomes available for expenditure on goods and services, the suppliers of which employ people and pay taxes. So the profit goes around in the system.

However, if we set a target of 20% and achieve a superprofit of 25%, I think capitalists should be prepared to share some of the surplus with the people responsible for creating it. Arguably, this should be not just the management team, but the whole staff.

Thus, I think profit is necessary not just to compensate capital, but to incentivize and motivate the joint venturers (including staff).

## #12 Taxation

Just as the Left has had to give up on the idea of a revolution, the Right has to give up on the abolition of the State. In fact, this is a reality that Capitalists, Socialists, Communists and Anarchists all have to recognise. It ain't going to happen.

That doesn't mean that the existence of the State is an excuse to squander taxpayers' funds. There has to be clarity about what the State has to do, how it will do it most efficiently, how much it will cost and how it will be funded by taxation. A budget needs to be set, just as if we had established a corporation to carry out the task.

One of the many insights I got from Heath's book is the view that the State is a consumer, but that it is effectively a mandatory collective consumer on our behalf. It buys things that Capitalism and we as individuals mightn't have been able or prepared to produce or buy (e.g., roads, hospitals, police, health care). Hopefully, by buying collectively, it is able to leverage its bargaining power and buy so more cost-effectively. Heath writes far more eloquently and persuasively on this topic than I could in the space that I have allowed myself. His book deserves to be read for that reason alone.

Taxation is also a vehicle for achieving some redistribution of wealth. Heath argues convincingly that the State should not manipulate prices. Equally, it shouldn't be too punitive in its taxation of Capitalism or those who make more money because, perhaps, they have displayed more initiative.

Personally, I don't believe in achieving financial equality, especially by pulling the top income earners down to the level of everybody else (i.e., "leveling down"). However, I do advocate a progressive tax system, so that those who earn more money pay more taxes.

I also advocate a minimum wage, that would be at least enough for a subsistence standard of living for a couple with two children. The goal is to pull people up, rather than pull people down.

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## Szplug says

Joseph Heath debunks the myths of modern capitalism, hoping that, by doing so, this book's readers will gain an understanding of economics without the illusions that arise from tendentiousness and/or wrongful intuition: a bit of filthy lucre wherein we better grasp the lucre itself, as well as why the grime accumulates, how we occasionally mistake the lucre as being grimy, and that washing off the grime doesn't always cleanse the lucre.

Heath is a lefty himself from way back, and one who, as he notes in his thoughtful introduction, held many of the Left fallacies he explicates in detail, ere exposure to center and right-thinkers in the course of his university profession revealed how ignorant of the economic bases he actually was. Thus, despite its split into six fallacies held by and addressed towards either side, it seemed clear to me that it's the *Gauche* ones into which he pours the better strength of his spirit: basically, he desires left-oriented ends, but despairs of the means and arguments that are typically pursued and presented by his fellow progressives; and which, in his estimation, tend to arise from a lack of understanding of how modern capitalist economies work, and that certain ameliorations or extinctions are simply not possible—or, at any rate, not without debilitating effects and consequences. That's not to say it isn't a useful primer for the reader of any particular political stance—rather, that the unveiling of the right fallacies strike me as being less-aimed towards achievable goals, whereas Heath believes in progressive reform and hopes that the exposure of fallacious thinking will channel those efforts into better achievable results. I once heard Heath state, in a Bloggingheads conversation with Will Wilkinson, that over the years he had gradually come to the conclusion that *John Stuart Mill was right about everything*—a tongue-in-cheek admission that nonetheless illustrates how utilitarianism seems prone to filling the abscesses left by deflated enthusiasms, tempered optimisms, and diminished radicalization.

I took 1 1/2 pages of notes of the right ones, and nearly 3 full ones of the Left (JN-M, with the best of intentions, created a monster) and which—in a move that will shock absolutely no-one—I am including below. This probably reflects that the latter six are both more interesting in their timber, and that they are ones I used to be more strongly aligned to, and, hence, would stand to learn more from in having their

erroneous natures clearly revealed. And clarity is both what Heath strives mightily for and impressively achieves: his analogies are superb, his foundation-laying thorough, and the impartiality he musters for his logical presentation appreciable and appreciated. Those with a mid or high level understanding of economics might find all of what he covers to be nothing new, but for those others, like myself, whose grasp is never better than middling and tenuous, oftentimes emotionally driven, the entirety of its contents went a long way towards clearing the miasmatic air of the dismal science.

Two extra chapters that Heath wrote for the book but decided against including:

*Spare the Rod, Spoil the Child.*

*More Democracy.*

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Heath opens the book by disparaging Naomi Klein for intellectual laziness and illiteracy in favor of the aura of activism once again. Old reliable!

## **FALLACIES EXISTING ON THE RIGHT:**

*Evolution does not optimize.* Individuals cannot be counted upon to do what is necessary to promote their own interests as a group. *What is good for the individual is not necessarily good for the group/species.*

There is an element of irrationality in our moral and legal reasoning. The *consequentialist* position, wherein outcomes are evaluated only in regard to one's actions is a minority position.

Capitalism does not derive from *Spontaneous Order*—it requires a state to secure even the most basic conditions of private property, free exchange, contracts—and inevitably comes to require more of the state to solve *Collective Action Problems* via various social programs. Which of these latter to pursue is not a function of ideology and preference, but of reasoned, evidentiary consideration—it is not *Natural* but rather of *empirical questions regarding the occurrence and severity of collective action problems*, that is, *Prisoner Dilemmas*.

**Extreme Incentive Bias:** *People have a tendency to overestimate the importance of external incentives in motivating human conduct.* In particular, we are prone to overestimating them in regard to *power, money and status*. External incentives do matter; but such as morality and social norms also act as a constraint upon human conduct.

Welfare states are *incentivized* to streamline and tighten their tax systems to maximize revenue and minimize evasion and growth-inhibitors (taxes on corporations and investment). These last two combined are also why governments prefer to tax dividends and make debt interest payments tax deductible.

Humans are incredibly complex psychologically. Behavioral Economics must be taken into account to explain why Standard *Rational Actor* models sometimes get things wrong. Behavioral Economics has not proven itself to generate results with the same explanatory and predictive power of the Standard Economic Model, but it is a real influence on incentives—external incentives aren't everything and incentives can be very complex business.

Economists use *efficiency* to describe outcomes—not means—where one person's satisfaction cannot be increased without worsening someone else's. For example: kid's exchanging candy at a party; shoppers

picking cashier queues at supermarkets. The *Invisible Hand Theorem* states that a perfectly competitive market—ie, all market exchanges as per above—will generate a perfectly efficient outcome. The *Second Best Theorem* of Lancaster and Lipsey, which Heath describes as *one of the most powerful arguments against laissez-faire capitalism ever invented*, stands potently against the IHT mentioned directly above: with respect to perfect competition, the more conditions you satisfy—short of satisfying them all, which is an impossibility—the *farther* you get from the ideal of perfect efficiency. *The argument for market solutions must be made on a case-by-case basis—it cannot be derived from an abstract model of how an ideal economy would function.*

Neither the state nor the market produce or consume anything—they are rather the institutions through which people coordinate their production and consumption.

Taxes are, in essence, *club fees*: as with condo or health club fees, what you pay is spent collectively to pay for all that is offered *for free*; and they are mandatory because their benefits are relatively non-excludable. One of the goods that can be purchased most efficiently in this way is insurance—the larger the pot, the larger the gain for the individual. Taxes are simply the financing of your own consumption, and your money will be spent on club goods instead of private goods. With taxes, what we should ask is if the benefits that come from the formation of an optimal sharing group outweigh the costs that we associate with it. Tax deadbeats are just like market frauds—an expense of market exchange and consumption.

Heath conducts a great discussion of club goods like state pensions as pooled annuity purchases, an instance of insurance—whereas what those who wish to privatize pensions are asking for is individuals to invest money in the market to fund their own retirement. This is an attempt to change apples into oranges, with much different risk levels and optimization points, and this should be the *first* thing factored in any discussion about doing so.

Final note on taxes: the state does provide limited choice and limited right of exit (to opt out) because they are mandatory—but choice can often be *tripped-up* privately and there is also a limited right of exclusion to balance this. This is a reality that tends toward bringing peace of mind, an effect that most people unjustly discount.

Heath is solid on how to conceive of free trade: countries *exchange* with one another, they do not *compete*—only companies do so. Free trade basically is an exchange of vouchers—currency—that can *only* be used to buy goods or services from the other country. Even if these *vouchers* are exchanged for other currency, at some point down the line someone, somewhere, will want them to buy goods and services from the issuing country. The sole exception to this is the US Dollar—but currency muddies the picture, and ignorant people believe, erroneously, that countries are structured like and compete with each other like corporations.

Free trade is all about *comparative advantages*: our productivity, a nebulous measure of all the factors of growth that cannot be accounted for, has a bearing only within a country: Detroit auto-workers compete with Iowa farmers for car production, not with Japanese auto-workers.

*There are two ways for Americans to produce automobiles: they can build them in Detroit, or they can grow them in Iowa. Growing them in Iowa makes use of a special technology that turns wheat into Toyotas: simply put wheat onto ships and send them out on the Pacific Ocean. The ships come back a short while later with Toyotas on them.*

Productivity helps give comparative advantages to certain sectors. Countries *do* compete for foreign investment, and the factors involved vary, depending upon the industry in question. English speakers, high-

skilled/quality native craft, mandatory risk-pooling, patent laws and copyright protections for intellectual property, local and national culture, etc, may all or in part contribute to making one country more attractive than another. What is important is that comparative advantage comes about through *differences* between countries—in fallacy, the Left misunderstands this to seek trade restrictions; the Right misunderstands it to seek the pauperization of labour.

Insurance comes from pooling risk, so that the bell curve of outcomes has a decreased *variance*. This pooling is intended to increase win-win efficiency gains. Examples can be found in two Canadian provinces: Saskatchewan is mostly farming country with stringent weather and a single-crop season, so pooling risk is a popular solution. On the other hand, Alberta, with an industry mostly comprised of ranching and oil, faces a larger threat from theft—so property rights become paramount therein. Moral hazard comes from the *disincentives* created by risk pooling, the tendency for *free riders* to avail of the efforts of others from the spreading of risk—this tends to shift the bell curve so that the hazardous left-right extremes, of previous low incidence, become more likely. Reason says that moral hazard, though real, should be managed, because the benefits of risk-pooling mostly outweigh the costs of moral hazard (a rather relevant exception? Exotic Investment Vehicles and their insuring prior to the crash of 2008).

Heath offers good stuff on the Left and Right perceptions of moral hazard among the *lower-classes*, or rule-breaking based on ideology and views on responsibility. While perverse incentives and moral hazard are serious, the question asked should be do the benefits of pooling *poverty* risk outweigh the costs? If you allow private property, then you have to accept some theft along with it; if you want insurance, you have to accept some moral hazard as well. Insurance and actuarial sciences have accompanied the stable rise of Capitalism. Most right-wing decrying of the welfare state is actually aimed against insurance. Moral hazard is an inescapable part of insurance and risk-pooling schemes; and insurance lubricates our economic systems. What's more, the government welfare programs tend to all be of the *insurer of last resort* type, where private insurance would face asymmetries and information problems and inevitably fail. That the latter proves the case is shown by Heath in a well-delineated walk-through of all of the interconnectedness and complexity of the finance industry during the housing bubble, and how the burgeoning asymmetries made the gauging of actual risk difficult, and the payouts demanded during the collapse impossible. In similar manner can the case be made for government-operated insurance pooling for such expensive, complex, disincentivized and information-intensive industries as healthcare.

## **FALLACIES EXISTING ON THE LEFT**

*To come when I summon the energy to enter once more into the chicken coop.*

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### **Kevin Vejrup says**

The book is written by a Canadian philosopher. It scrutinizes economic arguments in the political debate. It does so without any technical difficulties, and by very well formulated and intuitive argumentation.

Interesting that paper recycling can reduce amount of trees, as vegetarians reduce cow population, and that car safety increases cancer due prolonged life expectancy. Ch. 1 explains the fallacies of libertarianism in extreme form, that is why we need a government. Ch. 2 claims that economists overestimate the importance of incentives, exemplified by controlled experiments where people act unexpectedly. Extensive welfare state may be inefficient due to high taxation, but regains efficiency by social programs such as maternity leave, which cause higher labor force participation and lower population growth. Ch. 3 exaggerates the second best

theorem. Ch. 4 suggests an educational effect by replacing government with all of us. It equates public and private markets, arguing no effect of tax cuts, without accounting for differences in efficiencies. Ch. 5 states obviousness about international trade. Ch. 6 suggests that socialist institutions might reflect risk pooling, which is counterweighted by moral hazard (relate it to Peter Singer and donations). Ch. 7 argues not to fiddle with prices, and thus that politicians tend to fuck up the economy. Ch. 8 explains features of companies/cooperatives, and argues that it is easier to have public control over private firms than over state controlled firms. Ch. 9 presents business cycles, to which he prefers a Keynesian solution. He eloquently refutes the idea of technologically induced unemployment. Ch. 10 justifies wages based on replaceability. This must mean that a constant immigration of unskilled labor cause extreme wage inequality. That occupations don't get squeezed out by increased cost. Ch. 11 argues that impatience (in consuming) cause poverty in industrial nations, explained by a discount function. He suggests restructuring incentives, to make future costs and benefits be accounted for presently. Ch. 12 is a discussion of equality and taxation. He blames status competition for the upper bound of happiness that we seem to have reached. Though status completion can be beneficial insofar as spending is for altruistic purposes.

Very good book that improves ones understanding of economics.

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### **Shoshannah Cohen says**

I read a paperback version, not an ebook. I read this both because I had liked something else by this author, and because I was hoping to learn more than I know, which is almost nothing, about economics. It was okay for that, but there were many points at which I wasn't sure how much was the author's theory and how much was based on seeing how people actually behave.

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### **Tim K says**

Real rating should be 3.5. This book had some very interesting viewpoints it also was very confusing and in my opinion sometimes also wrong viewpoints..... but the amount of new ideas that it gave me outweighed the not so good material.

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### **Jack Oughton says**

This made me rethink quite a few things I'd taken for granted in economics. I'm not sure how true a lot of the statements he makes are, but the fact it makes you re-examine your commonly held micro/macro-economic beliefs makes it worth a read. Quite interesting

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### **Westcoastsusan says**

So it turns out that 'hyperbolic discounting' is not actually an annoying debate technique but rather a description of the universal human tendency to over-weight near term costs and to over-discount long term ones.

We already know this about ourselves. We don't stick to our own virtuous long term plans; Yeah, we're better at it as older adults than we were as teenagers, but we 'sign up to show up' and lock ourselves in to accountability because we know; We know the power of appetite; We know that the horizon can seem infinitely far away.

Heath writes:

"A proper understanding of hyperbolic discounting [...] serves to dissolve much of [the] old-fashioned antagonism between liberty and paternalism. Many social policies that force people to act in their own best interests can be understood not as the high-handed intervention of the "nanny state", but rather as a self-binding strategy that individuals themselves may be perfectly happy to support."

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### Alex says

I was surprised at how much I learned from reading this book. The author's explanations are clear and easy to understand, while at the same time not sounding like one of the neo-liberals who seem to dominate the economic literature. The book also takes lessons from behavioral economics, as well as from other fields often ignored by the dismal science. It might also be important to some people that this author is Canadian and uses Canadian examples. While there are parts that ought to be taken with a grain, such as his view on paper recycling(which isn't as helpful as you'd think but still has a small positive impact) overall it is one of the best books I read this year.

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### Marco says

*Economics without Illusions* is a rare case of "myth-busting" book that actually does its intended job, rather than simply exposing a contrarian position as if it were divine revelation.

Writing from a Leftist position, the author starts by showing how some positions traditionally associated with Conservative politics (even if the author is a bit too prone to lump everybody outside of the Left tent, blurring some relevant policy distinctions with a convenient label) are not a natural consequence of economical science; indeed, some common pro-market arguments go against the findings of contemporary economical science, especially as they disregard the importance of insurance in a risk society, favouring instead approaches based on individual responsibility alone.

The Left, however, is not spared from Heath's criticism. Quite the contrary: the second part of the book addresses some common banners of anti-capitalist activism and show how the traditional Leftist approaches and intuitions can end up actually harming the people they intend to assist. In his analysis of topics such as "just prices", Heath argues that knowledge of modern Economics is essential for the design of policies that solve critical issues such as inequality without causing nasty side effects (like the scarcity traditionally associated with "real-world Socialism").

While the book simplifies many positions -- the hand-waving of Libertarianism in Chapter 1 is a particularly low point, lacking the nuance seen elsewhere on the book --, it does so not as strawman-building, but as an attempt to engage what is seen in popular discourse. The policies proposed by the author are not above criticism, either, both from Leftist and Rightist perspectives.

*Economics without Illusions* is still a very thought-provoking and nuanced book on the "dismal science" and the consequences of Economics on political and social activity. The discussion of the role played by risk and insurance in modern society alone would be worth the read, but the book successfully shows that each of its discussed topics is way more complicated than the received wisdom -- both on the Left and the Right -- would lead one to think.

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### **Rachel says**

I finally finished! And it only took almost three months! I learned a lot from this book, although I've probably already forgotten a significant proportion of it. The book mostly puts forth good explanations of broad economic theories and truths/falsehoods, but he also explains some specific things, too. For example, I now have a much better handle on the current economic/housing crisis.

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### **Jack Greenrose says**

Economics without illusions, why not. Considering that Joseph Heath is neither an economist nor political scientist, I didn't expect much from a book about political biases from an economic standpoint. But this is actually a decent package of information. This is not a perfect book on economics by any means. Heath cuts corners here and there and is occasionally quite repetitive. Whether minimum wage causes unemployment or not is an unsettled issue, for example, but Heath tries to paint a picture as if it were and that economics 101 (and the political right) has been proven to be wrong. Yet he is sophisticated enough to approach most of the issues from multiple angles and balance contradictory evidence and views in a meaningful way. This is a feat rarely achieved even by those who pride themselves on their imagined objectivity.

In short, the world is getting better (read Steven Pinker's *Better Angels of Our Nature* and *Enlightenment Now* if you want an overwhelming amount of evidence to support this claim) and, in many ways, capitalism deserves our gratitude for it—but it comes with some systemic errors, which is why markets cannot be 100% unregulated or exist without strong institutions. And this book tells you why this is a fact (while helping you break out of your political echo chamber).

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### **Nick says**

This is a "landmark" book which anyone on the political "Right" and, especially anyone on the political "Left" should read. The author challenged, and in many cases destroyed my economic assumptions. Heath is a very witty, intelligent and, when need be, blunt writer, who isn't afraid to tell it like he sees it and back up his points logically. His being a philosopher first, instead of an economist or activist enabled a relatively balanced book, and produced a paradigm of constructive critical thought. The book is not flawless, but it is very, very good, and very powerful.

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