On Booms and Busts

Anthony M. Reinach

BOOMS are often identified with inflation, and *BUSTS* with deflation, but the extremes of economic activity that are called booms or busts are frequently the result of sheer emotionalism. Most booms start slowly and pick up speed as more and more people grasp the happy but insane notion that trade (which is increasing) will continue to increase indefinitely. In its latter stages, a boom may be fueled by propaganda spread by the few psychologically sophisticated persons who intend to profit from the frenzy.

Such special booms as the tulipmania in seventeenth century Holland, the Florida real estate boom in the 1920's, and the recent Davy Crockett boom in the world of children are commonplace in every generation. Among children, the bust that followed the Davy Crockett fad resulted in no more than the discarding of outdated toys and costumes—with hardly a tear being shed. In the world of adults, however, busts bring despair, and ruined lives and fortunes.

The imagery applied to booms and busts is so colorful that it is likely to obscure the comparatively simple economic forces at work.

The more general kind of boom, currently known as "good times," usually starts as a result of an artificial increase in the monetary supply by government. Prices of certain goods and services start to rise. Then trade increases, because prudent people begin to realize that tomorrow an item will cost more and had therefore better be purchased today.

The initial moderation soon mushrooms into a buying spree. Goods and services are bid to unrealistic prices, even in terms of the increased monetary supply. The briskness of trade permeates society with the delusion of "good business."

After buying and prices have reached a peak, a bust inevitably follows, no matter what controls government may attempt to apply. There is an abrupt let-up in general trade, and on its heels comes a condition known as a business "recession" or a business "depression," the difference being the degree of unemployment. At such times some economists allege that "overpro-

Mr. Reinach is a financial consultant.

duction" of goods has resulted in "surpluses."

Why after a bust must a man be plagued for years with a seeming "surplus" of goods, services, and labor?

The law of supply and demand furnishes the answer. Take, for example, the baker and barber who every week have been trading two loaves of bread for one haircut. During the boom, loaves of bread went from 25¢ to 40¢ apiece, while the price of a haircut advanced from 50¢ to 80¢. The baker and the barber continued their weekly transaction. Not even the frenzy of the boom incited them to barter two haircuts for four loaves of bread every week.

Then came the bust, the panic, the depression. Haircuts declined to 40¢; a loaf of bread to 20¢. Still, trade between the baker and the barber kept its usual pace.

With respect to each other, the two acted as sane men would. But neither was that rational in his dealings with customers who pay cash. The baker tried not to cut his price. But when he charged 22¢ for a loaf, he found that unbought bread grew stale on his shelves.

The barber, like his all too-human friend, was also a bit stubborn. He could not quite comprehend why his service, which had recently commanded 80¢, should now be worth only 40¢. He tried to "hold the line" by charging 50¢. But a good many of his customers went to other barbers, or got fewer haircuts, or even trimmed their own hair. He partially disemployed himself.

Admittedly, not every business venture can survive a depression by simply cutting its own selling prices. Some will be saddled with contracts and commitments that preclude continuous production. Thus, there will be business stoppage and unemployment unless wage contracts and other costs are also repriced in line with the new market situation. Even in a panic, "unemployment," "overproduction," and "surplus" as such do not exist. There are only unemployment at a price, overproduction at a price, and surpluses at a price.

THUS came a collapse in manufacturing and commerce just as . . . in all countries where men have tried to build up prosperity on irredeemable paper. . . . The merchant was forced to add to his ordinary profit a sum sufficient to cover probable or possible fluctuations in value, and while prices of products thus went higher, the wages of labor, owing to the number of workmen who were thrown out of employment, went lower.

ANDREW DICKSON WHITE, *Fiat Money Inflation in France*

Politics in the Market Place

Edmund A. Opitz

HUMAN EXISTENCE has always been precarious. Man is always exposed to natural calamities—including other men. Famines and epidemics have recurred with appalling frequency during history, and entire populations have been ravaged from time to time. There cannot be, in the nature of things, any guarantee that a man will reap where he has sown. Drought or flood may ruin his crops, or some other man may raid the harvest. The producer is constantly threatened by a forcible transfer of his wealth—effected on a small scale by robbery, and on a large scale by war. Men have never learned to live comfortably with the all-pervading uncertainty of life, and they have grasped at every straw which promises to introduce a reasonable security into it.

It is economic uncertainty which makes the modern man most nervous. The Great Depression of the 1930's is kept so fresh in his mind that he is willing to allow a lot of political intervention by the federal government because he believes that there is no other way to prevent a recurrence of the big bust of 1929. If we grant the premise that political action can make the economy depression-proof, it becomes easy to accept the conclusion that it is the duty of government to shore up the economy at every critical point. But is the premise sound? "Probably not," is the conclusion forced upon us by an analysis of the economic and political factors in the situation.

THE MARKET PLACE is the cornerstone of society. The human community does not flower except as men are able to exchange their surplus energies voluntarily as goods, services, and ideas. If individuals were completely self-sufficient, society would be unnecessary, if not inconceivable. A society is impossible unless there be some exchange, and it is rich and complex in the degree to which exchanges multiply; and on every level exchanges multiply naturally unless they are sabotaged. The quality of goods, services, and ideas exchanged will depend, of course, on the endowment and enlightenment of the people who do the exchanging. When economic

The Reverend Mr. Opitz is a member of the staff of the Foundation for Economic Education.