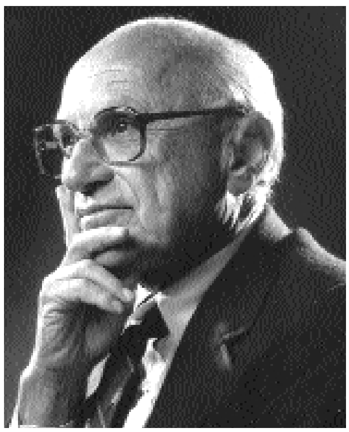
Milton Friedman (1912-2006)

BY RICHARD M. EBELING AND SHELDON RICHMAN

Milton Friedman, who died last month at age 94, was one of the twentieth century's most influential champions of individual liberty and free markets. The 1976 winner of the Nobel Prize in economics and an early associate of FEE, Friedman did more than any single person in our time to teach the public the merits of deregulation, privatization, low taxes, and free trade. His work inspired the economic agendas of President Ronald Reagan and British Prime Minister Margaret Thatcher, as well as the liberalization of economies in eastern Europe and the former Soviet Union.

Born in New York City in 1912 to Jewish immigrants, Friedman went on to become a major force in theoretical economics in the second half of the century and the leading figure of the Chicago, or monetarist, school. As a professor of economics at the prestigious University of Chicago, he is widely credited with overturning the dominant Keynesian paradigm regarding the tradeoff between unemployment and inflation. He made monumental (if controversial) contributions to monetary theory, policy, and history in such books as *Studies in the Quantity Theory of Money* (1956) and *A Monetary History of the United States, 1867–1960* (co-written with Anna Schwartz, 1963).



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Slayer of Keynesianism

In the post-World War II era, when Keynesianism dominated the economics profession, Friedman undertook a series of studies to undermine some of Keynes's leading assumptions. In the late 1940s he challenged the Keynesian position that discretionary government policy was essential to assure full employment. Friedman was able to show that the macroeconomic policymakers would never have sufficient knowledge about changing market conditions to successfully manipulate the fiscal and monetary policy tools in a timely manner. Instead, he argued, the wisest long-run policy was for government to follow a small number of predictable policy rules.

Beginning in the 1950s Friedman presented a restatement of the quantity theory of money, arguing that all prolonged and sustained general rises in prices were caused by an increase in the supply of money. "Inflation," he said, "is always and everywhere a monetary phenomenon." His *Monetary History of the United States* demonstrated that government manipulation of the money supply was the primary factor behind the boom-and-bust cycles experienced in the twentieth century. In addition he argued that it was misguided Federal Reserve policy in the early 1930s that generated the severity of the Great Depression—and not any inherent failures in the market economy.

This led Friedman to make the case for a "monetary rule," under which the monetary authority would be denied any discretionary powers over the money supply. Instead, the Federal Reserve would be limited to increasing the supply of money at a fixed annual rate of

Richard Ebeling(rebeling@fee.org) is the president of FEE. Sheldon Richman (srichman@fee.org) is the editor of The Freeman.

around 3 percent. This would create a high degree of predictability about monetary policy and generate a relatively stable price level in a growing economy.

In making the case for a monetary rule, Friedman advocated a paper-money standard rather than the gold standard, arguing that this would save on the resource costs of digging the metal out of the ground just to store it away in bank vaults. But in the years after he received the Nobel Prize he had second thoughts about his monetary rule and the gold standard. In a series of articles in the 1980s Friedman stated that Public Choice theory had convinced him it will never be in the long-run interest of governments or their monetary authorities to follow the type of rule he proposed, since the temptation to abuse the printing press for political reasons would always be too strong. He therefore concluded that, given the actual history of Federal Reserve policy in the twentieth century, remaining on the gold standard would have been far less costly for America than the Fed-created inflations and recessions.

One final and lasting contribution of Friedman's was his formulation of the "natural rate" of unemployment. The Keynesians of the 1950s and 1960s believed that it was possible to permanently lower the rate of unemployment through manipulation of the rate of inflation. In his presidential address before the American Economic Association in 1967, Friedman argued that, at most, monetary policy could temporarily lower the level of unemployment. But in the long run it would return to its "natural rate."

He said that the amount of unemployment at any time was determined by changing supply-and-demand conditions in the market and people's expectations about the future rate of inflation, which influenced their resource-price and wage demands. The monetary authority could fool people by increasing the inflation rate above people's expectations, resulting in prices rising faster than wages, and the resulting larger profit margins would create an incentive for employers to increase output and hire more workers. But over time, as people discovered the truth about the rate of inflation, they would demand higher wages and resource prices to compensate for lost purchasing power. That would reduce profit margins and return unemployment to its "natural" level.

Unless the monetary authority was willing to continuously increase the rate of price inflation above people's adjusted expectations, the lesson had to be accepted that in the long run, monetary policy cannot influence levels of employment and output. These are ultimately determined by market conditions and not by government manipulation.

Through these contributions, Friedman permanently transformed the debate in macroeconomics and in the process undermined many of the most cherished assumptions of Keynesian economics.

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Public Intellectual

As influential as Friedman's academic work was among professional economists, he had as profound an impact on non-economists' thinking about the virtues of free markets and limited government. At a time when popular writing that went against the collectivist grain had few mass outlets, Friedman managed to reach a wide audience with his clear and good-natured style. He accomplished this through many books, a long-running *Newsweek* column, and his 1980 television series, "Free to Choose," based on his bestselling book of the same title.

His 1962 book *Capitalism and Freedom* was an accessible volume that presented bold free-market thinking on such issues as medical licensing, the volunteer army, and antitrust laws. It was also the book in which Friedman unveiled controversial proposals for school vouchers and the negative income tax as transitions from the welfare state. The book undoubtedly inspired many youthful readers to pursue careers in economics.

Friedman started addressing a large popular audience in 1966, when he inaugurated a regular column in *Newsweek*, succeeding Henry Hazlitt. Friedman's column, which rotated with those of the Keynesian Paul Samuelson and Henry Wallich, presented the case for free-market policies across a wide range of issues—such as wage and price controls (imposed by President Nixon in 1971) and the minimum wage—and did much to inject the libertarian perspective into the public debate. The column ran until 1983. (A compilation of columns was published as *Bright Promises, Dismal Performance*.)

Meanwhile, on December 19, 1969, Friedman's picture made the cover of *Time* under the title "Will There Be a Recession?" It was a rare distinction for an academic economist, but by then, Friedman was more than that: he was a public intellectual.

Friedman achieved bona fide star status in 1980 with release of his book *Free to Choose*, written with his wife Rose Friedman, also an economist. In *Free to Choose* Friedman explained the unparalleled contributions to human well-being of the division of labor and free exchange, the tyranny of government regulation, the dangers of inflation and the welfare state, and the problems intrinsic to the government school monopoly. His chapters on how the competitive marketplace protects consumers and workers were eye-openers for an audience that until then had been led to believe that only coercive government could do those things.

Free to Choose, according to the *Fortune Encyclopedia of Economics,* became the best-selling nonfiction book of 1980. Sales were boosted by the ten-part companion television series on PBS. Each week viewers saw the congenial Friedman clearly explain why free markets serve individuals and society best, and why government creates chaos and poverty—all well illustrated with beautiful location footage, including scenes of Hong Kong's success.

Four years later Friedman again combined a book with a television series in *The Tyranny of the Status Quo*, also co-written with Rose Friedman.

Friedman was fearless in the face of controversy, vigorously opposing the military draft during the Vietnam War and drug prohibition. But he was no idle author. In 1969-70 he participated in the President's Commission on an All-Volunteer Armed Force. His pro-freedom credentials made his a powerful voice in the effort to end the involuntary servitude of conscription.

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Friedman won many honors for his work. Besides the Nobel Prize he also won the Presidential Medal of Freedom and the National Medal of Science, both in 1988. He served as president of the American Economic Association.

In 1947 Friedman was one of a select group of some 40 economists and writers invited by F. A. Hayek to attend the founding meeting of the Mont Pelerin Society in Switzerland. Leonard Read, FEE's founding president, Henry Hazlitt, and Ludwig von Mises also participated in that meeting to establish a worldwide network of classical-liberal scholars.

Friedman co-wrote (with George Stigler, who also later won the Nobel Prize) one of the first publications FEE released, the 1946 pamphlet "Roofs or Ceilings? The Current Housing Problem," a critique of rent control (www.fee.org/library/books/Roofs_or_Ceilings.asp).

Sadly, Milton Friedman is gone from us now. But his legacy and devotion to liberty will inspire freedom lovers for many generations.