Capitalism, Money, and Interest

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It is proposed that basic the tenets of capitalism have an inherit flaw. Capitalism asserts that humanity's desires are unlimited and that it is a good thing to satisfy them in an unlimited way. Thus, money, as a means to satisfying these desires, must be earned and increased by every rational means; even to the extent of charging interest on money itself. It is shown, however, that man's desires are not infinite; and that it is healthy and normal to curb desires through training and habit. In fact, it is the constant drive to acquire money that leads to surpluses, unemployment, and war. Furthermore, interest on money is an abomination, since charging interest is the act of money begetting money.

INTRODUCTION

The basis on which modern capitalism is founded is inherently flawed and contrary to the nature of the human person. It is quite difficult, however, to detect this fundamental philosophical error in the day to day workings of society. The average citizen is constantly bombarded with messages, overt and subliminal, that promote the success and value of capitalism. Thus, if one tries to question the principle of capitalism, the effort is made difficult because the thought process must go contrary to the very same values that are being emphatically promulgated by the capitalist system in question.

Nonetheless, this work makes an attempt to find the underlying contradictions promoted by the economic system known as capitalism. It is not an easy task if one is immersed in such a system for one's entire life. In the movie, "The Matrix", Morpheus describes how vexing such an enterprise is.

> It's that feeling you have had all your life. That feeling that something was wrong with the world. You don't know what it is but it's there, like a splinter in your mind, driving you mad, driving you to me. But what is it?

This work makes an attempt to remove that "splinter".

CAPITALISM

The basic axioms of capitalism are simple:

- Wants, needs and desires are unlimited.
- Economics is the science of how to allocate resources to satisfy unlimited wants.
- Unlimited wants are best satisfied by pursuing one's own self interest.

To the casual observer, these axioms appear horrifying. They could be interpreted as, "Do whatever it takes to get all and as much as you can, and look out for Number One." These axioms, stated verbatim, are considered deplorable by any traditional church or Sunday school class.

Karl Marx in "The Economic and Philosophic Manuscripts of 1844", basically frames capitalism as a system where the objective is to use money to make more money. The goal is neither the acquisition of land nor the increase of production capacity; rather, the goal of capitalism is to generate as much money as possible.

Now, consider the following proposal. In the American capitalistic economic system, nearly everything is defined in terms of money: a person's worth is defined in terms of money on their tax return, national output (GDP) is stated in dollars, a parent's value in raising a child is reduced to the dollar value of child support payments, even restitution for negligence is put in terms of dollars paid in punitive damages. In a system so fixated on money, it follows that the best way to satisfy unlimited wants is through maximum money generation.

MONEY

Before delving too far into questions regarding money, it is best to present how economists define money. Economists say that money must have the following characteristics:

- Medium of exchange. In other words, sellers accept money as payment; barter is not needed.
- Unit of account. Products are defined in terms of money so the relative value of products is known. If an apple is worth $1 and a pear is worth $2, then it is clear that one pear is worth two apples.
- Store of value. Corn is perishable, but once the farmer converts it into cash, the value of his labor is preserved.

This is a basic outline of how economists define money. It is important to keep this definition in mind for the proceeding discussion: the Aristotelian view of money and interest.

ARISTOTLE

Aristotle states that the goal of all human activity is to achieve happiness. He claims that happiness is achieved through good moral character. For Aristotle, happiness is an act of volition; and it is achieved by developing good habits in both thought and deed.

As for capitalism, Aristotle does not have good things to say; even though he does not use the term specifically. His most forceful condemnation is evident in his book called the Politics. Here he claims that the pursuit of money is a lower form of human activity and to charge interest on money is an unnatural act.

Before entering into the Politics, Aristotle first defines money, and outlines its proper use and purpose in his famous book called the Ethics.

> Now proportionate returns are brought about by cross-exchange. Thus let A represent a builder, B a shoemaker, C a house, and D a shoe. The builder then must get from the cobbler a part of his work and give him his own work in return. If there is, first, proportionate equality in the goods and then reciprocity follows, the result of which we are speaking is attained. Otherwise the bargain will not be equal or permanent. For the work of one man may perhaps be superior to that of the other, and then they must be equalized. (This is equally true in all the arts; they would be ruined if the result for the receiver were not, in kind, quantity and quality, the same as the result for the doer.) For it is not two doctors who combine to exchange, but a doctor and a farmer, and in general people who are different and not equal and who need to be equalized.
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> Then the things they have to exchange must somehow be made comparable. This is why money was invented. Money is a sort of medium or mean; for it measures everything and consequently measures excess and defect, for instance, the number of shoes equivalent to a house or a meal. As a builder then is to a shoemaker, so must so many shoes be to a house; otherwise there would be no exchange and no intermingling. And the calculation will be impossible, unless the goods are somehow equalized. Hence the necessity of a single universal standard of measurement, as we said before. Actually this standard is the demand for mutual services, which holds society together; for if people wanted nothing of each other, or wanted it irregularly, there would be either no exchange or it would not be the same as it is now. But money is a sort of recognized representative of demand. That is the reason why it is called money (nomisma), because it is not nature but law (nomos) that gives it existence, and it is in our power to change it and make it useless . . .
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> The fact that it is demand which binds society together as a unit is evident. For if there is no mutual demand on the part of two persons, if neither of them or one only needs the services of the other, they do not exchange; whereas if someone wants what someone else has, they exchange, getting wine, for instance, and exporting corn in return. Here then the wine and the corn must be equated.
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> Money is useful too for future exchange; it is a sort of security which we possess that, if we do not want a thing now, we shall be able to get it when we do want it; for if we bring money, it will be in our power to get what we want. Money, it is true, is subject to the same laws as other goods; its value is not always the same; however, it tends to be more constant in value than anything else. All things then must have a money value to make exchange possible, and therewith the association of man and man. Money then is like a measure that equates things by making them commensurable; for association would be impossible without exchange, exchange without equality, and equality without commensurability . . .

Note that Aristotle crystallizes, in the discussion above, some of the most important concepts known in the study of economics: barter, trade, comparative advantage, and double coincidence of wants. He further lists the 3 characteristics of money previously discussed in this work.

In the Politics, Aristotle states that there are 2 principle and common reasons for acquiring money: for proper household management and for making more money. Household management is simply another way of saying that one must strive to acquire only the things needed for a good and modest living. Aristotle sees household management as a natural act. The art of money making for the sake of making money, however, is seen as unnatural. Note that remarks in parenthesis are added.

> The origin of this disposition (a disposition for the art of making money) in men is that they are intent upon living only, and not upon living well. And, as their desires are unlimited, they also desire that the means of gratifying them should be without limit. Even those who aim at a good life seek the means of obtaining bodily pleasures; and, since the enjoyment of these appears to depend on property, they are absorbed in making money. Thus arises the second species of wealth getting. For, as their enjoyment is in excess, they seek an art which produces the excess of enjoyment; and, when they are not able to supply their pleasures by the art of money making, they try other arts, using in turn every faculty in a manner contrary to nature. The quality of courage, for example, is not intended to make money, but to inspire a confidence; neither is this the aim of the general's or of the physician's art; but one aims at victory and the other at health. Nevertheless, some men turn every quality or art into a means of making money; this they conceive to be the end, and to the promotion of the end all things must contribute.
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> Thus, then, we have considered the art of money making, which is unnecessary, and why men want it; and also the necessary art of wealth getting, which we have seen to be different from the other, and to be a natural part of the art of managing a household, and concerned with the provision of food, not, however, like the former art, unlimited, but having a limit.

For Aristotle, making money in excess, beyond what is necessary to obtain one's "daily bread", is a perversion. He extends this thought and states that charging interest on money is the greatest perversion in the sphere of economic activity. This is because interest is not money obtained by trade; but rather, the creation of money from money. Money is the direct offspring of money. Again, comments in parenthesis are added.

> Of the two sorts of wealth getting one, as I have just said, is a part of household management, the other is commerce. The former is necessary and honorable, the latter a kind of exchange which is justly censured; for it is unnatural, and a mode by which men gain from one another. The most hated sort, and with the greatest reason, is usury, which makes a gain out of money itself, and not from the natural use of it (medium of exchange, unit of account, and store of value). For money was intended to be used in exchange, but not to increase at interest. And the term "interest", which means the birth of money from money, is applied to the breeding of money because the offspring resembles the parent. Wherefore of all modes of making money this is the most unnatural.

According to Aristotle, human appetites are trained by habit to be either controlled or uncontrolled. This philosophy is outlined completely in the Ethics. If one is in control of his human appetites, he is concerned only with proper household management and with obtaining “the good life”. If one’s appetites are out of control, then one is obsessed with making money, since money is the instrument used to satisfy those excessive desires. Unchecked desires lead to turning all forms of human endeavor into money making opportunities; and ultimately to charging interest on money – the lowest form of economic activity.

Aristotle disagrees with modern economics’ premise that humans naturally have unlimited wants. Rather, he asserts that one’s disposition, behavior formed by habit, determines whether wants are limited or unlimited. A well developed character leads to happiness, and as a consequence, one is concerned with good household management and content for his “daily bread”.

CARTER ADMINISTRATION, 1977 - 1981

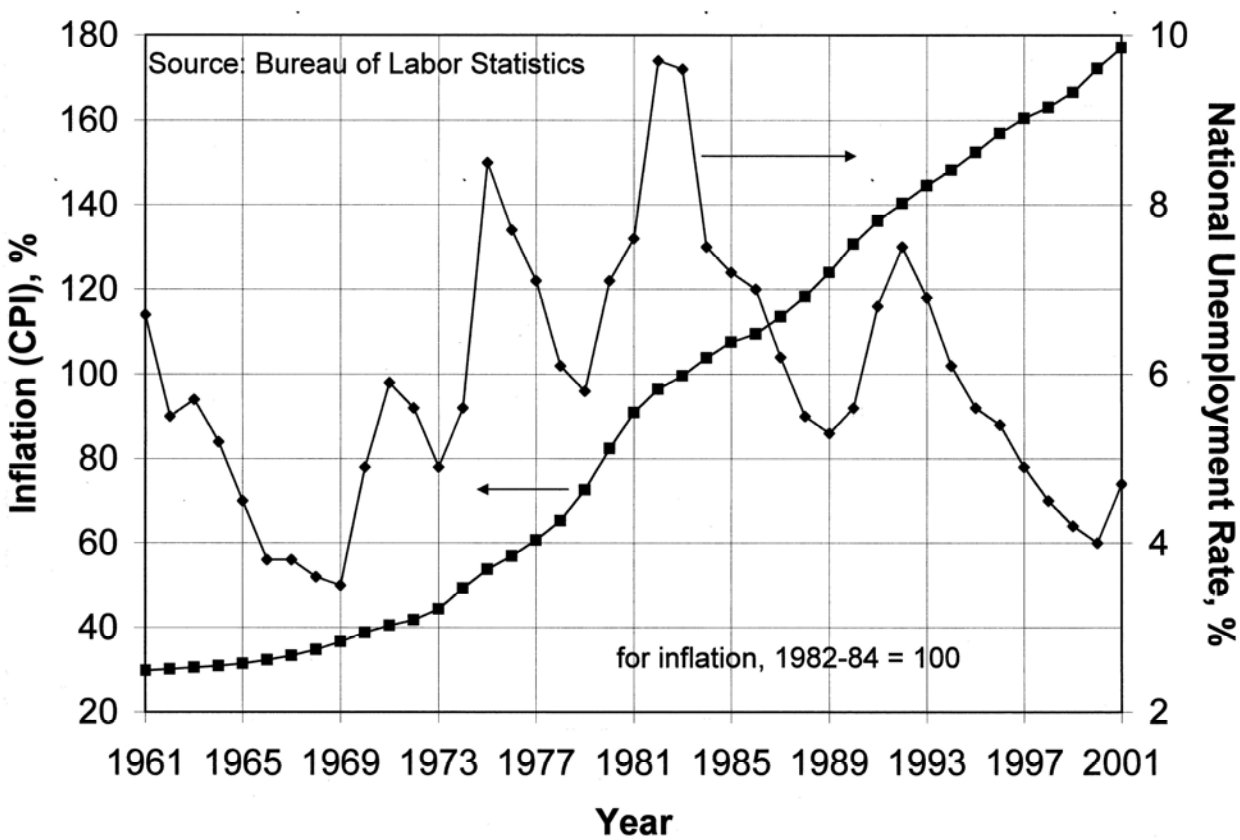
Before further examining the nature of money and interest, it is worthwhile to review the affect of the Carter Administration on the national economy. The reason is that Jimmy Carter is perhaps the only president in American history to understand that there is a dichotomy between high employment rates and inflation rates. Modern economics states that at excessively high employment, output hits a wall and wages are simply bid up; inflation occurs. Higher wages lead to higher prices until eventually inventories rise due to lack of demand. Likewise, employees are laid-off, production is cut back, workers must take lower wages to gain employment and inflation is reduced. The cycle just continues this way indefinitely.

Jimmy Carter sees something wrong with this pattern and makes this clear at the 1976 Democratic National Convention.

> I believe that anyone who is able to work ought to work – and ought to have a chance to work. We will never have an end to the inflationary spiral, we will never have a balanced budget - which I am determined to see - as long as we have eight or nine million Americans out of work who cannot find a job. Any system of economics is bankrupt if it sees either value or virtue in unemployment. We simply cannot check inflation by keeping people out of work.

Figure 1 is a plot of the U. S. inflation and unemployment rates from 1961 to 2001. The Consumer Price Index is used as a measure of inflation. From 1977 – 1979, unemployment is dropping – Carter fulfills his promise and puts people to work during the early part of his administration. Inflation, however, sky rockets between 1977 and 1981. The slope of the inflation curve is the highest it has ever been during this 40 year time span.

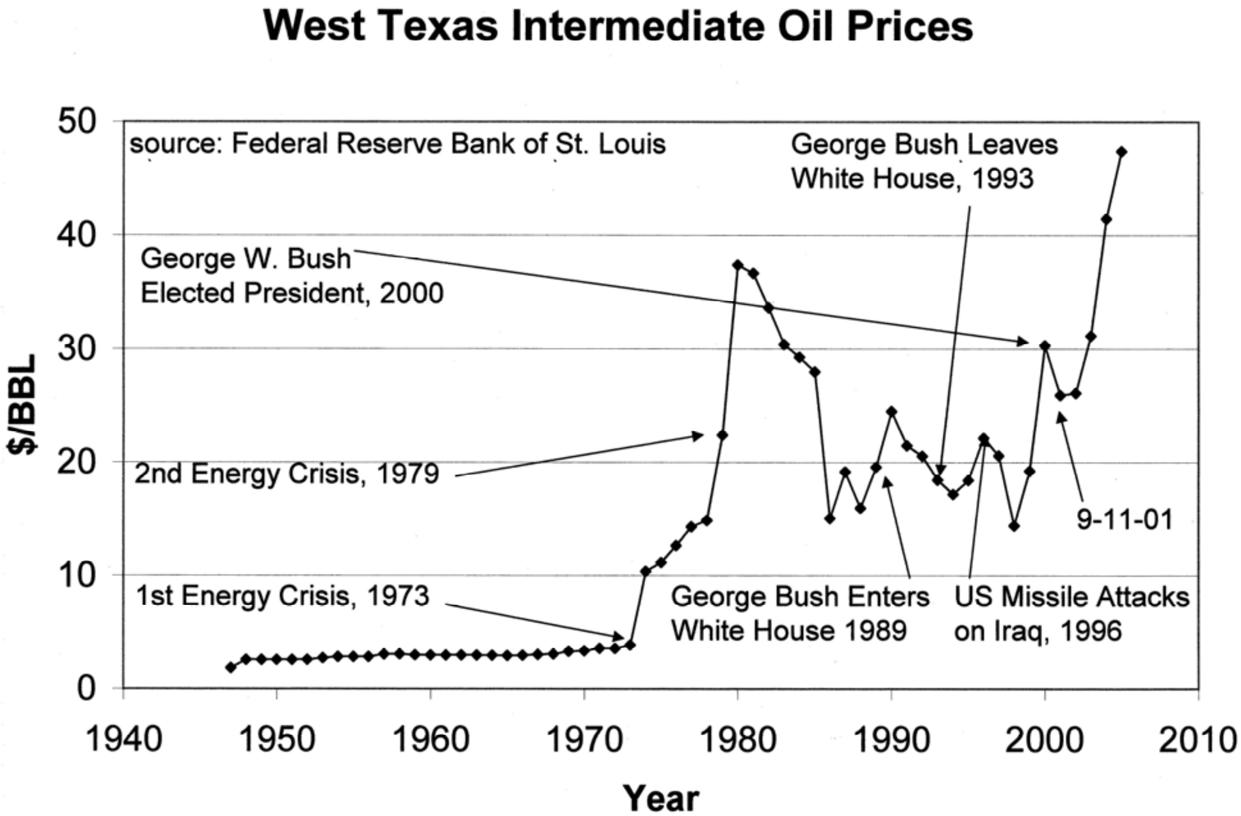
Figure 1. U. S. Inflation and Unemployment Rates between 1961 and 2001.



It makes economic sense that inflation and employment rise together from 1977 -1979. During this period, unemployment hovers around the natural rate of unemployment – within the time period of the Carter Administration, the natural rate of unemployment is about 6% (Congressional Budget Office, 2002). Thus, output is at full capacity and wages are simply bid up; inflation sets in.

Though Carter fulfills his promise to put people to work during the first part of his administration, unemployment rises markedly from 1979 -1981. In reality, this sudden rise in unemployment cannot be blamed on Carter. Please refer to Figure 2, a plot of oil prices from 1946 to 2005 (Carranza, 2005).

Figure 2. Prices for West Texas Intermediate Oil since 1946.



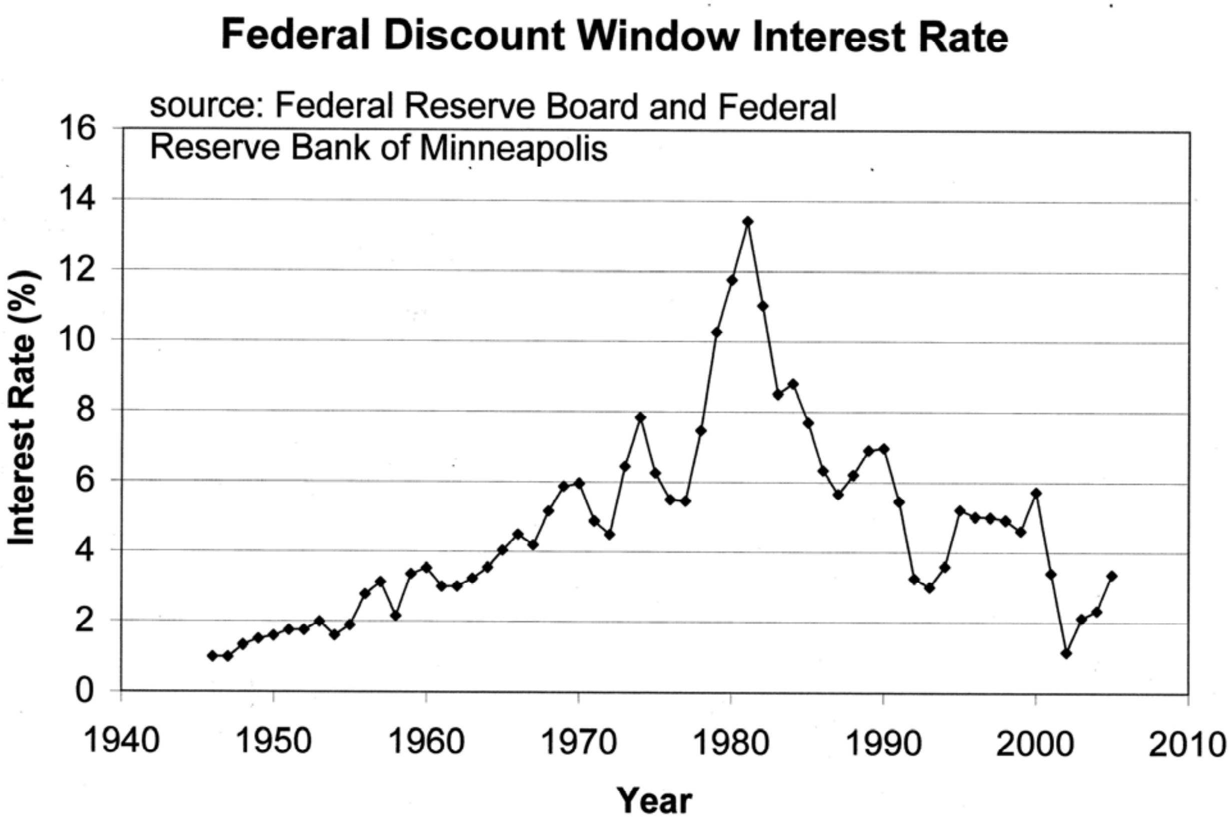
Note that in 1979, a second oil shock is given to the American economy – due to conflicts in the Middle East. This leads to oil prices hitting all time highs in 1981. As is predicted by the study of economics, employment drops steadily between 1979 ad 1981 – increased resource cost causes inflation, inventories build up, jobs must be slashed to meet the reduced demand.

There is just one problem, from 1979 to 1981, both unemployment and inflation are rising at the same time (note that the slope of the inflation curve is particularly steep between 1979 and 1981) – contrary to economic theory. A new phenomenon is discovered, Stagflation. Though stagflation is not explained by economic theory, it is more than likely a transitory condition; and not indicative of a system at equilibrium. That is to say that even though workers are laid off, they are not immediately put back to work because wages are “sticky downward”. It takes time for workers to accept lower wages, and until that time, consumer prices remain elevated.

Please refer to Figure 3, a plot of the Federal Reserve discount window interest rates over time (Carranza, 2005). One can see easily that the Fed raises interest rates dramatically between 1979 and 1981 – compounding the unemployment problem. Furthermore, this leads to unbelievable interest rates on credit cards (as high as 21%), student loans, and home mortgages.

The Federal Reserve raises interest rates because, according to economic theory, inflation is due to overemployment; also stated as unemployment below the natural rate of unemployment. The economic data show that circa 1979 the rate of unemployment is just slightly below the natural rate of unemployment (Congressional Budget Office, 2002). Nevertheless, the Fed does not seem to realize that the cause for high inflation between 1979 and 1981 is high oil prices, and not high employment. Thus, the Fed reacts by raising interest rates, hoping to discourage investment and turn down aggregate demand.

Figure 3. Federal Discount Window Interest Rates since 1946.



Jimmy Carter is a brave and heroic character in American history because he dared to defy conventional wisdom. He did not blame the worker for inflation and other economic ills. Jimmy Carter refused to say that high employment is a bad thing; but rather, a good thing. But as economic theory predicts, the early Carter years bring high inflation along with high employment. The later Carter years are filled with stagflation, but as has already been stated, this is due to high oil prices and not a function of the Carter fiscal policy.

How could Jimmy Carter be so wrong? Can a person having a job ever be a bad thing? Is there really such a thing as overemployment? The fact is that Jimmy Carter is not wrong, rather the economic system is flawed; and at the heart of this flaw is usury.

MODERN ECONOMICS

One of the great tools of modern economic theory is to make good use of the thought experiment. Through the thought experiment, economists go back to fundamentals and examine the root causes of why the science of economics even exists in the first place. What economists find is that economic activity is based on the following important first principles:

- Humans have unlimited wants.

- Humans are wise to maximize the quality and quantity of goods and services that make their lives better – this is known as self interest.
- The most efficient way to pursue self interest is to specialize in what one does best and trade for what else one needs.

This sounds good and fine on the surface, until one looks at the world around them. Any scientific theory is always judged for its validity by observable results. By simply looking at the world around, one sees large cities in the USA drowning in a sea of bone crushing poverty; meanwhile, one observes isolated pockets of affluent neighborhoods, safe behind iron gates, security guards, and surveillance cameras. The Dow Jones Industrial Average, between 1990 and 2005, goes from about 2800 in 1990 to an all time closing high of 11722.98 in January of 2000 (www.djindexes.com). In that same time period, nonconsumer bankruptcies go from 718,107 in 1990 to an all time high of 2,039,214 in 2005 (www.uscourts.gov). The 1980's brought a devastating banking crash that uncovers tremendous fraud in the business and governmental sectors; and ultimately leads to the complete collapse of the Savings and Loan industry. The new millennium is starting out no better. So far this century is overrun with sensational court cases involving white collar crime: Enron, Tyco, MCI, Martha Stewart, etc.

There is something terribly wrong with this economic system. A simple thought experiment reveals that the problem is in the system's fundamental principles. The key fallacy is money interest – usury.

Free Trade

Free trade is something in which every one engages. Everyone gets money by means of work and goes to the store to buy stuff. Economists explain this natural phenomena via precise terms like comparative advantage and specialization. Take as an example two cavemen called Gog and Magog.

Table 1 is a schedule of what Gog and Magog can produce in one day, assuming they are the only two people in the economy and all they presently need are shirts and pants. Case 1 is simply the maximum output that Gog and Magog produce if each spends all day on either shirts or pants. Case 2 is what each can produce if each spends half a day on both shirts and pants. Note that for the same amount of time Gog has a comparative advantage in making pants over Magog; and likewise, Magog has a comparative advantage over Gog in making shirts. Thus, each should specialize in what they do best. Case 3 shows that, with specialization, Gog produces 20 pants and Magog produces 20 shirts.

Table 1. Production Schedule for Gog and Magog

	Gog		Magog	
Case	Shirts	Pants	Shirts	Pants
1	10	20	20	10
2	5	10	10	5
3	0	20	20	0
4	10	10	10	10

In Case 4, Gog and Magog specialize in their respective comparative advantages and trade 1 shirt for 1 pair of pants. When Gog splits his time, he has 5 shirts and 10 pants; but when he specializes and trades, he has 10 shirts and still has 10 pants. When Magog splits his time, he has 10 shirts and 5 pants; but when he specializes and trades, he has the same 10 shirts but also gains 5 more pants. Gog and Magog are better off specializing and trading than they are by splitting their time. By specializing in one's comparative advantage and trading, one is pursuing one's self interest; and thus, maximizes one's quality of life and the quantity of goods for enjoyment.

The one subtle fact to glean from this example is that it is very difficult to get rich under these circumstances. Though, Gog and Magog are better off by trade, the degree to which they are better off is still limited by how much they can produce in their respective area of specialization. Exploitation is easily avoided in a barter system; but more probable when the terms of trade are done in the form of money and an interest rate is charged regardless of whether or not any fruitful production occurs as a result of money being loaned and invested.

The Profit Motive

It is time now for Gog and Magog to expand their business. The first step is to take out a loan for investment in capital (machinery) and for floor space, etc. The second step is to hire employees (machine workers, packers, dock personnel, accountants, etc). In essence, Gog and Magog open their two person economy, and thereby, include their neighbors. The very people they hire are those to whom they sell.

It is important to note that expanding an economy and providing a good life with ample food and comfort is not a bad thing in itself. The problem is greed or acquiring more than one needs to live a good life - when one is not content with his "daily bread".

This is an ancient theme. Socrates proposes this idea in ancient Greece. He says that when people want more than they need, war is the result. Comments in parenthesis are added.

> Let us then consider, first of all, what will be their way of life, now that we have thus established them (the people of the simple economy). Will they not produce corn and wine and clothes and shoes, and build houses for themselves? And when they are housed, they will work, in summer, commonly, stripped and barefoot, but in winter substantially clothed and shod. They will feed on barley-meal and flour of wheat, baking and kneading them, making noble cakes and loaves; these they will serve up on a mat of reeds or on clean leaves, themselves reclining the while upon beds strewn with yew or myrtle. And they and their children will feast, drinking of the wine which they have made, wearing garlands on their heads, and hymning the praises of the gods, in happy converse with one another. And they will take care that their families do not exceed their means; having an eye to poverty or war.
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> But, said Glaucon, interposing, you have not given them a relish to their meal.
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> True, I replied, I had forgotten; of course they must have a relish--salt and olives and cheese--and they will boil roots and herbs such as country people prepare; for a dessert we shall give them figs and peas and beans; and they will roast myrtle-berries and acorns at the fire, drinking in moderation. And with such a diet they may be expected to live in peace and health to a good old age, and bequeath a similar life to their children after them.
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> Yes, Socrates, he said, and if you were providing for a city of pigs, how else would you feed the beasts?
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> But what would you have, Glaucon? I replied.

Why, he said, you should give them the ordinary conveniences of life. People who are to be comfortable are accustomed to lie on sofas, and dine off tables, and they should have sauces and sweets in the modern style.

Yes, I said, now I understand: the question which you would have me consider is, not only how a State, but how a luxurious State is created; and possibly there is no harm in this, for in such a State we shall be more likely to see how justice and injustice originate. In my opinion the true and healthy constitution of the State is the one which I have described. But if you wish also to see a State at fever-heat, I have no objection. For I suspect that many will not be satisfied with the simpler way of life. They will be for adding sofas and tables and other furniture; also dainties and perfumes and incense and courtesans and cakes, all these not of one sort only, but in every variety. We must go beyond the necessaries of which I was at first speaking, such as houses and clothes and shoes; the arts of the painter and the embroiderer will have to be set in motion, and gold and ivory and all sorts of materials must be procured.

True, he said.

Then we must enlarge our borders; for the original healthy State is no longer sufficient. Now will the city have to fill and swell with a multitude of callings which are not required by any natural want; such as the whole tribe of hunters and actors, of whom one large class have to do with forms and colors; another will be the votaries of music--poets and their attendant train of rhapsodists, players, dancers, contractors; also makers of divers kinds of articles, including women's dresses. And we shall want more servants. Will not tutors be also in request, and nurses wet and dry, tirewomen and barbers, as well as confectioners and cooks; and swineherds, too, who were not needed and therefore had no place in the former edition of our State, but are needed now? They must not be forgotten: and there will be animals of many other kinds, if people eat them.

Certainly.

And living in this way we shall have much greater need of physicians than before?

Much greater.

And the country which was enough to support the original inhabitants will be too small now, and not enough?

Quite true.

Then a slice of our neighbors' land will be wanted by us for pasture and tillage, and they will want a slice of ours, if, like ourselves, they exceed the limit of necessity, and give themselves up to the unlimited accumulation of wealth?

That, Socrates, will be inevitable.

And so we shall go to war, Glaucon. Shall we not?

Most certainly, he replied.

Then, without determining as yet whether war does good or harm, thus much we may affirm, that now we have discovered war to be derived from causes which are also the causes of almost all the evils in States, private as well as public.

Undoubtedly.

> And our State must once more enlarge; and this time the enlargement will be nothing short of a whole army, which will have to go out and fight with the invaders for all that we have, as well as for the things and persons whom we were describing above. (Plato's Republic, Book 2)

The proposition a man is entitled to acquire those things that he needs to live the simple life or the good life is an old theme used by many famous thinkers. On the other hand, capitalism asserts that man's desires are unlimited and that it is only right that he strives to maximize the quantity and quality of goods and services he consumes.

According to capitalism, Gog and Magog are only doing the natural thing by the investment of capital and the increase in production. Contrarily, Karl Marx claims that Gog and Magog have launched a war against labor. Since the capitalist owns the means of production, he cannot resist the urge to exploit the worker.

In principle, Gog and Magog still trade at the rate of 1 shirt for 1 pair of pants. There is no room for exploitation here. Thus, in an effort to make a profit on their investment, the only alternative for Gog and Magog is to cheat their workers. This is done by pushing down wages and getting more production out of labor than is paid in wages.

In other words, corporations cannot cheat each other very easily because they are equals, competing on a level playing field. Goods and services are traded for their worth in business transactions. And as the simple two person economy shows, a good is only worth the value of labor that it takes to create that good. In a perfect world, there is no room for profit inside the corporation because the owner, the boss, and the workers are all paid what they are worth – the true value of their labor. Goods are sold for a price equal to the value of the labor required to make that product. Therefore, profit is generated by cheating the worker and the capitalist has the power to cheat labor because the capitalist owns the means of production.

> . . . For the laborer, like the capitalist, sells his product for exactly what it is worth – for its value. And its value, like the value of everything else that is sold, is the amount of labor that goes into it – in this case, the amount of labor that it takes to 'make' labor power. In other words, a laborer's salable energies are worth the amount of socially necessary labor it takes to keep that laborer alive. Smith and Ricardo would have agreed entirely: the value of a workman is the money he needs in order to exist. It is his subsistence wage.
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> So far so good. But here comes the key to profit. The laborer who contracts to work can ask only for a wage that is his due. What that wage will be depends, as we have seen, on the amount of labor-time it takes to keep a man alive. If it takes six hours of society's labor to maintain a workingman, then (if labor is priced at one dollar an hour), he is 'worth' six dollars a day. No more.
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> But the laborer who gets a job does not contract to work only six hours a day. That would be just long enough to support himself. On the contrary, he agrees to work a full eight-hour, or in Marx's time a ten- or eleven-hour, day. Hence he will produce a full 10 or eleven hours' worth of value and he will get paid for only six. His wage will cover his subsistence, which is his true 'value', but in return he will make available to the capitalist the value he produces in a full working day. And this is how profit enters the system.

> Marx called this layer of unpaid work 'surplus value'. The words do not imply moral indignation. The worker is entitled only to the value of his labor-power. He gets it in full. But meanwhile, the capitalist gets the full value of his worker's whole working day, and this is longer than the hours for which he paid. Hence when the capitalist sells his products, he can afford to sell them at their true value and still realize a profit. For there is more labor-time embodied in his products than the labor-time for which he was forced to pay.
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> How can this state of affairs come about? It happens because the capitalists monopolize one thing – access to the means of production themselves. Under the legal arrangements of private property, capitalists 'own' jobs, in sofar as they own the machines and equipment without which men and women cannot work. If someone isn't willing to work the number of hours that a capitalist asks, he or she doesn't get a job. Like everyone else in the system a worker has no right and no power to ask for more than his own worth as a commodity. The system is perfectly 'equitable', and yet all workers are cheated, for they are forced to work a longer time than their own self-sustenance demands. (Heilbroner, 1992)

Hence, a byproduct of capitalism is the unequal distribution of wealth. Remember that the capitalists sell back their goods and services to the very workers that are cheated. The problem is that the worker produces more goods than he can afford to buy. Moreover, the capitalist makes more money than he needs to survive and cannot consume all the goods that are leftover. The result is surplus. Workers are laid off. The employees that maintain their jobs are still producing more goods than they can consume due to their low wages, so surplus continues. Economic collapse is inevitable - investments are lost, plants close, loans default, unemployment surges.

John A. Hobson claims that the only solution for the capitalist is imperialism. The capitalist nation must dump its surplus on its colonies and other nations, and the military must be used if necessary. Take for example the British government that forces nations and colonies in Asia and the Americas to trade, and uses its military power to do so. The British East India Company is, essentially, a collaboration between business and the military. Such activities lead to the well known "Boston Tea Party" and the phrase "No Taxation Without Representation".

> What was the substance of Hobson's charge?
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> It was an argument almost Marxian in its impersonality and inexorable development (although Hobson had no sympathy for the Marxists and their aims). It claimed that capitalism faced an insoluble internal difficulty and that it was forced to turn to imperialism, not out of pure lust for conquest, but to ensure its own economic survival.
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> That internal capitalist difficulty was an aspect of the system which had received surprisingly little attention in the past – capitalism's unequal distribution of wealth. The fact that the workings of the profit system very often resulted in a lopsided distribution of wealth had long been a topic for moral concern, but its economic consequences were left for Hobson to point out.
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> The consequence he saw was most surprising. The inequality of incomes led to the strangest of dilemmas – a paradoxical situation in which neither rich nor poor could consume enough goods. The poor could not consume enough because their incomes were too small, and the rich could not consume enough because

their incomes were too big! In other words, said Hobson, in order to clear its own market, an economy must consume everything that it makes: each good must have a buyer. Now, if he poor cannot afford to take more than the bare essentials, who is there to take the rest? Obviously, the rich. But while the rich have the money, they lack the physical capacity for that much consumption: a man with a million-dollar income would have to consume goods worth a thousand times those bought by a man with only a thousand dollars to spend.

And so, as a consequence of an inequitable division of wealth, the rich were forced to save. They saved not only because most of them wished to, anyway, but because they could not very well help themselves – their incomes were simply too large to be consumed.

It was this saving that led to trouble. The automatic savings of the rich strata of society had to be put to use, if the economy was not to suffer from the disastrous effects of an insufficiency of purchasing power. But the question was how to put the saving to work. The classical answer was to invest them in ever more factories and more production and thus to ascend to an even higher level of output and productivity: Smith, Ricardo, Mill, all the great economists agreed on this solution to the problem. But Hobson saw a difficulty in the way. For if the mass of the people were already having trouble buying all the goods thrown on the market because their incomes were too small, how, he asked, could a sensible capitalist invest in equipment that would throw still more goods on an over crowded market? What would be gained from investing savings in another shoe factory, let us say, when the market was already swamped with more shoes than could be readily absorbed? What was to be done?

And this is the genesis of imperialism. It is, wrote Hobson, 'the endeavor of the great controllers of industry to broaden the channel for the flow of their surplus wealth by seeking foreign markets and foreign investments to take off the goods and capital they cannot use at home.'

The result is disastrous. For it is not one nation only which is sending its surplus wealth abroad. All nations are in the same boat. Hence there ensues a race to partition the world, with each nation trying to fence off for its investors the richest and most lucrative markets it can seize. Thus Africa becomes a huge market (and a source of cheap raw materials) to be split among the capitalists of England and Germany and Italy and Belgium; Asia becomes a rich pie to be carved up among the Japanese and the Russians and the Dutch. India becomes a dumping ground for British industry, and China becomes an India for Japan.

Imperialism thus paves the way to war – not by swashbuckling adventures or high tragedy, but through a sordid process in which capitalist nations compete for outlets for their unemployed wealth. A less-inspiring cause for bloodshed could hardly be imagined. (Heilbroner, 1992)

Interest and Unemployment

Missing from the discussion so far is the question of money interest. Remember that Gog and Magog must borrow money in order to install machinery for their businesses. Interest is a major source of income in the capitalist model of the economy.

Economists say that all production starts with the factors of production: labor, entrepreneurship, land, and capital (that is, equipment). The payments to the owners of the factors of production are wages, profits, rents and interest, respectively. In business terminology, capital is used to describe money as well as equipment. This is because investment in equipment is usually done using loans. Thus, equipment and money secured by stock, bonds, and loans are usually all defined as capital.

To understand the relationship between the factors of production and the payment for the factors of production, a simple economic model commonly used by economist is presented in Figure 4. It is called the Circular Flow of Goods and Services Model.

In this model, only two sectors of society exist: households and firms. All people are part of households, even firm owners; firms are nonhuman entities. Households sell their factors of production to firms and firms pay households for the factors of production. In this example, payment is set nominally at $100. Households then save $20. The other $80 is used to purchase the goods and services that households helped to produce with their factors of production. Firms generate $100 worth of goods and services because the value of a product is equal to the cost that goes into making it. Such being the case, only $80 worth of goods and services are consumed. $20 of savings leads to $20 of surplus or inventories.

The only way to restore equilibrium to the economy is for households to loan $20 to firms in the next round of the circular flow of goods and services. Firms then buy up the inventories and turn it into working machinery or capital. Payment for the loan in the next round of the circular flow is made in the form of interest. Assume the interest is $1 (capitalism says that charging interest is good as long as it reflects the amount of goods produced due to expanded capital, that is, equipment); thus, a $20 investment augments output by $1 – no problem. Households still save $20 and buy $81 dollars of goods and services and again $20 worth of inventories accumulate. Remember that $20 of principle on the loan still has to be repayed. Where is the money coming from? How can this vicious cycle end?

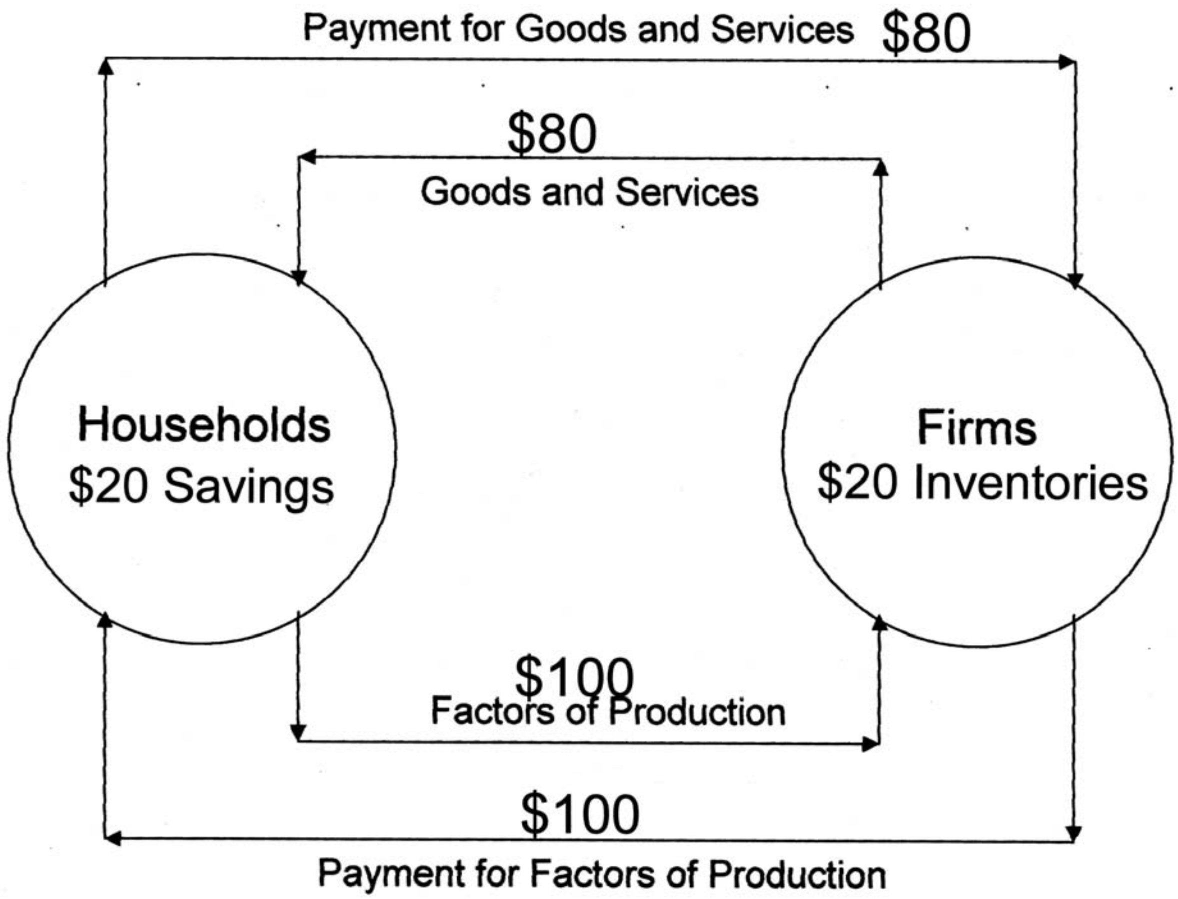
There is another issue that compounds this problem of accumulating inventories. The problem is inflation. When a deposit is made in a bank, a certain fraction is reserved at the bank by law. The rest can be loaned out. Assume, for example, that the reserve requirement is 20%. In the previous example, households save $20; that means $16 dollars can be loaned out. If that $16 dollars is put in the bank first before it is used to purchase machinery, then $12.8 dollars can be subsequently turned into loans. This process goes on infinitely. Economist even have an equation for this process, it is called the Deposit Expansion Multiplier:

$$\text{Deposit Expansion Multiplier} = \frac{1}{\text{Reserve Requirement}}$$

In this example, the Multiplier is 5. That means a simple deposit of $20 can potentially increase the money supply of an economy by $100, rather than by just $20.

Economists say this is a good thing. The increase in money capital increases the quantity of capital investment for machinery, tools, etc. More people are put to work and the quantity of goods and services is augmented. The aspect that economists do not address, however, is the fact that an increase in output leads to more employment and consequently higher volumes of savings. More money is available for capital investment and must be loaned out. Capital investment in machinery continues to expand. The increase in savings combined with the increase in production finally lead to a flood of inventories. Sooner or later the system crashes with a huge wave of unemployment, default loans, and accounting scandals. The tax payer and the government are left to clean up the mess via higher taxes and government insurance programs like unemployment compensation and the Federal Deposit Insurance Corporation.

Figure 4. Circular Flow of Goods and Services.



The other problem with deposit expansion is that the money supply is increased several orders of magnitude by a single deposit. This causes inflation because money is generated that is not immediately backed by tangible goods and services. In cases where the business fails, the goods and services are never produced. If the goods are not created then the prices of existing goods simply go up to match the quantity of available money people have to spend.

For this reason, advanced economies have established a national bank. In the USA, this bank is called the Federal Reserve. The "Fed" tries to control deposit expansion and inflation by fine tuning the economy through a tool called the Federal Discount Window Interest Rate. This is the rate that the Fed charges banks when they borrow from the federal government and serves as the baseline interest rate for all other interest rates. Firms are less likely to borrow at extremely high interest rates; hopefully the creation of money is restrained. It is intuitively clear even to the government that there is something inherently wrong with loaning and charging interest, to the extent an entire government entity is established to oversee this process.

CONCLUSION – THE SIMPLE LIFE

Returning to Gog and Magog, a full circle is made. When Gog and Magog trade their goods in the form of barter, no interest is charged; there is no exploitation. Each is better off from trade and cooperation is mutually beneficial; although no one is getting rich quickly.

As Gog and Magog follow the capitalist philosophy that desires are unlimited, the profit motive enters into the picture. The first step over the line is the acquisition of capital in the form of a loan at interest. It is granted that the true root of the problem is greed, lust, and avarice in the human heart; but men cannot know the hearts of other men. What men can know is that interest is the driving force behind deposit expansion.

If there were no such thing as interest, there would be no motive for making large quantities of loans – no profit motive. Rather, lending would occur only in special cases when one is in great need; and those in need would be loaned just enough to obtain their "daily bread". In such situations, loans are given carefully. Though the recipient of the loan is on one's honor to repay the loan, the loan is given with the understanding that it may not be repayed. In this scenario, a loan has very little effect on inflation. The likelihood of a great deposit expansion is very low.

Making loans to the needy and not exacting interest is an ancient theme in Jewish, Christian, and Islamic cultures

> When one of your fellow countrymen is reduced to poverty and is unable to hold out beside you, extend to him the privileges of an alien or a tenant, so that he may continue to live with you. Do not exact interest from your countryman either in money or in kind, but out of fear of God let him live with you. You are to lend him neither money at interest nor food at a profit. (Leviticus 25:35-37)

> At the end of every seven-year period you shall have a relaxation of debts, which shall be observed as follows. Every creditor shall relax his claim on what he has loaned his neighbor; he must not press his neighbor, his kinsman, because a relaxation in honor of the Lord has been proclaimed. (Deuteronomy 15:1-2)

> You shall not demand interest from your countrymen on a loan of money or of food or of anything else on which interest is usually demanded. (Deuteronomy 23:20)

> Those that live on usury shall rise up before Allah like men whom Satan has demented by his touch; for they claim that usury is like trading. But Allah has permitted trading and forbidden usury. (The Koran 2:275)

> Believers, have fear of Allah and waive what is still due to you from usury, if your faith be true; or war shall be declared against you by Allah and His apostle. If you repent, you may retain your principal, suffering no loss and causing loss to none. (The Koran 2:278-279)

> If your debtor be in straits, grant him a delay until he can discharge his debt; but if you waive the sum as alms it will be better for you, if you but knew it. (The Koran 2:280)

> The Carolingian rulers likewise struggled against the rampant evil of usury, which Charlemagne had occasion to define in 806: 'Usury exists when one claims back more than one has given, for example, if you have given six solidi and ask for more back, or if you have given one modius of wheat and then demand an extra one back.' In another capitulary, Charlemagne also forbade claiming interest on loans under a penalty of sixty solidi, that is, the fine for violating the bannum of the king. His successors continued to support the church's attempts to eliminate interest-bearing loans. Thus, Charles the Bald intervened to mitigate the effects of 'mortgages.' Originally, these loans bore a veiled form of interest. The borrower promised his creditor income or services from a possession (the gage, in French) that secured the loan, and the possession was often the borrower's person. When the loan came due, the original sum had to be repaid, or ownership of the security was forfeit (mort) to the lender. In the Edict of Pitres of 864, Charles limited to seven years the period for which a mortgagor might be indentured, and he also stipulated that the children of a woman entangled in a mortgage remained free.
>
> Royal power thus came to affect economic life significantly. Religious as well as practical concerns spurred the Carolingian rulers to act in ways that contributed to new economic and material progress. (Riche, 1993)
>
> The nature of the sin called usury has its proper place and origin in a loan contract. This financial contract between consenting parties demands, by its very nature, that one return to another only as much as he has received. The sin rests on the fact that sometimes the creditor desires more than he has given. Therefore he contends some gain is owed him beyond that which he loaned, but any gain which exceeds the amount he gave is illicit and usurious. (Pope Benedict XIV, 1745)

For this reason, a central bank is instituted - to control money that is multiplied when loans are made from loans. Loans are not made so easily if the profit motive is not the objective, that is, profit due to interest. Despite this fundamental flaw in capitalist economic theory, the worker is blamed for economic ills. The Federal Reserve watches very closely the level of unemployment. When too many people have a job, the Fed claims that inflation is eminent. Though this may be true, a person having a job can never be a bad thing. Nevertheless, the Fed insists that resource costs, wages, are being bid up and that the economy must be restored to "full employment".

The Federal Reserve then begins a series of interest rate hikes in an effort to curb the rate of loans being issued for investment. Companies then stop replacing machinery and stop plant expansions. Demand for housing, construction materials, trucks, and machinery slows; and ultimately, jobs are lost – jobs that the Fed says are jobs that are not really wanted, that is, frictional unemployment or transitional unemployment due to people changing jobs. Jimmy Carter is right: any economic system that manages inflation by putting their people out of work is bankrupt.

It is so clear to see that the system is bankrupt. The only thing a person can do is "give to Caesar what is Caesar's ." In other words, one does not have to accept the life style proposed by the capitalist system. One can simply live within one's means. "Neither lender nor borrower be".

Socrates, Aristotle, Moses, Jesus, and Muhammad, are all saying the same thing: live the simple life. Build slowly. Be content with what you have. Do not rush off to purchase homes, furniture, automobiles, vacations, etc and get buried in a mountain of debt. It is known from experience that as soon as corporations see their profit margins shrinking, the worker is blamed. All those material possessions can be gone in a flash after a few interest rate hikes.

There is so much more to life than money. It does not take a lot of money to sustain life. Yet, so many lives around the world cannot be sustained due to lack of food. The difference in wealth between the first and third worlds is staggering. Even within first world nations, the gulf between rich and poor is tremendous.

So the only solution is to live the simple life and help others in need when one can. If a neighbor down the street is suffocating due to mounting medical bills or has lost the roof of their house due to a tornado, then offer to fill their refrigerator with groceries or offer to help fix their roof with labor and materials. It is a good thing to help the needy and expect nothing in return. One can live in the capitalist system, but one does not have to be a part of it.

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