

Free Enterprise in America

by Robert Nozick

America has flourished under a system that includes a large, but not unlimited, scope for free enterprise. Is this a coincidence, or is the large component of free enterprise a cause of America's flourishing? And have the limits placed on free enterprise been beneficial or detrimental?

Framework of the System. A system of free enterprise has several components: property rights, freedom of action, of exchange, of association, and of contract. There are private and transferable property rights. Each adult may contract to provide or purchase goods and services in the present or for the future. The markets in which such rights to means of production, goods, and services are transferred or exchanged are open. There are no regulations limiting any adult from buying or selling in the market and there are no regulations limiting the terms of any agreements made except, of course, that no agreement may be made to inflict violence on another or to defraud another. Within this same limitation, which sets forth the rights of others, individuals may associate as they choose with contractual commitments setting the terms of their association and fixing their obligations and liabilities to one another. Activities, enterprises, or projects take place when supported by private parties, voluntary groupings, customers, benefactors, or patrons and there are no government subsidies for particular activities. Under such a system there will be competition in diverse markets, but there is no need to look for some economist's abstract notion of "perfect competition."

The components of free enterprise are protected by a governmental structure. But it is important to notice that the relationship is reciprocal, that the U.S. structure itself rests to a large extent on free enterprise. It is difficult to see how freedom of the press, for example, can flourish in the absence of private owners of such resources as paper or printing presses who can help disseminate, if only to profit from, opinions that the general public or the government finds objectionable.

Within the framework of free enterprise are accomplished the tasks that any ongoing society must carry out. The tasks are accomplished without central direction and perhaps even without anyone noticing them. Three features of the human condition are that people are not omniscient, that they have separate interests, and that resources are not sufficient for everyone to have everything he desires. Any society, therefore, will have some way of determining what particular mix of consumer goods is to be produced, how many resources are to be held back from current con-

sumption, and how much is to be invested to increase future production. Also, to effect these decisions the society will have to transmit information to the many people whose cooperation is needed for joint production.

The price system of an unhampered market in a free enterprise system provides people with a summary of far-flung information about the diverse uses of their labour and the material they control. They learn where its use is most wanted as compared with all other feasible uses. The retention of returns from performing these activities provides people with the requisite incentives to do them. In this way a market transmits knowledge of economic opportunities and coordinates the activities of people in an efficient manner, allowing people to spend their gained incentives for whatever purposes they choose.

Consumers pay for purchases with the results of their own previous economic activity, or with gifts received from the economic activity of others. Their desires for particular products are reflected back within the price system, ultimately to the owners of factors of production, who are eager to direct their resources so they will bring the highest return. Miscalculations about what consumers want or a lesser ability to serve these wants leads to losses rather than profits and so eventually to a redirection of these resources to more productive tasks. The risks of production for the market are borne, in a division of labour, by those who choose to carry them, by entrepreneurs who guarantee payment to factors of production including labour (even if their product, as it turns out, cannot profitably be sold) and who pay the producers before receiving returns from the sale of the final product. In organizing production of new products or new ways of producing old products the entrepreneur is ever alert, trying to out-produce or outfigure or outguess competitors to increase his profits. These profits (or losses) are the difference between what the entrepreneur must pay for the factors and labour utilized in production and the total payment for the final product.

Opportunities for profitable future use also lead people to hold back resources from current consumption and to turn them to the production of capital goods used for future production. Private and transferable property rights lead owners to take a long-term view of their resources and to forgo quick gains in order to realize future profits. With transferable rights future developments are capitalized into the present value of capital goods. In contrast, workers in a system of democratic workers' control, lacking transferable property rights, would downplay far-future benefits to be gotten from certain uses or preserving of current capital. It is precisely in activities where such property rights were lacking, for example in timbering on public lands, that future consequences were ignored. Allocation of goods over time is aided by speculators who

Robert Nozick, professor of philosophy at Harvard University, is the author of Anarchy, State, and Utopia (1974), a widely acclaimed defense of private enterprise and critique of the welfare state which won the National Book Award in 1975.

hold back goods from current consumption in anticipation of a higher future price. Time also enters in futures contracts, which enable the owner of a commodity to divest himself of the risk of fluctuations in its value.

Sometimes they are one and the same person but often they are not, and so savers who wish to invest and entrepreneurs who wish to organize factors of production must be brought together. This is done through private capital markets. The more developed a private capital market, the more sophisticated its money and credit instruments, the more intricate the enterprises it can sustain.

In a noncoercive fashion a system of free enterprise lures resources and people's activities into serving the desires of others and utilizes widely diverse information which no one person or central planning group does or can possess. Individuals, of course, may choose to pursue less lucrative activities; they may become artists rather than industrialists.

In theory a large number of different market forms are possible—each individual worker could act as an independent contractor, buying and selling intermediate products. But most production in the U.S. is carried on by business firms, wherein great economies are gained by specification and direction of labour. Corporations have come to the fore as vehicles allowing persons to invest and capitalize on increases in value without also having to manage the firm. Aided by transferable ownership shares and continuity through the death of owners, this division of tasks within the corporate form facilitates the raising of large amounts of capital.

Origins of Free Enterprise. U.S. history provides the prime example of how free enterprise operates. With the lifting of English mercantilist restrictions, the United States came to be an arena of largely free enterprise, at least as compared with other countries. The government was restricted to maintaining the peace within which economic activities could proceed and enforcing and making more precise laws of contracts and of property, including patent laws securing intellectual property. But there were some notable legal carry-overs from the English distrust of capitalism. America constituted a wide and open market with extensive division of labour and economies of scale. It was populated by persons desiring more goods and services who were willing to work, save, and bear risks for profit, and who were willing to learn and adapt to new situations and ideas. It contained large doses of entrepreneurial talent. Immigrants replenished its spirit of innovation and energy bringing scarce skills and a desire to work and advance into a situation that contained no established guilds, professional associations, restrictive trade unions, or government licensing. Anyone could market and benefit from the skills he had or could acquire. No land tenure system stopped enterprising persons from acquiring and utilizing more land, nor was there envy sufficient to exert strong social pressure against success.

Over a short period of time the U.S. equaled and then economically surpassed England, the home of the Industrial Revolution. There was an enormous increase in the population the U.S. supported, along with a great growth in per capita output, a widespread diffusion of material well-being, and high levels of health. Manufacturing

thrived. There was large-scale utilization of technology in both industry and agriculture. Supporting, sustaining, and producing this was a high investment of capital per head, guided into diverse forms, areas, and uses by the opportunities for profit in the market. Without the market's wise and intricate detailing, specification, and continuous reshuffling and reorganization of capital, even a large amount of capital per head would avail little. From great entrepreneurs such as Andrew Carnegie and Henry Ford came an industry that was the wonder of the world. Fortunes were made and lost and much of investment came from the profits of industry reinvested. All were not equally well-off, but there was no serious attempt before the 20th century to redistribute wealth so as to inhibit capital formation or the exercise of special skills.

Economic Role of Natural Resources. We have spoken of free enterprise as a framework for entrepreneurship, saving, investment, and work and of an American population well fitted to utilize this framework. What role was played by the country's abundant natural resources and fertile land? These resources were not utilized to any great extent by the native Americans. To play an economic role, resources must be discovered and utilized and capital must be applied to them. Only in an appropriate economic context and environment do resources have economic value. Letting few opportunities for profit go unrealized, free enterprise encourages the efficient use of resources. Does the experience of the socialist countries show that free enterprise is unnecessary for economic prosperity and so cast doubt on its causal role in the U.S.? The hesitant and reluctant movements toward market forms in socialist bloc countries, driven by economic necessity, testify to the efficiency of allocation in a market and price system; but they will not reap its full benefits without private and transferable property rights.

Government Involvement. In what ways has the government aided the United States in achieving economic prosperity? The major governmental benefit was providing the framework of protection, specification of property, and enforcement of contract within which the voluntary and enterprising actions of persons caused the economy to flourish. Furthermore, there were government policies, from auctioning land to the homesteading act, that put land into private hands with the effect of aiding the cultivation and care of the land and long-term investment in it.

These government activities reinforced the system of free private enterprise by providing the framework within which it operated and extending its scope. But the U.S. did not have a completely free and unhampered enterprise system. There were government activities, national and local, which changed, diverted, or stopped certain market processes. Did these activities play a significant role in U.S. prosperity? Some examples of limits placed on free enterprise include the enslavement of blacks, whose liberty of activity and reward were severely limited with no adequate attempt at recompense. Another limit is government expansion of the credit supply (now through the Federal Reserve System), which brings malinvestment, an intensification of the trade cycle, inflation, and then depression, in which are eliminated the previous uneconomic investments induced by the distortion of price and interest rates

caused by the credit expansion. In the 20th century there has been movement toward the cartelization of industry. Each of these deviations from a system of free enterprise has catastrophic results, some still occurring.

Government regulation of industries, supposedly to protect consumers, leads to industry-dominated regulatory bodies that act to restrict competition and to protect established firms from new competitors. This is not surprising because these regulatory bodies were favoured by the industries from the beginning as ways of securing their own positions. Antitrust regulation has acted to penalize efficient firms and keep prices up. Occupations are licensed, limiting entry and competition at a cost to the consumer. Prices, interest rates, rents, and wages are controlled, resulting in scarcities, unemployment, and misallocation of resources. Firms are subsidized by tax money and tariffs. Railroads received land grants and legal monopolistic positions and, secure from competition, proceeded to exploit their legally granted monopoly in the rates they charged farmers. It is generally true that the bad things attributed to free enterprise are effects of government interferences with free enterprise. These effects are then intensified by the further interventions made in an attempt to avoid or mitigate the unfortunate but predictable effects of the prior interferences.

The 19th-century governmental interventions most plausibly argued to be beneficial were those subsidies to transportation (turnpikes, canals, and some railroads) and education. Even with the most significant of these, the railroads, the 12.9% rate of return (according to a recent estimate) on private capital used in building railroads probably would have been sufficient to get them built. In education local government expenditure was high and education played a role in producing a literate labour force. But because in the absence of government provision there would have been more private expenditure it is difficult to know how much difference the government made.

Perhaps the actual government interventions were detrimental, but does not unlimited free enterprise have its own faults? Some of the most popular complaints are that it leads to monopolies, war and imperialism, capitalist bribing of government officials, pollution and nonconservation of resources, and to multinational corporations eroding national sovereignty. But these complaints do not hold up under scrutiny. It is the protection provided by the government regulatory agencies that has most aided monopolies and there is no indication that open markets over time will not erode any temporarily monopolistic position, especially with a well-developed capital market that will finance enterprise in areas with an especially high rate of return. International markets and free trade do not flourish under the rupture of wartime. Wars are made by nations who try to gain benefits by seizure rather than purchase. Pollution problems stem from imperfect enforcement and specification of the property rights of those polluted, while the future orientation of the market entrepreneur encourages conservation before any government might become alerted to its importance. Businessmen and others seek to influence government officials in order to gain special benefits from them. The solution is to eliminate or drastically restrict that illegitimate power to confer special

benefits. Multinational corporations are new, but as a cement for international ties and peace they are promising. These and other objections to free enterprise can be met one by one, yet this has little effect. A puzzle whose satisfactory solution still evades us is why many persons, especially intellectuals, so desire there to be some conclusive objection to free enterprise.

If the economic activities of government beyond the maintenance of the free enterprise framework work out so badly, why are they allowed to continue? They work out badly for most of us, but they don't work out badly for each and every person. Those who specially and greatly benefit do so at the expense of the vast majority of others. The cost of one government intervention may be small to each person, but is great in total. The cost of all government intervention together is great to each person. Those benefiting greatly are willing to devote their energy and resources to inducing the government to intervene in their own behalf, whereas it is usually not sufficiently in any one other person's or consumer's interest to devote significant resources to opposing any particular governmental intervention and favouritism. Therefore a system that takes each case of intervention "on its own merits," allows, due to its dynamics, many harmful interventions strongly favoured by special interests. Only the adherence to a general prohibition of governmental interventions could prevent the pork barrel and because such a general prohibition is in everyone's interests, therein lies some hope.

Rights of the Individual. A system of free enterprise is productive and beneficial but is it just? Complaints sometimes are made against the distribution of wealth and the income that result. Some of the complaints about the actual distribution in the U.S. turn out, upon examination, to be about the effect of interference with free enterprise. If people gain what they have by legitimate market means, through voluntary transactions that others choose to enter, then they are entitled to what they have. A just distribution is one in which everyone is entitled to what he has and it would be unjust to forcibly impose some pattern of distribution by coercive government means. Nothing stops anyone who favours some alternative pattern not brought about by the total of previous voluntary choices from transferring some of his own holdings to others or convincing others to do this, so as to more nearly realize his preferred pattern. The liberty to engage in market transactions, unhampered, is itself a component of liberty. People have a moral right to engage in cooperative activities with others on mutually agreed on terms, including exchanges of goods, services, and labour. Governments have no moral right to prohibit capitalist acts between consenting adults.

The United States broke away from mercantilist England and stood, though imperfectly, for liberty (including economic liberty) and for property rights. These two ideals are right not only for their economic and productive fruits and for the allowing of new ideas to be tried out, picked up, imitated, and modified, important though these be, but also they are right, important, and valuable in themselves. If we fail to stop the drift away from these ideals, the drift in which England has preceded us, the apparent dismal fate of the country we broke away from will become our own.