

## **EIR**SpecialReport

# Mont Pelerin's hatchetman: Milton Friedman

by David Goldman

Except in Keynes's Bretton Woods heyday, no twentieth-century economist has attained the influence Milton Friedman currently wields over several major governments, including America and Great Britain. That is a principal reason for the divergence of the world economy into a relatively prosperous European Monetary System zone on one side, and a plunging "Anglo-Saxon business cycle" on the other, in the phrase of self-described Friedmanesque economist Paul McCracken.

Friedman's supremacy among Reagan's economic advisors was unchallenged as of last week's Republican Party platform discussions, when Friedman's supposed antipode, Rep. Jack Kemp, embraced the Friedman formula of reducing both taxes and the absolute size of government spending. The policy constellation around Governor Reagan is now composed exclusively of the men who brought off the economic disasters of the Nixon Administration, including ex-Labor and Treasury Secretary George Schultz, SEC and Eximbank chief William Casey, and Ford senior officials William E. Simon and Alan Greenspan.

With Nixon Treasury Undersecretary Paul A. Volcker in the Federal Reserve slot conducting a monetary program based on Friedman's formula, the circle is closed between both parties. Both party platforms will defend the present depression, if Carter and Reagan are the nominees. Novel as this approach is for the Democratic Party, it is no less astonishing that the Republican Party should retain the policies that account for most of its policy and electoral disasters during the past 30 years.

American politics does not make sense without a look behind Milton Friedman's public relations image as presented on the public television series "Free to Choose," or in Friedman's book of the same name. The man's partisans, e.g., Lindley Clarke in the July 8 *Wall Street Journal*, argue that Friedman's theories are in danger of being abandoned before they are given a fair chance of success. That is another way of saying that Friedman's leading role in the economic disasters at home during the Nixon administra-



tion, and abroad in Britain, Israel, and Chile, have forced the early abandonment of his policies wherever adopted previously.

But Friedman's old mugging-mate and publisher, *National Review* editor William F. Buckley, summed up the entire problem with some accuracy after Nixon dumped Friedman as White House advisor. Buckley wrote after the dollar devaluation package of Aug. 15, 1971, "Mr. Friedman can absolutely be counted upon to say that his theories were not given an adequate exercise. There is no doubting that he is correct. But it is possible that his theories suffer from the overriding disqualification that they simply cannot get a sufficient exercise in democratic situations."

### **Friedman's leverage**

We will demonstrate in some detail that Buckley's judgement is accurate, although not for the reasons Buckley would cite. Friedman's role as the *controller*—not the mere theoretician—of the fascist Chilean junta's economic policies is more significant than the moral atrocity his opponents have cited. Since its 1947 founding, Friedman has been a member and more recently the Vice-President of an Austro-Hungarian Empire secret society, the so-called Mont Pelerin Society. Founded by Friedrich von Hayek and Ludwig von Mises at Mont Pelerin on Lake Geneva, the Mont Pelerin group was the economic policy arm of Count Coudenhove-Kalergi's (and later Otto von Hapsburg's) Pan-European Union, the recentralization after World

War II of leading Nazi collaborators in Europe. The world headquarters of the Mont Pelerin group is in Madrid, at Otto von Hapsburg's Center for Documentation and Information. William Buckley has, for years, made thrice-yearly visits there.

This seemingly arcane information is, in fact, of the greatest relevance to understanding the current shape of American policy. Friedman's influence in the Reagan campaign has nothing, properly speaking, to do with economics. He is a member in good standing of the Austro-Hungarian mafia that currently runs most of Reagan's policies. Its base is Georgetown University's Center for Strategic and International Studies, the Jesuit institution founded by Father Walsh, a vocal partisan for the return of Europe to Hapsburg dominion until his death. Former Treasury Secretary William Simon is currently the Chairman of the Board of Trustees of Georgetown University. The Hapsburg circuit includes:

- Reagan foreign policy advisor Richard V. Allen, who works out of Georgetown CSIS.
- Foreign policy advisor Robert Strausz-Hupe, a Viennese emigré of the 1930s who now heads the Philadelphia-based Foreign Policy Research Institute.
- The Hoover Institution at Stanford University, where Milton Friedman is Senior Research Fellow. Hoover president Glenn Campbell, like Friedman, is a Mont Pelerin Society member.

All this could be read too simply. Dr. Edward Teller, one of the nation's most respected physicists, is also at

Hoover, and a number of well-intended individuals, including the late French economist Jacques Rueff, found their way at different times into the Mont Pelerin Society. However, Friedman—apart from his performance in Chile—stands out in a striking fashion. The core thinking of the Hapsburg Empire remnants has been that Hitler botched what was, in their final analysis, the right direction to take. Friedman's contribution to this has been an explicit defense of Nazi monetary policies, published in 1956 in the "classic" *Studies in the Quantity Theory of Money*. Friedman's leading argument is that Hitler—contrary to the objections of his finance minister Dr. Schacht—was successful in controlling wartime inflation, despite the huge costs of war preparations. Friedman arrived at this conclusion by reducing his index of German money supply every time Hitler conquered new populations.

In essence, Friedman endorsed Hitler's statement, as reported in *Hitler's Table Talk*: "Even to Schacht, I had to begin by explaining this elementary truth: that the essential cause of the stability of our currency was to be sought for in our concentration camps." There is no reason to suspect Friedman of innocence in the matter of the Chilean junta. He and his friends have been dealing with Latin American Nazis for some decades.

### **The Mont Pelerin crew**

Otto von Hapsburg and his friends are not merely intellectual terrorists, but terrorists in fact—something that will become more relevant when we discuss Milton Friedman's relationship to the Chilean dictatorship. Apart from Skorzeny, whose association with his father-in-law Hjalmar Schacht persisted through their escapades in Egypt during the early 1950s, Hapsburg's Center for Documentation and Information housed some of the most despised ex-Nazis in Europe throughout the 1950s. One was Leon Degrelle, the Belgian quisling who joined the Waffen SS in 1943, an action which forced him to seek asylum in fascist Spain in 1945. While Degrelle was associated with Hapsburg in Madrid—according to reports published in the West German weekly *Der Spiegel* in 1959—he collaborated with a putschist movement in Germany centered around Josef Goebbels' old propaganda chief Werner Naumann.

Another Hapsburg contact was the Nazis' puppet Prime Minister in wartime Hungary, Ferenc Nagy, who later founded the terrorist organization Permindex. Permindex—as Kalimtgis, Steinberg and Goldman documented in the book *Dope, Inc.*—was booted out of Europe by Charles de Gaulle after discovering that the supposed trading company had conduited the funds to his would-be assassins. Nagy personally handled the money transfers through White Russian sub-agents based out of New Orleans. In New Orleans District

Attorney Jim Garrison's investigation of the Kennedy assassination, Nagy figured as a principal suspect; he had been in Dallas immediately before Kennedy was killed and was in close touch with all the principal suspects in the Garrison investigation, including Permindex New Orleans representative Clay Shaw. When Nagy conduited funds to the Secret Army Organization (OAS) generals for a projected hit against de Gaulle, Skorzeny was in collaboration with the coup plotters.

Leader of the Latin American contingent in Hapsburg's Madrid Center is the chief of Colombia's drug lobby, Alvaro Gómez Hurtado, who wrote in his daily newspaper *El Siglo* in August 1977:

"Colombians must think very seriously about legalizing marijuana immediately, first, because it will yield us foreign exchange. And second, because we have proven that to prohibit it, to help a country that is not interested in its promotion, is damaging to the morals of those charged with enforcing the law." Buckley's and Friedman's endorsement of marijuana legalization dates from the same year.

Gómez' paper *El Siglo* was founded in 1936 by his father, Laureano Gómez, who had just returned from Germany after a stint as Colombia's ambassador. In a founding editorial, Laureano echoed what could pass as the credo of the Mont Pelerin Society:

"Hitler has proven that it is possible to wage a long, difficult and immensely costly war without money. The Jews thought they could boycott Germany by removing all the gold and transferring it to the U.S. They were mistaken. The Führer has made a truly miraculous discovery: he has found that he and his people can get along on the work standard."

Laureano Gómez used the Nazi salute in public. He became President in 1950, and launched the series of massacres known as *La Violencia* (The Violence)—in which 300,000 Colombian men, women and children were systematically murdered in an attempted "purge" of "heretics" and "liberals," including newborn infants. His son Alvaro took over the paper's editorship in 1952—at the height of his father's massacres—the same year that he became a member of Hapsburg's Center in Madrid.

Another Latin American member of the Center for Documentation and Information is Andrés Marcelo Sada, a former graduate student of Ludwig von Mises. As head of the Mexican Employers Confederation in 1977, Sada attempted to bring down the Echeverría government in response to the Mexican President's aggressive land reform program. Documents introduced into evidence in the Mexican Parliament on Sept. 7, 1978 indicate that Sada had tried to persuade the CIA to join in a plan to overthrow the Mexican government, along with Spanish right-wing terrorists and agents of the fascist Chilean secret police.

Otto von Hapsburg's operation is a barely cleaned-up version of Count Coudenhove-Kalergi's Nazi support organization, integrating sections of the old Nazi machine itself. The Mont Pelerin Society is merely Hapsburg's economic thinktank. The monarchist terror network affiliated with Otto von Hapsburg in Madrid is composed of men trained personally by Ludwig von Mises and Count Coudenhove-Kalergi at their New York University Seminar in the 1940s. One of these is Andrés Marcelo Sada. Another is Gustavo R. Velasco, professor and founder of the Free School of Law in Mexico City. Velasco, head of the Mont Pelerin Society in Latin America, dates back to the Hitler sympathizers in the old Mexican National Action Party, who funded his "Free School" in 1944.

Velasco's student at the Free School, Luís Pasos, is Milton Friedman's closest personal contact in Mexico, arranging Friedman's speaking engagements in that country. The author of several books praising Friedman, Pasos was a founder of what Mexican intelligence sources call "a rightwing shock troop and terrorist unit," the Spanish-American Unification Guard, or *Guía*—"Führer" in its Spanish acronym. Pasos is director of the "Institute of Interamerican Integration."

When Milton Friedman's old University of Chicago students in the junta that seized Chile in 1973 proceeded to butcher the Chilean population, Friedman's personal role in the affair drew attention internationally. To the detriment of clear thinking, the furor over Friedman's support for Chilean fascism became a silly back-and-forth over Friedman's actual relationship to the Pinochet junta. This is all wasted breath. The point is not *merely* that Friedman got his hands—and possibly his elbows—dipped in blood in Chile, but that he has been part of a neo-Nazi movement since 1947. Worse, he is an officer of a Nazi organization, vice-president of the Mont Pelerin Society. Milton Friedman is not sullied by contact with the Chilean Nazis. He, Pinochet, Alvaro Gómez Hurtado and the rest are part of a fascist machine that has been in place for 35 years.

All this helps to clarify why a mediocrity like Friedman won an international reputation, and why he is so fond of the economic policies of Adolf Hitler.

### **Not an economist**

Friedman's lengthy public television discussions of "free enterprise" and libertarianism should not be taken any more seriously than face-cream commercials. The most important thing about these books and broadcasts for popular audiences is what is missing: the subject of economics. Friedman strings together numbers of interesting criticisms of government stumbling, but never discusses what makes economic growth possible. Indeed, in his theoretical writings, he insists that his theory is one of "nominal income," i.e., monetary

income, and explicitly excludes the real economy, i.e., the tangible economy, from consideration.

Of course, once you define economics to exclude the economy other than the monetary system, you can explain away virtually anything, including the Nazi or Chilean junta's economic performance.

Personally, Friedman is a synthetic man. The much-vaunted theoretical brilliance that won him the Nobel Prize—or provided the excuse for it—is much less impressive on inspection. His supposed contributions are first in the area of "price theory," the most-abstruse and least-applied branch of Marshallian economics, used by no one but Friedman's graduate students. Friedman's receipt of a scholarship to the University of Chicago in 1932, arranged by National Bureau of Economic Research founder Wesley Clair Mitchell, was a minor feature of the buildup of the university, under Robert Hutchins, as the depot for the emigrating University of Vienna. Friedman's brand of "conservatism" is not American, but rather a retreaded version of Austro-Hungarian Empire monarchist-restorationism. Widely regarded as a kook, Friedman gained national prominence only by virtue of the Mont Pelerin connection during the Goldwater campaign. He came on board along with Strausz-Hupe, Viennese economist Gottfried Haberler (now at the American Enterprise Institute), William Buckley, and others. Friedman's brand of conservatism is pure Viennese import, as much as Georgetown's "geopolitics" is the product of the Wittelsbach court at Munich which sponsored the early sprees of Adolf Hitler.

Friedman's prestige as the losing spokesman on economic policy for Barry Goldwater gave him sufficient momentum to influence the first year of Nixon administration economic policy, long enough to provoke the 1970 recession and the events that led to Aug. 15, 1971.

Ironically, it is possible that Friedman's influence may diminish rapidly in the near future, if only because the mafia that sponsored him no longer has use for his formulas or for his services as public relations man. The next American President will have to address the problem now subject to great publicity under the slogan "reindustrialization," namely, the collapse of America's international position in world markets and defense capabilities with respect to the Soviet Union. Friedman has done a marvelous job of wrecking both industrial and developing sector economies. But that is not a viable policy objective for the United States, if only because Friedman's sponsors cannot prevent Western Europe from leaving the U.S. to its self-inflicted miseries. They require something better than Friedman's "theory of nominal income" merely to survive. And Friedman, who at bottom is a jumped-up graduate student, is expendable.

# Friedman's Nazi economics: turning inflation inward

EIR is pleased to present excerpts from the forthcoming book *The Two Faces of Milton Friedman*, by Contributing Editor Lyndon H. LaRouche, Jr. and Economics Editor David Goldman. These selections are taken from Chapters 1 and 6 of the volume, which will be published in the fall in paperback form by the New Benjamin Franklin House Publishing Co., New York. The excerpts begin with a discussion of Friedman's favorable analysis of Nazi financial practices.

## Friedman's Nazi economics

We define "Nazi economics" to mean the combination of "fiscal austerity" and diversion of all national resources to the investment requirements of war autarchy.

Volcker's objective is to repeat Schacht's achievements, as described by Milton Friedman in *Studies on the Quantity Theory of Money*: to maintain gigantic nonproductive expenditures while preventing inflationary collapse of the monetary system. Inherently, war production, especially "Blitzkrieg" production in width at a stagnant level of technology, is violently inflationary.

Production of energy at costs several times in excess of the cost of nuclear-generated electricity, and several hundred times the estimated cost of fusion-generated electricity, is also inflationary.

The collapse of industrial efficiency throughout the economy due to Schachtian investments lets loose a hyperinflationary tendency.

Despite the *tendency* towards hyperinflation under fascism, it is possible to suppress inflation, as Milton Friedman proved in his now-classic study of Nazi economics, at least for some period of time. In a 1976 discussion with LaRouche, the great French economist Jacques Rueff, who died last year, proposed an alternative definition of fascist economics as "inflation turned inward against the economy," leading to the same conclusion as LaRouche's different approach.

Instead of absorbing the consequences of massive nonproductive spending through increasing price levels,

the Nazi economy absorbed these consequences by cannibalizing the economy's own flesh and bone, "turning inflation inward." Rueff's definition is precise and correct, and stands in striking contrast to Milton Friedman, who leaves the consequences for the real economy out of his analysis altogether.

In a somewhat horrifying way, Milton Friedman takes real economic resources into indirect account, by factoring in the slave populations of Nazi-conquered Europe to "adjust the money supply figures." But he insists that real economic resources had nothing whatever to do with the problems of the Nazi economy, by arguing that the Nazis permitted civilian economic activity "to operate in a leisurely, semi-peace fashion," and failed to "restrict civilian consumption" until efficiency expert Albert Speer took over.

One critical instance of lying by omission must be cited in Milton Friedman's account of Nazi economics. Jacques Rueff pointed it out, with some bitterness: "Contrary to general belief, Dr. Schacht did not invent Hitler's monetary policy." Germany's British and American creditors, Rueff reported, "advised Germany to suspend its foreign commitments and authorized it to put into effect, with the blessing of its creditors, the system that was to enable Dr. Schacht and Hitler to finance war preparations and finally unleash war itself."

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## Through the looking-glass

If, as an intellectual exercise, we asked the reader to construct an "economic theory" that could describe Nazi economics as a possibly "successful" system, he would probably start this way: the first condition of this new economic theory would have to be that the real economy never had to be taken into account, and the second condition would have to be that the theorizer can define "reality" to be whatever he wanted it to be wherever he wanted it to be that way.

You have now grasped the essence of Milton Friedman's economic theory. . . .

In his published output, Friedman carefully distinguishes between his “popular” books such as *Capitalism and Freedom* or *Free to Choose*, and his technical work, including *Studies in the Quantity Theory of Money*, *Essays in Positive Economics*, *A Monetary History of the United States*, and *Milton Friedman’s Monetary Framework*.

They are unreadable academic jargon. Virtually no one reads them.

One of Friedman’s old Chicago School colleagues, Prof. Arthur Laffer (now at the University of Southern California), was asked by the authors to suggest a method of proving to a wide audience that Friedman was a fascist. Laffer replied, “Quote him.”

Friedman’s early notoriety as a “theorist” sprang from an essay published in 1953 in *Essays in Positive Economics*, entitled, “The Methodology of Positive Economics.” He insisted in this essay that his approach was “positive,” which he said meant “objective,” while everyone else’s was by implication “normative,” i.e. cooked up to fit preconceived conclusions. Let us quote what Friedman had to say on the subject:

In so far as a theory can be said to have ‘assumption’s at all, and in so far as their ‘realism’ can be judged independently of the validity of predictions, the relation between the significance of a theory and the ‘realism’ of its ‘assumptions’ is almost the opposite of that suggested by the view under criticism. Truly important and significant hypotheses will be found to have assumptions that are wildly inaccurate descriptive representations of reality, and, in general, the more significant the theory, the more unrealistic the assumptions (in this sense). The reason is simple. A hypothesis is important if it “explains” much by little, that is, if it abstracts the common and crucial elements from the mass of complex and detailed circumstances surrounding the phenomena to be explained and permits valid predictions on the basis of them alone. To be important, therefore, a hypothesis must be descriptively false in its assumptions; it takes account of, and accounts for, none of the many other attendant circumstances, since its very success shows them to be irrelevant for the phenomena to be explained.

This is an unabashed defense of irrationality. . . . In a later chapter we will review Friedman’s career and note, in passing, that he has the worst predictive record in the economics profession, itself notorious for failed predictions in general. But that is not the important point here. Friedman is making a statement in the general tradition of the Bertrand Russell-Ludwig Wittgenstein positivists, restricting the pursuit of knowledge to some abstract juggling of empirical data.

But none of the most extreme Vienna positivists would ever argue that some simple extrapolation of a tendency one chances to hit upon in a data series proves any hypothesis, merely because some other data collected in the future happen to fit into the linear extrapolation trend. In any event, Friedman never succeeded once in explaining anything in this fashion, as readers who have puzzled through “A Monetary History of the United States” well know.

### **Money, prices and output**

What precisely is it that Friedman claims to have achieved as a theoretical economist? In a “debate with his critics” published by the University of Chicago in 1970, Friedman stated his claim to fame to be a method of describing economics *in monetary terms only*, without reference to the problem of real economic growth. As we guessed earlier, something like this must have stood behind Friedman’s assertion that the Nazi economy was “successful” from the standpoint of monetary analysis. Waspishly, Friedman accused his critics of misunderstanding him by assuming gratuitously that he was talking about real economic growth, whereas the “quantity theory of money” has nothing to do with anything but money and prices.

“We have always tried to qualify our statements about the importance of changes in M [Friedman’s symbol for money supply] by referring to their effect on *nominal* income [original emphasis]. But this qualification appeared meaningless to economists who implicitly identified nominal with real magnitudes. Hence, they have misunderstood our conclusions. . . .” he wrote in *Milton Friedman’s Monetary Framework*. “I regard the description of our position as ‘money is all that matters for changes in *nominal* income and for *short-run* changes in real income’ as an exaggeration but one that gives the right flavor of our conclusions.”

Friedman correctly points out that neither he nor the Keynesians have got what he calls the “missing equation” that tells us what the relationship might be between prices and real economic activity. That is very true; the “Phillips curve” that the Keynesians proudly hailed in 1970 said that prices went up when unemployment went down and prices went down when unemployment went up. In the years of combined depressed real economic activity and high inflation, the “Phillips curve” has disappeared from the academic journals and the financial pages, and retired to the closet with other similar skeletons.

The remedy Friedman proposes to the terrible predicament of the economics profession, which admittedly could not find any relationship between prices and output, is breathtakingly simple: ignore the problem altogether. . . .

Friedman proposes “*bypassing* the breakdown of

nominal income between real income and prices and using the quantity theory to derive a theory of nominal income rather than a theory of either prices or real income." This works out nicely, Friedman discovered. . . "Nominal quantity of money" means how many dollars are sloshing around, and "nominal income" means how much money individuals get, regardless of how much this money can buy. Friedman says that there is a "close and dependable" link between these two things, a conclusion that does not seem particularly striking.

Note that he says that the relationship between money and prices and money and output is *not* so dependable—although he does not say so in his *Newsweek* columns or his television programs. "If you are a yokel, he gives you a hokum answer," Paul Samuelson said.

Where his peers in the academic world were concerned, Friedman's famous assertion that changes in the money supply cause changes in prices actually fell by the wayside on the last page of his *magnum opus*, *A Monetary History of the United States*. Friedman could not find any consistent behavior for what is called the "velocity of circulation" of money during the entire post-war period. The way the "Quantity Theory of Money" is supposed to work, Friedman reports, is according to a turn-of-the-century formula penned by Yale professor Irving Fisher, now best-known for a prediction in mid-1929 that the stock market rise proved that the United States would have permanent prosperity.

The formula reads  $MV=PT$ , where M is money supply, V is its velocity (how fast people spend it), and P is the price level, T is the amount of goods available per unit of time. It says that if there is more money and people spend it faster, prices will rise.

The "bogey" variable is the "velocity of circulation," or V. Monetarists from Jevons and Marshall a century ago to Friedman now have put tomes of statistics through analysis in an attempt to explain why it goes up or down, without measurable success, as Friedman admitted in the volume we started with, *Studies in the Quantity Theory of Money* and later in his 1963-published monetary history, finally giving up the attempt in 1970, in the "debate" cited earlier.

In conclusion, that leaves us with a theory that says if there is a lot of money about, individuals are likely to have a lot of it, the "theory of nominal income." If this sounds like gibberish, that is not our fault; our responsibility was to present to the reader exactly what it is that Friedman says. It should not be a surprise that Friedman's academic opponents do not come outright and say that all of Friedman's theories are irrelevant, boring nonsense, considering the quality of their own opposing theories.

## Setting up Nixon for August 1971

Americans defeated Goldwater by a landslide margin, which he richly deserved, more than the country deserved Lyndon Johnson. Friedman, whom any person in his right mind would recognize as "utterly irresponsible," led Goldwater all the way down the garden path.

This makes even more astonishing Richard Nixon's decision to make Friedman the Administration's chief, if unofficial, economic advisor, after his election in 1969. Journalist Leonard Silk, who chronicled the tortuous route of Nixon economic policy with partisan glee, suggested it was because Nixon and his colleagues were stupid.

Nixon, in any event, had been a wartime pal of Friedman's at the Office of Price Stability at Treasury, and learned his economics at the White House at Arthur Burns' knee. Burns now moved back to the White House from Columbia as Counselor to the President. The next year, Burns replaced the aging William McChesney Martin as Chairman of the Federal Reserve's Board of Governors.

During the first half of 1969, the Federal Reserve held the rate of money supply growth to 4.4 percent per year, right in the middle of Friedman's recommended range of 3 to 5 percent. Prices rose by an annual rate of 5.8 percent, faster than they had during what Nixon considered a period of monetary laxity under Lyndon Johnson, when they had risen by 4.6 percent per year. This did not upset Friedman, who believed that monetary policy operated with a six-month lag. He wrote, however, in August 1969, "If the rate of price rise has not begun to abate by the fourth quarter of this year, it will be time to ask us for an explanation."

But the rate of price inflation did not abate. It continued at 5.8 percent per year through the second half of 1969, and showed no signs of improvement.

Friedman prescribed more of the same medicine, and the Federal Reserve under Nixon's imprimatur obeyed. Monetary growth stopped dead in the half-year from June 1969 to December 1969, and the economy collapsed. Industrial production fell starting in the summer, and unemployment rose from 3.5 percent in 1969 to 5 percent in May 1970. Despite the deterioration of economic conditions, inflation did not fall. During the first half of 1970, inflation was *higher* than it had been the previous year. Leonard Silk summed up, "Interest rates had climbed to levels not seen in a hundred years, with

devastating effects on housing. The federal budget was dropping into deficit, aggravating pressures on money markets. The stock market went into the worst decline it had experienced since the Great Depression.”

Friedman nearly brought the American economy through a repetition of the 1929 crash, by identical methods. In May the Penn Central Railroad went bankrupt, leaving hundreds of millions of dollars in short-term commercial paper outstanding. The entire structure of American short-term credit, which depended on tens of billions of dollars in short-term promissory notes secured only by the faith of the borrower, was in danger. Bankers sat in their offices deciding whether or not to panic, and Arthur Burns made a series of frantic phone calls to New York and Chicago promising that the Fed would provide as much money as needed as soon as they needed it. From dead zero, the rate of money supply growth jumped to 13 percent. Penn Central did not lead to a general panic in the American credit markets. However, the sudden lurch from monetary strangulation to a postwar extreme in monetary laxity sent the American dollar skidding down towards the great debacle of August 1971. The first big dollar crisis of the Nixon administration broke out almost as soon as Burns opened the floodgates in May 1970.

Nixon was stupid, but not that stupid. On the next moonless night he buried Milton Friedman's reputation in the White House back lawn. Immediately after followed Nixon's great recantation, "We are all Keynesians now," meaning, "We are no longer Friedmanites!" That didn't get either the White House or the United States out of the hole that a year of Friedman's medicine had put it in. By August 15, 1971, Nixon caved in to the demands of Rep. Henry Reuss and Paul Volcker, de-linked the dollar from gold, and placed the wage-price controls on the American economy that would, within two years, lead to double-digit inflation.

## The case of Chile

As it turned out, Friedman did not have long to cool his heels at the University of Chicago. The overthrow of the Allende regime in September 1973 gave Friedman's students, known locally as "the Chicago boys," a semi-industrial country to experiment with.

It is not merely that the Pinochet regime, staffed by Friedman's University of Chicago trainees, engaged in torture on a scale that disgusted the civilized world. They took a country that had the makings of industrial republicanism—with or without the help of overthrown Presi-

dent Salvador Allende—and broke its industry, turned it over to raw materials extraction, and bled it dry for debt service. The economics of the Pinochet regime were no different from those of a loan shark's heavy who does business with brass knuckles.

This is the unfortunate nation which, Milton Friedman told *Business Week* magazine Nov. 26, 1979, "will be regarded as one of the economic miracles of the twentieth century."

Friedman represents Chile as a nation of "free trade." This is an outrageous lie. Chile has become a creditors' dictatorship. Between the coup in 1973 and the beginning of 1979, Chile's annual payment of debt service to international banks rose from \$200 million annually to \$1.6 billion—an eightfold increase, unparalleled in modern history. And this stupendous increase in debt service payments occurred while the economy had collapsed to production levels barely half of what they were under the deposed Allende regime. At the time of the coup, debt service consumed about 10 percent of all export revenues. By 1979 two-thirds of exports went to debt service.

A few fortuitous factors, such as an increase in the world market price of Chile's major export, copper, helped pay some of the debt burden. But the Pinochet regime did the bulk of it by eliminating food imports, reducing average caloric consumption in 1975 to less than 1200 calories per day.

Friedman was in this one up to his ears. Friedman's reaction to being caught in the act was about the same as that of a four-year-old who has drowned his baby sister in the bathtub. For example: *Business Week* magazine—whose economics editors are professed Friedmanites—reported as a bland matter of fact on May 11, 1976, "The Chilean coup that overthrew Salvador Allende in late 1973 replaced one set of economic ideologues with another. The Marxists who strove for total regulation of the economy have been succeeded by a group of policymakers known as the 'Chicago Boys.' Reason: they ardently embrace the free-market teachings of University of Chicago economist Milton Friedman, who visited Chile for six days last year to counsel them."

*Business Week* squeamishly reported that the Chicago boys had taken their toll: "Despite the fearful repression, people still cautiously complain. In Conchali, a northern district of Santiago, the families are decidedly lower middle class—taxi drivers, mechanics, seamstresses. Over the years they had hauled themselves out of poverty. Now unemployment and recession have pushed them back again. 'My husband drives a cab from curfew to curfew,' says one housewife, 'but still he does not make enough to feed us all.'"

Friedman blew up at the staid magazine that usually supports his views. "I have no regrets except for the utter irresponsibility of American publications, including



*Business Week*, in dealing with this," he said a few months later. But he frantically tried to disassociate himself from the practices of the closest thing to the Hitler regime now in power. "I did not then and do not now condone the regime in Chile," he said. "I had no contact with people in Chile prior to the visit, and have had none since."

Considering that Economics Minister Sergio de Castro and Central Bank President Pablo Barahona were personally trained by Friedman at the University of Chicago, Friedman's disclaimer is astonishing. The truth is that Friedman took a more extreme stand on cutting consumption than any of the military junta. When he traveled to Chile in early 1975, at the absolute nadir of economic collapse, Friedman "chided the Chileans for not cutting their spending enough," according to *Business Week*.

He did more than make such demands in private: he issued them in Spanish-language public press in Latin America. In one particularly egregious example, he warned the Chileans not to take any measures to relieve the genocidal conditions of mass impoverishment brought on by his economic policies, in the Peruvian daily *La Prensa*, Jan. 16, 1977:

"Whenever social programs either in the United States or in Chile have been initiated on the basis of 'helping the poor,' they have ended up hurting the poor and helping middle and upper income people. It is not possible to maintain healthy prosperity by this route. . . . We must not be equivocal: the end of inflation will not be achieved without costs."

He continued in the same essay, "I have been informed that the government of Chile has adopted many measures which are in agreement with the orientation that I affirm and defend. It has been a force for the return of economic activity to the private sector. It has taken measures to reduce government expenditures and the government deficit. . . . All this is positive. I am confident that Chile will have the courage, the strength and the wisdom to accelerate this process and to get past this initial difficult period." So much for Friedman's hypocritical attempt to distance himself from the junta's malnutrition economics.

The statistics for Chile's economic performance tell a horror story. All categories of consumables produced domestically fell by drastic amounts, while food imports—on which Chile is still dependent—fell from \$500 million in 1974 to \$300 million in 1977.

Unemployment, which reached 20 percent by the official numbers and more than 40 percent by unofficial calculations, was still 14 percent (officially) in 1978 and 21 percent by University of Chile estimates. Gross Domestic Product never recovered from the 13 percent fall during the worst year, 1975. Real wages fell during 1974 to barely *half* their 1971 level, and are still a full third below the 1971 level. By the 1978 harvest, agricultural production was off by 27 percent.

The one "success" of the Chicago Boys was to reduce government expenditure from 15.8 percent of national consumption in 1972 to 12.1 percent of national consumption in 1977, a figure that understates the real decline, because total consumption fell sharply over



*Chile's brass knuckles*

the period. However, the decline in the budget deficit was achieved by laying off hundreds of thousands of state employees, virtually eliminating public health and education services, and by auctioning off 454 enterprises owned by the state at about 10 cents on the dollar.

In 1979, *Institutional Investor* magazine reported, "The de Castro economic policies have their spiritual roots in the so-called Chicago School of economic thought pioneered by Nobel Prize-winning economist Milton Friedman. In fact, one Chilean critic of those policies, successful banker and industrialist Orlando Saenz, cracks that 'what's happened here is as if Jimmy Carter had appointed Milton Friedman and then left him to get on with the economy just as he pleased.' "

*Institutional Investor* published this encomium in March 1979, six months before Jimmy Carter and Paul Volcker did precisely that.

## The case of Israel

... Friedman avoids talking about his role as chief economic advisor to Israel's now-failing Begin government, which began the week after Begin was elected in the Spring of 1978. It is hard to say at this writing which will go first: Begin or the Israeli currency. Now suffering a 120 percent annual rate of inflation, and devalued on the international markets by several percent per month, the Israeli currency of legal tender since Independence is scheduled to be withdrawn from circulation in September. At that time, the battered Israeli lira will cease to circulate, and will be traded in for a new Israeli "shekel" at ten shekels for every lira.

The Israeli government, after two years of Milton Friedman's economic program, does not have much choice but to call in the old money and issue new. From 1978, when Begin invited Friedman to Jerusalem for consultations, to February 1980, inflation tripled from 40 percent to 120 percent. Begin's first finance minister Erlich took Friedman's advice and eliminated government subsidies and price controls on consumer goods, producing a 25 percent across the board increase. In a country where a cheap two-bedroom apartment costs \$50,000, and a small car costs \$16,000, that was a brutal exercise. It provoked a short-lived general strike by the Israel Labor Federation, controlled by Begin's Labor Party opponents.

Erlich lasted barely a year. Last fall, Begin dumped the unpopular minister for Yigal Hurvitz, because of "the finance minister's inability to make any dent in the inflation figure, and (because of) the gaping balance of payments deficit created by his own policy," the London *Financial Times'* *World Business Weekly* reported April

14. Hurvitz's "prescribed medicine" was more of the same Friedman formula, according to *World Business Weekly*: "tight credit restrictions, savagely pruned subsidies on basic consumer items, warnings of unemployment, and a promise of a no-growth budget." flopped as badly as Erlich had before him. . . .

Of course, Friedman's role in Israel's Begin government cannot be cast in the same light as his relationship to Chile's Pinochet. In the view of most of Israel's supporters abroad, Begin is much, much worse. He has transformed Israel into a model Schachtian state, where military expenditures consume one-third of all government expenditures. The nightmare of the Zionist movement is that Begin will adopt Goebbels' solution to the Schachtian economic paradox. Despite the "savage" cuts in social expenditures under his government, Begin has had to increase military expenditures even further, pushing Israel into hyperinflation. Since debt service already consumes one-quarter of the Israeli budget, Begin's failure to find a peace settlement, or rather his attempt to use the Camp David agreement with Egypt as flank-covering for an overt territorial expansion policy on the West Bank and possibly Lebanon has produced the same results that Schacht's did in the great 1938 crisis.

Friedman's role in the matter is somewhat ironic, because Israel's hidden source of export strength—the compensation for the greatest military and debt-service dependencies of any country in the world—is a special kind of old-fashioned "free trade." More than one-third of total Israeli exports is polished diamonds, a trade established by emigrés from South Africa and encouraged by De Beers, the Oppenheimer cartel that controls 85 percent of world diamond marketing. Marketed through Amsterdam, Antwerp, and New York, the diamond trade is not only the most secretive of any major commodity—all transactions in the diamond exchanges are verbal and unreported—but also the most untraceable. Next to pure refined heroin, diamonds are the most easily concealed high-value medium of exchange, and about half the trade in diamonds runs into illegal, including narcotics trade, channels. That figure is surprising only out of context; Consolidated Gold Fields of South Africa estimates that half of world gold production as well flows into illegal operations. In consequence, Israel's market has been the Mont Pelerin Society circuit of Latin American dictatorships, and whatever other countries find it uncomfortable to purchase weapons directly from either the United States or Western Europe, including South Africa and the Soviet Union. Until last year Israel's biggest customer in Latin America was deposed dictator Anastasio Somoza, whose military forces—which made the Chilean junta look like Peace Corps volunteers—were largely Israeli-equipped.