

The Chicago School Poison

Frank Knight is another pivotal figure. We have seen that he learned his J.B. Clark through Alvin Johnson at Cornell. Then he ruled the Chicago School for many years, bending it to his strong will and commanding personality. "The close personal relations of the Knight coterie, maintained for over half a century, has reinforced the strong common elements in their idea systems ..." (Reder, 1987: 415).

How did Knight come to Chicago? John D. Rockefeller funded Chicago spectacularly in 1892, and started raiding other campuses by raising salaries. Rockefeller picked the first President, William Rainey Harper. Harper picked the first economist, J. Laurence Laughlin, from Andrew Dickson White's Cornell (he liked Laughlin's rigid conservative and anti-populist views). Harper drove out Veblen in 1906, then died, leaving Laughlin in charge of economics until he retired in 1916. He passed the torch to J.M. Clark, the son and collaborator of J.B. Clark.⁶⁰ Frank Knight first came to Chicago in 1917 from Laughlin's Cornell. The apostolic succession is fairly clear from Rockefeller to Harper to Laughlin to Clark to Knight.

According to William Barber, the early institutional decisions helped shape the "observable outcome" at Chicago to this day: in plain English, Chicago is still the lengthened shadow of John D. Rockefeller (Barber, 1988d: 242, 248, 263-4, 265). We may assume that the man who hired publicist Ivy Lee to polish his tarnished reputation also picked his own private University President with that in mind. Rockefeller and Harper are long gone, but the problem they exemplify is as perpetual as the maldistribution of wealth and the corruption of politics. "It is not what has been given but what is hoped for that influences most the policy of

university authorities" (Ross, 1914: 166).

In terms of numbers, and intensity of feeling generated, Knight probably produced more NCEists and NCEism than anyone in history. He made no secret of his firm opposition to Henry George and ideas that might aid or comfort Georgists. His enduring interest and his viewpoint are clear from the title "Fallacies in the Single Tax" (1953).

In treating rent, Knight totally fuses the individual and the social viewpoints. A cost to one firm is a cost to society: there is no aggregation problem, no fallacy of composition, and no remote possibility that "rent" might have more than the one meaning he assigned to it.

Anyway, to Knight all land value is a human product. The single tax, says Knight, is an invention of city men who never knew the soil (recall Alvin Johnson and his "fresh cheeked maidens"). Among the human activities and investments that create land, by Knight, is "killing off previous claimants" (1924, rpt. 1952, pp. 167-69). It reads like a caricature of Chicago, but it *is* Chicago, from the fountainhead himself. The American Economic Association has laid on its hands, reprinting it as a "classic".

Consistently, Knight also argues that slave-owners had just title to their slaves, because of society's sanction, and - note this well - because there was open competition for the capture of slaves (1953: 810). Competition is the key, it can justify anything. Presumably this would also justify lesser forms of larceny and embezzlement, so long as thieves compete, but Knight does not address this matter. There is some irony in that Knight's roots lay deep in the "Land of Lincoln". "Summary liberation" of slaves, i.e. Lincoln's Emancipation Proclamation, was unethical according to Knight. Compensation was due the owners - not, apparently, the slaves. He does not tell us what persons in "Society" should bear the necessary taxes to do so. One wonders if the young Knight had ever been allowed to read *Huckleberry Finn*. His paramount value is protecting property in unearned wealth.

"Society" was to blame for slavery, wrote Knight, and society should pay (cf. Ely, 1914: 779, cit. Young, 1916: 305). Could this be the origin of the allegedly "knee-jerk liberal" doctrine that hoodlums who gun down robbery victims are blameless because it is society's fault? Little wonder that Knight later wrote that the competitive system lacks most elements of fairness (1935: 60). Was he not projecting onto the system his own grim fairy-tale of what it should be, and reacting against his own travesty?

Consistently, again, Knight wrote that land yields no unearned surplus so long as competition keeps the returns to individuals at market levels (1924, rpt. 1952: 167-69). A "run of free income" (as Veblen called it), ceases being a surplus to Knight as soon as someone buys it from someone else. Similarly, monopoly profits would become competitive as soon as B bought a share in the monopoly from A. This ideological position was taken also in the same decade by W.I. King (1921), R.T. Ely (1927), and Shannon and Bodfish (an Ely employee) (1929), and has grown universal among NCEists. An "efficient market" is now one in which arbitrage has adjusted purchase prices such that every new buyer makes just a competitive return on what he bought, regardless of what that might be (we have already seen Knight apply this to slaves). The origins of property are of no concern, only the trade in property.

The market is also "efficient" so long as no opportunity for arbitrage goes unexploited. It's a wonderfully circular, self-vouching system of thought: by definition, no such opportunity does go unexploited. Getting back to basics, an efficient land market would seem to be one that got land allocated to its highest and best use. In NCE, this is assumed to be the by-product and result of arbitrage. It is as though betting on a horse-race is what makes a certain horse win. Indeed, William T. Ziemba, Professor of Management Science at the University of British Columbia, has provided us with an appropriate model, a perfect travesty of Knight's idea of an efficient market. "My system is based on the premise that the racetrack, like the stock market, is an *efficient market* - ..". Betting is efficient, says Ziemba, because "The odds created by the betting public generally reflect a horse's actual chances of winning a given race" (Ziemba, 1988). Those ideas overlook that the odds do not affect the outcome (plus, in this case, it does not matter which horse wins anyway). Land prices are in some ways like the horse race. They rise and fall from exogenous causes. Buyers bet on the outcome without affecting it. Knight's thought takes us so far away from basics that a professor of management science can mistake arbitrage for social efficiency.

"Choice" is everything to Knight. "Apart from a necessity of choosing, values have no meaning or existence". "...The cost of any value is simply the value that is given up when it is chosen" (1924, rpt. 1952: 167-69). Knight is clear that this undercuts classical ideas about taxing rent.

Knight did not rest with just defining away land rent. He also saw the need to define away land itself, following J.B. Clark. A strong and easily conveyed argument for untaxing buildings while "uptaxing" land is that it removes a disincentive to replace or remodel decrepit, obsolete buildings and other capital. Capital, unlike land, has a finite life. It depreciates and is reproduced. That is, it turns over. The reciprocal of turnover is a period of time, which the Austrians call a "period of production". This was anathema to Clark, who wanted to erase the difference of land and capital by making capital deathless, like land, and have capital consist of a mystical essence that could "transmigrate" into land and explain its value.

Knight took up Clark's anti-Austrian attack with multiplied vigor. In this context, anti-Austrian means anti-Georgist. Clark attacked Boehm-Bawerk in one or two articles; Knight churned out twelve, by Stigler's count (1987: 57, col. 1), against Hayek, Machlup, Lange, and Kaldor. "Knight denies the existence of any 'primary' factors of production [read land] which contain no capital, and equally he denies the possibility of measuring the period of production ..". Stigler claims "victory" for his old master, using the rather circular survival test that he has used elsewhere to define industrial efficiency. It is doubtful if Stigler would accept a popular vote to choose truth over error. It is no better, and perhaps a good deal worse, to accept the verdict, if that is what it is, of a profession whose role models are the likes of Clark, Edgeworth, Walker, Pareto, Ely, and Knight himself.

In the course of this anti-Austrian attack, Knight goes so far as to commit the "fallacy of the disappearing inventory". According to him, the existence of capital lets us treat inflow and outflow of goods through inventories as simultaneous. Likewise we may treat production and consumption as simultaneous, however long goods are stored up in inventory (Knight, 1946: 387; this traces back to Clark, 1893a). It is something like saying we may treat collegiate matriculation and graduation as simultaneous, so long as there is a stock of students. The result of such thinking is to bypass the whole question of what capital is and does, and, damagingly for George, to erase a primary distinction of capital from land. Knight uses the point for this very purpose.

The lost distinction is that capital turns over; it is continuously being used up and replaced by hiring labor to produce more. The longer it takes

capital to work through the pipeline, the more capital is required per worker and per unit of output, and the higher is the ratio of capital to labor. Add to that, the pipeline itself is capital. Likewise, since pipes occupy space, the more land is required. To keep the distinction of land and capital well lost, Clark and Knight were forced to dispute the Austrian capital theory,⁶¹ which each of them did in their oft-cited debates with, respectively, Boehm-Bawerk and Hayek. These celebrated exchanges seem quite tedious and pointless, and even mystical, until one realizes their essential role in the imperative to slam the lid on Henry George and his idea of treating land and capital separately. They were essentially battles of Anti-Georgists vs. Anti-Marxists.

August Comte, founder of "Positivism," taught that all science deals either with relations of coexistence or relations of sequence. Production economics as taught today deals solely with relations of coexistence, ignoring relations of sequence. The popular Cobb-Douglas function⁶² exemplifies the point. "Capital" there simply exists as a quantity at a point in time. Sequence virtually disappeared from standard economics until Keynes revived it in a macroeconomic context. Even Keynesians had to work out a "vertical" or instantaneous multiplier to communicate with people whose system of cognition left them uncomfortable with matters of sequence over time.

Production economics, meanwhile, has evolved into manipulation of symbols purporting to represent quantities of labor and capital conceived as substitutes at a point in time. Micro theorists avoid handling the sequential relationships, that labor produces capital and investment employs labor. They avoid defining capital, and explaining what unit of quantity measures it. The abstract axiomatic reasoning in micro-economic theory that students are forced to take as "The Core" of economics deals exclusively with these stylized relations of co-existence. This reasoning ignores the formation, measurement, meaning, depreciation and replacement of capital. Appreciation of land gets short shrift.

Knight, like Edgeworth and Pareto, had a dark, cynical, misanthropic outlook. "Truth in society is like strychnine in the individual body, medicinal in special conditions and minute doses; otherwise, and in general, a deadly poison. ..." (1947: 325, cit. Stigler, 1987: 59). The spirit is at an opposite pole from that of Henry George. Knight was not born to love

anyone so *Menschlich* as George.