Investment and Consumption: A Critique of Rothbard's Claim that There Can Be No Such Thing as Governmental 'Investment'

Abstract – We take Rothbard to task for claiming that governmental agents must of necessity engage in consumption in their expenditures; that it would be equivalent to a logical contradiction to suppose the inverse.

Keywords – Consumption, investment, praxeology, morality

JEL classification code – O16, R42

1. – Introduction

Investment may be defined, non controversially, as an expenditure on an item with the intention that it will, in future, help promote a greater amount of consumption than would otherwise have been forthcoming. An investment good, such as a steel mill, would be an example of an item purchased for this purpose. In contrast, equally non controversially, a consumption expenditure is one made on an item that will yield immediate satisfaction to the purchaser. A ham sandwich would be an example of a consumer good.

It is impossible to answer, of any given good or service, whether it is an example of investment or consumption. To say of a given steel mill 'It is investment' or, of a ham sandwich 'It is a consumption good' is erroneous. It all depends upon the purposes to which these things are intended to be put. Now,
it cannot be denied that for virtually all steel mills, the goal of those who construct them is that they aid in the creation of intermediate goods such as steel beams, and final ones such as rulers, staples, paper clips, etc. That is, the purpose of most people who build a steel mill is investment. Nor can it be gainsaid that virtually all ham sandwiches that have ever been put together have been assembled for the purposes of eating them; that is, consuming them.

However, there are exceptions, in both cases. For instance, Bauer talks of the 3 M’s of foreign aid: Monuments, Mercedes and Machine guns\(^1\). These are the actual purchases often made with such government to government transfers of income, despite false claims to the contrary. Well, some monuments consist of large statues in the likeness of the dictator aid recipient. But others could include, wait for it, a steel mill. The goal here is not so much to actually produce steel, which can be purchased on the open market for a fraction of the cost of that generated by this ‘investment’. Rather, the purpose for erecting the steel mill is indistinguishable from that behind the creation of the statue in the dictator’s likeness. It is to give honor to the recipient of the foreign ‘aid’. Here, then, the steel mill functions not as a capital good, but rather as a consumer durable; akin to any other statue or painting.

A similar analysis applies to the ham sandwich. Of course, the overwhelming majority of such items are put together to be eaten, consumed. But there are of course exceptions. The ham sandwich in the hand of the restaurant, for example, is not a consumer good. He at least, will not (directly) consume it. Rather, he offers it to the customer. For the latter it is indeed a consumer good; for the former, it can only be characterized as some sort of capital good. In Section 2 we make the case that there is no logical contradiction in asserting that the governmental operator engages in investment, not consumption. We conclude in Section 3.

2. – Governmental investment?

With this introduction, we are now ready to consider a rather controversial claim of Rothbard to the effect that there can be no such thing as governmental investment. Any expenditure made by government must of necessity be considered consumption. Let us allow him to speak for himself\(^2\) on this matter.

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\(^1\) See on this http://www.free-eco.org/pdfs/outourcing_primer.pdf. We owe this cite to Lisa Casanova.

\(^2\) We are in debt to Ludwig van den Hauwe, Matt Machaj and Sam Bostaph for bibliographical recommendations.

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ROTHBARD [1997, pp. 85-86] states as follows:

«The problem of the diffusion of expenditures and benefits is, however, more complicated when the government spends money for its various activities and enterprises. In this case, it acts always as a consumer of resources (e.g., military expenditures, public works, etc.), and it puts tax money into circulation by spending it on factors of production. Suppose, to make the illustration clearer, the government taxes the codfish industry and uses the proceeds of this tax to spend money on armaments. The first receiver of the money is the armament manufacturer, who pays it out to his suppliers and the owners of original factors, etc. In the meantime, the codfish industry, stripped of capital, reduces its demand for factors. In both cases, the burdens and benefits diffuse themselves throughout the economy. ‘Consumer’ demand, by virtue of State coercion, has shifted from codfish to armaments. The result imposes short-run losses on the codfish industry and those who supply it, and short-run gains on the armaments industry and those who supply it. As the ripples of expenditure are pushed further and further back, the impact dies out, having been strongest at the points of first contact, i.e., the codfish and the armament industries. In the long run, however, all firms and all industries earn a uniform return, and any gains or losses are imputed back to original factors. The nonspecific or convertible factors will tend to shift out of the codfish and into the armaments industry. The purely specific or nonconvertible original factors will remain to bear the full burden of the loss and to reap the gain respectively. Even the nonspecific factors will bear losses and reap gains, though to a lesser degree. The major effect of the change, however, will eventually be felt by the owners of the specific original factors, largely the landowners of the two industries. Taxes are compatible with equilibrium, and therefore we may trace long-run effects of a tax and expenditure in this manner. In the short run, of course, entrepreneurs suffer losses and earn profits because of the shift in demand».

«All government expenditure for resources is a form of consumption expenditure, in the sense that the money is spent on various items because the government officials so decree. The purchases may therefore be called the consumption expenditure of government officials. It is true that the officials do not consume the product directly, but their wish has altered the production pattern to make these goods, and therefore they may be called its ‘consumers’. As will be seen further below, all talk of government ‘investment’ is fallacious».

ROTHBARD [1997, p. 173] continues in this vein:

«Resource-using expenditures by government are often considered ‘investment’, and this classification forms an essential part of the Keynesian doctrine. We have argued that, on the contrary, all of this expenditure must be considered consumption.

\(^1\) Gordon [2007, p. 23] cites this paragraph of Rothbard’s and says of it: «A simple, even self-evident point, once Rothbard has called it to our attention, but it was hardly very obvious to previous writers».
Investment occurs where producers’ goods are bought by entrepreneurs, not at all for their own use or satisfaction, but merely to reshape and resell them to others—ultimately to the consumers. But government redirects the resources of society to its ends, chosen by it and backed by the use of force. Hence, these purchases must be considered consumption expenditures, whatever their intention or physical result. They are a particularly wasteful form of ‘consumption’, however, since they are generally not regarded as consumption expenditures by government officials».

ROTHBARD [1975, p. 26] says this:

«We have seen that more saving and less consumption would speed recovery; more consumption and less saving aggravate the shortage of saved capital even further. Government can encourage consumption by ‘food stamp plans’ and relief payments. It can discourage savings and investment by higher taxes, particularly on the wealthy and on corporations and estates. As a matter of fact, any increase of taxes and government spending will discourage saving and investment and stimulate consumption, since government spending is all consumption. Some of the private funds would have been saved and invested; all of the government funds are consumed (fn 15. omitted). Any increase in the relative size of government in the economy, therefore, shifts the societal consumption–investment ratio in favor of consumption, and prolongs the depression».

ROTHBARD [1975, p. 308, fn. 15] continues:

«In recent years, particularly in the literature on the ‘under-developed countries’, there has been a great deal of discussion of government ‘investment’. There can be no such investment, however. ‘Investment’ is defined as expenditures made not for the direct satisfaction of those who make it, but for other, ultimate consumers. Machines are produced not to serve the entrepreneur, but to serve the ultimate consumers, who in turn remunerate the entrepreneurs. But government acquires its funds by seizing them from private individuals; the spending of the funds, therefore, gratifies the desires of government officials. Government officials have forcibly shifted production from satisfying private consumers to satisfying themselves; their spending is therefore pure consumption and can by no stretch of the term be called ‘investment’. (Of course, to the extent that government officials do not realize this, their ‘consumption’ is really waste-spending)».

One problem⁴ with the foregoing is that Rothbard is guilty of taking an objective, as opposed to subjective perspective on this matter. He is ignoring the purposes that the minions of the state may or may not entertain with regard to these expenditures. Yes, we agree with Rothbard that if the goal of the bureaucrat or politician in spending these monies is self-aggrandizement, as in financing the building of a statue, or a bridge that bears their name, then this is indeed consumption. But, suppose the statist is future-oriented. He robs Peter through taxes and gives the money to Paul, in order to safeguard, or attain, the votes and/or good will of the latter, which he regards as more numerous or powerful than the former. This forward looking behavior would appear to satisfy the strict requirements of ‘investment’.

As we have quoted above, Rothbard’s [1997, p. 173] view is that «Investment occurs where producers’ goods are bought by entrepreneurs, not at all for their own use or satisfaction, but merely to reshape and resell them to others—ultimately to the consumers». And again [ROTHBARD, 1975, p. 308, fn. 15], «‘Investment’ is defined as expenditures made not for the direct satisfaction of those who make it, but for other, ultimate consumers». Well, when the politician acts not for his own ‘direct satisfaction’, but rather for the sake of future goals of his, it is difficult to see why this cannot properly count as investment.

Rothbard (and Gordon) make much of the fact that the «officials do not consume the product directly, but their wish has altered the production pattern to make these goods, and therefore they may be called its ‘consumers’». But no less can be said of private investors. In that case, too, the wish of these private individuals is what sets in motion the process of investment. Of course, there are wishes and then there are wishes. Those of the statist thief are not at all to be equated with those of the honest businessman, the rightful owner of the property in question. The latter operates with his own money or wealth, the former with that of another. But these are ethical questions, and we are here attempting to conduct a purely praxeological analysis. Thus, the moral status of the two economic actors can play no role in this regard whatsoever.

3. – Conclusion

Consider again this point by Rothbard that it is praxeologically impossible for a government agent to engage in investment. He must, upon pain of logical contradiction, engage, only, in consumption, never in investment. How would this play out in the case of another kind of thief, a non-governmental one? Suppose a member of the underworld steals some money from someone, and purchases a truck with which to cart around his supplies of marijuana. He does not use this as a consumption item, at least this is not his intention; instead, his purpose is to use it as a capital good, to promote

⁴ Gordon [2007, p. 26] very wisely opines that «economics is a strict science; as such, it must be purged of all that does not properly belong to it».
his illegal drug business. Why is this necessarily, instead, a matter of consumption? Were he instead an honest businessman, and had purchased a truck to bring his crops to market, we would have had no compunction in labeling this vehicle as a capital, not a consumer good. As there is no praxeological difference between the honest businessman, the criminal hoodlum, and the statist operator, we conclude that depending upon their purposes and goals, none of them are precluded from investment; none of them are logically and necessarily confined to having their expenditures regarded as consumption.

REFERENCES


http://www.mises.org/rothbard/agd.pdf