

The “Invisible Hand” and “Reverse Invisible Hand”

Gordon Anderson
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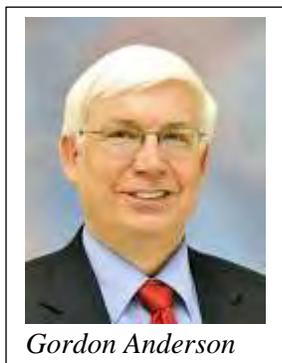


The economic debates we hear between the right and left today tend to be wars of words based on unscientific suppositions, or statements of faith. Thus, the battles between economic ideologies that often underpin the rhetoric of Republican and Democratic candidates tend to reflect the type of belief we would call “primitive religion” if it were a discussion of some other aspect of human life. Both statements that “an invisible hand of the market can bring happiness to all” and “government redistribution can bring happiness to all” are suppositions that contain an element of magic akin to the common religious belief that “if

you are faithful to scripture, God will bless you.”

The Book of Job in the Old Testament is about a faithful man who suffered afflictions, not blessings. The Holocaust is another example of a people faithful to scripture not being protected by their God. Similarly, poverty in the West serves as evidence that a free market economic system does not automatically lead to the happiness of all who live under it. And, the collapse of communism in the USSR is evidence that government allocation of economic resources leads to economic collapse and misery. It is time to move beyond the naïve rhetoric of our inherited economic dogmas and attempt to understand why they rely on a lot of magic and how the scientific study of human economic nature can lead to better solutions.

The Invisible Hand



Gordon Anderson

In the debates between left and right, free marketers on the right often cite Adam Smith and his “invisible hand” of the market, while socialists on the left consider the invisible hand to be an article of faith. The socialists are right. The term “invisible hand” is a non-scientific name given by Smith to explain a phenomenon he observed. Like the idea “the tree god makes the wind blow,” this type of supposition is a label attached to an observed phenomenon to describe human experience and observation without scientific explanation.

What Smith referred to as the invisible hand has been studied scientifically by psychologists and economists who understand that, in competitive market environments, human beings pursuing their own ends are forced to serve others or starve. In a free market transaction, the seller has to provide something to the buyer that he is willing to pay for, and both buyer and seller “win.”

By pursuing their own happiness, sellers are motivated to produce and buyers are motivated to buy, if they have the money or goods to trade. To get money to trade, buyers also have to produce something they can sell or trade to others.

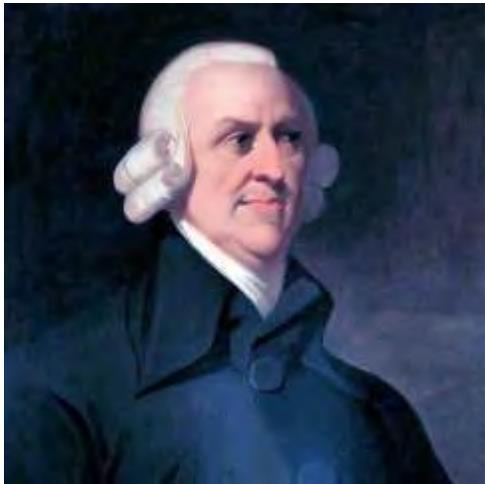
In order to understand what the invisible hand does and does not do, it needs to become far less invisible and the economic forces it represents have to be better understood. The invisible hand only functions fully under the following conditions:

- Every human being is producing and selling things that other people want, and earning enough in return to provide for his basic needs and to be a good consumer.
- There is pure competition in the market, e.g., there is a virtually unlimited number of sellers and buyers, and everyone has equal opportunity to produce, sell, and buy.
- There is no government regulation that provides an economic advantage to any player.
- There is a virtually unlimited supply of natural resources, or what resources exist are equally available at the same price to all producers or sellers.

In real life none of these conditions apply. Not every person is able to compete competitively, or even wants to. Many people are raised in economic subcultures or without adequate education and skills to function in a purely competitive market. Such people either end up working at a low wage job for others, receive some form of welfare, or starve. There is almost never pure competition in a market, but either a

market in which a few sellers dominate with asymmetric economic advantage, or government protections through devices like patents that allow some players a competitive advantage or make it illegal for most people to enter a particular market. And, the earth's resources are not unlimited and many resources are controlled by large economic players or governments, who allocate to their favorites.

Because the invisible hand is a theory for economic growth, encouraging the production of goods and services, the West has prospered tremendously in the past 200 years by adopting a belief in it. The economic conditions that existed at the time of Adam Smith in the U.S. were such that each family was able to run a farm, a shop, or a service that could be sold to others. There was also the necessary protection of private property that enabled a market to function. Except for the handicapped or the willfully indigent, the economic system was of such a type that the "invisible hand" appeared to work.



Portrait of the political economist and philosopher Adam Smith (1723-1790) by an unknown artist

However, the development of large consolidated corporations, funded with capital investment from Wall Street or elsewhere, has radically changed the dynamics of the economy in a way that the "invisible hand," to the extent it exists, only applies to a few players, and not the majority of citizens. For example, there may be competition between BP, Shell Oil, and Exxon-Mobil in the oil market, but hardly anyone else is really able to play that game. Today almost every traditional family business, from farms and restaurants to industrial production, has become consolidated with owners being investment bankers or stockholders. The profits are divided among these people and not among the masses of middle-class buyers and sellers who engage in the trades.

The current system creates a growing disparity between rich and poor and shrinks the size of the middle class. In our present economic system, the conditions required for the invisible hand to work no longer exist. Despite what many on the left may say, the current economic system does not invalidate the principles that Smith spoke about, it only reflects the fact that the conditions required for economic growth for all are no longer operative in our social system.

The Reverse Invisible Hand

The ideological rhetoric used by the left reflects a basic awareness that the economic system promoted by the right is not delivering a good life for all, and that human compassion demands that something must be done to change the present situation. But so far, the left appeals to the simplistic notion that government is capable of delivering the solution. In reality, government redistribution can serve as a safety net for a few, if most people are carrying their own economic weight, but the idea that governments can create economic prosperity is sadly no more true than it is "the tree god makes the wind blow."

The scientific study of government reveals that governments have the power to redistribute wealth by force, and can modify inequity to some degree. However, governments not only need producers to create the wealth that they will divide, but they also cost money to operate and take a chunk out of the pie that would otherwise be divided between producers and dependents. Thus government redistribution is not only a win-lose situation, unlike the win-win of the competitive market, but the expense of government comes at the cost of reduced overall economic growth.

Just as Smith's invisible hand works in an economic market environment with an unlimited number of players of equal economic size, in the economic environment of a government structure a "reverse invisible hand" is at work. Economist Milton Friedman wrote:

...there is a reverse invisible hand: People who intend to serve only the public interest are led by an invisible hand to serve private interests, which was no plan of their intention.

The "reverse invisible hand" is a label used to describe observed behavior in present Western governments. The economic laws that govern the nature of human beings serving in modern government, and the actual dynamics of government agencies regarding the use and distribution of money have been increasingly studied and described by economists like Friedman and sociologists like Max Weber. And, as the invisible hand required certain social and economic conditions to apply, there are ideal conditions for the "reverse invisible hand" not to work.

- Government work should be voluntary service, and workers produce their personal economic support outside their government job. Social services of churches tend to function along these lines.
- Government decisions would need to be free of conflicts of interest, and reflect the will of a large

majority of the people. The will of political parties and government agencies whose members would benefit financially from the government program are the primary shapers of policy today and have near-total conflicts of interest.

- Government agencies would need to be structured to reduce the number of beneficiaries of welfare by successfully enabling them to become capable producers in a competitive marketplace. But today agencies are paid based upon the number of people they serve, so it is in their interest to keep people dependent and increase the number of people in their care.

Understanding the necessary economic principles for growth for all in a properly regulated market, and normal economic principles at work in governments will lead to policies far different from those currently advocated by the Republican or Democratic parties. Generally the criticisms of each party by the other are accurate, but the solutions advocated by both are self-serving and against the interest of the “ideal of creation,” where every human being is a perfected individual truth body contributing their unique talents to the well-being of themselves, and to society as a whole.

The laws that foster the lack of economic equality can be fixed, but there is no reason to expect the policymakers we appeal to will want them repealed. It is not in their interest. Rather, like the system the U.S. founders created, legislation must be designed for systemic functionality, not based on political pressure from economic interest groups. Things like eliminating political party affiliation on ballots, and restriction of campaign contributions to individual citizens with \$100 per candidate per campaign, would have huge positive consequences. Voters would have to become aware of candidates’ skills and would be unable to vote a “party line.” Candidates would be restricted in the funds they could use for advertising, and journalists would be forced to return to investigative reporting on candidate skills rather than commentary on political ads. The power that the money that influences politics represents would be widely distributed across a large swath of citizens, with labor unions, corporations, and other interest groups reducing their importance to politicians.

My book, *Life, Liberty, and the Pursuit of Happiness, Version 4.0*, provides an overview of how a constitutional representative republic was turned into a plutocracy and ways to return the present government to a system that serves all its citizens equally. It explains how each law or rule that gave more power to political interests is similar to a computer virus that feeds itself by taking information or memory from personal computers. Anti-virus software must be constantly updated to keep computers running free of infection. So it must be with keeping government free of viruses. The laws that prevent political viruses must be recognized as more important than the use of a political party by a citizen, or a bureaucratic office by a government administrator to gain something for himself at the expense of the whole.

Dr. Gordon L. Anderson (UTS Class of 1978) is the President of Paragon House, Editor-in-Chief of the International Journal on World Peace, and Adjunct Professor at the California Institute of Integral Studies. He earned an M.Div. in Christian Ethics at Union Theological Seminary and a Ph.D. in Philosophy of Religion from Claremont Graduate University.