The Real History of the Fed

Plenty of people want to "end the Fed"—but who started it? In **"New York's Bank: The National Monetary Commission and the Founding of the Fed"** (Policy Analysis no. 793), George Selgin, the director of Cato's Center for Monetary and Financial Alternatives, explains the little-known origins of the Fed and reveals how the real story differs from the more conventional and laudatory accounts you might find elsewhere. Selgin details how the National Monetary Commission, convened over a century ago, was heavily influenced by New York bankers whose primary interest was preserving their own power. Many of their crony schemes eventually made it into the later Federal Reserve Act. "Not surprisingly, that Act proved more effective in preserving New York's financial hegemony than in securing financial stability," Selgin writes.

A FUTILE NEW WAR STRATEGY

As the wars in Iraq and Afghanistan have become deeply unpopular, President Obama has been careful not to involve himself in another conventional ground war. Instead, he has adopted a "light footprint" approach: employing standoff strike capabilities and special operations forces, often in support of local ground forces, rather than major contingents of U.S. ground troops. In **"The Problem with the Light Footprint: Shifting Tactics in Lieu of Strategy"** (Policy Analysis no. 792), Cato visiting research fellow Brad Stapleton argues that this is little more than a futile tactical shift—the United States is no more likely to defeat terrorism or establish democracy with a "light" footprint than it was with a heavy one. These new strategies may succeed in overthrowing regimes temporarily, but as he writes, "They are of little use, however, in promoting the development of stable democracies or the eradication of the root causes of terrorism."

THE BENEFITS OF CREDIT CHECKS

Employers often use credit checks as a means of screening potential hires, but politicians and activists claim that this practice disproportionately disadvantages minorities. Ten state governments have banned the practice, while 31 other states have considered similar laws. In **"'No More Credit Score': Employer Credit Check Bans and Signal Substitution"** (Research Briefs in Economic Policy no. 54), Robert

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Clifford of the Federal Reserve Bank of Boston and Daniel Shoag of Harvard University find that, rather than helping minorities, these bans are actually associated with a 1 percentage point increase in the likelihood of being unemployed for African Americans aged 25–65. This may be because employers replace the credit check with more stringent requirements, like college degrees or prior work experience—which harms minority applicants even more.

THE PRIVATIZATION WAVE

Since the 1980s governments in more than 100 countries have transferred thousands of state-owned businesses to the private sector, from railroads and airports to energy companies and postal services. In **"Options for Federal Privatization and Reform Lessons from Abroad"** (Policy Analysis no. 794), Cato's director of tax policy studies Chris Edwards argues that it's high time America followed suit in this worldwide move toward privatization. "The United States has a government postal system, but European countries are privatizing their systems and opening them to competition," he writes. "The United States has a government air traffic control system, but Canada and the United Kingdom have privatized their systems." Among other things Edwards recommends privatizing: Amtrak, the Tennessee Valley Authority, federal lands, buildings, and more.

WHAT ADAM SMITH GOT WRONG

For over a century (1716–1845) Scottish banks were largely unregulated. They had no central bank or lender of last resort, no limits on bank size, and no public or private monopoly on the issue of currency. Overall, those 130 years were a time of rapid economic growth and financial stability—except for 1772, when Scotland experienced a dire financial crisis. This crisis inspired Adam Smith to critique unregulated banking, and to advocate certain regulations. But in **"Legislating Instability"** (Research Briefs in Economic Policy no. 55), Tyler Goodspeed of the University of Oxford argues that, in fact, those very regulations, implemented a few years before the crisis, had "critically undermined the flexibility and resilience previously exhibited by Scottish finance."

LESSONS FROM THE FALL OF COMMUNISM

It's been over 25 years since the fall of the Berlin Wall—25 years since ex-communist countries began transitioning to market economies. Scholars once debated how best to govern those transitions—would it be more prudent to take a gradual approach, or to reform the entire system rapidly? In **"25 Years of Reforms in Ex-Communist Countries: Fast and Extensive Reforms Led to Higher Growth and More Political Freedom"** (Policy Analysis no. 795) Cato's Marian Tupy, along with Oleh Havrylyshyn and Xiaofen Meng of George Washington University, demonstrate that the countries that implemented early and rapid reforms gained the most freedom and prosperity. In contrast, they write, "postponement of reform proved to be an opening for rent-seeking and the rise of oligarchs."

PROPERTY RIGHTS IN ASIA

Many have researched the question of why developed nations become rich—but in this body of research, the continent of Asia is often neglected. In **"Property Rights and Financial Development: The Legacy of Japanese Colonial Institutions"** (Research Briefs in Economic Policy no. 56), Dongwoo Yoo of West Virginia University and Richard H. Steckel of Ohio State University examine the contrasting systems of property rights that existed in Asian countries throughout the 20th century. In Palau, for example—an island country in Micronesia—Japan began to establish private property ownership just before the outbreak of World War II. The war prevented Japan from continuing this process throughout Micronesia—meaning the rest of the countries remained largely controlled by clan systems rather than individuals. By 2007, Palau was three times richer than other Micronesian countries. ■

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State promotion of religion used to be thought of as one of the main functions of government. What could be more important than that? Over time, at least in the Western world, we've realized not that religion isn't important but that governments tend to make bad decisions about it. The same thing might happen on some other issues.

Secondly some advanced modern democracies have actually succeeded in greatly reducing or decentralizing their government: recent examples include places like Canada, Ireland, New Zealand, and a couple of others mentioned in the last chapter of the book. I don't think there can be a libertarian revolution any time soon. Indeed most revolutions of any kind tend to cause more harm than good, in part because of political ignorance. But it might be possible to have an evolution, if not toward libertarianism as such, then toward greater decentralization and limitation of government power. I would point to recent survey data, including some collected in a Cato paper you co-authored, which shows that, on average, Americans have more confidence in state and local government than in the federal government. This suggests that there might be at least some prospect of a constituency for decentralizing government power on some important issues. ■

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