

CHAPTER THREE

Government Spending Did Not Create the Internet, and Has Never Created a Job

Work expands so as to fill the time available for its completion.

—C. Northcote Parkinson, *Parkinson's Law*

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84 *Charing Cross Road* was one of the better movies of 1987. Starring Anne Bancroft, Anthony Hopkins, and Judi Dench, the art house film chronicles a transatlantic friendship between two bibliophiles over twenty years.

What strikes the viewer today is the cumbersome way that people acquired out-of-print books in the mid-twentieth century. The prohibitive expense of an international telephone call required ordinary people to communicate by letter. So Helene Hanff (played by Bancroft), a customer in New York, writes to Frank Doel (played by Hopkins), a second-hand-book seller in London, about buying several volumes from him by mail and pays with a check.

From our perspective, the transaction seems intolerably slow. The absence of the internet, email, and cheap long distance telephone service made something as simple as purchasing a book a difficult endeavor.

Fast forward to the 2000s, and Hanff would not have to contact Doel at all. Instead, she would go to Amazon.com or the AbeBooks website, where she could search the inventories of second-hand booksellers from the entire English-speaking world and purchase the desired books with her credit card. Thanks to the visionary Jeff Bezos, *84 Charing Cross Road* is available on Amazon.com, but it no longer describes how we live.

Jeff Bezos has a net worth in the billions because the company he founded led online retailers in transforming the way people shop. The market has rewarded his creative genius so handsomely because exchanges that were once difficult and time-consuming now take place in a matter of minutes or even seconds.

What does any of this have to do with government spending? First of all, many people believe that government spending created the internet. In 2013, *Fortune* magazine's Allan Sloan wrote,

Bezos's company, after all, is based on the Internet, which was created during the Cold War by a military research-and-development arm of the federal government, the Advanced Research Projects Agency. No Arpanet, no Internet. No Internet, no Amazon, no \$25 billion personal fortune for Jeff Bezos.¹

Absolutely false. Government by definition has no resources, as your annual income tax return demonstrates. Government can spend, and for that matter borrow, only to the extent that it can tax away

wealth. Nor does government create jobs. The work government “creates” is a function of what it can tax away from workers’ earnings or borrow based on that power to tax. All jobs—public or private—trace their origin to private sector productivity. The only wealth that politicians and bureaucrats have to invest was taken from someone else.

What about the internet? Government investment had a role in creating a crude and largely unusable version of the internet, and even that was accomplished only by taking something from the private sector first. It was private production by individuals motivated by profit that made the internet of today possible. Allan Sloan’s paeon to government investment notwithstanding, government can give only what is first taken away.

Not so in the private sector. We have already seen how Henry Ford’s reinvestment of his profits made the automobile ubiquitous. Personal computers are an equally powerful example. In the 1970s, a personal computer cost over a million dollars. But thanks to people like Michael Dell, computers today are the low-cost rule across all income classes in the United States and much of the developed world. The proliferation of inexpensive smartphones created by entrepreneurs at BlackBerry and Apple shows how the profit motive has democratized access to information and communication on devices that fit in our pockets. And since you will usually enjoy a profit if you come up with ways to improve people’s lives, capitalism provides in abundance.

The important question is not how much should government spend to create something as transformative and life-enhancing as the internet, but how much sooner would something as transformative and life-enhancing as the internet appear without the heavy spending of government? Government spending does not create jobs. It erects barriers to investment and therefore job creation.

Remember—entrepreneurs cannot be entrepreneurs without capital, whether it is their own savings, funds borrowed from family members, or investment from others. One of the best examples is Google. It's easy to forget that this omnipresent company was once neither large nor influential. Back in 1998, Jeff Bezos put \$250,000 of his own money into the venture.² Google was eventually able to attract a great deal more investment, but it was Bezos's funds that made the company's early ascent possible. He was also an early investor in Twitter, a company so successful that its name, like Google's, has become a verb.³

Facebook has been instrumental in reuniting long lost friends and acquaintances, and it has become the way hundreds of millions of people announce life events, share their political views, or simply wish friends a happy birthday. It is a public company now worth billions of dollars, but at one time it was a tiny social media site meant to bring together college students at elite universities. Recognizing its potential early on, the billionaire Peter Thiel invested five hundred thousand dollars, laying the groundwork for the world's foremost social network to become infinitely more than its creators could have imagined.⁴

Then there is Apple, Inc., one of the most valuable companies in the world today. But when Steve Jobs returned in 1997, Apple was in serious trouble. Jobs eventually righted the ship, but it is not well known that Bill Gates put \$150 million into the sagging technology firm when its future was dubious and other sources of credit were not interested.⁵

The point is elementary: entrepreneurial ideas need capital. Government doesn't provide that capital. It competes for it. Corporate taxes are a penalty on production. They take precious capital that could be invested in new products or improvements to existing ones.

Government spending acts like another tax on production. Government has money to spend because it first takes money in taxes or borrows it from the private sector, reducing the amount of investment capital available to those who need it. Government spending represents the extraction of limited funds that, if not consumed by politicians, might reach a future Microsoft or a company like Apple that is on the verge of huge technological advances.

Sadly, the government often wastes the money it takes from the private sector. It's a long and sad story, as we see if we go back to the Great Depression of the 1930s, when the conceit that government could spend society into prosperity became political orthodoxy in America.

Arthurdale is a largely forgotten town in West Virginia, but in the '30s it was the scene of an ambitious experiment by federal government. A state historical marker at the site reads: "Established 1933–34 under Federal Homestead Act, one of several model planned-communities nationwide, and a pet project of Eleanor Roosevelt, to assist unemployed through self-sufficient farming and handicrafts."⁶

Eleanor Roosevelt discovered the area that became Arthurdale in 1933. Author C. J. Maloney describes in his 2011 book *Back to the Land* how, upon seeing the destitution at Scots Run near Morgantown, "she demanded of her husband, President Franklin Delano Roosevelt, that something be done for them. The town of Arthurdale, West Virginia, created and sustained expressly on FDR's command, was that something."⁷

"Eleanor's Little Village" ultimately failed, as you would expect a government-planning experiment to do, but at least it left us some important lessons about government spending. One of these is about waste. Private homebuilders erect houses intending to sell them for

more than it cost to build them. But there was no such market discipline in Arthurdale, where homes built by the federal government at an average cost of \$16,600 each were sold for \$750 to \$1,249.⁸ That's what happens when the party allocating capital faces no discipline from the marketplace. Private lenders generally don't tolerate the blatant waste of their money, and they would have quickly pulled their funds if a private construction company had been building those houses in Arthurdale.

The cost overruns in Arthurdale manifest how the federal government labored under no such market discipline. Why should it have? This is not to speak ill of those who work in government, but to say that the federal government has no private investors to please. Instead, it has the bottomless well of taxpayer dollars perpetually to draw from when funds are running short.

Government programs are about waste not because all government officials are crooks, inept, or both. The problem is that government programs are funded regardless of their effectiveness. Every day poorly run businesses fail. Just how many government programs does Congress shut down annually? Is it conceivable that the politicians who fund government programs have a better rate of success than private investors? The answer is obvious: of course not. Incentives matter. Administrators of government programs, enjoying endless funding, feel no urgency to adapt to new realities in the marketplace. Waste is the natural result of such an arrangement.

One response to complaints about "wasteful government spending" (a redundant phrase if ever there was one) is that government must invest where even the most intrepid of private investors will not. More to the point, government must play the role of the venture capitalist for projects that are seemingly too risky for even the boldest of investors—a plausible argument at first blush, yet it quickly

succumbs to numerous contradictions. Although federal pay has recently eclipsed the wages of some private-sector work,⁹ successful investors remain some of the richest people in the world. Warren Buffett tops this list, but a perusal of the Forbes 400 confirms that plenty of capital allocators would love to replace Buffett at the top. Net worth is a market signal, and it tells us that the most astute investors do not toil for the relatively puny salaries offered by the federal government.

The notion that private investors lack the nerve to put capital into the most perilous new ideas is belied by history. Recall the early days of the automobile. Investment in that contraption was the very definition of risky. Still, at the dawn of the automotive age, there were over two thousand automobile companies in the United States. Only 1 percent survived.¹⁰

The failure of formerly high-flying companies has been commonplace in the computer and technology industry for a long time. Yet investment in Silicon Valley continues to soar. Apologists for government investment would have us believe that investors will never wade into certain risky areas, but the truth is that the greater the risk, the greater the reward. Intrepid investors are to varying degrees attracted to the riskiest investment opportunities *precisely because* of the potential for outsized gains.

Governments, then, are not only experts at wasting limited capital but are also filled with individuals who are incapable of directing capital toward successful ideas. The good ones are earning billions in the private sector. The unconvinced should read the late Robert Bartley's essential 1992 book, *The Seven Fat Years*, in which he asks readers to "Rank in order the most likely recipient of capital from an industrial planning bureaucracy:

(A) Steve Jobs's garage.

(B) IBM

(C) A company in the district of the most powerful congressman.”¹¹

The obvious answer to Bartley’s question shows why politicians who talk about government “investment” deserve our skepticism. The oft-repeated phrase “follow the money” is apt here in that government is rather conservative in the non-ideological sense. Steve Jobs, as is well known, was a college dropout who founded Apple in his garage. Apple today is a monument to American innovation, but garage start-ups are by the very adjective that describes them not the companies that politicians will migrate toward.

They tend to invest in the Solyndras of the world. The failed solar panel company received an infamous \$535 million loan from the Department of Energy that taxpayers will ultimately swallow. Solyndra’s biggest private backer was George Kaiser, a top donor to President Barack Obama and other Democratic Party causes.¹²

All of this matters a great deal in discussions about economic growth simply because a dollar is a dollar is a dollar. The “seen” of Arthurdale, Solyndra, and every other government “investment” is the funds taken from the citizenry in order to build houses or solar panels with little regard to cost or return on investment. The “unseen” is what profit-disciplined businesses might have done with the capital that the government has consumed.

How many Googles and Facebooks will never come to be because the federal government extracts so much money from its productive citizenry? What struggling companies might have been saved as Apple was if not for the federal government’s spendthrift ways? These questions are painful to ponder. But they reveal the scope of the opportunities we will enjoy if we ever shrink Leviathan.