Off the Books

A Radical Blueprint for the Eradication of Poverty

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Abstract:

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Austrian economics is a descriptive science that illustrates the phenomena of human interaction. It is urgent to point out that this paper deals with specific prescriptive proposals concerning the world’s most enduring problem. Therefore I take caution when linking this set of prescriptions with Austrian economics; however it is the case that my worldview is filtered through an Austrian lens. With that said, capital accumulation is the pre-requisite for development; this implies that access to capital and secure property rights are necessary preconditions to human progress.

Throughout most of human history people have lived short, decrepit lives and the persistence of poverty has been the norm. An honest inquiry reveals that people are not put into poverty per se; instead most people of the world are never able to escape it, due to the lack of economic freedom and secure property rights. Through the correct construction of institutions and rules society can rise out of the pit of impoverishment. Unfortunately institutions are not designed correctly as long as individuals have adverse incentives to do ill to others- either directly or indirectly- as a matter of government policy. Government intervention lays the foundation for poverty by imposing prohibitions on peaceful economic activities; through creating licensing laws; imposing tariffs and quotas; subsidies to favored industries; upholding intellectual property rights; through the state-capitalist monopoly on money and credit; most significantly through the government’s monopoly of land. In short the government actively prevents capital accumulation, which is the necessary requisite for economic development.

With the problem laid out the solution seems to establish itself. All of these interventions give rise to informal economic centers of the world; astonishingly 1.8 billion people already making their living in the underground economy. People will participate in economic relations whether or not the market is strangled by government interference. The problem, however, is that the informality and illegality of these markets are not conducive to property accumulation. When investigating the informal sectors of the world one is left to wonder “Could these informal markets assist in the eradication of poverty if they allowed for capital accumulation?”

The purpose of this paper is to explore a revolutionary strategy for eradicating poverty and increasing the standard of living for all people of the world. The creation of an NGO (non-governmental organization) which promotes secure property rights for the people of the informal sectors will help to ensure that people can participate in rational economic calculation, since the traders will have a reasonable expectation of security from fraud and theft. The NGO must also have an avenue for loaning capital to entrepreneurs of the informal sectors, as well as encourage the development of mutual aid committees that serve as voluntary social safety nets. In short the NGO must promote property rights and capital accumulation. The NGO is inimitable in entrepreneurial spirit because the
consequence is the de-legitimization of the state by using tools outside of the government’s influence. To paraphrase Professor Steve Horowitz, there is not a market solution for everything, but there is not a government solution for anything. The creation of an NGO like the one proposed is that middle way. It falls under the side of market solutions because it is voluntary, but its existence does not depend purely on profit and loss signals. The existence of an NGO as proposed owes its existence to people of the world that are serious about empowering people with economic freedom, and willing to provide low interest loans and charitable donations in order to alleviate the misery of poverty.
1) Introduction

Since the emergence of the nation-state, governments all around the world have attempted to regulate people’s economic relationships. This has been done by the establishment of prohibitions on certain economic actions such as restricting the free flow of people; through creating licensing laws; through imposing tariffs and quotas; by imposing taxes on products and services; through subsidies to favored industries; by upholding intellectual property rights and through failure to uphold selfearned property rights in land. Governments disallow competition for vital industries, such as money—including credit—and systems of justice making these goods and services inherently inefficient and unjust. Due to all of this government intervention economic freedom has withered away and as a corollary poverty has persisted. An unintended consequence of economic centralization and intervention has been the growth of the informal economies of the world.

Journalist and practicing economist Robert Neuwirth maintains that a low estimate for a “collective GDP” of the world’s informal sectors is 10 trillion dollars annually. He claims that half of the world’s population is making their living off the books; that’s an astonishing 1.8 billion people benefiting from the underground economy. Many economists, philosophers and talking heads would view this unregulated market activity as a tragedy, since the state loses out on income. The LA Times recently wrote an article about how the state of California is starting to crack down on “cheats” because the bourgeoning 7 billion dollar informal sector results in so called “lost revenue” for the government. Even more significant is the process by which entrepreneurs, looking to make a living, have demonstrated the irrelevance of the state. The beauty of these informal markets is that the traders are paving a path for the future, by depriving the state of resources and by demonstrating how nonessential governments are for human cooperation. The informal markets are vessels for cooperation and gains through trade, even establishing mutual aid networks and voluntary social safety nets. Though it is clear that these informal markets are sufficiently providing people with a day-to-day living, it is also apparent
that a lot has to be done in order to enable these informal sectors to avert the pangs of poverty.

Economists that consider themselves part of the Austrian tradition usually focus on entrepreneurship, institutions and capital accumulation when considering developmental issues. The Austrian emphasis is on institutions that promote “rules of the game, provide a framework which guides economic activity, removes uncertainty and makes the actions of others predictable.”

The correct construction of institutions allows the accumulation of capital, which is at the core of all economic development. The acquisition of capital implies secure property rights and access to investment capital. Beyond that, voluntary social safety nets can provide a more satisfactory state of being for those who are barely getting by. Thus we find the necessity for a privately funded non-governmental organization that actively secures property rights, provides micro loans and promotes mutual aid for the world’s impoverished populations.

2) Imposing poverty

In these perilous days, amid the daily suffering of the planet’s population, we find institutions that exist through the use of force conducting society’s most vital services. We also find political and economic centralization very popular among academics, corporations and power seeking politicians alike. Many of the most impoverished places of the world are wretched because of the states’ attempt to control resources and regulate peaceful economic activity. People cannot get vital goods and services because the economy has been cartelized and monopolized through government force. This has happened different ways in different places, either in the form of complete central planning or through reformatory interventions. The consequence, always and everywhere, is a lag in capital accumulation, which stumps economic growth and human progress.

Most people mistakenly understand poverty as a symptom of markets; some falsely believe that humans live in a “zero sum game” which implies that some are poor precisely because some others are better off. Instead poverty should be
understood as a systemic problem due to barriers to entry into the market and increasing fixed costs of living, which make it much more difficult to be a successful entrepreneur. As Charles Johnson explains, “Fixed costs of living- rent, food, clothing and so on- consume most or all of a family’s income, with little or no access to credit, savings or insurance to safeguard them from unexpected disasters.” The cost of living is ratcheted up due to government policies regarding land use, building codes and zoning codes. Licensing requirements and taxation significantly contribute to increased overhead costs making it more expensive and more difficult to start entrepreneurial ventures. If economic barriers to entry were eliminated the possibility for employment would be more bountiful and the division of labor would be expanded to previously unchartered territory. The informal sectors, though far from perfect, provide an opportunity for those who are otherwise excluded from economic improvement.

The costs of entry into the legal market are ever increasing and poor people have become incapable of participating in the process known as the market. For example many people living in poverty in the Southwestern United States are in the business of selling fruit from South and Central America. As traders they are officially off the books and, as such, it is reasonable to assume that their fruit arrived to the United States outside of the legal means. These vendors pay no taxes and have no business licenses and their products have not been approved for sale. Like many impoverished people in the United States, their vehicle is their most important asset since it is the place where they live and make their living. They have no collateral for a loan from regular banks and have no recourse for making a living save in the informal sector. They know little about the laws they are violating and are more concerned with arbitrage and seeking innovative ways to get their goods to market. Given the choice and opportunity these fruit vendors would be selling their goods legally. Due to structural blockades at least half of the world’s working population is forced into informal economies.

Some thinkers within the libertarian tradition, namely Kevin Carson, consider the enforcement of intellectual property rights a “cause of economic
inefficiency by leveling a monopoly charge on the use of existing technology."vi This is especially true for music pirates who use their own computers, internet service, and cd’s to copy music from various sources on the Internet. It is hardly conceivable that sharing virtual files amounts to theft, instead file sharing is much more of a mutually aiding endeavor. Entrepreneurs are able to provide almost identical products to consumers without the monopoly pricing of the legal market. Due to burgeoning informal sectors fiat property rights are rapidly disintegrating. For example according to Neuwirth “The highest-end knockoff Puma soccer jerseys or sneakers are indistinguishable from the genuine items. And indeed, word on the street is that the same factories that subcontract with Puma and Adidas and other companies are sometimes the ones making the knockoffs.”vii Enforcement of intellectual property rights ensures that companies can charge a monopoly price for their products and results in less competitive environment. It is evident that the economic activity spurred by disobeying IP protections– everything from burned cd’s to knock-off Gucci bags– greatly contributes to a higher standard of living for the impoverished people of developing nations.

As one views poverty retrospectively it becomes evident that impoverishment has been the norm throughout human history. The anomaly has actually been those who have been fortunate enough to enjoy a higher standard of living, and not those who have lived wretched and intolerable lives. Liberation of markets, tacit rules and capital accumulation have been the key to prosperity for those fortunate few. Institutions must be arranged in such a way that provide people with socially conducive incentives. With barriers to entry eliminated and decreased costs of living the assurance of well-being is extended to all people of the world.

3) The Shadow Economy

The size of the world’s shadow economy is astounding, such that by 2020 two-thirds of the working human population will be off the books.viii The importance of these alternative markets cannot go understated. In many developing nations
entrepreneurs seeking a means of income provide essential services such as water and trash collection. In an interview with Wired Magazine, Robert Neuwirth explains how the people throughout Western Africa purchase their drinking water in bags from private vendors. In Nakuru, Kenya market actors provide trash pickup and ground transportation. As a Kenyan man told researcher and scholar Zachary Caceres, "In other places the City Council pays the garbage men, but in Kenya the garbage men pay the City Council." The necessity of bribing officials in order to conduct business is a part of everyday life in many developing nations. The corruption in developing countries reveals the state as a criminal organization, instead of a benevolent protector of private property. Regarding the protection of property there are countless circumstances in which market actors competitively and illegally provide security for people. When the police actively help the criminal class by hindering investigations competitive entrepreneurs in the form of vigilante groups, such as the Bakassi Boys, secure personhood and property rights. The private provision of these vital goods and services illustrates the Austrian insight that “public goods” are a consequence of economic development and not the cause.

Austrian economists are seeking to understand how institutional structures alter market activity. Underground economies should be understood through the same context. After reviewing three studies that attempted to measure the aggregated informal economies, Professor Boettke explains the relationship between the institutional structure and unofficial economic activity. Boettke spells out that as regulations become more intense the portion of GDP comprised by the informal sector increases. Second, higher taxes correlate to greater levels of unofficial activity. Thirdly, with higher levels of corruption, particularly amongst police and courts, we find more economic activities occurring off the books. When Austrians say that institutions matter, they are emphasizing the importance of “rules of the game”. To free market economists concerned with development this means secure property rights and the rule of law.

Some obstacles for those living within the shadow economies are ill-defined property rights and the lack of legal recourse. Traders are dealing with outlaws
because they themselves are outside the law; exposed to people who are in dire poverty, facing destitution and willing to steal through coercion or fraud. If traders are robbed they are unwilling, and reasonably so, to solicit help from the police since the state itself made the trader's lifestyle illegal. In short informal economic actors are at risk from both private criminals and those wielding a government badge. Therefore these traders are in the most terrible institutional structure since their property rights are perpetually endangered and there is not an alternative mechanism for securing their property.

To demonstrate the importance of the informal sector let us briefly consider the Tunisian Revolution. Al Bouazizi was a young fruit vendor whose property was seized by the government for selling unlicensed merchandise. The young trader, with the Tunisian capitol as his stage, set himself ablaze in protest of those who were restricting his economic freedom. Temporally this aligned with the emergence of the Wiki-leaks that exposed the rampant corruption and wealth of the president Ben Ali. The Tunisian people took to the streets in outrage and the revolution that gave birth to the Arab Spring commenced. It is ironic that economic intervention lays the foundation for alternative markets and in turn these informal sectors help to delegitimize the structure from which they arose.

4) Towards a Non-Government Solution

Conventional approaches have not addressed the root causes of poverty and instead have been geared towards combating its consequences. When governments are in charge of distributing aid it rarely makes it into the hands of those who need it most. For example in Afghanistan, one of the world's most aid-rich and war torn nations, many vulnerable people presumably will starve to death this winter due to a recent drought. As one Afghani told a BBC reporter, "There is no fighting here and nobody cultivates poppies. All the international aid seems to go to Kandahar and Helmand, none of it comes here." Pure and simple governments are political institutions; therefore actions taken by governments are inherently political in manner. Considering the provision of aid is no different, is it even possible for
governments to give aid to those who need it most? Undoubtedly there is a huge moral hazard for politicians and bureaucrats to allocate aid to places that benefit them politically. It shall not come as a surprise to anyone that government granted international aid has not done very much to alleviate the misery of poverty. Therefore after all these years it is finally evident that there is not a government solution if we want to be serious about eradicating structural poverty.

To paraphrase Professor Steve Horwitz, there is not a market solution for everything, but there is not a government solution for anything. With this in mind we need to ask ourselves, how can we provide better institutions that lead to economic development with an approach outside the conventional means? Non-governmental organizations are unique because they are not government entities and they exist despite the absence of profit and loss signals. If designed correctly an NGO can have no funding from governments and sustain through voluntary contribution. An NGO of this sort is of the utmost necessity if human beings are ever to see the eradication of poverty because it can provide alternatives for people whether they need secure property rights, investment capital, or social safety nets. The revolutionary capacity of an NGO of this caliber is its ability to undermine the foundation of all poverty by illustrating the harmful consequences of central economic planning and the restriction of economic freedom.

Traders in the world’s informal sectors are particularly vulnerable to traumatic circumstances under which their life and property are at risk. Humans respond to incentives and sometimes the circumstances are such that people have the incentive to do things that are not conducive to social living. Lack of legal recourse, i.e., rule of law, puts private property under a certain risk from the exploitative tendencies of those responding to negative incentives. With the police and the courts incapable or unwilling to provide the essential service of enforcing property rights there are not alternative ways to seek justice. While acknowledging that an essential feature of government is a monopoly on violence, it would be near impossible to provide competition for the enforcement of private property in any state approved fashion. Doing what the government does would be considered
kidnapping if a non-governmental entity committed the same actions. In a more ethical sense putting someone in a cage provides no recourse for the individual that was violated in the first place.

The least an NGO can do in this regard is encourage a network, wherein traders are encouraged to use societal pressure for deterrence. NGO's can help by publicizing those individuals who commit fraud and theft and economically disabling those responsible. The most that an NGO could do would be to assist in the construction of private and illegal courts that facilitate property disputes. Libertarians have had much to say regarding the private provision of justice and enforcement of property rights. It would be revolutionary to see these theories put to practice. Rules and institutions do not always have to come from the top down; in fact the best ones arise spontaneously from the bottom up. With the enormity of the world’s informal sectors there would be no shortage of alternative ways to secure property, each depending on the individuality of the situation.

While on the topic of the protection of property rights it is important to note that Peruvian economist Hernando de Soto teaches that “dead capital” is one reason that the poor are perpetually impoverished. Dead capital is an asset that cannot be easily bought, sold or used as an investment. This capital comes about due to lack of clear property titles. In many slums of the world the poor hardly ever actually own the land they live on. The squatter villages and shantytowns arise when desperate people have no option but homesteading and building on tiny empty spaces. They do not possess clear titles to their land they have no collateral for loans and therefore cannot claim ownership of much. De Soto estimates that there is over 9 trillion dollars of potential capital if the informal sectors’ property rights were formalized. De Soto proposes that third party participants, such as NGO’s, create “shadow economy maps” which will help to formalize people’s capital. Though it is not likely that governments will comply with the findings of a “shadow economy map” this type of service could be extremely helpful for lenders in the informal sectors. This is yet another way in which an NGO can help to enforce and protect private property rights and promote capital accumulation.
For many, micro loan programs have done a considerable amount in easing poverty and establishing formal and informal enterprises. Micro loans are usually small loans targeted towards poor people. The principle difference from conventional investment capital programs being that micro loans usually do not require collateral. Micro credit traditionally has been done through banking cooperatives, NGO’s and for-profit moneylenders. Poor people are usually excluded from loans through formal institutions because of the expected high risk, high cost per transaction and low profitability. Because of these additional costs many microcredit organizations are associated with high interest rates. In spite of the higher rates, micro loan programs have helped many of the world’s poor attain capital in an environment where it was unavailable before.

Professor Frederic Sautet is a Senior Research Fellow at the Mercatus Center at George Mason University and explains one success story of micro loan programs; Josephine Posada lives in a slum in Manila and starting receiving micro loans in 2003 and since then,

“...her family’s combined income has more than tripled and their food consumption has dramatically improved. Four years ago her family was eating one meal a day: rice. Today Josephine’s family not only eat regular meals, they also eat the food they like...Her business provides employment for others, enabling boys still attending school to earn more than a minimum wage...an opportunity to lift themselves out of poverty. Josephine’s story seems miraculous but it is not unique.”

There have been countless triumphs of many micro programs around the world. Interestingly Sautet considers these results a “successful band-aid but a band-aid never the less”. He identifies success as when the individual “graduates” from microloans to the commercially operated banks and when the individual leaves the informal sector for the legal economy. Measuring success in these terms does not accurately measure standard of living. Properly understood, success is when people increase their quality of life and no longer have to go hungry. Success is when
entrepreneurs have access to capital and can then provide public goods and help strengthen community solidarity. Professor Sautet shares the story of another micro credit recipient Elvira. Even though the loans helped to bring Elvira and her family out of poverty and despite the fact that her husband left his minimum wage job to work in her business, Sautet still does not consider this micro credit to be anything more than a temporary band-aid. According to Sautet, Elvira did not “graduate” and “despite her success she is unwilling to use the local banks. She believes that formal institutions, like banks, are all part of the pervasive corruption of her country.”

With that said another measure of success should be the preference of the consumers. The fact that she chooses to remain of the books and with her local informal lender is telling. If these micro loan recipients had the same institutional advantages of those in the formal sector, one is left to wonder if Dr. Sautet would still consider the micro approach more than just a band-aid.

A non-governmental organization could assist in broadening loan opportunities for poor people all around the world. As with all loans, available funds for lending come from the savings of other individuals; in the case of NGO’s that use microfinance, funds for loans can come directly from anyone, particularly those who are politically or morally motivated. The approach of an NGO must be one of presenting loans not as opportunity for making a return on their investment, but as loaning a principle amount that goes to help those who need it most and to be returned with little to no interest. In other words those who contribute to an NGO’s micro loan program must be willing to forgo the opportunity cost of putting their money in formal banks and accumulating interest. Micro loans are especially appealing because loans as small as 50-100 dollars make a huge difference. Poverty is not something that is necessarily imposed on humankind and efficient micro loan programs can help out a great deal.

Collaborating in the development of mutual aid groups is a viable option for NGO’s to assist with. To understand mutual aid societies we can look to Professor Gary Chartier’s recent explanation, “Societies in which people pooled risk and provided pensions, health care, and other services functioned effectively before the
rise of State social services, and there’s no reason they couldn’t do so again in the
government’s absence.”xx Mutual aid societies can be any voluntary association in
which social safety nets are established for the betterment of those involved. In the
world’s informal sectors this can mean people associating with one another through
market activity as Zachary Caceres explains, “The traders of Kisumu band together
for their own benefit. In addition to learning from one another (many groups are
based on particular markets, like clothing dealers or salonists), they share a joint
bank account for loaning to one another in emergencies and on a revolving basis in
normal times.”xxi By establishing mutual aid groups in the informal economic
sectors, NGO’s can help alleviate the plight of the poor. NGO’s do not need to wait for
governments to come around and reform the institutions; instead people are
already helping to build the foundation of the future society within the skeleton of
the current one.

5) Conclusion

In a world where people are free to interact with others in ways that are
conducive to social living and where fixed costs of living are not artificially raised
poverty as we know it would be impossible. Once poverty is understood as a
structural problem the underlying institutional flaws become easily perceivable.
Unfortunately, the human population is in a situation that was imposed upon us by
governments to which few ever consented. The monopolization of land and vital
institutions gave birth to grave abuses of power. This power is exercised over
people’s economic relations and always has the net result of stifling economic
growth thus preventing the elimination of poverty.

Government intervention ensures that poverty remains a way of life for the
world’s poor but at the same time steers us towards the solution. Vast and
unregulated markets spontaneously arise out of the hindrance of economic freedom.
These markets delegitimize the state by depriving it of the resources it would have
expropriated otherwise. Informal traders also demonstrate that vital goods and
services can be delivered without the inherit violence of government. If the world’s
underground economies had some of the institutional advantages of legal markets, these informal sectors would be the promise of a better world.

The state’s imposition on people’s economic freedom perpetuates poverty and creates illegal and unregulated markets. These markets demonstrate the entrepreneurial spirit of humankind while providing essential goods and services to those that desperately need it. Underground markets are fertile fields for experimentation with alternative forms of association. Practicing different forms of economic participation inadvertently helps to undermine the state and can therefore help to eradicate the root of structural poverty. Informal traders are forced to band together for mutual aid and initiate the emergence of a new society. A non-governmental organization can commence and expedite this process by promoting better rules and providing capital to traders. A revolutionary characteristic of such an NGO fiercely engages in competition with a detrimentally flawed institutional environment in order to win hearts and minds; only then can the form of a new society emerge out of the ashes of the old one and systemic impoverishment be a relic of the 20th century.

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iii Entrepreneurship and Development: Cause or Consequence? Boettke, Peter J. and Conye, Christopher J. http://mercatus.org/uploadedFiles/Mercatus/Publications/Cause%20or%20Consequence.pdf.


xv In many cases so-called Non Governmental Organizations are heavily subsidized; in some cases NGOs are created by Inter Governmental Organizations. We need to be clear that a revolutionary NGO must exist without government funding and its lifeline must be due to the spontaneous actions of individuals and not because of some central planning authority.

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