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**THE IMPACT OF POLITICS AND ECONOMICS ON  
NATIONAL AND INTERNATIONAL UNDERSTANDING**

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## The Impact of Politics and Economics on National and International Understanding

### Abstract

This article analyzes the political-economic relationships and interdependencies in different political-economic regimes. It argues that one of the main tasks of education is to teach students the nature of these relationships so that a realistic outlook concerning the consequences of different political-economic systems is provided. Only such an outlook can provide a firm basis for furthering international understanding.

It is stressed that only a democratic market-coordinated system with wide-spread private property, rule of law and limited jurisdiction of government can guarantee freedom, efficiency, innovative capability and thus welfare of the whole population. Centrally planned or socialist market regimes are much inferior alternatives, as they are systems severely limiting the free movement of goods, services and capital. Also, innovativeness, efficiency and freedom are even threatened in democracies if government activity is not strictly limited by constitutional or other checks and balances.

### INTRODUCTION

The subject of the present paper has to be seen in context with the topic of the Icus Committee on "Nationalism and World Unity. How to Educate for the 21st Century". I interpret this as an attempt to find an educational program suited to further the development of a more peaceful, prosperous and tolerant world. A world of free people, rule of law and with less wars, civil strife, racial, nationalistic and religious conflicts. A world mitigating poverty and ending population explosion, deterioration of environment and preventing exhaustion of resources. These problems cannot just be solved by furthering mutual understanding. Moreover, the latter is usually a consequence of economic, political and other institutions.

It is even not clear, whether and how the above problems can be solved and whether and how education can help to solve them. But to have a chance to find solutions, a clear understanding of the underlying economic and political relationships and of the working of present-day institutions is needed. Economics and political science can help to understand if, how and when a better world can be reached by which institutional changes. Realism and a clear perception of feasible goals is needed for future education to make a meaningful contribution to these ends. Purely idealistic actions will usually lead to a worsening of the situation. An education only trying to further mutual national and international understanding will be in vain, if understanding itself is shaped by persistent political and economic institutions.

Present educational efforts are clearly inadequate to reach the goals thus stated. The knowledge transmitted to students on economic and political relationships is severely limited and often distorted or plainly wrong. Teachers themselves lack a sufficient background on such matters. Unfortunately limits of time and space do not allow to discuss how the educational system and instruction could and would have to be changed to make them capable to inculcate the necessary information.

In the following paper I will thus concentrate on some of the main insights of economics and political science concerning economic system, domestic political regime and the workings of the international system. Only with the knowledge of these relationships can the impact on national and international understanding be evaluated and proposals for adequate changes in institutions and of education be made.

#### I. THE IMPORTANCE OF THE ECONOMIC SYSTEM

Though some people still deny it, economic theory supported by empirical evidence has, by now, clearly demonstrated that only a free market economy with private property rights and developed credit and capital markets can overcome wide-spread poverty and produce affluence of reproducible goods. Only in such a system are people adequately informed by price signals about the scarcity of goods and are motivated by incomes, profits and the threat of losing jobs or of losses, to make an efficient use of resources and to

innovate, i.e., to invent and to introduce new goods and production processes.

The dismal failure of more or less centrally planned socialist economies has been predicted by economists (see e.g., v. Mises 1920; Hayek 1935; Bernholz 1975, chapter 6; Pejovich 1987) and has now become obvious to anybody following recent developments in Eastern Europe, the Soviet Union and China as well as by the statements of their politicians. Such a system cannot solve the informational problems and misguides the motivation of its members by its property rights to work inefficiently and to stifle innovation.

Moreover, "socialism with a human face", some kind of socialist market economy, does not seem to provide a much better solution (Ward 1967; Bernholz 1979, chapters 1-2; Pejovich 1987). Though informational problems can be solved better with the help of markets, inefficiency, a strong tendency towards unemployment and inflation, and distorted investment policies of labor-managed firms with weak and unsaleable property rights of workers remain. The empirical evidence from Yugoslavia with very high unemployment, inefficiency and rampaging inflation is also not encouraging.

On the other hand, it should not be overlooked that free market economies only work adequately, if certain conditions are met. A legal framework assuring the safety of property rights and a stable monetary system (Dorn and Schwartz 1987) allowing extensive credit and capital markets are among these conditions. The same holds true for the absence of too many government regulations and interventions, of too high taxes and of unsustainable high budget deficits. Where some or all of these conditions are not met, no adequate economic efficiency and development can be expected, as is shown by the example of several Latin American and other underdeveloped countries.

It has also to be stressed that a regime of at least relatively free international trade in goods and services and of free international capital movements is of the greatest importance for an efficient allocation of resources and a high level of innovative activity. Not only efficiency and thus welfare is increased by the international division of labor and the international allocation of capital according to its greatest productivity.

But foreign competition is also necessary to limit the power of domestic cartels and monopolies and to motivate firms to innovate to keep abreast with competitors from abroad.

The recent literature on economic development has demonstrated (Donges 1976; Krueger 1978; Little, Scitovsky and Scott 1970) that a foreign trade regime trying to further development through import substitution by creating import barriers or by using foreign exchange controls, has been a dismal failure. Cartels and monopolies sheltered from foreign competition produce inefficiently and need not innovate. Productive activity and resources are misdirected because of distorted relative prices. Firms are competing for import or foreign exchange quotas and thus dissipate resources to obtain rents. Corruption of politicians and bureaucracy are furthered.

It is thus not surprising that the so-called newly developing countries (Taiwan, South Korea, Singapore, Hongkong, Thailand, Malaysia) have all pursued an export-oriented policy and in time reduced import and foreign exchange restrictions. Unfortunately, especially in democracies, political forces are usually working for restrictions on foreign trade and foreign exchange. We will turn to this problem in Section 3.

The better performance of "pure" market economics with private property does not imply that they can solve all problems adequately. Among these are the so-called negative externalities, e.g., environmental pollution, the scarcity of non-reproducible and of "positional" goods and the just distribution of income and wealth. Though environmental pollution seems to fare even worse in planned economies, measures by the government to internalize these negative externalities are clearly needed to reduce pollution to permanently sustainable levels. Economists have shown that these measures should, whenever possible, consist not in regulations but in taxes or fees on the firms, households and communities according to the amounts of pollution caused by them. Only then are they strongly motivated not only to reduce the level of pollution but also to find and to introduce more adequate new technologies (Faber and Manstetten 1989).

Some goods, by their very nature, cannot be (re)produced in increasing amounts. This is true for land and for outstanding works of art. But it is

also true for "positional" goods, i.e., for certain highly estimated positions in a society (Hirsch 1978). There can only be one most beautiful girl, one mayor in a city and one president of a nation. The scarcity of such goods cannot be solved by any economic system. Thus, if such goods are strongly demanded in a society, the supply cannot be adequately increased. But the demand will probably increase more than proportionately with growing per capita incomes provided in time by market economies with private property. As a consequence, the relative prices and(or) scarcity of such goods rise strongly, whereas the demand for them of most or many people remains unsatisfied.

Another reason for dissatisfaction in capitalist market economies can be a strongly unequal distribution of incomes and wealth resulting from the workings of markets, property rights and inheritance laws. It seems to be not only unjust but even unbearable, especially in a rich society, that people are unemployed, sick or poor without adequate means to support themselves. Also such dissatisfactions may be used to arouse nationalistic and racial feelings in search of scapegoats. It seems that the modern welfare state with its heavy income transfers and its social security system has been a response to these problems. The possibilities to move into this direction appear, however, to be limited. Too high taxes (including social security taxes), especially too high marginal taxes and too high transfers, erode the motivation to work efficiently, to save, to invest and to innovate. Instead, more and more effort is spent on getting transfer benefits and to escape taxation (Bernholz 1982). The empirical evidence seems to support this analysis. Difficulties in balancing the balance of payments and the budget have turned up in recent years in Sweden and Denmark (Paldam 1990), whereas real growth rates of Gross National Products seem to be negatively related to total government expenditures as a percentage of GNP in OECD countries (Bernholz 1986, 1990; Weede 1986).

We conclude that a free market economy with private property rights is up to today, the only economic system capable of freeing masses of people from poverty and to develop high living standards. With adequate government measures it can also solve environmental problems and provide through transfers, to a limited degree, for the basic needs of those disfavoured by economic developments, for the poor, unemployed and sick. All this presumably leads to a removal not only of misery, but makes national,

racial and ideological movements less attractive and thus encourages better human understanding in society.

The scarcity of non-producible and of positional goods can, however, not be solved by any economic system. It will even increase with the very success of a market economy because of higher real per capita incomes. This may lead to new tensions in society. How could this threat to human understanding be mitigated? As far as the scarcity of land and thus of accommodation are concerned, they could certainly be removed by a reduction of the size of the population. This would also help greatly to reduce the environmental problem. But how a reduction of the population could be accomplished is yet an unsolved problem, though we are now certain that a rise in per capita income and perhaps the development of the welfare state helps to solve it.

A reduction in the demand for positional goods and thus of the resulting problems for human understanding can probably, if at all, only be reached by an adequate education.

Another task for education would be to prevent the envy which might be engendered by the necessarily remaining inequality of income and wealth caused by the limits of the welfare state.

If we mention these and other tasks of education (see Section 5) we presuppose, of course, that the educational system is organized in a way to allow and to motivate an instruction of students about the underlying economic and political relationships. A training limited to providing only skills needed for future jobs would prohibit this important task. Tendencies to look at education mainly as a training for future jobs (as in several decisions of the European Court see Grabitz 1989, pp. 9-10; NJW 1988, pp. 2165-2167) should be checked by constitutional safeguards.

Finally, let me note, that I see no specific problems in a capitalist market economy resulting from the exhaustion of resources, if prices are allowed to increase with scarcity. Given the incentives provided by private property and higher prices, people will find, invent and introduce new substitutes, with their creativity driven by competition and the hope of future profits.

## II. THE INFLUENCE OF THE DOMESTIC POLITICAL REGIME

A developed system of free markets and of private property requires the existence of a strong but limited state to protect the safety of property rights and, if necessary, to adjudicate and enforce privately agreed on contracts. Government has to be limited to prevent excessive tax burdens, frequent and uncalculable changes in law, discretionary interventions in the economy and excessive taxes. Only under such conditions can private initiative unfold its benevolent consequences.

Government has, moreover, to provide public goods like internal order and safety and defence against foreign aggression. We have already seen that it has also to play a role in removing and preventing environmental pollution and in bringing about some income or wealth redistribution.

It has to be stressed that not democracy but limited government and some rule of law is necessary for the success of a free market economy with private property. The rapid economic development of Hongkong, Taiwan and South Korea provides empirical evidence for this proposition. By contrast, a decentralized market economy seems to be a precondition for long-lasting democratic regimes.

Let us point out in this context what we understand by a democracy. A democracy is a political regime in which all issues within the jurisdiction of government are decided upon by majority voting in legislative bodies (parliaments) or in referenda, and in which the members of parliament are elected by the population at regular intervals. A democracy, in this sense, is not congruent with a regime dominated by the rule of law. First, the rule of law can also be present in monarchies, aristocracies and in pluralistic regimes not dominated by one specific group. Secondly, in a democracy with a total domain, i.e., in which all problems can be taken up and be decided by government and/or parliament, the rule of law may be threatened. For if shifting majorities can legislate on everything they select, individuals have no secure rights. Their rights can be abrogated any time by the legislature. Majorities in the latter are not bound by the rule of law, and thus individuals have only rights conditional on the intentions of different potential majorities. Ethnic and other minorities may be suppressed or disadvantaged by the majority. This, in its turn, may



engender international tensions, especially if the respective minority group forms a majority in other states. We will see later in this section that unrestricted or even only moderately limited democracies show tendencies not only to weaken the rights and thus the freedom of individuals, but also to erode the efficiency and innovative capabilities of market economies with dominating private property.

Democracy is not only no precondition for a capitalist market economy but may even endanger it in the long-run and, from the above remark, thus even threaten its own existence. This usually happens if a democratic regime is not restricted in its domain by constitutional or other safeguards, so that shifting majorities in parliament, i.e., small minorities of the population only inadequately controlled by rationally uninformed voters, can impose their will on the rest of the population. With several parties competing for votes and the necessity of financial assistance to cover the costs of their organizations and election campaigns, this results in excessive regulations by government, tax loopholes and subsidies to special minority interests and pressure groups whenever the majority of voters is rationally uninformed about the issues. This will be the case if decisions impinge only marginally on the situations of citizens, since then they have little reason to inform themselves, given the fact that the influence of individual votes on election outcomes is negligible. As a consequence, we observe, e.g., protection of certain industries against foreign competition, the fixing of agricultural prices above market clearing levels or subsidies to the coal industry, although it is clear that a majority of voters is hurt by higher taxes and(or) prices. Only if economic developments like rent increases are perceived by a majority of people, since the respective expenditures amount to a substantial part of their budgets, will government action favor the majority e.g., by imposing rent controls (Downs 1957; Bernholz 1966).

It follows from the above analysis that unlimited democracies show a tendency to introduce subsidies, transfers and regulations in favor of different minorities of voters, of interest groups and, in some cases, of shifting majorities. Since it is often difficult to form interest groups because they provide a public good to their members, it takes time to organize them. The more diverse the interests and the greater the number of potential members, the more difficult the task to form an interest group

and the more time this will take (Olson 1965; Bernholz 1969). Moreover, time is needed to introduce new legislation, taxes and subsidies. Finally, political interests and party competition will respond to shifting economic conditions, which are at least partially brought about by the process of economic growth itself.

From all these factors it has to be expected that state activity will be growing in time. A democratic regime with competing parties responds to the demands of different groups of voters and of special interest groups arising over time. Thus the older and the less disturbed by wars or revolution a democracy the higher the level of regulations, of taxes, subsidies and transfers one would expect with comparable levels of per capita incomes (Olson 1982, 1983). But since excessive state activity also makes for less efficiency and innovation - as stated in the last section - one would also expect negative consequences for real economic growth, a result which seems to be corroborated by empirical evidence (Bernholz 1986, 1990; Marlow 1986; Peden and Bradley 1989; Weede 1984, 1990).

A democracy mitigates tensions among different parts of the population by responding to needs and wishes perceived strongly by different minorities and majorities of the population. If opposition parties with a democratic understanding are available, a change to nationalistic or ideological parties aiming to abolish democracy has a low probability even in difficult situations since there are always democratic alternatives available. True, the democratic process reacts more clumsily and slowly to a changed situation than does the market, but not all problems can be solved with the help of the latter. Democracy also solves the problems of legitimizing rulers and of an orderly succession among powerholders. With all these characteristics it helps to solve conflicts of interest by peaceful means and promotes mutual understanding among rulers and ruled. If democracy is unrestricted however, government activity tends to grow to unsupportable levels and to erode the efficiency, productivity and innovative capabilities of the capitalistic market system. In doing so, it not only destroys the economic basis of the welfare state it has developed, but by necessity, restricts more and more the freedom of its citizens by regulations and discretionary interventions, high taxes and obligatory social security premia. Since the underlying process feeds on the rational ignorance of voters and depends on the high initial productivity of the

capitalist market economy, the erosion of the basis of a free society, the burdens and disadvantages are not felt by citizens for a long time. Thus a crisis has to develop to cause a political turn-around through political entrepreneurs, which may, but need not, come too late and may lead in the wrong direction of a dictatorship or an oligarchic regime. Argentina and Uruguay, which were around 1930 among the wealthiest democracies, are telling examples for such developments.

It is perhaps appropriate to state quite clearly in this context what is understood by a free and democratic society. A free society is a society with unconditional human and property rights of individuals. This implies a strictly limited domain and jurisdiction of government. The decisions of the latter are made by majority voting in a democratically elected parliament. This means, of course, that rights are not only held by collectivities like firms, groups, religious bodies, guilds and other organizations, but mainly by private persons.

To preserve freedom, productivity and innovative capabilities in the long-run, a democracy with a capitalistic market regime has thus to limit constitutionally or by other means the domain of majority decision-making by parliament. How such restrictions can be reached and maintained permanently is still an open question (Buchanan 1987; Gwartney and Wagner 1989). We know that a division of government power, an independent judiciary, federalism, an independent central bank, a guarantee of property and constitutional restrictions on the domain of government all help. But historical examples like that of the USA show that even such provisions hold, at best, only for several decades, and will slowly be eroded.

We have already mentioned that not a democratic but only a restricted government and the rule of law are necessary to maintain a productive free market economy. But in an authoritarian system safeguards against a removal of the limitations of government are obviously weak. For the rulers can themselves determine the domain of their power, if they are not bound by religious, quasi-religious or social conventions or by a delicate balance among several oligarchs. With the modern weakening of such conventions the capitalist market regime and the domain of freedom for citizens from state intervention are always threatened under authoritarian regimes, since they

depend mainly on the goodwill of rulers or even on the delicate balance of power among oligarchs.

Freedom, rule of law and capitalistic economic regime can also be threatened by the emergence of totalitarian movements striving for government power. According to them the whole fabric, organizations and institutions of society have to be reshaped in subordination to their supreme values, like those of the Nazis, the Communists and of recent Islamic Fundamentalism. Thus, if such movements gain power, individual freedom will be limited to the domain allowed by the corresponding supreme value system. The former organization of government, the constitution, the legal system and even the capitalist market regime will be reshaped, abolished and substituted by radically new institutions as far as they do not correspond to the goals of the supreme value system. We have thus to conclude that a free democratic society with a capitalist market regime has to take precautions to prevent totalitarian movements from grasping power. It can allow their adherents to follow the values of their creed or ideology, but not allow them to coerce others to follow them by economic or social pressure or by force. If one or more supreme value movements are part of a wider society, only tolerance, i.e., an agreement not to use pressure or force to influence the belief and behavior of others can prevent mutual hate and civil conflict (Bernholz 1989).

### III. THE INTERNATIONAL SYSTEM

The international system of more or less sovereign nation states is, until today, characterized by partial anarchy characteristic of the Hobbesian state of nature. Preaching of peace and pacifism have not helped to prevent international aggression, reprisals and wars. The most pacifying influence in recent decades has been the threat of nuclear arsenals. It has preserved peace among the superpowers USA and USSR and their allies, but not in other parts of the world where no such threat existed. Disarmament is also no recipe for peace. If it is one-sided or unbalanced it may even provoke an aggressor to follow its expansionist goals.

One should clearly recognize that the "law of minimal morality" pervades the international system (Bernholz 1985). For if only one of the big powers rearms and follows a course of aggression, the others have also to arm, to

take precautions and even, perhaps, to embark on a preemptive war if they want to assert their independence. Moreover, they have always to look for coalition partners not to be outmaneuvered by a coalition formed by a potential adversary (Bernholz 1990b).

The partial anarchy of an international system of states not bound by a superimposed world authority, does not imply complete anarchy. International treaties can be concluded to gain mutual economic, political and cultural advantages. Often they and thus international law will be respected, since in this repeated game of interactions a violation might lead to future violations and reprisals by the governments hurt. Thus a vast body of international economic and cultural relations of international law and even an international court exist (Bull 1981). But it is also clear that these institutions can be broken at any time by a government having the means and the goals to pursue aggression.

Which forces can be identified to work for and against peaceful international relations and understanding? It seems that economic exchange and cultural relations are usually beneficial for international peace if they take place among states where the rule of law, freedom and competitive capitalist market economics are present.

Let us first look at economic relations. If competitive market economies are present in several countries, exchange of goods and services is beneficial to partners freely entering contracts. The theorems of economic welfare theory show that international trade is always better for nations than autarchy. But this does not imply that certain sectors cannot be worse off after the opening of trade if they are not compensated out of the general gains. Moreover, it does not preclude that even greater gains from international trade could be reaped by one country at the expense of others, if export or import monopolies or cartels could be established for certain goods in the former.

Perhaps more important, we have seen in Section 2 that domestic producer interests can influence the policies of government. The benefits of import restrictions to the respective capitalists, managers and workers are sizable and are thus perceived, whereas the disadvantages are spread on many consumers who are rationally ignorant voters and do not feel the

negative consequences of government measures. Moreover, interest groups may offer financial contributions to competing parties in exchange for beneficial policy measures, or influence the government with (the threat of) strikes etc. Now, foreign producers have no right to vote. Thus, if the home country is a net importer of certain goods, the best political strategy of the government may be to restrict imports by duties, import quota etc. (Hillman 1989). The foreign government may retaliate and thus even a trade war result, if the governments do not reach some agreement which need, however, not be optimal. Anyhow, international tensions seem to be inescapable during the process.

Another problem arises in international debt relations. Whenever creditor and debtor enter an agreement it must be to their mutual advantage. But after the credit has been paid to the debtor, the latter has some incentive not to pay interest or not to repay his debt. After he has spent the money he may even feel resentment for having to repay the debt. Inside nations such problems are settled if necessary, by courts, and this is usually also the case in international transactions among private agents. But obviously governments may interfere with debt relations and there exists no international authority to enforce them, if the government is itself the debtor. Thus, again, international tensions may arise.

If we look next at centrally planned socialist economies, we realize that international transactions are usually performed by government trade monopolies. Obviously among and with such monopolies not disciplined by market competition bilateral bargaining about quantities and qualities of goods to be exchanged and prices may arise, all supported by state authority. Thus, political tensions are intertwined with economic relations from the beginning, since each partner wants to subordinate its partners to the requirements of its central plan (Bernholz 1990b).

Finally, it cannot be precluded that economic measures like boycotts, cancelling of debts, etc. will be used directly for preventing foreign governments from executing certain policies or from reaching certain goals. Also, they may be subordinated to the ends of one's own foreign policy. But then such measures are certainly damaging to peaceful relations and may be even a prelude to outright war (Bernholz 1966b).

Let us finally turn to some consequences of large differences between per capita incomes of rich and poor countries. This may lead to tensions if people from poor countries try to migrate to rich countries, for the latter cannot grant entrance to all of them and the domestic population resents too many foreigners, if a certain threshold of say 10-15% of the population is reached. Nationalistic, racial and religious strife may arise and result in violence. Also, extensive tourism may set in from the rich to the poor countries and lead to additional tensions.

We said above that cultural exchange may promote international peace and understanding. But if value systems, behavioral norms and habits are too different in two societies, an exchange may rather lead to conflict and even violence. If such differences are coupled with migration and tourism, caused by great differences in income, severe conflicts may arise. No doubt that such conflicts become most dangerous if totalitarian states with conflicting supreme value systems confront each other which are bent on expanding their dominion to foreign nations.

The last remark brings up the question of the relationship between the kind of domestic political regime of nations and the probability of international conflict and war. One would intuitively expect that democratic regimes are less likely to become involved in international conflicts and wars than authoritarian countries. It turns out that this intuitive feeling is only partly true. Since politicians and parties compete for power in democracies, they have to follow the wishes of citizens, as far as the latter are informed about the issue. On the whole, most voters are interested in their own well-being and in that of their family and friends. Costly armaments, conflicts and wars of expansion only raise their tax burdens and are not in their interest. But there are exceptions among voters: military personnel, (potential) colonial administrations and some business firms and their employees with their families may expect to fare better if corresponding measures are taken. But the people concerned form only a minority of the population. Thus an expansionary policy, implying the risk of conflict and war, will only be followed if the majority of voters is rationally uninformed. This can only be the case if the burden of such policies is small for the individual voter and thus not perceived by him. We suspect that this has been the case for European colonial expansion before 1914. The increased costs of

maintaining colonial empires especially after 1945, could then explain the abolishment of these empires, since the domestic public became aware of the increased burdens (Bernholz 1966b, chapter 6).

Substantial outlays for rearmament in a democracy would be felt by a majority of voters. Such outlays are thus only possible if voters feel their nation to be severely threatened by strong foreign powers. An aggressive policy against peaceful foreign states is excluded because of the same reasons except, as already mentioned, if this could be done with very low costs. On the other hand, since a majority of citizens are rationally uninformed about the international and the military situation (Rosenau 1961), it has to be expected that it is difficult to introduce and maintain an adequate level of defence even against the threatening preparations of other nations. Democracies are notorious for doing too little too late in the face of foreign danger. Energetic steps and sacrifices will only be undertaken when conflict is imminent and thus highly visible (Bernholz 1985). This tendency is strengthened by the fact that national security is a public good which is not promoted by any interest group, perhaps with the exception of the arms industry. But even the latter is mainly interested in high defence outlays and not in the efficiency of military defence (Weede 1990).

Which consequences can be drawn from the above analysis for the probability of democracies to be involved in wars and conflicts? It should be clear that democracies are not likely to initiate wars. But their neglect of defence in the face of autocratic nations bent on expansion will, in many cases, invite threats and aggression and thus lead to war (Weede 1984; Kammler 1986). We would thus expect that the probability of war among democracies is low, but that this is not true for their relations with autocratic nations. This conclusion seems to be supported by the empirical evidence (Chan 1984; Doyle 1986; Rummel 1983, 1985; Small and Singer 1976).

Autocratic regimes, on the other hand, are not restricted as much in their foreign policies by the wishes of citizens. They may follow expansionary aims without finding the same resistance. Also international conflict may distract the attention of citizens from domestic problems faced by autocratic leaders. If, moreover, supreme values in a totalitarian



regime call for expansion, war will become inevitable if the leadership is not restricted by the weakness of a small nation. Autocratic regimes, on the other hand, can follow a more consistent foreign policy over longer periods of time, since rulers are not exchanged by elections and are not restricted as much by the requirements of domestic policies. They can thus not only follow consistently expansionary policies, but also prepare in time against threatening foreign aggression. The latter possibility, however, mitigates the danger of war.

We have just mentioned the size of nations (We use the term "nation" in the same sense as "state"). Small states, whatever their domestic regime, have no chance of winning on their own, wars against great powers. And even wars with other nations of comparable size can only be successful if the great powers do not intervene, which is always a possibility, since the latter seek to preserve the balance of power (Bernholz 1985, 1990). It has thus to be expected that the probability of a country to become involved in wars becomes the smaller, the less important it is.

Finally, wars are the less probable, the fewer nations exist on the globe. For fewer independent actors can go to war to further their ends. The formation of a greater state out of several independent nations reduces the probability of war, since conflicts can be solved, in many cases, by the existing political institutions or by the courts. Civil wars are less likely than international wars, as seems to be confirmed by empirical evidence (Richardson 1960).

Unfortunately, we cannot conclude from this result that a world state would be the best solution to all problems. A world state might be more peaceful but if it were dominated by a totalitarian regime, no escape to other nations would be possible. Also, imagine a planned economy with its miserable provision of goods dominating a world state. Then no competition from more efficient and innovative economic regimes would cause rulers to try to reform the economic system, as has happened recently in the Eastern Bloc.

In fact, it seems rather probable today that the system of free markets and private property rights, of a corresponding legal system, of pluralism and the rule of law, of democracy could only evolve in Europe beginning in

the Middle Ages because of the competition for power by many states and among spiritual and secular authority (Pope against Emperor and kings). In this fierce competition sufficient means to finance military power were only available on the basis of a flourishing economy. Thus princes, cities, popes and emperors had to grant freedom of markets and private property rights, and to tolerate and further the development of safety and law (Berman 1983; Jones 1981; North 1981; North and Thomas 1973). It seems that later reforms, like those in Japan after the Meiji restoration of 1868, and even recent Soviet reform attempts were motivated by foreign policy considerations. According to press reports, Michael Gorbachow said in a December 1984 meeting of the Central Committee that far-reaching (economic) reforms were inescapable to reach a better supply of goods for the population and to maintain the position of the Soviet Union as a Super Power in the 21st century (Neue Zürcher Zeitung, December 11, 1984).

#### IV. SUMMARY AND CONCLUSIONS

The above analysis is consistent with the assumption that human nature cannot be changed fundamentally, as witnessed by the negligible influence of Christianity and Buddhism over two thousand years on the occurrence of violence and wars, and also by the failure of seventy years of Communism in the Soviet Union to create the new man. By this statement we do not want to deny that there are sometimes people who strongly believe in certain ideal values and who are thus prepared to sacrifice some well-being, time or even their lives for these values (Bernholz 1991). But their number and influence is limited and the latter tends to vanish in time. This does, however, not imply that human behavior, in contrast to fundamental human aims or preferences, cannot be changed. According to the economic approach (for an easy exposition see Radnitzky 1990) to explain social reality, human behavior is not only determined by individual aims or preferences, but also by the environmental restrictions or conditions, including institutions and norms, with which each individual finds himself confronted. If it is true that the fundamental nature of preferences of most people cannot be altered much by moral appeals and education, a change in human behavior can best be brought about by a change of institutions. Wars will become less improbable if more and more countries become democracies, poverty will be diminished if market economies with private property and limited government are introduced. Environmental pollution

will not be reduced by appealing to people to drive less and to consume less energy, but by high taxes on gasoline, on pollution and on waste they produce. Industry, innovative activity and thriftiness will be furthered if individuals can reap profits, incomes or wealth from such activities and are threatened by losses if they are less innovative or productive than their competitors. On the other hand, too much beaurocratic interference, too high marginal taxes and too much social security not dependent on individual efforts will reduce private savings, productive investments and the incentive to work hard and efficiently.

Now, if these are, as I suspect, immutable laws, what can be the role of education to promote national and international understanding? Obviously, the first task of education would be to teach students as much realism about political, economic and social relationships as possible. An engineer, not understanding the laws of nature, may make terrible mistakes in building a bridge. And he will be unable to construct a plane or a computer. Similarly, somebody not understanding economic and political relationships or laws may get more instead of less wars, more instead of less understanding, poverty instead of more equality in spite of most noble aims. To reach them, he must at least know, which institutional changes would or might help to accomplish them.

Unfortunately, we know rather little about how to move from inefficient, non-innovative economic and political regimes to pluralistic, market-oriented systems with extended private property. Here the social sciences and especially political economics is confronted with a huge research agenda. It follows, that as a second task of education, we can, for the moment, only recommend to make students aware of the huge difficulties of such processes and of the lack of our knowledge in understanding them. This would, at least, help to prevent exaggerated hopes and utopian aims.

Moreover, it is even not easy to reach the first aim. For economic and political relationships are complex, so that it is difficult to spread their understanding. Moreover, as already stated by Schumpeter (1950), intellectuals are mostly hostile to a capitalistic market economy. They are outsiders without practical experience and without concrete responsibility in economic and business affairs, but often live or at least benefit from their critique of economic and social institutions. No doubt that teachers

and intellectuals working for the mass media mostly belong to this group. Can then future generations be educated to maintain a positive attitude towards a free market economy with private property?

A third task of education would be to teach students about the danger of fundamentalism, of any religious or pseudo-religious creed promoting supreme values, if such movements do not abstain from forcing or pressuring others to become believers. Only tolerance, even if one believes in the absolute truth of some last values, can prevent totalitarian movements and regimes with their obnoxious or even deadly consequences (Arendt 1968; Bernholz 1989) and thus maintain the basis for peace and human understanding.

A final task of education I perceive in this connection, is the preservation of the collective memory of society. We forget as individuals and society forgets even more easily because of the change of generations. Aims like freedom and welfare reached by a society are taken as "natural" by later generations. It is felt that they need no further effort or caution to be maintained. The institutional preconditions for their continued presence are forgotten. Other aims like substantive justice, equality, unspoiled nature preoccupy people. Since the memory of past efforts and of the necessary institutions to establish and to preserve freedom and wealth have been lost, all efforts may now be spent on reaching the other goals. In doing so, the very institutions like the rule of law, freedom of markets and private property may be abolished, which are necessary for freedom and wealth. Or too high marginal taxes and too much redistribution may be introduced with similar consequences. Here again, there exists a challenging task for education. Whether and how these tasks can be accomplished, I have to leave to educators. But to me at least, their completion seems necessary if we want to further well-being, freedom, sound environment, peace and mutual human understanding in the future.

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