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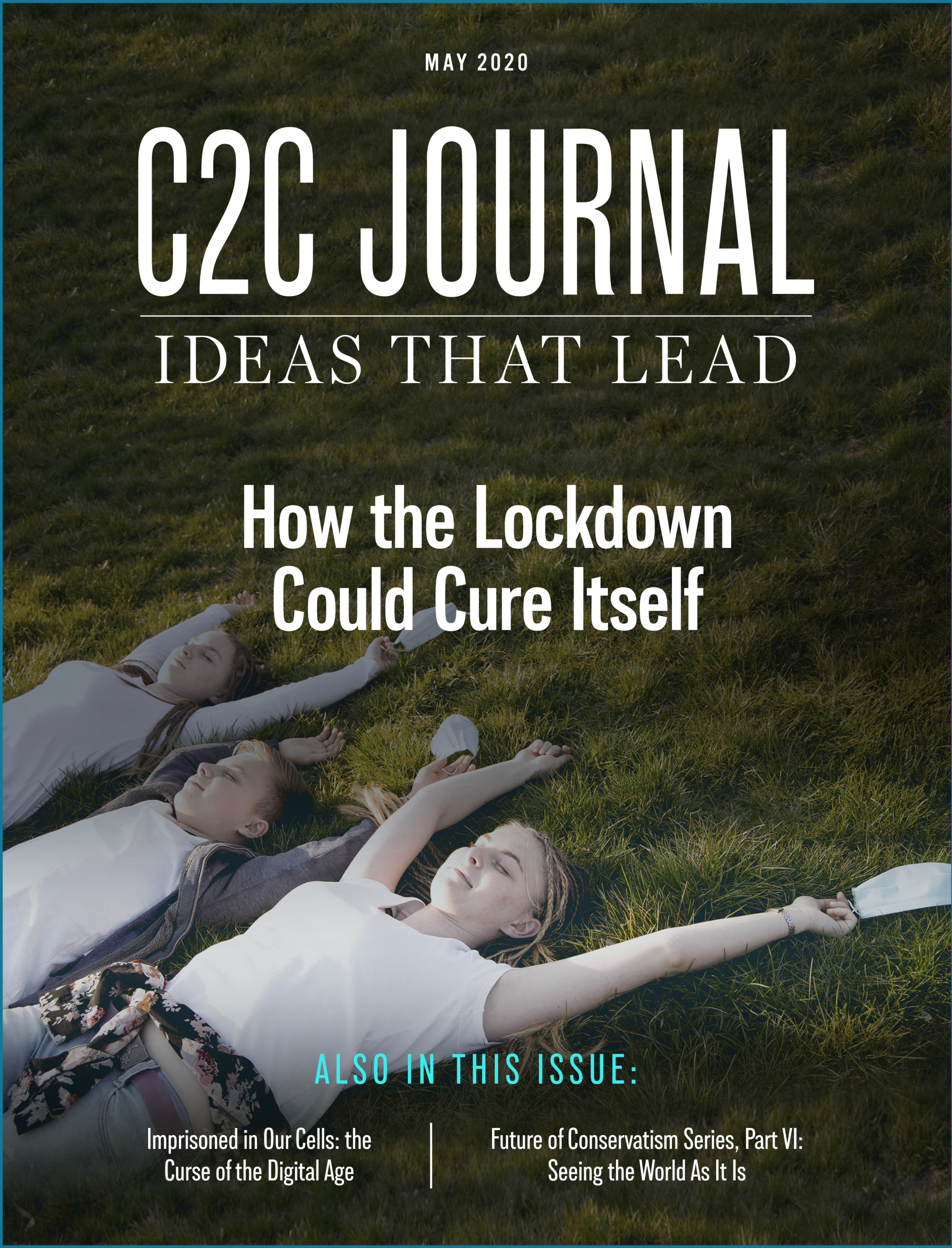
C2C JOURNAL

IDEAS THAT LEAD



How the Lockdown Could Cure Itself

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How the Lockdown Could Cure Itself

By Peter Shawn Taylor

These are heady, if unsettling, times for anyone with an eye for the lessons of history. The Spanish flu epidemic of 1919-20 – which killed an estimated 40 million people worldwide, and 55,000 Canadians – is today frequently enlisted as a cautionary tale about the dangers of unchecked viral threats. The Black Death, a rat-borne plague that left nearly one-third of Europe dead in the 14th century, has similarly become a widely-shared example of the damage done by past pandemics.

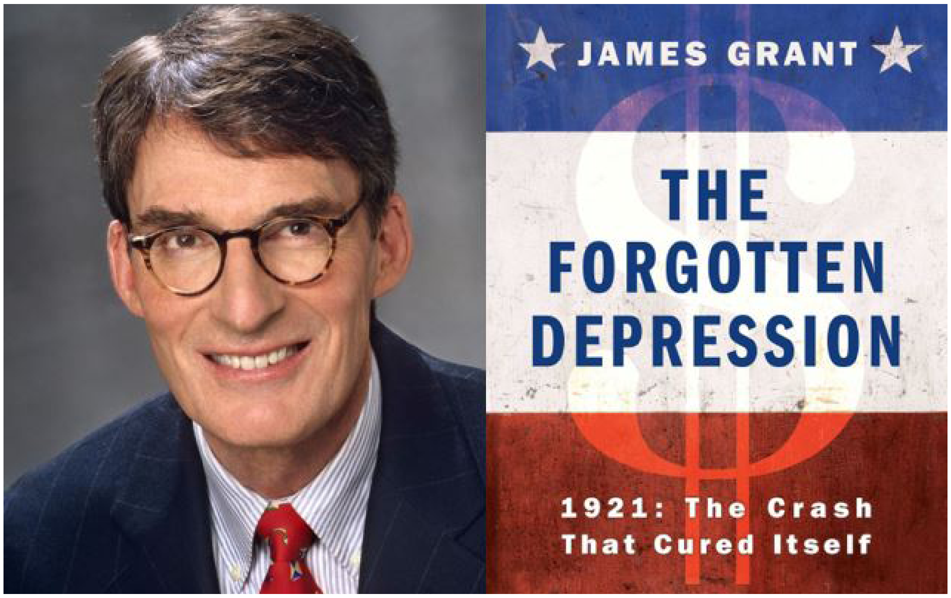
Economic analogies for the grim spring of 2020 are proving to be just as forbidding as the Black Death or Spanish flu. The cost of the current lockdown, in terms of unemployment, business failures, lost market value, and government deficits, has long since surpassed the Great Recession of 2008-09, heretofore the 21st century's most significant downturn. According to Statistics Canada, "The employment decline in March was larger than in any of the three significant recessions experienced since 1980."

Cautionary tales of past pandemics abound, such as (depicted) the Black Death, which ravaged Europe in the 14th century.

Many commentators are reaching even further back into the previous century. "We are facing a period of profound adversity unlike any we have since the 1930s," Alberta Premier Jason Kenney noted glumly. In similar fashion, William White, former deputy governor of the Bank of Canada, recently advised policymakers to "remember the lessons of the Great Depression" – a refrain that's now as common as invocations of the Spanish flu.

But with historical references so much in vogue, we should be mindful that the lessons we're remembering are the ones most salutary to our current situation. While no one wants a repeat of the Dirty Thirties, anyone hoping for the quickest possible return to economic normalcy once the coronavirus pandemic is over – a V-shaped recovery, in current parlance – should probably pay less attention to the many, many policy mistakes of the Great Depression and focus instead on government responses to past economic disasters that actually worked. And with this in mind, one well-regarded Wall Street soothsayer and historian says North America's remarkable recovery from the severe slump in 1920-21 – an event that is all-but forgotten today – deserves a lot more attention. What was the secret to that miraculous success a century ago? Governments that did nothing.

For the past 37 years James Grant has been proprietor and editor of *Grant's Interest Rate Observer,* a widely-respected US$1,295-a-year Wall Street newsletter noteworthy for its conservative – some might say curmudgeonly – approach to investing. His legendary skepticism about expansionary monetary and fiscal policy meant he was "notably prescient in 2007-08 when he warned of



the debt bubble" that set off the Great Recession, according to Burton Malkiel, author of the famous *A Random Walk Down Wall Street* investment guide. Yet Grant's most prescient and revelatory work may be a book he wrote in 2013 about a century-old economic event, *THE FORGOTTEN DEPRESSION: 1921: The Crash that Cured Itself.*

"I wrote the book because the one and only historical reference point served up during the recession of 2007-08 was the Great Depression," Grant explains in a lengthy interview with *C2C Journal.* The same thing could be said about today. "But the Great Depression isn't the only historical example we can learn from," he says. "There was a depression in 1920-21 that was similar in depth and severity, but remarkable for its brevity. And I thought maybe we should make that our model for what to do."

Grant's forgotten depression (whether the economic downturn of 1920-21 was a depression or just a severe recession remains a matter of debate) began shortly after the conclusion of the First World War, as the Spanish flu was tightening its grip on the world. "You had this double blow of a pandemic laid on top of a global war that had just ended," he explains. Inflation also became a problem as the world drifted away from the gold standard. Then came a collapse in global commodity prices and a stock market crash. The Dow Industrial stock index fell by 40 percent. U.S. corporate profits declined by 92 percent. Industrial production was down by a third.

Predictably, this economic chaos was followed by a rapid increase in unemployment as the private sector retrenched. While the labour market was not measured scientifically in the early 1920s, Grant suggests the unemployment rate may have hit 19 percent. (The current U.S. unemployment rate of 14.7 percent is the highest recorded since the beginning of reliable statistics in 1939.) "Unemployment was considerable," he deadpans. It was an economic collapse every bit as significant as the Great Depression ten years later, or our situation today with the Covid lockdown. And if that sounds like political trouble, consider 1920 was also a presidential election year. "But here is the truly intriguing part of this story for a 21st century spectator," says Grant, warming to his story. "What did the government do? Essentially nothing."

Despite all the economic bad news, Republican Warren Harding won the 1920 election with a promise to balance the budget and rein in government spending. To battle inflation, interest rates were hiked to 7 percent. It was the very opposite of the nearly continuous monetary expansion of the past 20 years, events so large and frequent they've required the invention of a succession of new terms, such as "quantitative easing." When Congress tried to hand out a "Soldier's Bonus" to all First World War veterans in 1921 as a thinly-veiled stimulus package, Harding vetoed it. The President's slogan: "Less government in business and more business in government."

The Harding administration was intent on letting market forces return the economy to equilibrium and voters seemed to agree. "It was a more stoical age," Grant notes. "People were more inclined to keep their personal troubles to themselves." And such stoicism was reflected in the bureaucracy

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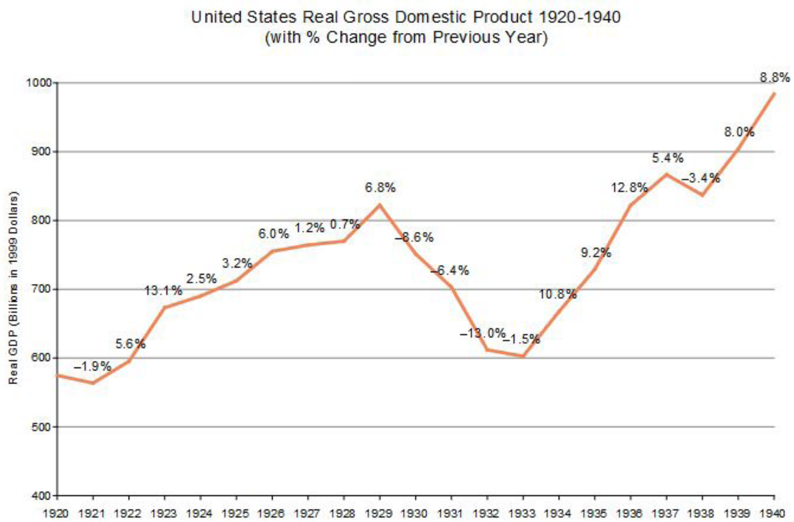
as well as the electorate and administration. Consider the private correspondence of Benjamin Strong, president of the Federal Reserve Bank of New York and the country's *de facto* central banker in the 1920s. Despite vociferous demands from the banking sector and elsewhere, Strong refused to lower interest rates as the downturn took hold. "I believe that this period will be accompanied by a considerable degree of unemployment, but not for very long, and after a year or two of discomfort, embarrassment, some losses, some disorders caused by unemployment, we will emerge with an almost invincible banking position," he wrote to another economist.

Warren Harding won a landslide election victory in 1920 on his platform of letting market forces sort things out, ushering in the Roaring Twenties.



It seems impossible to imagine a central banker today even counselling such a hands-off approach to monetary policy, either privately or publicly, let alone implementing it. Yet Strong's tough medicine proved entirely correct. "Wages fell, but this allowed businesses to reset at a lower level," observes Grant. Interest rates came down in step once inflation had been tamed. And soon investment capital poured in to take advantage of the new, lower market level. While the downturn of 1920-21 was undoubtedly a difficult time, what stands out today is its brevity. It was over and done in a mere 18 months, just as Strong predicted. And without any substantial government intervention; in essence the economy cured itself. Thereafter followed what Grant calls a "spring-loaded recovery."

After the downturn ended in 1921, the Twenties proverbially roared with exuberant growth and experimentation. Beyond a sharp rebound in the stock market and economic activity, the remainder of the decade is also notable for major developments in music, literature and cinema. It was called the Jazz Age. Women got the vote. Electrification took hold. Cars became a consumer item. At mid-decade production of Ford's Model T, due to recently developed assembly line production techniques, reached 2 million cars per year. Price: $260. The U.S. economy grew by an astounding [42 percent in the 1920s] – even including the effects of the downturn that kicked off the decade. Economic growth in Canada was similarly robust.

"If you look back at what the world had been through – the worst war imaginable, and then a pandemic and a depression – it was a tremendous release and relief that it was all over," says Grant. On New Year's Day 1923, the *Wall Street Journal* declared, "1922 can be recorded as the renaissance of prosperity." Such an ebullient recovery should be our goal for the 21st century's Twenties as well. (Although we'd want to avoid the subsequent stock market crash of 1929.)

There is no Canadian work equivalent to Grant's book describing this country's economic experience during 1920-21 – he calls it the *Forgotten Depression* for good reason. Typical of the scant coverage given to this period, the widely-used undergraduate textbook *History of the Canadian Economy* states simply "There was a sharp recession in 1921…[and] unlike the downturn a decade later, this recession was very brief." It doesn't discuss why. Yet plenty of historical evidence suggests our nation's trajectory in wages, prices and jobs was remarkably similar to that in the U.S.

According to the *Historical Statistics of Canada,* a general labourer in Montreal earned 45¢ per hour in 1920. A year later, his wages fell 22 percent to 35¢ – equivalent to Alberta's current $15 per hour minimum wage falling to $11.70 per hour. As Grant observes, however, while falling wages may be temporarily painful, they allow the labour market to clear quickly and recover. While the whole era's economic statistics are woefully incomplete, the available historical data suggests Canadian wages largely stabilized by 1922.

For the remainder of the decade, the industrial composite employment index rose steadily, reflecting a healthy and growing labour market. The online high school history textbook *Canadian History: Post-Confederation* offers a bit more detail on the recovery: "In 1920-21 there was a brief but sharp economic collapse…the state pulled back at this time, trying to allow the capitalist market economy to take the lead…The substantial improvement in the economy after 1921 vindicated this approach."

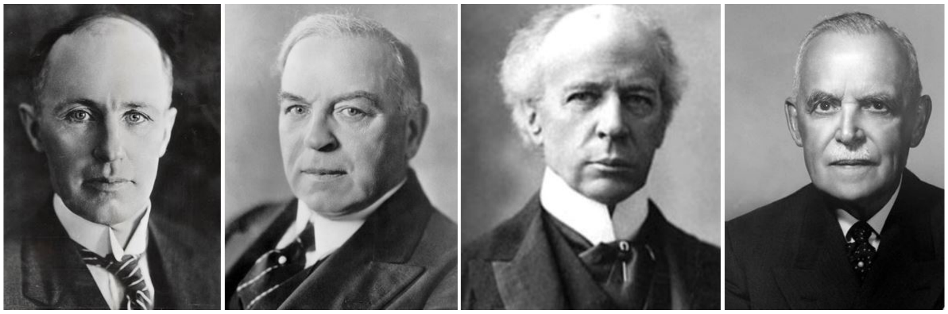
On New Year's Day 1923, the *Wall Street Journal* declared, "1922 can be recorded as the renaissance of prosperity." Such an ebullient recovery should be our goal for the 21st century's Twenties as well.

Unlike in the U.S., however, in Canada there was a political cost to be paid for such a hands-off approach. Conservative Prime Minister Arthur Meighen took office in 1920 at the beginning of the downturn and largely followed the intervention-avoiding Harding model. According to the Fraser Institute, Meighen is a member of an exclusive club of four Canadian prime ministers to have cut government spending during an economic downturn. The others are William Lyon Mackenzie King, Wilfrid Laurier and Louis St. Laurent. (The list of prime ministers who increased spending during a recession or depression is much longer, at 11.) Meighen badly lost the 1921 election to Mackenzie King, largely due to a shift in farm voters from Conservative to the new Progressive Party; today Meighen is remembered more for his long retirement than his very brief term as prime minister.

Politics aside, the real lesson of the 1920s lies in its comparison with the Great Depression. While there are numerous story lines involved in the Great Depression, including a banking crisis and the curtailment of international trade, Grant's book focuses on the key role played by government intervention in the labour market in prolonging the crisis. Following the devastating stock market crash on Black Tuesday, October 29, 1929, U.S. President Herbert Hoover (an engineer by training who'd been Harding's Commerce Secretary) declared it was politically untenable to allow wages to fall as abruptly as they had a decade earlier. "It was Hoover's conviction that capitalists should bear the brunt of this depression," observes Grant. Nascent labour unions eagerly abetted such a policy. And it was effective, at least in the short term.

According to the U.S. Bureau of Labor Statistics, 92 percent of firms lowered their wages in 1920 in response to the downturn, whereas only 7 percent did so in 1930. But the longer-term result proved crippling to the economy. Businesses became caught in a vice of falling prices and artificially high wages from which they could not escape. "Without flexibility in wages, it is very difficult for businesses to reset at a new lower level of reality," says Grant. Mass unemployment and chronically low wages thus lingered in the U.S. for the entire decade. Our Montreal labourer suffered similarly. His wages actually rose in the first year of the Great Depression, from 38¢ in 1929 to 40¢ in 1930. But this proved unsustainable as the economy collapsed, and his hourly pay ultimately fell to 28¢ by 1933; the national labour index also dropped nearly continuously throughout the 1930s, reflecting worsening unemployment.

The length of the two economic slumps tells the tale. The Great Depression officially lasted for 43 months, from 1929 to 1933, and then returned again in 1937-38. The Forgotten Depression of 1920-21 was every bit as nasty as its better-known successor, but was over and done in a year-and-half. While the short-term pain was undoubtedly severe, the cumulative damage on every level – including the total earnings of our humble wage-earner – was a fraction of the size. Of the two great economic downturns of the 20th century, it seems painfully ironic that the "forgotten depression" is the one that we ought to remember for the remarkable success of its recovery.



An exclusive Canadian Club: The only Prime Ministers who cut government spending during economic downturns: (l-r) Arthur Meighen, William Lyon Mackenzie King, Wilfrid Laurier and Louis St. Laurent. Meighen was crushed, however.

While Grant says he wrote his book as a response to government missteps during the credit crunch that preceded the Great Recession, the lessons of 1920-1921 seem equally appropriate to today's pandemic-inflicted economic lockdown.

"The political response [to an economic crisis] is always 'let's protect the citizenry from a repeat of the 1930s,'" says Grant. That's certainly been the dominant theme of 2020 as governments around the world are pouring unprecedented amounts of borrowed or conjured fiat money into the economy to protect wages and prop up businesses.

If Canada's national goal is to enjoy a supercharged recovery once the Covid crisis ends, then the central lesson from a century ago remains valid today. Government should interfere as little as possible in the labour market, and thus allow wages to find their own level commensurate with prices and output.

In Canada, nearly 8 million workers have applied for the federal government's Canada Emergency Relief Benefit (CERB), which provides $500 per week to almost anyone who asks for it. This week it was revealed government bureaucrats are actually under orders to let cheaters continue to collect CERB or regular EI benefits. Over $30 billion has been paid out on CERB as of this month, with no end in sight. This has been followed by additional special programs for students, small businesses, large businesses, banks, landlords, farmers and the energy sector, plus wage subsidies for nearly every other imaginable group or component of the economy. Combined, the Parliamentary Budget Officer expects this year's federal deficit to hit $252 billion, nearly an order of magnitude larger than last year's projected $26 billion deficit, and a truly unsustainable 11 percent of the nation's nominal GDP.

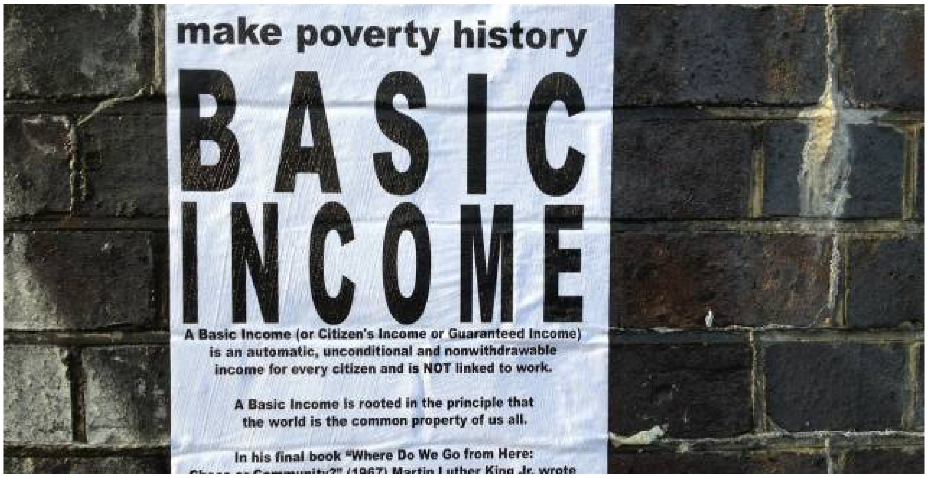
There are, of course, many good political reasons for unleashing this torrent of federal largesse. No politician wants to appear hard-hearted or oblivious to the many social costs of the economic lockdown and the mass unemployment it has engendered. And perhaps most important, unlike all previous downturns, people have been forced out of their jobs and into hiding by deliberate government edict, rather than through the collective actions of the market. But Grant's historical evidence still serves as a strong note of caution to policymakers regarding the costs of allowing wages to calcify at current rates when conditions have changed so dramatically. "People had to get back to work in 1921, whereas now it's not so clear," he says.

For many workers, their various subsidies and benefits amount to more than they were making when the economy was still in fine fettle. There is also increasing talk of turning the CERB into a universal basic income program, which would remove the need to work from a large swath of the population. Plus, many unions are now demanding low-skilled workers in frontline service industry positions should receive permanent wage increases in addition to any temporary bonuses currently being earned. All this threatens to drive a wedge through the heart of the labour market by delinking marginal productivity from wage rates. Plus, why would anyone return to work if staying at home is more profitable, not to mention easier and seemingly safer?

Governments have found it difficult to resist political pressure to prop up wages during sudden downturns, but history demonstrates the negative long-term effects.

Yet politicians who point this out can expect a fiery blast from softer hearts. Earlier this month, for example, Manitoba Premier Brian Pallister correctly noted how CERB posed an obstacle to his government's efforts to encourage a return to economic normalcy. "We are fighting against a federal program that is actually paying people to stay out of the workforce," he said. "I don't like the fact… people are being paid to stay home and not work." For his honesty, the *Winnipeg Free Press* editorial board labelled Pallister's comments "inexcusable."

But truth in policy-making, Grant argues, should require politicians to inform voters about the real choices involved in massive government intervention of the sort we are now experiencing. "Prices must be allowed to reach levels at which the market clears, whether that's in the jobs market, stock market or real estate market. We can either let prices clear quickly and live with the short-term problems that creates, or the



Enacting a Universal Basic Income Program or permanent wage increases could slow the economic recovery and hold back employment growth.

government can intervene to try to soften the blow, and in the process prolong the return to normalcy by years, or perhaps decades," he says. Post-pandemic, encouraging workers to continue to stay home rather than work, or creating expectations that wages are fixed and must not fall as conditions change, will simply delay the recovery.

If Canada's national goal is to enjoy a supercharged recovery once the Covid crisis ends, then the central lesson from a century ago remains valid today. Government should interfere as little as possible in the labour market, and thus allow wages to find their own level commensurate with prices and output. If anything, governments should reduce minimum wages to enable struggling small businesses to rehire as early and as much as possible. Alberta's NDP-era minimum wage hikes several years ago severely damaged thousands of businesses without any need for a pandemic. Maximum flexibility is what the labour market requires now. Less regulation and government interference, rather than more.

"The economic logic is sound," Grant says of his bold and controversial policy proposal. "But," he admits, "Given today's attitudes, the politics seem like a long shot." *Laissez-faire* policies are nearly impossible to promote during times of crisis. The need to be seen to be doing something, even if that something severely harms the economy, is simply overwhelming for most politicians. Yet often, doing nothing is provably the best course of action.

So having resigned himself to the fact the lessons from his Forgotten Depression are likely to stay that way, what does our investment guru predict for the prospects of a much-hoped for V-shaped recovery when the current pandemic ends? "It will be a different letter, that's for sure," Grant laments. "Maybe a U if we're lucky. Maybe an L if we're not."

Imprisoned in Our Cells: the Curse of the Digital Age

By David Solway

I'm sitting on a bench on the river boardwalk that skirts our quayside building, resting for a few minutes, sipping a coffee and taking my leisure after a pleasant saunter. I recall Henry David Thoreau's glorious passages in his essay *Walking* in which he stressed the importance of "sauntering," described as "the enterprise and adventure of the day." The word "saunter," he points out, derives from people "who roved about the country, in the Middle Ages, and asked charity, under pretense of going *à la Sainte Terre,* to the Holy Land, till the children exclaimed, 'There goes a Sainte-Terrer,'" in other words, a saunterer, a seeker capable of "sympathy with Intelligence."

Idly watching people walk by, I can't help noticing the ubiquity of the cell phone, the constant companion of pedestrians everywhere. Just for the fun of it, I begin keeping score. Several individuals amble past, consulting their phones held like a wand or talisman in a raised arm. Then a couple, each with that obligatory device into which they stare with rapt attention, completely oblivious to one another. Next, a girl walking her dog, leash in one hand, smartphone in the other, followed by a young man, ditto. Then, a young mother pushing a pram while intently reading the screen. Someone else walks by talking into plastic. A number of people are taking selfies. Almost miraculously, nobody stumbles or walks into a lamp post. Clearly, though, one cannot saunter while wielding a mobile.

Meanwhile, the scene around is alive with beauty and interest: flaming dogwood and Japanese cherry shedding their pink light into the air; plump koi speckled gold and cream gliding lazily in the ornamental pools and water gardens dotting the leafy esplanade; on the river, a tug hauling an immense freighter toward the docks and another towing a Seaspan chip barge to the sawmill, a loon preparing to dive and a seal or otter lifting its head from the waves. The tallest tin soldier in the world guards the entrance to the River Market, which seems to interest only children too young for smartphones. The largest sea gulls I have ever seen, some white, some gray, strut on a narrow sandbar. My friend Howard the Heron is busy deciding which of the logging bollards and pilings to perch on, his flight an act of pure grace.

So much to look at! A passage from Walt Whitman's *Crossing Brooklyn Ferry* comes to mind:

The sea-gulls oscillating their bodies, the hay-boat in the twilight…
The scallop-edged waves in the twilight, the ladled cups, the frolicsome crests and glistening…
the gray walls of the granite storehouses by the docks…
the big steam-tug closely flank'd on each side by the barges…

But it is as if none of this exists – the extraordinary richness of ordinary experience drifting by unremarked. There is also the inner world of one's thoughts, memories and observations, which had always seemed to me more than sufficient to occupy one's waking moments. Communing with oneself, one might learn that one is both an excellent conversationalist and a good listener, a dispenser of ageless wisdom and a gold-medal student. OK, kidding, but an inner landscape obliterated by the omnipresent cell phone is a melancholy thing to contemplate.

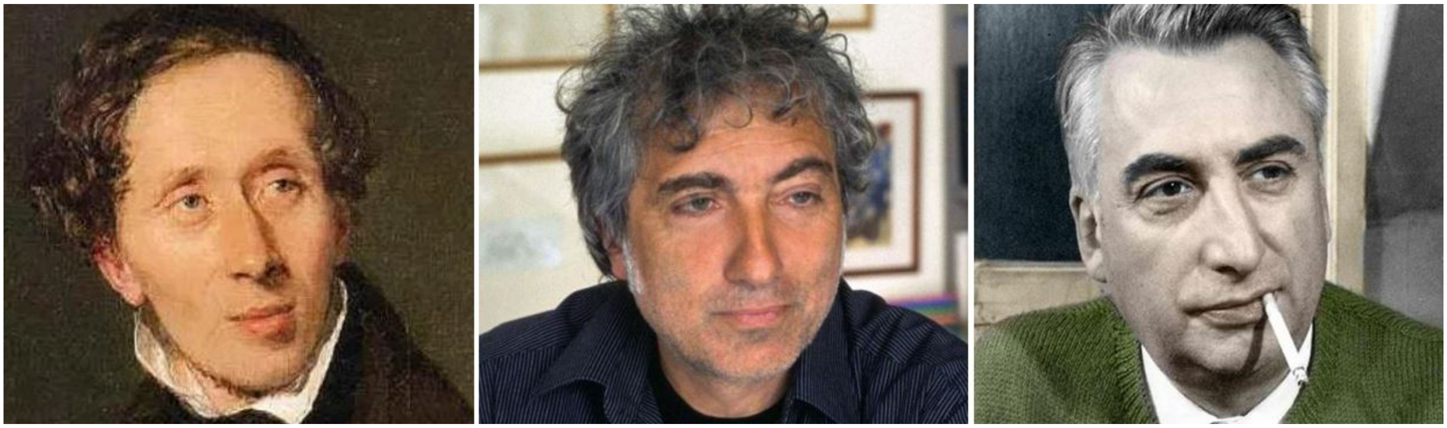
I recall some years back sharing a ride with a twenty-something girl in a car-dealership van on the way to pick up our newly inspected vehicles. She made no conversation with the driver or me, too absorbed in her screen, stroking it tenderly like a lover's cheek. Finally, I asked her, no doubt intrusively, why she paid so much attention to her device. "Because I'm bored," she replied.

I was struck by her answer. After all, boredom has its upside. It can lead to a renewed appreciation of the sparkle of the world around one. It can force one to plumb one's inner resources. It can toughen one's resolve to see things through. It may provoke one to read a book. It's an anagram for bedroom. As Søren Kierkegaard put it in *Either/Or,* "Those who bore others are the plebeians, the crowd, the endless train of humanity in general; those who bore themselves are the chosen ones, the nobility," since they are the ones who are able to "entertain others." Boredom, said Adam Phillips in *On Kissing, Tickling and Being Bored,* "is akin to free-floating attention…Boredom is integral to the process of taking one's time." And, as French critic and semiotician Roland Barthes observed in a delightful collection of essays, *Mythologies,* "Boredom is bliss viewed from the shores of pleasure." Indeed, figuring out Barthes' apothegm may also be a cure for boredom.

The lost art of contemplation: There is something to be said for observing life go by.

All these people I see walking by, eyes glued to the cell phone screen, trading trivialities with online friends, playing thumb-twiddling games, slavishly following directions from a machine instead of looking at signs and landmarks and learning the way for themselves, and surfing social media while the world is happening around them convince me that we are stumbling blindly into a new dark age. This is the future we are blithely welcoming. As James Bridle argues in *New Dark Age: Technology and the End of the Future,* "A kind of transport or transference [of information] is achieved, but at the same time a kind of disassociation, an offloading of…a way of thinking into a tool, where it no longer needs thinking to activate."

This is what Bridle calls a "chasm," a gap or crevice "that opens up between us when we fail to acknowledge and articulate present conditions." He believes the overall effect is more than merely trivial or annoying, but is bringing about "aspects of a new dark age that are real and immediate existential threats." Bridle is no Luddite and champions the proper use of our digital technology. Doing so, however, "depends upon attention to the here and now" and upon arriving at a symbiotic relation with our machines – "the things we think and discover together." He is concerned with avoiding "crashing ecosystems" and the like. His outlook remains positive, based on his belief that we "are not…without agency, and not limited by darkness." He remains convinced we are able to control our technological accomplices.



Great thinkers who were excited by the notion of boredom: (l-r) Søren Kierkegaard, Adam Phillips, and Roland Barthes.

But it is hard to deny that the ecosystem governing thought, meaning and interpersonal relations is disintegrating. Something has been manifestly lost in our all-encompassing digital age: the free exchange of reflective minds, the habit of meditation, lateral awareness of the real world, and the very contours of the introspective and stable self. Libraries are growing obsolete. "In the age of Google and the iPhone," asks Michael Walsh in *The Fiery Angel*, "Do we even need a 'library'?" We are swamped in a flood of information, most of it superficial and distracting, much of it false or misleading. We are constantly "connected" in a massive irony of disconnection from both self and other. A dystopian future we could once scarcely imagine may be coming to pass, a world no longer confined to fiction.

The mobile phone, for all its uses and convenience, is the bane of wakeful existence. Italian detective story writer Andrea Camilleri has a striking passage in *The Safety Net*, in which his protagonist, Chief Inspector Salvo Montalbano, approaches a group of teenagers absorbed in their cell phones, locked in "their personal bubbles of isolation." Gazing at their faces, he sees that "all of them had pinpoint pupils and looked lost" and that none raised their heads to acknowledge him, "as would have been natural." He walks away, wondering how it was possible, "in the age of global communication, where all cultural, linguistic, geographical, and economic borders had been erased from the face of the earth, that this vast new realm had only created a multitude of loners, infinite numbers of lonely people in communication with one another, yes, but still in a state of utter solitude."

Hope embedded in knowledge: Stills from the movie A Canticle for Leibowitz, *a post-nuclear-apocalypse tale of how a devastated civilization might rebuild itself.*

The cell phone, of course, is both an object and a symbol—a symbol of a far-flung network, as Bridle says, of "computational prediction, surveillance, ideology and representation [that] inform[s] and shape[s] our present perceptions of reality." And that is the issue. For it is, in effect, precisely what it says, a "cell," in which we lock ourselves and throw away the key. The "phone" part is beside the point, and not only because hardly anyone under 40 even uses their devices to talk to others (except perhaps grandparents), but since we cannot take advantage of the one permitted call to a lawyer to arrange for our release – there is no lawyer in the cell phone world.

"Stone walls do not a prison make," wrote poet Richard Lovelace in 1642, "Nor iron bars a cage." If the soul is free, he affirmed, "minds innocent and quiet" may experience a "Hermitage" consecrated to the enjoyment of liberty. The same cannot be said for Gorilla Glass and the latest OLED display, which is not a hermitage but a confinement whose parameters appear to be absolute.

George Steiner may have been right when he imagined a future of small, monastic flares of intellectual light sprinkled across a desolate landscape, reviving Max Weber's notion of frail enclaves of enlightenment as the last resort of a civilization sinking into darkness. I think, too, of Walter M. Miller Jr.'s classic *A Canticle for Leibowitz* with its obscure abbey in the Utah desert where historical knowledge is kept alive in a blighted world, even if it's only a sacred

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shopping list. The problem, as Barry Lopez says in *Arctic Dreams,* is that, "The good minds still do not find each other often enough." Certainly not, especially if they, too, are wired to their cell phones.

Perhaps among the crowd of strollers I observe from my bench on the boardwalk, Brother Blacktooth, whom we first meet in Miller's sequel *Saint Leibowitz and the Wild Horse Woman,* bearing a staff instead of a mobile phone, has embarked on an immense journey, a prolonged and adventurous saunter into the future and toward the distant light. The monk represents a ray of attenuated hope for the survival of intellect, discernment, thoughtfulness and what we used to call "spirit." But such a possibility is by no means clear. "A new world was rising," he notes, "but it could not grow as fast as the old." The new world he refers to is not the high-tech, solipsistic world we see around us but the world of a reconnected humanity pursuing its adventure of exploration and discovery. But Brother Blacktooth is right. It is not growing very fast.

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Future of Conservatism Series, Part VI: Seeing the World as It Is

By Sean Speer and Sam Duncan

Last year a major conference of conservative intellectuals and public figures including J.D. Vance, Peter Thiel, and Tucker Carlson generated considerable buzz in Washington. Characterized as an intra-discussion about the so-called "crisis of conservatism", the conference featured heterodox thinking on culture, foreign policy, nationalism, and various other topics. One of the most unconventional areas though was economic policy. Two thirds of the attendees affirmed the resolution: "America needs an industrial policy."

The basic premise here is that the United States should pursue a new, more activist economic programme that places a greater emphasis on the interrelationship between economics and geopolitics and the importance of cultivating key strategic sectors and industrial capacities. This is obviously a far cry from the free-market orthodoxy that conservatives have broadly subscribed to (though not necessarily faithfully implemented) for the better part of 30 years. But there is evidence that its intellectual and political resonance is growing. And the Covid-19 pandemic has only reinforced and accelerated this trend in conservative policy thinking.

Prominent Republican senators Josh Hawley (Missouri), Marco Rubio (Florida), and Tom Cotton (Arkansas) have become the political leaders of this movement. Public intellectuals such as Oren Cass, Michael Lind, and Samuel Hammond (who is Canadian) have contributed the theoretical and empirical foundations. There is a strong likelihood that this perspective will persist irrespective of whether President Trump wins re-election.

Why is industrial policy gaining renewed interest? What does it mean for Canada? And how should Canadian conservatives think about it?

The case for a new form of industrial strategy is increasingly justified due to the confluence of two recent developments. One is the rise of the intangibles economy, driven by intellectual property, data, and software, which has unique features and characteristics that distinguish it from what one might call the production economy. The other is the heightened geopolitical competition between the United States and China. The intensifying interplay of these two vast (and conceptually unrelated) trends – between technology and geopolitics – amounts to a renewal of political economy. Lind has called it "the return of geo-economics."

This is placing strains on conventional economic policymaking, which is based on the post-Cold War order of open markets, global cooperation and dispute resolution through liberal international institutions. This view increasingly fails to fully account for the "winner-take-all" character of intangibles capital and the extent to which it is reinforcing geopolitical rivalry. There is a good case that conservatives need to adjust their economic policy framework accordingly.

The same goes for Canada. The case may even be stronger here due to our smaller market size and greater vulnerability to the U.S.-China rivalry and how it manifests itself in supply chain disruption, market access challenges, and economic nationalism more generally. A new industrial strategy for Canada as it is conceived and advanced here would not mean a surrender to *dirigisme.* It is above all an expression of economic realism. It is a recognition that Canada will need to cultivate scale in certain strategic sectors and technologies if it is to compete in the new geo-economic environment.

And, in our view, it ought to be something that Conservatives (and conservatives) champion as part of a renewed programme for economic growth and opportunity in our country. It is tailor-made for a Conservative Party leadership candidate to make the animating idea of his or her leadership campaign and, following that, central to the party's effort to differentiate itself from the other parties in a federal election campaign, and ultimately to inform and shape a pro-growth governing agenda.

Advocates of a new industrial strategy: (top l-r) Republican senators Josh Hawley (Missouri), Marco Rubio (Florida), and Tom Cotton (Arkansas) and (bottom l-r) foundational intellects Oren Cass, Michael Lind, and Samuel Hammond.

Conservative Realism

Realism is part of the conservative DNA. Conservatism has always been at its core a rejection of abstraction and utopianism in favour of the practical and the prudent. Russell Kirk famously described it as the "negation of ideology."

Conservatism is best understood as a political persuasion that aims to see the world as it is rather than a universalized theory to which the world is expected to conform. It is instead the accumulation of historical wisdom about human nature, the limits of perfectibility, and so on, that can be applied in practical ways to new circumstances or conditions. One might describe it as a "living tradition" that is refined, adjusted, and reshaped for a particular moment or place.

This emphasis on practicality and particularism is what our old boss, former Prime Minister Stephen Harper, had in mind when he observed that "Conservatism is successful over time because conservatism works." He was conveying that conservatism is ultimately about applying collected insights and principles to emerging issues. The principles are fixed but the issues are necessarily dynamic.

The "stagflation" crisis of the 1970s is a good example. Conservatives recognized that various forms of government overreach – including high levels of state ownership, burdensome regulation, punitive taxation, and large-scale deficit spending – were causing simultaneous economic stagnation and inflation. The right response was to roll back the state to free up resources, improve economic incentives, and generally reduce the role of the state in the economy.

This agenda, which was implemented and came to be personified in Margaret Thatcher and Ronald Reagan, was deeply infused with conservative ideas but was not an exercise in dogmatism. It set out to apply conservative insights and principles to a specific set of challenges facing Western societies. It was, as one of us has written, "an inherently problem-solving project."

We are now confronted by a new set of challenges. The main problem today is the interplay between the unique features and characteristics of intangible capital and the new geopolitics. It is our view that the confluence of these issues is sufficiently new and different that it will require Conservatives (and conservatives) to adjust our basic policy framework.

We do not come to this conclusion lightly. We are as skeptical as other conservatives about "presentism" – the notion that "everything has changed" and past ideas need to be discarded to confront contemporary challenges. Yet the evidence seems clear to us that our current thinking about markets, globalized trade, and the role of government do not fully apply to the twin forces of intangible capital and the rise of China. It would be wrong, as one of us has written, to throw Friedrich Hayek and Milton Friedman out with the bathwater.

Ronald Reagan and Margaret Thatcher personified the successful conservative response to the declinism of the 1970s. Stephen Harper governed near the end of the post-Cold War era. Today brings new challenges.

But Conservatives must also be prepared to adjust our thinking and policy agenda to remain rooted in conservative realism. Not doing so would amount to a form of dogmatism, something conservatives have rightly tended to reject.

Intangibles Capital

What is the intangibles economy? The term refers to an economy that is steadily less driven by tangible assets such as plants, machinery, and equipment and more by intangible assets such as intellectual property, data, and software. Former British Conservative policy adviser Stian Westlake and his co-author, Jonathan Westlake, referred to this new asset mix as "capitalism without capital" in their award-winning book of the same title in 2017.

Intangible assets are becoming a greater source of investment and economic value in modern society. Just consider, for instance, that annual Canadian investment in data alone has grown by more than 40 percent since 2005, while investment in machinery and equipment has only increased by 8 percent. The transition to the intangibles economy is even more significant in the U.S. where these assets have gone from 16 percent of the value of the S&P 500 in 1976 to 91 percent in 2019.

The rise of the intangibles economy is most evident in market capitalization and equity markets. Here in Canada, Shopify, an online retail firm, recently supplanted the Royal Bank as the country's largest publicly-traded company. And in the U.S., five intangibles-based companies – Microsoft, Apple, Amazon, Google, and Facebook – now account for more than 20 percent of the S&P 500's market capitalization.

It is important to recognize that the rise of the intangibles economy and its distinct features and characteristics is not unique to particular sectors or parts of the economy. We are witnessing the growing importance of intangible assets even among so-called "traditional sectors." John Deere, for instance, is transforming its business model from purely a traditional manufacturer of farm implements into a data management company that it claims will "revolutionize farming." Suncor Inc. similarly has a new partnership with Microsoft to harness cloud computing and artificial intelligence to realize efficiencies and reduce climate emissions in its oil sands projects. More generally, data, proprietary algorithms, and other forms of intangible assets are reshaping traditional sectors as much as they are creating new ones.

These trends are important because, as others have documented, intangible capital has unique characteristics and features relative to physical assets. The biggest may be its scalability at close to zero marginal cost. Think of data, for instance. A single dataset can fuel multiple algorithms, analytics and applications, and so the data owner operates with minimal costs and with a much greater chance of dominating a market. It can become highly challenging for competitors to gain a foothold or eventually catch up.

The result is a tendency towards what has been described as a "winner-take-all" paradigm. This has unique economic and geopolitical consequences relative to traditional industrial models. The production economy, which is the basis for our theories of economic growth and comparative advantage, tends towards mutually beneficial exchange and, in turn, encourages global cooperation. The intangible economy, by contrast, tends towards monopolistic outcomes and, in turn, accentuates geopolitical competition. The West's assumption that

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China would passively accept the rise of Western-controlled intangible capital while contenting itself to remain rooted in the production economy proved a huge mistake. China's own view turned out to be rather the opposite.

Geopolitical Competition

The interplay between the rise of intangible capital and the U.S.-China rivalry is reshaping the technological and geopolitical landscape. The zero-sum dynamic of the intangibles economy is hastening a profound struggle for global dominance in these new forms of economic value. That these technologies typically have dual commercial and military or national security purposes has only intensified the competition.

The Trump Administration's National Security Statement has described it as the renewal of "great power competition." U.S. Vice President Mike Pence has called it a battle for the "commanding heights of the 21st century economy." And the Covid-19 crisis is only accelerating these trends. It is, according to journalist Fareed Zakaria, shifting the U.S.-China technological competition from a "soft rivalry to a hard rivalry."

The evidence is hard to dismiss. China's "Made in China 2025" policy statement is both highly ambitious and nationalistic. It not only aims to develop comparative advantages in key sectors and technologies such as artificial intelligence, aerospace, and biopharma, it targets raising domestic content of core components and materials to 40 percent by this year and 70 percent by 2025. This amounts to a hardened agenda of technological mercantilism in industries with major economic and national security implications.

The global pandemic has exposed the negative consequences of our dependency on China for pharmaceutical inputs and medical devices. The vulnerabilities exposed in this particular crisis have, in turn, become a touchstone for the entire relationship, causing reflection over supply chains ranging from rare earth metals to components and materials whose sudden absence in a future crisis could bring entire industries to a halt.

Rise of the intangibles economy: Canadian market leader Shopify, and John Deere's metamorphosis from tractor builder to data management company.

U.S. policymakers are responding with renewed calls for their own domestic industrial policies to match Chinese ambitions. Senator Rubio in particular has argued such a case. In a high-profile speech in December 2019, he called for a "21st-century pro-American industrial policy" to maintain a technological advantage over the Chinese in strategic sectors. As mentioned, the Covid-19 crisis is exacerbating this trend. Even traditional libertarian voices such as former House Speaker Paul Ryan have come to recognize the risks associated with supply chain dependence on China and the consequences for national security.

How these nascent political developments manifest themselves is too early to say. It is reasonable to expect that we will see a deliberate policy effort to repatriate U.S. supply chains from China in the aftermath of the current crisis. But even Senator Cotton, who has consistently been the Senate's leading China hawk, concedes that full decoupling is improbable. As he wrote in a recent essay for a new, pro-industrial-policy think-tank called American Compass:

"Cold War One [between the U.S. and the Soviet Union] could be thought of as an arms race, featuring two contestants running in separate lanes, striving for the finish line. Cold War Two [between the U.S. and China] will be more akin to a wrestling match, its contestants tangled up, seeking to exploit their leverage over each other, and straining, ultimately, to force the other to the mat."

One thing seems clear, though: the United States is poised to adopt a more nationalistic industrial policy model with measures likely to include greater public-private partnership in industrial research, more managed trade, more active foreign investment restrictions, more domestic procurement preferences, and much stronger emphasis on domestic intellectual property protection and commercialization.

Other countries are observing these trends keenly. The European Union, the United Kingdom, and others are responding to these technological and geopolitical changes by shifting from a mostly *laissez-faire* approach to a regional and national interest-driven model focused on key sectors and technologies based on national priorities and competitive advantages.

Industrial Policy

It seems clear to us that Canada must be prepared to recognize and assert its economic interests. We cannot count on others to do it for us. This is starting to register among the Canadian political class. But the focus thus far is mostly defensive. Several politicians, for instance, have spoken about the need to establish a domestic capacity to produce personal protective equipment. Others have lamented Canada's economic dependence on China and called for greater "self-reliance" or "economic sovereignty" more generally.

These ideas may be amply justified in light of the Covid-19 crisis. But they do not seem a proportionate response to the structural and longer-term forces that were manifesting themselves prior to the current crisis.

We are of the view that conservative realism points toward an industrial strategy for the new age of geo-economics. In particular, we see a role for public policy to cultivate capacity and scale in key sectors, sub-sectors and technologies where Canada has pre-existing comparative advantages and can come to have influence in global supply chains.

We emphasize scale on purpose. Intangible capital has dramatically increased the returns to scale. Yet Canada's economy, due primarily to its smaller market size, has too few firms of a global scale. This is evidenced by Canada's mediocre performance on intellectual property and commercialization. We cannot continue on this dismal track if Canadians are going to fully participate in the intangibles economy and benefit from the huge returns it produces. There is a role for public policy to create a "homegrown advantage" for domestic firms in order to help them reach a scale that they can participate in global supply chains and compete for global market share.

We have done it before, and a good historical example is canola. It is a Canadian agricultural invention that originally involved a combination of public

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Canada should seek to build upon strategic sectors such as bio-agriculture and energy.

support for research and development, university researchers in Western Canada, and private-sector firms. It is now one of the world's most important oilseed crops and Canada represents nearly two-thirds of global exports.

A Canadian industrial strategy would aim to cultivate similar "made-in-Canada" innovations where we can develop domestic firms and technologies at scale. It would not be about conjuring magical new industries out of thin air or expecting Canadian firms to compete in areas where other countries are clearly dominant. It would be clear-eyed about where Canada can reasonably expect to build a competitive foothold and target scarce resources there. Energy and agriculture are two obvious examples. Mining and metals, aerospace, and financial services might be others. The key would be to assess industrial potential based on metrics such as exports, patents, global market share, high growth potential, and

Playing the regional game: Minister of Innovation, Science, and Economic Development Navdeep Bains doles out federal pork to five Supercluster Initiative winners last year.

so on.

This would not be merely about public spending, either. It would come to influence a wide range of public policies including programmatic and regulation design, trade negotiations, foreign investment reviews, procurement, and so on. The key would be to recognize that governing is, by default, about choosing and that Canadian policymakers should in turn tilt the country's policy framework in favour of high-value, strategic parts of the economy with growth potential.

It is important to emphasize here that this is by no means about commandeering the market. The innovation and commercialization processes would still be decentralized and subject to market forces. The canola case is a good example here as well. The intellectual property and financial returns rested fully with commercial interests. But it involved recognizing that government policy is a precursor to market exchange, that it is unavoidable for the state to preference certain market outcomes over others, and that public policy should prioritize those parts of the economy where we can drive productivity and economic growth.

Think of a free trade negotiation, for instance. The balancing of so-called "offensive" and "defensive" interests necessarily involves prioritizing some economic or industrial objectives over others. The same dynamic applies to other areas of policymaking. An industrial strategy merely recognizes this reality and aims to bring greater coherence and intentionality to these choices. There is nothing incompatible with a commitment to markets or free enterprise. It amounts to a clarion call for a greater policy focus on economic growth, productivity, and innovation.

Calling for a new industrial strategy will nevertheless face criticism from some libertarian quarters. One of us has already been accused of dabbling in neo-Marxism. This line of argument has theoretical and empirical flaws.

The theoretical problem is it is not rooted in conservative thought which, as discussed earlier, is about seeing the world as it is. There is considerable evidence that "there is something fundamentally different about intangible investment" and that it requires us to rethink our policy assumptions. Even Arnold Kling, who has been affiliated with libertarian organizations such as the Cato Institute and Mercatus Center, has observed that "trying to stuff the square peg of intangible investment into the round hole of neoclassical capital theory turns out to be an effort with a low benefit-cost ratio." It is not that past conservative thinking about markets and government is wrong. It is just that it no longer fully explains the economic and geopolitical conditions in which we find ourselves.

The empirical point is that Canadian governments currently spend billions of dollars annually on different firms and sectors. And that does not even account for the wide range of non-fiscal ways in which the state intervenes in the market. The questions, then, are not whether public policy ought to tilt in the direction of certain market outcomes, but rather which outcomes it ought to target and what would be the most efficient and least distortionary means of doing so.

Some concerns about an industrial strategy are certainly justified. We recognize the risks of rent-seeking, inefficiencies, and distortions. A major

> The Conservative Party is starting to grapple with some of these big questions. The candidates have rightly committed to exclude Huawei from participating in Canada's 5G network. But there had been only limited debate about the broader set of ideas and policies that ought to animate the party. The Covid-19 crisis should sharpen the candidates' thinking.

Rejecting Huawei from Canada's 5G network is one step, but the final four federal Conservative leadership candidates, (l-r) Peter MacKay, Erin O'Toole, Leslyn Lewis, and Derek Sloan, should make the case for strong economic growth and opportunity.

risk, for instance, is the tendency of our bureaucratic and political systems to allocate scarce resources based on regional considerations. The Trudeau government's Superclusters Initiative is a good (or bad) example. It was supposed to be a hard-headed exercise in identifying Canada's industrial strengths wherever they might actually be situated. And, yet, the projects that were ultimately approved were still distributed equally across the regions.

Achieving the correct design of an industrial strategy will thus be critical to minimize these risks. It will require a clear and transparent process and ultimately a high degree of political discipline. But even then the expectation of zero distortions seems unreasonable. It is ultimately a matter of trade-offs. And we have come to accept that the interplay of the intangibles economy and the U.S.-China geopolitical competition has delivered such significant shocks to Canada's economy that the risks are justified.

One penultimate point: it cannot be emphasized enough that the Western world seems poised to head in this direction in the coming weeks and months. The evidence from the U.S., U.K., and elsewhere is compelling. We are likely to enter a renewed era of "national developmentalism" and Canadian policymakers will need to be hyper-focused on protecting and advancing Canada's economic interests.

This will be especially important as U.S. policymakers move to repatriate supply chains from China. Canada competes with the U.S. for investment and jobs. As the U.S. moves to boost manufacturing in particular and industrial capacity in general, Canadian policy will need to adapt its tools or we will risk shedding more jobs and capital to competing U.S. states. Economic realism will be a crucial ingredient to how Canadian policymakers respond to these new and evolving pressures.

What does all of this mean for Canadian Conservatives?

The Conservative Party is starting to grapple with some of these big questions in its leadership campaign. The candidates have rightly committed, for instance, to exclude Huawei from participating in Canada's 5G network. But before the global pandemic there had been only limited debate about the broader set of ideas and policies that ought to animate the party. The Covid-19 crisis should sharpen the candidates' thinking.

The pandemic's economic fallout is likely to dominate our politics for the foreseeable future. The impetus for economic growth has never been stronger. Canada's rate of economic growth over the medium- and long-term will not only determine whether our public finances are sustainable, but will also be a crucial ingredient for broad-based jobs and opportunity. Economic growth and higher rates of productivity must therefore be the overriding priority. This will also be a key area for political differentiation between the Conservative Party and Liberal Party, whose agenda has become increasingly preoccupied with carving up the economic pie rather than enlarging it.

The Conservative Party should commit itself to an industrial policy framework as part of a renewed programme of economic growth and opportunity. It would not only distinguish the Conservatives from the growing redistributionism of their left-wing opponents, it would better position Canada to navigate the new interplay between the intangibles economy and the U.S.-China geopolitical competition that seems certain to mark the coming years. The new geo-economics are reshaping the economic and geopolitical landscape. Conservative (and conservative) thinking needs to adapt accordingly.

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