July 15, 2015

Guest Editorial

The Gazette

# Disasters hinder rather than boost economies

By Paul Prentice, Ph.D.

Professor of Economics, Colorado Technical University

Senior Fellow, Independence Institute



*The Gazette* has run a number of stories regarding the purportedly positive impact of disasters, such as the Waldo Canyon Fire, on the Colorado Springs economy. The most recent of these is the top-of-the-fold, front-page story, “Much Lost, Much Gained” (July 5, 2015). I beg to differ. Fires destroy economic wealth, they don’t create it. We must beware of accountants disguised as economists. Accountants add and subtract, multiply and divide economic data. But they have no idea about from where the data comes, or what it represents, because they do not understand what an economy is.

An economy, properly understood, is that sphere of human action in which people specialize, produce, and trade; using scarce resources of land, labor, and capital to meet un-scarce wants and needs. The only way an economy can grow is to either increase the resource base, or increase the productive capacity of existing resources, or some combination of these two. Which of these does a disaster, such as a killer fire, actually increase? Resources were destroyed. The capacity to use remaining resources in their most productive manner was diminished.

These “accountants disguised as economists” develop sophisticated mathematical models purporting to represent an economy, but do they really? Every dollar “injected” into the economy by rebuilding is a dollar that would otherwise have been spent on something else. These models exhibit the fatal flaw of what Frederic Bastiat called the “Broken Window Fallacy” (Google it to see his original writing on the subject). Yes, we can see and measure the resources used to generate economic activity from rebuilding. But we can’t see the unseen, i.e. what those resources would have otherwise produced.

To follow Bastiat’s logic, without the fire we would have had those intact structures and lives plus whatever would have been produced by the resources that were diverted for rebuilding. With the fire, all we have is the rebuilding. I ask you, logically, under which scenario are we better off, with the fire or without it?

This is not to deny that there were clear winners from the fire. The *Gazette* article lists some of them: homebuilders, laborers, producers and sellers of appliances and furnishings, among others. Other winners that were not identified are those homeowners who had chosen not to purchase fire insurance, who had instead spent their money on other things, but then were bailed out by taxpayer money. But having clearly-identified winners is not the same thing as having a net economic stimulus.

To be fair, this logical flaw identified by Bastiat is not confined to local accountants disguised as economists. Sadly, it is widespread throughout the economics profession. We saw it in the pronouncements by “experts” that the death and devastation produced by Hurricane Katrina resulted in a net economic stimulus to New Orleans. Similarly for Hurricane Sandy,experts went on record that the death and destruction led to a net economic stimulus to New Jersey.

The root of the fallacy is found in what is called Keynesian economics. This is the false idea that war creates a net economic stimulus through the production of war-related materials, the employment of soldiers, and government-spending on rebuilding. One might want to ask the citizens of Germany and Japan if they felt “stimulated” by their military spending. Had the U.S. lost World War II, would we have thought of those war resources as having stimulated our economy, or would they have been thought of as wasted? Do rational people actually think that we can bomb our way to prosperity?

If it were true that the Waldo Canyon fire stimulated the Colorado Springs economy, then we need look no further for the next economic development project – just light more fires. Think of all the money that would be spent on rebuilding. Think of all the labor that would be employed in the rebuilding. At least one professor of economics at UCCS believes that we can burn our way to prosperity. I challenge him to light the first match.