

CHAPTER

1

An Idea  
Is Born



Once upon a time there were three men—Able, Baker, and Charlie—who lived alone on an island. Far from a tropical paradise, the island was a rough place with no luxuries. In particular, food options were extremely limited. The menu consisted of just one item: fish.



How an Economy Grows  
and Why It Crashes

Fortunately, the island was surrounded by an abundant population of strangely homogeneous fish, any one of which was large enough to feed one human being for one day. However, this was an isolated place where none of mankind's many advancements in fish-catching technology had arrived. The best these guys could do was jump in and grab the slimy buggers by hand.



Using this inefficient technique, each could catch one fish per day, which was just enough to survive to the next day. This activity amounted to the sum total of their island economy. Wake, fish, eat, sleep. Not much of a life, but hey, it beats the alternative.

And so, in this super-simple, sushi-based island society there were . . .



*No savings!*

*No credit!*

*No investment!*

Everything that was produced was consumed! There was nothing saved for a rainy day, and there was nothing left to lend.

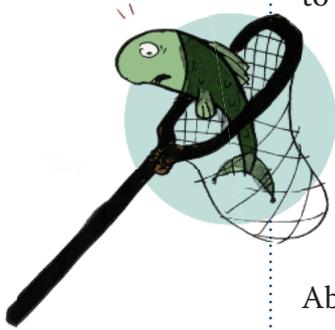
Although our island dwellers lived in a primitive society, it didn't mean that they were stupid or lacked ambition. Like all humans, Able, Baker, and Charlie wanted to improve their living standards. But in order to do this, they had to be able to catch more than one fish apiece per day, which was the minimum they needed to survive. Unfortunately, given the limitations of their bare hands and the agility of fish, the three were stuck at subsistence level.

One night, looking up into the star-studded sky, Able began pondering the meaning of his life. . . . "Is this all there is? There must be more to life than **this**."

You see, Able wanted to do something besides fishing by hand. He'd love to make some better, more fashion-forward palm-leaf clothing, he wanted a place to shelter himself from monsoons, and ultimately, of course, he wanted to direct feature films. But with his daily toil so devoted to fishing, how could these dreams ever come true?

His mental wheels started turning . . . and suddenly an idea for a **fish catcher** was born . . . a device that could vastly expand the reach of the human hand while severely reducing a fish's ability to escape after the initial grab. With such a contraption, perhaps more fish could be caught in less time! With his newfound time, perhaps he could start to make better clothes, build a shelter, and put the finishing touches on his screenplay.





As the device took shape in his mind, the orchestral music began to swell, and suddenly he conceived of a future free from daily fish drudgery.

He decided to call his device a “net,” and he set about finding materials to build one.

The next day, Baker and Charlie noticed that Able wasn’t fishing. Instead, he was standing in the sand, making string out of palm bark. “What gives?” asked Baker. “Are you on a diet or something? If you keep sitting there tying those strings, you’re gonna go hungry.”

Able explained, “I have been inspired to create a device that will unlock oceans of fishing possibilities. When I’m finished, I’ll spend less time fishing, and I’ll never go hungry again.”

Charlie rolled his eyes and wondered if his friend had finally lost his mind. “This is madness, I tell you . . . madness. When it doesn’t work, don’t come crying for a piece of my fish. Just because I’m sane doesn’t mean I’m gonna pay for your crazy.”

Undeterred, Able continued weaving.



By day's end Able had completed his net! He had **created capital** through his **self-sacrifice!**

## Reality Check



In this simple task, Able is demonstrating a basic economic principle that can lead to an improvement in living standards: He is **underconsuming** and he is taking **risk!**

**Underconsumption:** In order to build his net, Able is unable to fish that day. He has to forgo the income (the fish) that he would have otherwise caught and eaten. It's not that Able lacks the demand for fish. In fact, he loves fish and he will go hungry if he doesn't get one that day. Able has no more or less demand for fish than his two friends. But he is choosing to defer that consumption in order to potentially consume more in the future.

**Risk-taking:** Able is also taking risk because he has no idea that his device will actually work, or allow him to catch enough fish to compensate for his sacrifice. In the end, he might just have a bunch of string and an empty stomach. If his idea fails, he can expect no compensation from Baker and Charlie, who did, after all, try to warn him of his folly.

In economic terms, capital is a piece of equipment that is built and used not for its own sake, but for building or making something else that is wanted. Able doesn't want the net. He wants the fish. The net can, maybe, get him more fish. Therefore, the net, a piece of capital, is valuable.

That night, while Baker and Charlie slept with full stomachs, Able dealt with hunger pangs while images of luscious fish danced in his head. However, his pain was more than overcome by his hope that he had done the right thing and that a bright, fish-filled future awaited.

The next day, Baker and Charlie made much sport of Able's invention.

"Hey, that's quite a nice-looking hat," said Baker.



"A little hot for tennis, don't ya think?" added Charlie.

"Laugh it up, boys," responded Able, "but let's see who's laughing when I'm up to my armpits in fish guts."

As Able charged into the surf, the ridicule kept coming as he awkwardly handled his strange new device.

After a few minutes he got the hang of it and in no time snagged a doozy.



Baker and Charlie stopped laughing. When, in just a few hours, Able landed his second fish of the day, the boys were in awe. After all, it generally took them all day to get just one fish!

From this one simple act, the island's economy was about to change in a very big way. Able had just increased his productivity, and that was a good thing for everybody.

For the moment, Able pondered his sudden boon. "Since I can provide two days of food with only one day of fishing, I can use every other day to do something else. The possibilities are endless!"

## Reality Check



**B**y doubling his **productivity** Able is now able to produce more than he needs to consume. From gains in productivity all other economic benefits flow.

Before Able rolled the dice to build his net, the island had no store of savings. His willingness to take a chance and go hungry led to the island's first piece of capital equipment, which in turn produced savings (for the sake of this story we will assume that fish do not spoil). This spare production is the lifeblood of a healthy economy.



## Takeaway

**F**or all species, except our own, economics really boils down to day-to-day survival. Given the competition for scarce food, the harshness of the elements, the danger of predators, the vulnerability to disease, and the relative rarity of innovation, bare-bones survival (with some time left over for reproduction) is about all animals can attain. We would be in the same boat (as we were in the not-too-distant past) if not for two things: our big brains and our dexterous hands. Using the two together, we have been able to build tools and machines that magnify our ability to get more out of our environment.

Economist Thomas Woods likes to challenge his students with a simple thought experiment: What kind of economy would we have if all machines and tools disappeared? Cars, tractors, iron smelters, shovels, wheelbarrows, saws, hammers, spears, everything. What if they all went *poof* and all that we consumed had to be hunted, gathered, grown, and made, WITH OUR BARE HANDS?

Without question, life would be rough. Imagine how hard it would be to eat if we had to bring down game with our teeth, fists, and fingernails. Large game would be out of the question. Rabbits would be within our power to subdue . . . but you would

have to catch them first. What if vegetables had to be planted and picked by hand, and what if we didn't even have sacks in which to carry the harvest? Imagine if we had to make clothes and furniture without factories . . . without even scissors or nails?

Despite our intelligence, we would be no better off, economically at least, than chimps and orangutans.

Tools change everything and create the possibility of an economy. Spears help us bring down game, shovels help us plant crops, and nets help us catch fish. These devices magnify the efficacy of our labor. The more we can make, the more we can consume, and the more prosperous our lives become.

The simplest definition of *economics* is the effort to maximize the availability of limited resources (and just about every resource is limited) to meet as many human demands as possible. Tools, capital, and innovation are the keys to this equation.

Keeping this in mind, it is easy to see what makes economies grow: finding better ways of producing more stuff that humans want. This doesn't change . . . no matter how big an economy eventually gets.

