

U.S.—Mexican border made it more difficult to smuggle drugs between the two countries, which further squeezed the DTOs and exacerbated turf battles. Then Calderón launched his military offensive, and the number of killings shot up.

While it's easy to blame him for igniting the current brushfire of violence, we should not overlook the fact that political reform has also inflamed the drug wars. A quarter-century ago, Mexico was effectively a one-party state ruled by the Institutional Revolutionary Party (PRI); today, it is a full-blown democracy. Calderón represents the conservative National Action Party, as did his predecessor, Vicente Fox, who in 2000 broke the PRI's seven-decade stranglehold on the executive branch.

As Shirk points out, the relative peace and cooperation that prevailed among Mexican DTOs in the early 1980s was facilitated by ubiquitous corruption among members of the PRI. Decentralization and greater pluralism upset the crooked relationships that once shielded drug traffickers from internal competition and external law enforcement. In other words, Mexico's democratic progress has indirectly caused splintering and strife among the DTOs, which in turn has fomented violence.

The more we appreciate this paradox, the better we will understand the country's evolution. For all its warts, Mexico's record over the past 15 years is one of substantial political and economic maturation. Since the completion of NAFTA, it has signed a slew of free-trade pacts, including deals with the European Union, Israel, and Japan. The 2010 Index of Economic Freedom (compiled by the Heritage Foundation and the *Wall Street Journal*) ranks Mexico ahead of Costa Rica, Portugal, France, and Italy. Its score easily outpaces the global average, and is markedly higher than it was in the late 1990s.

"Mexico has a very well-managed economy," says Alberto Ramos, senior Latin America economist at Goldman Sachs. It has made huge improvements since the days of Pres. José López Portillo (1976–82), who nationalized the banks, and Pres. Carlos Salinas (1988–94), whose policy errors triggered the 1994–95 peso crisis. Following its post-Salinas financial meltdown, the country adopted inflation targeting and a flexible exchange-rate regime. As former Mexican central-bank governor Guillermo Ortiz has observed, these reforms boosted monetary freedom, aided capital-market development, and

strengthened the overall financial system.

The Mexican economy is deeply enmeshed with that of the United States, and was therefore pulverized by the Great Recession. Real GDP shrank by 6.5 percent in 2009. However, the global credit bust did not spark a domestic banking collapse, underscoring Mexico's new resilience, which stemmed from low inflation, a reduced debt burden, and a healthy stock of international reserves, among other things. While the country still needs sweeping labor, energy, and tax reforms—reforms that Calderón has championed but that probably won't happen anytime soon—its economic stewardship is much better today than it was two decades ago.

Moving forward, Mexico should also embrace structural political reforms designed to enhance accountability and tighten the connection between voters and their elected representatives. Calderón has offered a litany of proposals, such as permitting citizen initiatives, establishing a second round in presidential contests (if no candidate secures a majority on the first ballot), and allowing for the reelection of federal legislators and local officials. These measures could serve to alleviate the persistent scourge of institutionalized corruption, which continues to hinder economic growth and impede Calderón's anti-DTO campaign.

How can the U.S. help? Michael Shifter, president of the Inter-American Dialogue (a Washington think tank), says the Obama administration should increase police-training assistance and work more aggressively to curb the cross-border flow of assault weapons. Of course, as long as the U.S. both prohibits drugs and consumes an enormous quantity of them, Mexico will achieve only limited success in its fight against the cartels. Shifter and Campbell estimate that Mexican DTOs derive anywhere from 40 percent to 50 percent of their revenue from marijuana. Legalization is hardly a silver bullet, but if America did legalize pot, the traffickers would certainly feel a financial pinch.

Amid the grisly news of beheadings and other drug-related atrocities, it can be tough to remember just how far Mexico has come. Yet there are plenty of reasons to be encouraged. "I see Mexico responding to a real crisis in a very determined way," says Selee. Whether its response will be sufficient to quell the violence is unclear; but the situation is not nearly as hopeless as many Americans think. **NR**

Give Freely

In California and elsewhere, the Left wants the government to oversee philanthropy

BY JOHN J. MILLER

EARLIER this year, Thomas Perrin of the James Madison Institute visited the office of Florida state representative Greg Evers. As he pressed a copy of his think tank's latest report into the hands of a legislative aide, Evers walked by. "I overheard what they were talking about," says Evers, a Republican from the Panhandle. "So I put it in reverse and joined the conversation." Within a few minutes, Evers had adopted a new cause. "When I learned of what was going on, I knew we had to take action."

JMI's paper was on philanthropic freedom—and specifically on an emerging left-wing threat to it. In California, the state assembly had passed a bill that pried into the operations of private foundations. It demanded that they publish the race, gender, and sexual orientation of their trustees and of the leaders of the charities they support through grants. In other words, program officers at foundations would have been required to ask soup kitchens to identify their board members who are gay.

The California legislation didn't become a law—more on that in a moment—but it came close enough to set off alarms in the Tallahassee offices of JMI, a free-market public-policy group. "We keep an eye on Sacramento because that's where a lot of bad ideas are born," says JMI president Bob McClure. "We made it a priority to protect Florida's foundations and non-profits from what almost happened out there." Their efforts paid off: On May 27, Florida governor Charlie Crist signed a bill that explicitly bans the state from adopting regulations modeled on those almost enacted in California.

The fight is finished in Florida, at least for now. But the war over government control of philanthropies is set to break out in other state capitals as well as in Washington, D.C. As politicians seek to

close budget gaps, many are turning their gaze to high-income givers and foundation endowments—and wondering how they can plunder the wealth that allows Americans to give more than \$300 billion annually to support everything from churches to cancer research. President Obama has proposed slashing the charitable deduction for the richest Americans. So far, Congress has resisted. Yet some of its members would like to go even further than the White House. California Democrat Xavier Becerra, who sits on the House Ways and Means Committee, has referred to the tax-favored treatment of charitable donations as a “\$32 billion earmark” because that’s the amount of revenue Washington supposedly forgoes each year. Becerra wants Congress to play a stronger role in overseeing philanthropy: “I have an obligation to make sure that those \$32

the freedom of donors and foundations to decide where to give away their money,” says Adam Meyerson of the Philanthropy Roundtable, an association of grantmakers. “We are strongly opposed to the use of the political process to impose one set of preferences for philanthropy on the entire field.” Last year, the Roundtable felt threatened enough to put out a legal monograph on why tax exemptions for charity don’t transform private funds into public money.

Yet achieving this transformation is the goal of groups such as the Greenlining Institute, the Berkeley, Calif.-based organization that scored an astonishing success in Sacramento two years ago. It published a report claiming that California foundations didn’t spend enough on non-profits led by minorities. So its ally Joe Coto, a

Angeles. “It was about generating political pressure.”

The state assembly approved the bill, but then Coto yanked it. He had struck a deal with nine California foundations, including the William and Flora Hewlett Foundation (the sixth-largest foundation in the United States) and the David and Lucile Packard Foundation (the ninth-largest). In exchange for Coto’s dropping the bill, the foundations pledged \$30 million to “minority-led, community-based” groups. The political nature of the arrangement was obvious in the foundations’ euphemistic press release: It described the giveaway as the result of “productive discussions” with the chairs of the black, Latino, and Asian Pacific Islander legislative caucuses. “The big foundations are fooling themselves if they think they’ve bought off the activists,” says William Schambra of the

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billion that would have gone to the federal government are used for a . . . public good.”

The “public good” is in the eye of the beholder, of course. Last year, Becerra embraced a rather specific vision of it when he spoke at an event sponsored by the National Committee for Responsive Philanthropy. He praised the release of an NCRP report called “Criteria for Philanthropy at Its Best.” The document called on foundations to spend at least half of their grant dollars on “lower-income communities, communities of color, and other marginalized groups.” It also said grantors should spend at least a quarter of their donations on “advocacy, organizing, and civic engagement to promote equity, opportunity, and justice in our society.”

Foundations that want to abide by these standards certainly are free to do so. The point of the NCRP report, however, was not to encourage voluntary compliance but rather to build a consensus among political elites for a one-size-fits-all approach to philanthropy. “There’s a growing movement to limit

Democratic state assemblyman from San Jose, introduced a bill to require foundations to disclose the race, ethnicity, and sexual orientation of their staffs as well as their grantees. Supporters called for passage in the name of transparency, but the real motive was to exploit feelings of liberal guilt at large foundations and intimidate their boards and staffs into devoting more resources to an NCRP-style agenda. “This wasn’t about data collection,” says Wendy Garen of the Ralph M. Parsons Foundation, which concentrates its resources on disadvantaged populations in Los

Hudson Institute. “They’re going to keep coming back until they get their way. That’s how shakedowns work.”

The Greenlining Institute was anything but bought off. As the California foundations bartered with it, the organization set its sights on the Sunshine State. It pursued the same strategy, starting with a study claiming that Florida foundations weren’t giving enough money to minority groups. “The public expects foundations to serve the poor and needy,” said Al Pina of the Florida Minority Community Reinvestment Coalition, a local partner of the Greenlining Institute. “Unfortunately, foundations in Florida and around the United States have not held their end of the bargain.”

As in California, there were problems with the Greenlining Institute’s narrow-minded notion of how philanthropy benefits minorities. The group claimed that Publix, the grocery-store chain, gave less than 3 percent of its donations to minority-led organizations. Yet the company contributed almost \$39 million to the United Way through an employee-



*“How can you call yourself a paleoconservative?
I think you have a very nice tan.”*

giving program and its own charitable arm. In turn, the United Way supports everything from helping the mentally disabled to feeding hungry seniors—no matter the color of their skin. But because the United Way doesn't fit Greenlining's definition of a "minority-led" organization, Publix stands accused of exclusionary grantmaking. "How absurd," says McClure of JMI. "This is the 'ACORNization' of philanthropy."

When McClure learned about the Greenlining Institute's success in California and its new report on Florida, he had his think tank launch a counterattack. It commissioned Matthew Vadum of the Capital Research Center, a Washington, D.C.-based group, to investigate the Greenlining Institute and explain its scheme. Vadum's eight-page report, published by JMI last December, is what found its way into the hands of State Representative Evers and laid the groundwork for the legislation that now protects Florida foundations from the harassment that their California brethren have suffered.

It's not clear where the Greenlining Institute will strike next. Figures in the philanthropic community have said they're keeping an eye on New Jersey, New York, Pennsylvania, and Texas as possible targets. Meanwhile, the abuse continues among lawmakers who refuse to honor the intents of private donors. Earlier this year, Arizona's legislature snatched a \$250,000 bequest from the coffers of the Arizona State Parks Board. The politicians decided that the gift of Asta Forrest, a Danish immigrant who had wanted to support a park system that she had grown to love, instead would help close a budget gap. "She never would have given the money if she had known that the state was going to take it away from the parks board," a friend told the *Arizona Republic*.

The next attack on foundations may occur in Washington. In February, *CongressDaily* reported that "Senate aides are quietly exploring ways to tax the massive wealth tucked away in charitable foundations." In his most recent budget proposal, Obama once again proposed to reduce the charitable tax deduction on top earners. He thinks it's smart policy. But behind every governmental act to control or influence the philanthropic sector lies a sentiment that is the exact opposite of charity: envy. **NR**

Your Money Back

There is a strong economic case that the Federal Reserve should not exist

BY GARY WOLFRAM

Is Ron Paul's suggestion that the Federal Reserve be eliminated a "fringe position," as Josh Barro suggested in the last edition of *NATIONAL REVIEW* ("Mend the Fed," June 21)?

It depends on what "fringe" means. If it means simply that a large majority disagrees, then Representative Paul's position deserves that characterization. But if "fringe" is meant to imply that abolishing the Fed is a lunatic idea that is not supported by economic theory, then Paul's position is far from it. In fact, a number of economists argue that the economy would operate more smoothly without a Federal Reserve.

Paul's position is supported by Austrian business-cycle theory, an economic analysis that has its roots in the writings of Ludwig von Mises and Friedrich Hayek. This theory emphasizes the role of the interest rate in bringing together the plans of producers and consumers. The interest rate is the price of loanable funds—in effect, the price of money—and, like the price of any good or service, it gives producers information about consumers' behavior and the actions of other producers. For example, if consumers wish to save—to put their money in banks, which lend it out—they will increase the supply of loanable funds, putting downward pressure on the interest rate. Producers can then borrow that money cheaply and invest in capital goods such as machinery, factories, and housing—which they can use to create goods for consumers to buy in the future with the money they have saved. Thus do producers and consumers arrive at the equilibrium interest rate, which matches producers' plans to invest in capital goods with consumers' desire to save.

Central banks, by artificially expanding the supply of loanable funds in order to

generate a temporary boom, drive down the market interest rate and distort these signals. At a lower interest rate, producers are inclined to borrow money and invest it in capital goods, on the assumption that consumers are saving to purchase more goods and services in the future. In fact, consumers are not saving; they are continuing to consume goods in the present.

Those artificially low interest rates eventually must rise, usually when the government raises the interest rate to combat the inflation it created by lowering it. As a result, the cost of the labor and capital needed to produce capital goods rises beyond what producers expected, so they begin to lay off workers and abandon capital investments. The end result is that producers have used up resources in order to produce future goods for which there is not a sustainable demand. This is what Hayek calls "malinvestment," and it is the fundamental cause of the boom-bust cycle.

The longer the boom is maintained, the worse the bust will be. Mises likened the process to a builder who designs a house thinking he has more bricks than he does. The longer he continues to build, the harder it will be for him to redesign the building once he discovers how many bricks he actually has.

What's the alternative to the Fed? Hayek, in a lecture delivered to the Gold and Monetary Conference in 1977, proposed "free banking," the privatization of the money supply:

As a result [of new research], I am more convinced than ever that if we ever again are to have a decent money, it will not come from government: It will be issued by private enterprise, because providing the public with good money which it can trust and use can not only be an extremely profitable business; it imposes on the issuer a discipline to which the government has never been and cannot be subject.

There is no consensus on macroeconomic policy among economists, and monetary policy is especially contentious, but a good number of them argue that the Austrians got it right: The Fed causes the boom-bust cycle, and free banking is the solution.

For example, Prof. Lawrence White of George Mason University, in a 2008 paper for the Cato Institute ("How Did We Get into This Financial Mess?"), explains how

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