

BANKNOTES

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Liberal, Libertarian, and the Business Cycle

By L. Carlos Lara

What's in a word? Actually, a great deal. When it comes to the word "*Liberal*" or the word "*Libertarian*," it can be like opening Pandora's box. For this reason, I am going to try to decipher and separate some of the widespread misunderstandings about these two political philosophies. At the same time, I hope to end up explaining the relevancy of *Austrian Economics* in relation to these two philosophical views, and especially the *Austrian Business Cycle Theory (ABCT)*, in simple to understand language.

Background

The last ten years have convinced me that there is a great deal of confusion here. These two expressions, *liberal* and *libertarian*, often get co-mingled in conversations, and many people think they understand their true meaning when in fact they really don't. Consequently, when this lack of understanding gets compounded, it leads to gross misrepresentations and faulty stereotyping. When the term *Austrian Economics* gets dragged into the discussion, as it often does, its own definition suffers and is misunderstood as well. At that point, we wind up with a jumbled mess, and this is what I want to try to untangle.

However, my main concern, as I have already stated, is for you, the reader, to be left with the understanding of why *Austrian Economics* is so relevant to our modern world and its own set of financial confusions. This concern was one of the main reasons why Bob Murphy and I were so motivated to integrate *Austrian Economics* with Nelson Nash's Infinite Banking Concept (IBC) in the book that he and I ultimately wrote in 2010—*How Privatized Banking Really Works*. We recognized that the number one stranglehold in the lives of average 21st-century people is money related and that IBC provided the individual a way of escape. It was a message we felt needed to be spread before it became too late.

Yet I sense that the confusion I speak of with regards to these two philosophical designations may be the last remaining obstacle that

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stands in the way. It needs to be removed for many people to finally break through to a thoroughly sound economic way of thinking that allows them to embrace our message. So, my attempt in this article will be to make clear, in the plainest English that I am able to muster, the correct view of the first two confusing beliefs—*liberalism* and *libertarianism*—and then focus on making clear the more important one—the *Austrian Business Cycle Theory*.

Understanding How The First Gave Rise To The Second

Using the Internet's most popular dictionary, this is the brief introductory summation we find there about these two philosophies.

“*Liberalism* (from the Latin *liberalis*) is a political philosophy or worldview founded on the idea of liberty and equality. Liberals espouse a wide array of views depending on their understanding of these principles, but generally they support ideas such as freedom of speech, freedom of the press, freedom of religion, free markets, civil rights, democratic societies, secular governments, gender equality and international cooperation.”¹

“*Libertarianism* (Latin: *libertas*, “freedom”) is a collection of political philosophies and movements that uphold liberty as a core principle. Libertarians seek to maximize political freedom and autonomy, emphasizing freedom of choice, voluntary association, individual judgment, and self-ownership.”²

There is one other similar term that pops up in this mix of words from time to time, and that is “*Libertinism*” or “*Libertine*.”³ However, this term can easily be dismissed because it is not a political philosophy at all and belongs in the realm of physical pleasures. This is more of an ethical or moral philosophy.

But the terms *liberalism* and *libertarianism* are somewhat in the same camp, and from the two basic (incomplete) definitions I have listed above, we can already see how the confusion may have sprouted.

We will expand on these brief definitions as we move further into this article, but for now, note that both definitions start out with the word “*free*,” or “*freedom*” (from the word “*liber*” in Latin).

It can also be said from these definitions that both philosophies are very similar in core principles and, as we will soon discover, liberalism, in a sense, gave rise to libertarianism at a particular point in history. This is something we often discover about words. Time and events have a way of changing their meanings. Not only do the meanings change, but philosophical terms, especially, can develop numerous branches or derivatives and sometimes even flip sides.

For example, did you know that today's Republicans are yesterday's Democrats? Reasonably speaking, this is true. At one time, both Parties stood for just the opposite of what they stand for today. The conservative and progressive hats were switched. This change in political views started after the Civil War and continued changing for the next 135 years.

Today, the Republican Party's generally accepted ideology is “American conservatism.” This contrasts with the Democratic Party's more progressive platform, commonly known as “*modern liberalism*,” which actually traces its history to the popular 1930s presidency of Franklin D. Roosevelt.⁴ Here in the United States, this is the point in time when the meaning of the word liberal fully changed from what it previously meant.

On a global scale, the word changed meanings when the definitive explanation of the worldwide Great Depression was given to British economist John Maynard Keynes.⁵ This combined social, political and economic change of views eventually led to the strengthening of the popular demand for state controls over economic enterprises and affairs. More specifically, this means a conscious move toward centralized planning embodied in today's U.S. monetary policy.

However, the original term “*Liberal*” and “*Liberalism*,” not the new American modern variety we have been highlighting, is quite a different and distinct political movement that emerged during the age of the *Enlightenment* in the 17th century. It became popular with philosophers and economists who rejected *heredity privilege*, *state religion*, *absolute monarchy* and the *Divine Right of Kings*. These *liberals* argued for each man’s right to life, liberty and property, which they believed government must always uphold.

Notable individuals who espoused this *liberal* philosophy were John Locke, Jean-Baptiste Say, Thomas Malthus, David Ricardo and Adam Smith. The classical economists, such as the famous Ludwig von Mises and others of the Austrian School, also embraced this form of “*classical liberalism*.” In short, this was the great classical *liberal* movement that later came to be known as “*laissez-faire capitalism*,” which meant a policy of government non-interventionism with an emphasis on economic freedoms.

Leonard E. Read is a renowned free market advocate in the Austrian School tradition (and was a personal friend of Nelson Nash) and the individual who established the first *libertarian* institution of its kind in the U.S. in 1946— *The Foundation for Economic Education (FEE)*. In one of his famous books, *Castles in the Air*,⁶ Read makes these interesting remarks about the terms *Liberal* and *Libertarian*. They are especially appropriate for this article’s purpose, and it also helps me arrive at the concluding point I am most trying to make about these two philosophies. Here’s what he wrote.

“There was a word that I always liked, the classical economists used it: ‘liberal.’ The word liberal really meant, in the classical sense, the liberalization of the individuals from the tyranny of the State. That word was expropriated by our opponents and it has now come to mean ‘liberality’ with other people’s money. The word was taken over. And so I, more than anyone else, was responsible for introducing and publicizing

and perhaps making worldwide the word ‘libertarian.’ I am sorry I ever did it. Why? Because the word libertarian has now been just as much expropriated as the word liberal.”

Leonard Read actually stopped referring to himself as a libertarian because people would unknowingly associate him with everything from a pleasure-seeking *libertine* to a socialist, all due to the ignorance of the true meanings of these terms. And my point to all of this is simply this. Ultimately, this is the problem we all must face when associating with any political or philosophical label. We invariably increase the chances of being stereotyped incorrectly because their meanings tend to change with time. So we may want to think twice before applying one of these labels to ourselves. Hopefully, these explanations of these two political philosophies will be helpful in your decision-making.

Continuing to paraphrase Leonard Read’s additional thinking on this, he felt that *liberty* in the ideal form could only exist in the imagination, for it has never truly existed and probably never will. On the other hand, brute force, or the extreme left, has and does exist; therefore, it should always be labeled and exposed.

“We call it communism, socialism, fascism, and so on. It is a masterminding scheme, the parts of which can be seen as can a blueprint. It is a discrete politico-economic mechanism and specific to the core. This is definitely nameable, as is a constitution, or any document, or thing, or person.”

So naturally, I can’t help but to agree with all of Read’s final points and make it a good place to end this particular discussion and leave it to your consideration. But now we move to the more relevant subject, the boom-bust business cycle as theorized by the Austrian School of Economics and its relevancy for today.

The Austrian Theory of the Business Cycle

Readers of our books know that Bob and I are of

the belief that the actions of the Federal Reserve since the 2008 financial crisis have been ineffective and counterproductive. In essence, we feel the Fed has done nothing more than set us up for an even bigger and more painful crash when it arrives. But in addition to our merely making these predictions repeatedly in spoken word and print, what we really want is our audience's growth in understanding of the source of this insight and how to actually read the signs that tell this unpleasant story. By this, we mean understanding the key components of the *Austrian Business Cycle Theory (ABCT)*.⁷

It should go without saying, but let's cover it briefly to make sure we understand, that the thinkers who influenced and developed the *Austrian Business Cycle Theory* were from Austria, but most proponents of the theory are American.

Although not the entire Austrian argument, the theory in its simplest form suggests that government-mandated intervention through its central bank (in our case, the Federal Reserve) manipulates credit expansions. It does so in order to increase credit and drive up demand (spending) throughout the economy, which in turn leads to quantifiable asset bubbles and unsustainable business expansion. When these asset bubbles burst, or when it becomes apparent that the future demand will not be high enough to have warranted all the extra investment these businesses have made (malinvestments), they will invariably fail. This culminates in a painful recession complete with bankruptcies and unemployment.

One key insight in understanding the business cycle described in the theory is in the word "*manipulates*." Just to be clear, this is not a hidden maneuver on the part of the Fed, but at the same time, it is clearly not a natural rate of interest. In order to increase credit, the central bank must lower the rate of interest and does, but according to the Austrian School, interest rates aren't simply the price of borrowing money inexpensively, or even increasing the money supply by printing it—they are signals.

Low interest rates are signals that tell business owners and entrepreneurs that lenders are flush with money created by consumers who are putting off present consumption and saving their money.

For example, in an industry like home construction, which is a very capital-intensive business, a low interest rate can make it much more profitable. Consequently, when the rate of interest is lowered, businesses of this type will expand operations, causing this sector of the economy to develop into an asset bubble. Unfortunately, since the rate of interest is *manipulated*, it's really a false signal and consumer savings have not really accumulated. The vitality of the economy has been falsified, and the demand anticipated by these business owners will not be there. Under these falsified circumstances, these businesses are unsustainable past the initial boom phase.

One other very important Austrian insight is that *capital goods* (the tangible assets of a business) are not *homogeneous*, meaning that the assets are all different. The Keynesian treatment of capital ignores this insight altogether. Therefore, in the Keynesian model, producing \$75,000 in nails is exactly the same as producing a \$75,000 construction crane. Common sense tells us that this is a huge disparity in these assets that can't be ignored. For this reason, the Austrian School argument is that if the economy is set up to create the wrong capital goods, it leads to waste and painful consequences down the road.

When a crash does occur, what should government and the central bank do? The Austrian School says they should do NOTHING. You can expect that there will be a short-term business adjustment period where the unsustainable businesses and assets are liquidated, while unemployment rises temporarily, but only until new investment is redeployed toward feasible enterprises and the workforce can be reabsorbed.

Unfortunately, government and the central bank, going back since the Great Depression of the 1930s, has continued to use the Keynesian model by always

attempting to head off the unavoidable recession by lowering the interest rates even further. They will even prop up failed businesses using taxpayer money, which the Austrians argue only puts off the inevitable and makes the recession drag on and become even more harsh when it finally strikes.

Conclusion

Hopefully, this article has cleared up a few misconceptions and you have been able to see the connections between the political and philosophical views mentioned as they integrate with economics.

My attempt at clarity for these often confusing terms hopefully sheds light on why things are the way they are. These euphoric economic booms and disastrous busts that financially wipe out so many people don't just mysteriously happen—they are created.

This is why Austrian Economics is extremely relevant in today's world and learning to understand the *Austrian Business Cycle Theory* is just as crucial as understanding what we mean by *privatized banking*.

Resources

1. *Liberalism*, from Wikipedia the free encyclopedia, article, September 23, 2017, <https://en.wikipedia.org/wiki/Liberalism>
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3. *Libertine*, from Wikipedia, the free encyclopedia, article, September 23, 2017, <https://en.wikipedia.org/wiki/Libertine>
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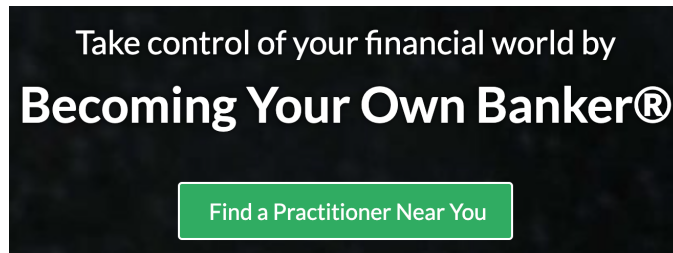
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a financial professional needs, in order to adequately discuss IBC with his or her clients.

Before you look for a practitioner, we suggest listening to the following two episodes of *The Lara Murphy Report*:

- [How-To Guide for Starting IBC, Part 1](#) How to begin your study of Infinite Banking, including finding an Authorized Practitioner.
- [How-To Guide for Starting IBC, Part 2](#) How to prepare for your first meeting with an Infinite Banking Authorized Practitioner.

The financial professionals listed below joined or renewed their membership as part of the *Authorized Infinite Banking Concepts Practitioners* team in July.

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- | | |
|---|---|
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Module 3, Part 3: How to Read a Policy Illustration

Module 4: Why Nelson Calls It The Infinite Banking Concept

Module 5: The Life Insurance Industry

Module 6: Why Not Buy Term and Invest the Difference?

Module 7: Using IBC to Pass Wealth to Future Generations

Module 8: The MEC Rule and Policy Design

Module 9: Does IBC Work for Older People?

Module 10, Part 1: IBC for the Business Owner

Module 10, Part 2: IBC for the Business Owner

Module 11, Part 1: Using Your IBC Policy: Premiums, Dividends, and Policy Loans

Module 11, Part 2: Using Your IBC Policy: Premiums, Dividends, and Policy Loans

Module 12: IBC as a Way of Life