



## WHY PRIVATE INVESTMENT WORKS & GOVT. INVESTMENT DOESN'T

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In 2011, a solar power company called Solyndra declared bankruptcy. A company going bankrupt is not news. But Solyndra was not just any company. Its biggest “investor” was the federal government which had given it \$500 million dollars. That was news.

But, really, it shouldn't have been. If history is any guide, it was quite predictable. The government is a very poor investor. And always has been. There are countless examples, but two should serve our purpose here.

After the Civil War, American leaders were anxious to bind the country's North, South, East, and West regions together with transcontinental railroads. Congress therefore gave massive federal aid to build the Union Pacific, the Central Pacific, and later the Northern Pacific Railroads. But all three of these roads had huge financial problems. The Union Pacific, for example, was mired in financial scandal from its inception, went bankrupt several times, and had to rebuild large sections of track thanks to shoddy construction practices.

At that same time, James J. Hill, with no federal aid whatsoever, built a railroad from St. Paul to Seattle – the Great Northern. How was Hill able to do with private funds what the Union Pacific failed to do with a gift of tens of millions of federal dollars?

The starting point is incentives. The Union Pacific was paid by the government for each mile of road it built. It was in the railroad's interest not to build the road straight. The more miles it took the UP to cross Nebraska, for example, the more money it made.

Hill, by contrast, used his own capital. To make a profit, he had to build his Great Northern Railroad sturdy and straight. Hill's company remained in business for almost a hundred years until 1970 when it merged with other railroads. The original Union Pacific, riddled with corruption and numerous other financial misdeeds, including the wholesale bribery of public officials, went broke within ten years.

The story of the airplane is even more stark. By the opening of the twentieth century, the major nations of Europe and America were frantically at work trying to invent a flying machine. The first nation to do so would have a huge military and commercial advantage.

In fact, leading American politicians of the day, such as Teddy Roosevelt, President William McKinley, and others argued that building an airplane was a national emergency. There was no time, they argued, to wait for private industry to get the job done. The government needed to pick the best aeronautics expert and give him the money he needed.

That expert was Samuel Langley, the president of the prestigious Smithsonian Institution and holder of honorary degrees from Harvard, Yale, Oxford, and Cambridge. Langley was already an accomplished inventor and he had written a highly praised book *Experiments in Aerodynamics*. Federal officials gave Langley funds for two trial flights. He immediately set to work. His theory was that his plane needed to be thrust into the air from a houseboat on the Potomac River. The big engine on the plane would then propel it through air for several minutes.

When his first attempt failed, and the plane splashed into the river, Langley was not deterred. But when his second flight did no better, Langley and the politicians gave up.

If Langley, with the full backing of the government, could not solve the problem, people simply assumed that it could not be solved. Indeed, *The New York Times* wrote that human flight might take a million years to accomplish.

But to everyone's surprise, nine days after Langley's failure, the Wright brothers, Orville and Wilbur, two bicycle mechanics from Dayton, Ohio, with \$2,000 of their own money, conquered the air. On a beach at Kitty Hawk, North Carolina, they flew the first plane. Within five years they had constructed an aircraft suitable to sell to the government for military defense.

Langley's subsidized failure was similar to that of the Union Pacific. And the Wright brothers' success resembled that of James J. Hill and the Great Northern Railroad. Langley and the Union Pacific were using other people's money. They did not spend it as carefully as Hill and the Wright brothers spent their own money. As the *San Francisco Chronicle* concluded at the time: "The destruction of Langley's machine should put an end to Congressional appropriations of any kind in every field of experiments which properly belongs to private enterprise."

That remains good advice.

Economic growth comes from entrepreneurs risking their own money, not from politicians risking your money.

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