The Fallacy of Fixed Proportions
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The Fallacy of Fixed Proportions

This fallacy is related to that of petty incrementalism, but is even more extreme and absolute. We saw and heard much of this following the OPEC price revolution in 1973. Energy use and national income, we were told, move in lock step together. To avoid national disaster we must subsidize oil exploration in every possible way, according to Charls (sic) Walker. Only crazy hippies could believe that conservation or reduced use were possible, said Dr. Walker, with his Ph.D. in Economics from the Wharton School.

We must increase the cash flow of the big oil corporations, said he, from the U.S. Treasury. (Some cynics even thought perhaps he was working for them.) However, since then we have reduced energy use in the United States some 23%, by such commonsense adaptations as going to compact cars. (As a reward for his foresight and public spirit, Dr. Walker was soon the top tax lobbyist in Washington, a frequent speaker at professional meetings, and a participant in crafting the Treasury's 1986 tax reform package. Today (1995) he is chief rainmaker for the American Council on Capital Formation.)

A subtle kind of change in proportions is that which occurs as capital grows older. Students are generally familiar with old autos. They are cheap, representing little capital; but they require much care and upkeep, representing much labor. Thus they provide labor-intensive transportation, in contrast with a new auto which is more capital-intensive: high cost upfront, followed by low maintenance.

It is somewhat the same with old vs. new housing. An old dwelling in a slum area in an older eastern city can be bought for 3 or 4 years' rental, representing low land value and very little capital. There are constant repairs, and struggles collecting rent, and high tenant turnover. Shelter is provided in a labor-intensive way. New housing is much more capital-intensive. A $200k mortgage at 13% (common in 1982) means interest around $26,000/year for the first few years.

Thus, over time the provision of shelter shifts from capital-intensive to labor-intensive, with the same house on the same lot.