



# The Present State of Austrian Economics

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[This paper was delivered at the Tenth Anniversary Scholars' Conference of the Ludwig von Mises Institute, October 9, 1992. Working Paper from the Ludwig von Mises Institute, November 1992. Reprinted in *The Logic of Action One: Method, Money, and the Austrian School*. Glos, UK: Edward Elgar Publishing Ltd., 1997, pp. 111-172. Reprinted in *Journal des Economistes et des Etudes Humaines*, Vol. 6 No. 1 (March 1995), pp. 43-89. ]

In the past two decades, there has been a seeming growth of methodological sophistication in the world of economics. Until the early 1970s, a blind Walrasian formalism held total sway in microeconomics, while a triumphant Keynesianism dominated macro, all held together by an unthinking and arrogant empiricist epistemology of logical positivism. The micro and macro synthesis of the neoclassical paradigm were both embodied and symbolized in the work of Paul Samuelson, while the positivist methodology was enshrined in the famed 1953 article of Milton Friedman and the later work of Mark Blaug.<sup>1</sup>

Since that point, however, the dominant positivist paradigm has been effectively overthrown, to be replaced by a bracing and near-chaotic Kuhnian “crisis situation” in the methodology of economics. For the last two decades, a dozen, if not a hundred, schools of economic thought have been allowed to bloom. Unfortunately, however, the orthodox paradigms in macro and especially microeconomics are still dominant, although less aggressively held than before; the crisis situation in methodology has not yet been allowed to trickle down fully to the substantive bread-and-butter areas where economists, after all, earn their livelihood. If methodology is in ferment, however, the rest of the substantive fortress may soon follow.

The deterioration of the dominant neoclassical paradigm starting in the early 1970s has numerous causes. I would contend that the main cause was the abject collapse of the Keynesian System upon the emergence of the first major inflationary recession in 1973—74, an anomalous situation that has marked every recession since. The inflationary recession of the early 1970s<sup>2</sup> was a shock for two reasons: (1) in the Keynesian model,

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<sup>1</sup>For my purposes, I am ignoring the allegedly wide gulf between the earlier positivists with their “verifiability” criterion and the Popperites and their emphasis on “falsifiability.” For those far outside the logical empiricist camp, this dispute has more of the appearance of a family feud than of a fundamental split in epistemology. The only point of interest here is that the Popperites are more nihilistic and therefore even less satisfactory than the original positivists, who at least are allowed to “verify” rather than merely “not falsify.”

For a brilliant and incisive discussion and demolition of the logical empiricist contention on many levels, see David Gordon, *The Philosophical Origins of Austrian Economics* (Auburn, Ala.: Ludwig von Mises Institute, 1993).

<sup>2</sup>Actually, inflationary recession had first emerged during the 1933-37 inflationary boom, which took place within a deep depression. But since the origins of that depression, in 1929-33, were seemingly not inflationary, this episode was considered anomalous, and irrelevant to future cycles. In addition, prices first began to creep upward, but only slightly, during the 1957-58 recession, an overlooked but important harbinger of things to come. During 1966, there was a recession again without the usual price fall, but this

recessions are supposed to be due to underspending, and inflation to overspending; how then could both occur at the same time? And what can fiscal (or even monetary) policy do about it? and (2) intervention and statist planning of fiscal policy and “growth economics” in the 1960s was supposed to have eliminated business cycles forevermore, to bring us, in the naive jargon of the economic Establishment of that day: full employment without inflation. Business cycle courses were purged from graduate curricula; for if business cycles had been rendered obsolete, such courses would only be antiquarian studies of economic history. The severe inflationary recession of 1973—74, followed by a similar and even more severe recession of 1979—82, ended the myth of the disappearance of business cycles.<sup>3</sup> And if planning for growth was seen to be flawed and even counter-productive, then perhaps government planning in general had severe problems; it was no coincidence, then, that the 1970s saw the resurgence of free-market economies and of free-market thinking among economists.

I contend, too, that the renaissance of Austrian economics beginning at about the same time was part and parcel of this general disillusion with both Keynesian economics and with government intervention, and part of a resurgence of free-market thinking. The Nobel Prize in economics granted to F.A. Hayek in 1974 has generally been credited with setting the spark for the Austrian revival, and there is much to be said for this thesis, especially considering the superstitious awe and veneration with which the Nobel Prize is regarded by the economics profession. But unless we really believe that the Swedish economists who award the Nobel annually are guided solely by divine inspiration, we must recognize that these gentlemen, too, reflect ideas current in the economics profession in Sweden and in Europe as a whole. After World War II, the Swedish profession, even more than their colleagues of other countries, was notoriously the home of Keynesianism and of econometrics; and the first Nobels, from 1969 through 1973, reflect that bias. It is no accident, then, that Hayek’s Nobel prize in 1974, shared ironically with the leftist maverick Gunnar Myrdal, was the first one to be granted to a free-market economist.<sup>4</sup> It is also significant that the first free-market Nobel went to Hayek, not for his later vaporings in “spontaneous order,” “knowledge,” “evolution,” and so on, for which he is unfortunately revered by most current Austrians, but instead for his elaboration of the Misesian business cycle theory which had been prominent in Britain in the 1930s, only to be swept away, in the late 1930s, by its great enemy, the Keynesian Revolution. To grant the first free-market Nobel to the antipode of Keynesian macro-

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was disregarded because the 1966 episode was not quite deep enough to meet the overly venerated National Bureau criteria for a recession. So the 1973-74 shock came like a bolt from the blue to the profession.

<sup>3</sup>We might even say of the business cycle as the great Etienne Gilson said about natural law: “the natural law always buries its undertakers.”

<sup>4</sup>Previous Nobels had been granted to: Keynesian econometricians Ragnar Frisch and Jan Tinbergen, Paul Samuelson, national income statistician Simon Kuznets, Kenneth Arrow and John R. Hicks, and input—output planner Wassily W. Leontief.

theory cannot be considered a coincidence: it symbolized the end of the unquestioned dominance of the Keynesian-statist paradigm in economics.<sup>5</sup>

The Austrian revival starting in 1974 has now lasted long enough and taken hold firmly enough to enjoy the luxury of its first published historian, who places central emphasis on the week-long South Royalton, Vermont, Austrian conference in the summer of 1974. Professor Karen Vaughn was a youthful participant, now turned participant-observer, at this conference, but unfortunately her account of that conference and of the revival generally is both biased and totally unsatisfactory. One of the minor purposes of this paper, in the course of a critique of that revival and of the current state of Austrian economics, is to analyze and correct the Vaughn record.<sup>6</sup>

### **Paradigms and the Whig Theory of the History of Science**

One of the most welcome aspects of the methodological ferment of the past twenty years has been the overthrow of the once-dominant “Whig” notion of the history of a scientific discipline: that it proceeds, onward and upward in linear fashion, testing hypotheses, accumulating knowledge, and discarding the dross, so that scientific knowledge embodied in the latest textbooks and journal articles at point  $t$  is always and necessarily greater than at point  $t-1$ . This means that since the scientific discipline always knows more, say in 1983 than in 1971 or 1962, that there is no point in reading any part of the discipline except the latest textbooks and journal articles. Oh, there could be an antiquarian point, in 1992, to reading 1956 physics or chemistry, to find out about the history of the earlier period, or to examine how a science grew, or how scientists influenced each other, but there is nothing to learn substantively about the discipline from reading older chemistry or physics.

But this sort of naively optimistic view has been rendered obsolete by the brilliant “paradigm” analysis of Thomas Kuhn, who shows that this fanciful tale is far from the truth, even in the physical sciences. Even if we are less relativist than Kuhn, and believe that later paradigms are usually superior to—closer to the truth than—earlier ones, there still can be a severe loss of knowledge in discarding earlier paradigms. At the very least,

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<sup>5</sup> Some of us harbor the suspicion that it is no coincidence that Hayek received the prize precisely in 1974, the year after the death of his great mentor, the founder of Austrian business cycle theory, Ludwig von Mises. The Swedish economics profession might have become partially liberated by 1974, but surely not liberated enough to grant the prize to as consistent and uncompromising an ideological and methodological “extremist” as Ludwig von Mises.

The next free-market economist to receive the Nobel was Friedman in 1976, to be followed by fellow Chicago school members Theodore Schultz in 1979 and George Stigler in 1982.

<sup>6</sup> Karen L. Vaughn, “The Mengerian Roots of the Austrian Revival,” in *Carl Menger and his Legacy in Economics*, Bruce J. Caldwell, ed., Annual Supplement to Vol. 22 of *History of Political Economy* (Durham, N.C.: Duke University Press, 1990): 395—405.

then, there can well be substantive knowledge gained by exploring earlier paradigms. If this is true even in the physical sciences, a fortiori it is even more true in the non-experimental disciplines such as philosophy and economics, where because of gross error, accident, or ideological or political bias, a later paradigm may well be inferior to earlier ones. There should not even be a presumption, much less a guarantee, of the later the better in the history of economic thought.

And yet, observers of the current Austrian school, as well as participants in it, have unwittingly and unthinkingly returned to Whig habits of thought when discussing or evaluating contributions of the Austrian school. They have unthinkingly assumed that the later the better, that is, that simply because, for example, the works of Don Lavoie or Ludwig M. Lachmann came later in time than those of Ludwig von Mises, that they must be better, or to put it differently, that these later contributions must constitute “development” and “growth” in the field. And yet, if later is not necessarily better, then the new may not at all constitute “growth”; newer may, in fact, constitute error and degeneration from an originally correct paradigm. But if the newer is not necessarily better, it follows that it might even be worse. And if a newer contribution is worse, and there is degeneration, then there must be some criterion or standard of truth with which to compare these temporally different contributions. On the other hand, if we take the fashionably nihilist view and claim that there is no truth, that anything, any methodology, goes, then it follows that contribution A can never be better or worse than contribution B, and then there can be no judgments of merit at all, regardless of the date of the contribution. Indeed, the entire scholarly enterprise may as well be abandoned.

To show how this inconsistency works: Professor Vaughn is horrified because a new work, in 1985, purportedly in Austrian economics, by O’Driscoll and Rizzo was severely criticized by other Austrians. She writes: “By the time of its completion, the book [by O’Driscoll and Rizzo] broke new ground in developing a coherent Austrian paradigm,” and adds: “and consequently was criticized by many Austrians who ‘knew’ it wasn’t faithful to Austrian principles.” But does this mean that Vaughn’s conception of the scholarly dialogue is that every new book, because new, must be above criticism, and that any criticism is somehow illegitimate? Is that the way she conceives of the search for truth? And what if the book is actually (a) fallacious to the core, and (b) totally violates Austrian principles? Are critics supposed to fall silent, because “Austrian principles” are to enjoy a definition so elastic that anyone should be allowed to call himself an “Austrian” without being subject to criticism or challenge?<sup>7</sup>

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<sup>7</sup> Vaughn, “Mengerian Roots,” p. 401n. Also see *ibid.*, p. 397n. Amusingly enough, Vaughn talks repeatedly of the O’Driscoll-Rizzo volume “garnering so much criticism” from Austrians without citing the major, indeed the *only*, place such criticism appeared: the devastating review by Professor Charles W. Baird, “The Economics of Time and Ignorance: A Review,” *Review of Austrian Economics* 1 (1987): 189—206.

*The Economics of Time and Ignorance* was a fortunately short-lived attempt to replace the Misesian paradigm with Bergsonian irrationalism; its rapid demise was assured by its demolition by Professor Baird. In the course of writing that work, Professor Rizzo, the philosophical leader of the duo, was moving visibly away from the Misesian paradigm. In a Mises centennial volume edited by Israel Kirzner, Rizzo first flirted with the then-fashionable philosophy of science of Imre Lakatos as a replacement for praxeology; in a

It is the contention of this paper, indeed, that several different and clashing paradigms have been allowed to develop and fester, all in the name of “Austrian economics”; that a great deal of confusion and incoherence have resulted; and that this coexistence of contradictory doctrine and proliferation of clutter should be brought to an end. In short, the rubble of Austrian economics must be cleared at last, the turgid undergrowth hacked away, Austrian doctrine re-clarified and truth enshrined, and the proliferation of error and fallacy swept away.

### **The New Methodology and the Burgeoning of “Austrian” Fallacies**

Part of what has happened to Austrian economics since 1974 was inevitable. Along with growth and flourishing, in numbers of economists, students, and contributions, there is bound to be a proliferation of error and of false leads and byways. That, in a sense, is a healthy development in the history of a science, but only if there are corrective forces who will periodically clear the underbrush and sweep away the rubble. That task has unfortunately not yet been done, although part of this necessary process has already begun.<sup>8</sup>

The idea of correction and demolition of error does not sit well with the now reigning paradigm in the epistemology of economics. The Old Methodology, dominant until the 1970s was frankly prescriptive, setting up criteria for valid and invalid theory. The problem with the Old Methodology was not that it presumed to methodological truth and validity, nor that it passed judgment on various methods and theories in economics, but that its criteria were systematically wrong: it was trapped by what Professor Mirowski calls “physics envy” to ape the assumed methodology of physics in the disciplines of human action. The problem with the Old Methodology (dominant until the 1970s) was not that it was prescriptive, but that its prescriptions were dead wrong. Unfortunately, in overturning the tyranny of the Old Methodology, the successful rebels focused not on the invalidity of the prescription but on the fact that any prescriptions were set forth at all. And so the prescriptive baby was thrown out with the positivist bathwater—to be replaced by the New Methodology of anything goes, of allowing all flowers, including noxious weeds, to bloom. The New Methodologists habitually deny that for them “anything goes,” but that is precisely what their proclaimed mission—to understand and

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postscript written a mere six months after the text, Rizzo announced another radical change of mind even further away from Mises. The final result in 1985 was the Bergsonian dead-end. See Mario J. Rizzo, “Mises and Lakatos: A Reformulation of Austrian Methodology,” in *Method, Process, and Austrian Economics*, Israel M. Kirzner, ed. (Lexington, Mass.: Lexington Books, 1982), pp. 53—73.

<sup>8</sup> See, for example, the demolitions of the fortunately short-lived “hermeneutical tendency” in Austrian economics, by David Gordon, *Hermeneutics vs. Austrian Economics* (Auburn, Ala.: Ludwig von Mises Institute, 1986); Hans-Hermann Hoppe, “In Defense of Extreme Rationalism: Thoughts on Donald McCloskey’s *The Rhetoric of Economics*,” *Review of Austrian Economics* 3 (1989): 179-214; and Murray N. Rothbard, “The Hermeneutical Invasion of Philosophy and Economics,” *Review of Austrian Economics* 3 (1989): 45—59.

clarify all theories, but never to judge or denounce them—amounts to. Clearly, the New Methodology is all too congruent with our New Age.<sup>9</sup>

There are two grievous and unwitting contradictions involved in this argument by our New anti-prescriptive Methodologists. In the first place, as we have pointed out in the case of Professor Vaughn, there is a glaring though unacknowledged bit of prescription: the Whig view that newer is necessarily better, a view that sits peculiarly in a system that offers no criteria for validity and no suggestion that there is any process or mechanism for learning about or adopting such criteria if they did exist. But there is also a deeper contradiction. For the New Methodologists are saying that it is wrong for economic methodology to be prescriptive, that it is only right for methodology to describe or clarify within each paradigm. But in that case, the New Methodologists are being very prescriptive indeed: they are saying that it is wrong or bad to say that any methodology is wrong or bad; but what argument, then, do they offer for their prescriptiveness? Various Old methodological schools, be they positivists, Austrians, or institutionalists, have offered various concrete arguments for their particular prescriptions: for their view that their particular methodologies are right or correct, and the others wrong. But the New Methodologists offer no argument whatsoever for their own, sweeping, hidden prescriptiveness: that all prescriptions (except their own) are necessarily bad or incorrect. In short, the New Methodologists offer no argument for their anything-goes prescription—all they have to offer is the mood of the moment, of the contemporary culture: the absurd, self-contradictory mood of our “therapeutic,” psycho-babbling, anti-“judgmentalist” culture. To state this fact is to reveal the absurd, counter-intuitive, anti-rational, fashionable mood of the New Methodologists—a mood that offers no, and is subject to no, argument, and is therefore simply not to be taken seriously.

My contentions are: that the correct Austrian paradigm is and can only be the Misesian, that is, the paradigm of Misesian praxeology; that the competing Austrian paradigms, in particular the fundamentally irrational “evolved rules,” “knowledge,” “plans,” and “spontaneous order” paradigm of Hayek and the more extreme “ultra-subjectivist” or nihilist paradigm of Lachmann, have both been fallacious and pernicious; that, as we shall see below in discussing the history of the modern Austrian revival as a movement, for various reasons the Misesian paradigm was almost totally cast aside and forgotten; but that now it is resurgent and rapidly becoming dominant and even triumphant within Austrian economics. And in the nick of time. The strong implication of Vaughn and of other anti-Misesian critics is that Misesians simply want Austrian economics to be static, to repeat endlessly Mises’s words and ideas by rote. Not so; that this is untrue may be seen in numerous creative developments and advances in Misesian economics over the past thirty years: in particular my own earlier work in monopoly theory, theory of rent,

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<sup>9</sup> For an incisive discussion of the Old and the New Methodologies, by one of the leading purveyors of the New, see Bruce J. Caldwell, “The Trend of Methodological Thinking,” *Ricerche Economiche* 43 (January/June 1989): 8—20.

welfare economics, government and the economy, and theory of property rights<sup>10</sup> and more recently by the work of Hans-Hermann Hoppe in the praxeological method, comparative economic systems, taxation, and a praxeological theory of rights; and by the work of Joseph T. Salerno in Mises vs. Hayek on reason, free exchange, and socialist calculation; and of Salerno on the work of Hutt and market coordination of prices as against the Hayekian “coordination of plans.” All this, as well as the recent work in the philosophical background of Austrian economics by Barry Smith and David Gordon, are notable and creative advances in developing, elaborating, and making more consistent and hard-edged, the original Misesian paradigm.<sup>11</sup> In addition, there are the papers delivered at this conference, as well as literally dozens of other contributions in the *Review of Austrian Economics* and elsewhere on numerous aspects of theory, method, history, and policy.

The desideratum is not to keep Austrian economics static; that can never be true of a growing and developing science. The desideratum is creative advance within the correct Misesian paradigm, as well as guarding against degeneration of the discipline into fallacy and error.

### **Misesian Praxeology versus Competing Paradigms**

It has unfortunately become habitual in summing up Austrian economics, or the Austrian paradigm, to present it as an unconnected grab-bag of separate principles, a laundry-list of various separate traits: In particular, “subjectivism”; “market process” or disequilibrium processes as against equilibrium or end-states; market coordination of plans; methodological individualism; stress on the “unintended consequences” rather than the intended consequences of human action; and writing in “literary” style or ordinary language rather than in formal mathematics. As we shall see, this emphasis on the unconnected laundry-list leads almost inevitably into gross error, for it leads to a one-sided overvaluation and therefore mis-emphasis on such particular traits as “subjectivism,” “market process,” or unintended consequences, thereby unfortunately denigrating such other crucial elements of Austrianism as objective reality and its laws, the end-state or

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<sup>10</sup> Murray N. Rothbard, *Man, Economy, and State: A Treatise on Economic Principles*, 2 vols. (1962; Los Angeles: Nash, 1970); Rothbard, *Power and Market: Government and the Economy* (1970; Kansas City: Sheed Andrews and McMeel, 1977); and Rothbard, *Toward a Reconstruction of Utility and Welfare Economics* (1956; New York: Center for Libertarian Studies, 1977).

<sup>11</sup> See, among others, Hans-Hermann Hoppe, *Praxeology and Economic Science* (Auburn, Ala.: Ludwig von Mises Institute, 1988); Hoppe, *A Theory of Socialism and Capitalism: Economics, Politics, and Ethics* (Boston: Kluwer, 1988); Hoppe, *The Economics and Ethics of Private Property* (Boston: Kluwer, 1993); Joseph T. Salerno, “Postscript: Why Socialist Economy is ‘Impossible,’” in Ludwig von Mises, *Economic Calculation in the Socialist Commonwealth* (1920; Auburn, Ala.: Ludwig von Mises Institute, 1990), pp.51—71; Salerno, “Ludwig von Mises as Social Rationalist,” *Review of Austrian Economics* 4 (1990): 26—54; Salerno, “Commentary: The Concept of Coordination in Austrian Macroeconomics,” in *Austrian Economics*, Richard Ebeling, ed. (Hillsdale, Mich.: Hillsdale College Press, 1991), pp. 325-43; Barry Smith, “Austrian Economics and Austrian Philosophy,” *Austrian Economics: Historical and Philosophical Background*, W. Grassi and Barry Smith, eds. (New York: New York University Press, 1986), pp. 1—36; and Gordon, *Philosophical Origins of Austrian Economics*.

equilibrium goals implicit in all human action, and the exercise of reason and therefore the intended consequences of such action.

If for no other reason, this disparate laundry-list of Austrian traits should be swept away with one mighty slash of Occam's Razor. For all of them can be integrated into, encompassed by, and deduced from, one central core concept: the Misesian concept of praxeology. The word praxeology means precisely what its etymology says: the logic of (human) action. All of economic theory can be deduced from the central axiom that human beings act—that they pursue means in order to arrive at ends.<sup>12</sup> One of Mises's central achievements was to realize that this was the methodology of the best economic theory before him, to be the first to systematize that methodology, and then to be the first to construct the entire edifice of economic theory in accordance with this praxeological prescription. Correct theory is based on the true and unrefutable axiom that human beings act, and proceeds by deducing the logical—and therefore true—implications from that formal fact.<sup>13</sup>

Armed with the central core of praxeology, of the implied logic of the existence of human action, let us examine each of the alleged Austrian traits as set forth by non-Misesian Austrians (Hayekians and others).

### Subjectivism

Subjectivism stems from the important point that individuals value only subjectively: that goods and resources are evaluated by individual minds, for example, by consumers, and that prices of goods and services are determined only by relative valuations of those goods by all individuals in the market. It is true, also, that Mises helped to purge economics of continuing vestiges of faulty objective value theories, from Ricardian cost and labor-pain theories preserved by Marshall, to the current pretensions to employ and even measure such invalid concepts as objective "social costs," objective "costs and benefits," and objective, measurable "transaction costs." All these concepts are illegitimate.

But, with the shunning and neglect of Mises and praxeology (shunned rather than consciously argued with or refuted), recent Austrian paradigms have allowed "subjectivism" to run riot: to extend from legitimate subjective value theory to a virtual denial of the objective existence of the real world, of the objective laws of cause and effect, and of the objective validity of deductive logic. In value theory, the non-Misesians, especially the Lachmannians, neglect or deny the objective fact that physical objects are being produced, exchanged, and evaluated, albeit that they are subjectively

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<sup>12</sup> The deduction is also aided by a few subsidiary axioms: such as the basic fact that human beings require leisure.

<sup>13</sup> For a statement of praxeology and the construction of an edifice of economic theory according to the praxeological method, see Ludwig von Mises's monumental work *Human Action* (1949, 3<sup>rd</sup> rev. ed.; Chicago: Henry Regnery, 1963). Also Rothbard, *Man, Economy, and State*.

evaluated by acting individuals.<sup>14</sup> Lachmannians and other pseudo-Austrians must be confronted with the fact that individual human beings exist, that their actions exist, and that the world of which they are a part also exists.

### Knowledge and Uncertainty

Intimately connected with the question of subjectivism is the problem of knowledge and uncertainty. Neoclassical economics has locked itself into the absurd view that everyone in the market—consumers, producers, and firms—have perfect knowledge: that demands, supplies, costs, prices, products, technologies, and markets are known fully to everyone, or to all relevant individuals. This absurd assumption can only begin to be defended on the positivist, or Friedmanite, view that it is all right to incorporate gross error into one’s assumptions so long as correct “predictions” can be made. In the praxeological view, however, quantitative predictions can never be made; in fact, it becomes necessary to guard against including error in the chain of axioms and propositions, which must be true at every step of the way. In recent years, the rational expectations theorists have compounded this absurdity even further by claiming that “the market”—as some reified all-knowing entity—has absolute knowledge not only of all present conditions, but also of all future demands, costs, products, and technologies: so that the market is omniscient about the future as well as the present.<sup>15</sup>

The Misesian praxeological view, in contrast, is that knowledge of the present, much less of the future, is never perfect, and that the world in general, and the market in particular, are eternally marked by uncertainty. On the other hand, man obtains knowledge, which one hopes increases over time, of natural laws, and of the laws of cause and effect, which enable him to discover more and better ways of mastering nature and of bringing about his goals ever more effectively. As for uncertainty, it is the task of the entrepreneur to meet that uncertainty by assuming risks, in search of profit and of avoiding loss.<sup>16</sup>

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<sup>14</sup> I find it helpful to regard the market demand-and-supply curves as interactions of a vertical line of an existing stock of things, goods, or resources, being evaluated by a falling demand curve comprised of aggregates of individual ordinal value or preference scales, marked of course by diminishing utility of each unit as the supply of a good increases. The intersection of the vertical supply (or stock) line with the falling demand curve determines the day-to-day market equilibrium price.

<sup>15</sup> More strictly, the rational expectation theorists claim that the *market* has absolute knowledge of the “probability distributions” of all future events, any errors being purely random. But this only compounds the problem since the concept of “probability distribution” can only be used for events that are homogeneous, random [path-independent], and infinitely replicable. But the events in the world of human action are almost exactly opposite: they are almost all heterogeneous, not random [path-dependent] and hardly replicable at all. Furthermore, even in the highly unlikely event that these conditions *did* apply, class probabilities could not at all be used to explain or predict events, which is what we face in human life. See Mises, *Human Action*, pp. 106–15; and Richard von Mises, *Probability, Statistics, and Truth* (1928, 2nd ed.; New York: Macmillan, 1957).

<sup>16</sup> Mises incorporated into his praxeology the useful Knightian distinction between insurable *risk* (such as lotteries, gambling on roulette), and uninsurable (because heterogeneous, not random, and not replicable) *uncertainty*, which the entrepreneur bears and for which he earns profit or suffers loss. See Mises, *Human Action*, pp. 289–94. Also see Mises’s neglected essay, “Profit and Loss,” Ludwig von Mises, *Planning for Freedom and other Essays and Addresses* (South Holland, Ill.: Libertarian Press, 1952), pp. 108–30.

Hence, to the praxeologist, Misesian Man faces the world emphatically knowing some things about his world and not knowing others. He knows absolutely that he and the world, including other people and resources, exist; he knows that natural laws and the laws of cause and effect exist; and that such knowledge cumulates over time. His technological knowledge of what goods will satisfy his wants and of how to acquire them continually increases. And yet he lives in a world of uncertainty, of uncertain future demands, resources, products, prices and costs, all problems which entrepreneurs tackle. Over time, entrepreneurs who are successful in bearing risks and forecasting their particular future will earn profits and expand their operations, while poor risk-bearers and forecasters will suffer losses and necessarily shrink their field of activity. Hence, entrepreneurs will tend to be kept on their toes and be successful in most of their forecasts.

The important point in relation to economic theory is that Misesian Man knows the body of economic laws that Misesians have built up; these laws, while absolute, are qualitative and *ceteris paribus* in their nature and cannot themselves forecast the future. Such forecasting can only be an entrepreneurial art, quantitative forecasts that can be helpfully guided though not determined by qualitative praxeological laws. These forecasts must also be guided by insight, by *Verstehen*, into present and future conditions and into the values, preferences, and changing habits of other human actors.

Suppose, for example, that Misesian Man, as forecaster, is trying to estimate how prices in general will behave in the next few years. He is armed with an absolutely true (as Mises would say, apodictic), qualitative, law of praxeological economic theory: that if the money supply increases, and people's demand for money remains the same, prices will rise. But, to forecast, he must go beyond such economic laws, and try to estimate: (a) how much, if at all, money will increase in the near future; (b) what will happen to the demand for money; and (c) what, then, will happen to general prices—considering also what is likely to happen to the supply of goods. Misesian Man knows a lot; but he does not know everything and he must try to estimate the future, given various quantitative and qualitative estimates of change. To show the absurdity of the neoclassical (monetarist subdivision) pretension of attempting to establish “scientific” quantitative laws between the money supply and prices, in estimating the course of the money supply in the near future, a person must try to figure out the psychology of, the ideas held by, and the political influence upon, the Federal Reserve Board.

But contrast to this “moderate” uncertainty of Misesian Man, the plight of Lachmannian Man, subject to Lachmann's radical uncertainty and nihilism. Professor Lachmann's favorite mantra, which he would repeat at every opportunity, and which I hold to be the key to his thought, was the following: “the past is, in principle, absolutely knowable; the future is absolutely unknowable.” Since the future, for Lachmann, is absolutely unknowable, Lachmannian Man knows no economic law, no law of cause and effect, qualitative or quantitative. In fact, he can have no *Verstehen* into patterns that are likely

to occur in the future. At every moment of succeeding time, Lachmannian Man steps into a trackless void.<sup>17</sup>

Since there are no laws of cause and effect in human action, Lachmannian Man would not be able to take the first step in figuring out what is happening, or likely to happen, with prices. Money? Prices? They can have no relation into the future, qualitative or quantitative, which means they are not causally related at all.

Once again, the Lachmannites have no real arguments in escalating from moderate to absolute uncertainty; they apparently think that repetition suffices for argument. It seems clear to me, on the contrary, that the entire Lachmannian paradigm is nonsense. Putting aside Lachmann's overweighing of the absolute unknowability of the past (Do we really know with certainty why Caesar crossed the Rubicon?), I know many things about the future with absolute certainty: I know with absolute certainty, for example, that I will never be elected president of the United States. I know, with even greater certainty, if possible, that I will never be named King of England. I submit that I am far more certain about these future events than I am of the reason that Lenin, at Finland Station, was the only Bolshevik to see that skipping several important stages could lead to a successful revolution in Russia.<sup>18</sup>

Since Lachmann denies the possibility of knowing the future at all, and therefore of any economic law, qualitative as well as quantitative, Lachmann and his followers inevitably become mere institutionalists, mere historians of the record of man's past economic activities. Mises would have called Lachmann and the Lachmannians, as he called all other institutionalists, "anti-economists," that phrase meant not merely as an epithet, but also as a deadly accurate summation of what they are about. Since the Lachmannians are opposed to even the possibility of economic theory, they must be set down as no longer economists at all. Faute de mieux, I suppose they could be called "historians" except (a) they do very little actual historical work, and (b) as Mises has made clear in his fundamental though much-neglected *Theory and History*,<sup>19</sup> to be a good historian you have to be able to use causal theories from various disciplines to help explain unique historical events, and the tools of economic law are indispensable parts of any genuine historian's armamentarium.<sup>20</sup> In a sense, Lachmannians and other institutionalists

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<sup>17</sup> When pressed, Lachmann, fortunately for Lachmannian Man, conceded that this total ignorance does *not* apply to the laws of the physical world; Lachmannian Man is fortunate that he can rely, *inter alia*, on the law of gravity. It is only laws and patterns in the human sphere that cannot exist for him.

<sup>18</sup> Lachmann's weasel-worded disclaimer, knowable "in principle," is scarcely enough to salvage his naively optimistic view of our knowledge of the past. *In principle*, how can we figure out why Lenin saw something in the Russian concatenation of events that none of the other Bolsheviks, even with very similar world-outlooks, could then see? At bottom, individual uniqueness, whether the uniqueness of the entrepreneur, the inventor, the forecaster of events or the creator, cannot be "explained" in determinist fashion.

<sup>19</sup> See Ludwig von Mises, *Theory and History* (1957; Auburn, Ala.: Ludwig von Mises Institute, 1985).

<sup>20</sup> Ludwig M. Lachmann had been a student of Hayek at the London School of Economics in the 1930s and his writings were generally Misesian until the mid-1970s, when he became converted to the nihilism of his old friend and fellow-Hayek student, the Englishman G.L.S. Shackle. Thus, see Lachmann's appreciative review of Mises's *Human Action*, "The Science of Human Action," *Economica* 18 (November 1951): 412—27. Lachmann's outstanding achievement was his Misesian *Capital and its Structure* (London:

function as professional anti-economists and “meta-historians,” expending their energies denouncing economics and urging other economists to act as historians.<sup>21</sup>

### Knowledge and the Role of the Entrepreneur

If Lachmannian Man knows nothing, his brother Hayekian Man (the third major paradigm within modern Austrian economics), is better off, but not by very much. Hayek is obsessed by Man’s allegedly pervasive and systemic ignorance. Indeed, Hayek’s virtually lone argument against government intervention and against socialism is that government planners can know nothing. Since reason can play little or no role in man’s affairs, government, or man through government, does not even know enough to establish general legal or constitutional rules for society. These general rules can only emerge from the blind, unconscious forces of “evolution”—the evolved rules that the later, post-Misesian Hayek, (in Hutchison’s felicitous term, Hayek II as compared to the Misesian Hayek I) wishes us to worship and follow blindly lest we perish.<sup>22</sup> For Hayekian Man, however, there is a way out: even though he knows virtually nothing, he can painfully learn through the processes of the free market, just as in law or constitutions, he can learn to accept the “evolved” rules. In contrast, Misesian Man can not only know and learn, he can do so by exercising his unique human power of reason; and reason—the body of praxeologically-deduced economic theory—can and does tell him that the market economy works extremely well, while government planning and socialism cannot work at all. Misesian Man knows the virtues of the free market and the devastating flaws of socialism by using his reason. In the case of general rules, Misesian Man would think it absurd to accept all rules simply because they are there, without also correcting them by use of his reason.

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London School of Economics, 1956) which, presumably for that reason, is never cited by modern Lachmannians. The watershed date for announcing his conversion to Shackleinism was Ludwig M. Lachmann, “From Mises to Shackle: An Essay on Austrian Economics and the Kaleidic Society.” *Journal of Economic Literature* 14 (March 1976): 54—62.

<sup>21</sup> An amusing but instructive event occurred on the occasion of the conference of American Austrians at Windsor Castle in the summer of 1976. Under the good offices of Professor Stephen C. Littlechild of the University of Birmingham, a kind of summit conference was arranged so that some of the American Misesians could meet the English Subjectivist School, as the Shackleians call themselves. The eminent Subjectivists at the meeting included the *doyen* of that school, Shackle himself, as well as Terence W. Hutchison, Jack Wiseman, and Brian Loasby. At one point, the Subjectivists were lamenting that they could not offer a program of graduate economics courses as alternatives to the neoclassical paradigm, since all they had produced were a few critical essays but no substantial body of economic theory. I replied in some surprise that there was indeed a great deal of systematic Austrian literature available, including works by Mises, the early Hayek, and my own work, in addition to volumes of Bohm-Bawerk and Frank A. Fetter, among others. The blank looks of incomprehension on the faces of the distinguished Subjectivists were a revelation of the enormous extent of the inherent gulf between Shackleian Subjectivists and Misesians.

<sup>22</sup> Since there can be nothing in social life corresponding to the biological gene, the use of the term “evolution” by Hayek and others to describe historical change simply serves to drape the mantle of pseudo-science upon such change and to smuggle in an unacknowledged and unsupported value-judgment (supported only by the alleged benevolence and necessity of the “evolutionary” process) to sanctify such rules.

The respective attitudes toward human knowledge and human capacity help account for the enormous differences in the various paradigms on the crucial role of the entrepreneur in the market. For Neoclassical Man, there is no need for an entrepreneur, since all men know everything about the market, its past and its future, perfectly; and all curves are tangent, and all things at rest, in the Never-Never Land of long-run general equilibrium. Austrians, in contrast, place great stress on the dynamic role of the entrepreneur, but their visions of that role are very different.

Hayekian Man, the Hayekian entrepreneur, starts by knowing nothing, but he painfully learns about the world and the market through the “signals” of the price system. Hayek, and Professor Israel Kirzner after him, habitually speak of the market, of competition on the market, as a “discovery process.” In contrast to Lachmann, who thinks there can be no knowledge of the world out there to learn, Hayek-Kirzner see a world of knowledge out there, with the unconscious forces of the market supplying man with that knowledge, through market price and profit-and-loss signals. The Hayek—Kirzner entrepreneur, indeed, is strangely passive; he scarcely acts like an entrepreneur at all. He risks nothing, and he really knows nothing, except what the signals of the price-system teach him, as he and the market economy wend their way toward general equilibrium. In his elaboration of the Hayekian theme, Kirzner sees the only function of the entrepreneur, and his only necessary quality, to exercise “alertness”: to catch the market signals earlier than the next guy. In Kirzner’s favorite metaphor, a \$10 bill lies on the ground. Many people do not see that bill; but the entrepreneur is more alert than his fellows, and so he is the first to see, and to snatch that bill. Superior alertness, alertness to the truth out there, accounts for entrepreneurial profits.

There are many problems with the Kirznerian schema. If superior alertness accounts for entrepreneurial profits, what in the Kirznerian world can account for entrepreneurial losses? The answer is nothing. And yet the crucial aspect of entrepreneurship is that stressed by Mises: that the entrepreneur takes risks, that he can make profits by risking resources and through superior forecasting of the future, while suffering losses from inferior forecasting. Yet, there are neither risks nor uncertainty of the future in the Kirznerian world. Kirznerian Man faces not the future but the present; he owns no capital resources and so he risks no losses; he simply sees present truth before others and alertly possesses it.

In the Misesian world, in contrast, the entrepreneur is not passive but extremely active.<sup>23</sup> He takes risks, and attempts to forecast the future; he grapples with uncertainty. The most important Misesian entrepreneurs, the driving force of the economy, are the capitalist-

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<sup>23</sup> For a critique of Kirznerian alertness, see Murray N. Rothbard, “The End of Socialism and the Calculation Debate Revisited,” *Review of Austrian Economics* 5, no. 2 (1991): 67; [reprinted here as Volume I, Chapter 21]. Also see Rothbard, “Professor Hébert on Entrepreneurship,” *Journal of Libertarian Studies* 7 (Fall 1985): 281—85; [reprinted here as Volume II, Chapter 14, and a title change]. The latter article was a comment on a paper by Professor Robert Hébert, both written for a tricentennial conference on Cantillon in August 1980. Hébert’s discussion on Kirzner’s view of entrepreneurship is in Robert F. Hébert, “Was Richard Cantillon an Austrian Economist?,” *ibid.*, pp. 272—75. For a further comment on Kirzner and on my paper, see Robert F. Hébert and Arthur N. Link, *The Entrepreneur Mainstream Views and Radical Critiques* (New York: Praeger, 1982), pp. 95-99.

entrepreneurs, those who own or partially own capital resources and risk them in projects hoping for future returns. And, in the area of knowledge, as professor Salerno has perceptively pointed out, Misesian Man knows a lot about his part of the market—not just prices, but all the qualitative knowledge that must also go into production and into risky ventures: the sort of customers he will have, the sort of products they will want, where to buy raw materials and how to transform them, and so on—that is, all the particular knowledge that Hayek has talked about in other contexts. The free price-system is vital to the entrepreneur but it is not, as in Hayek-Kirzner, his only source of knowledge.<sup>24</sup>

The Misesian entrepreneur, then, is not a passive, if alert, recipient of “knowledge” provided by the price system. He is a knowledgeable, active, risking, forecasting, man using the price system as an indispensable guide to enable him to calculate his costs, and to estimate his future revenues and profits.

As for Lachmannian Man, the entrepreneur may exist, but he loses all significance. In contrast to the Hayek-Kirznerian man, he cannot learn from market signals because he cannot know anything anyway, even through price signals. Lachmannian Man is totally bereft of knowledge, and his Man in the market economy is scarcely better off than, or knows more than, the Lachmannian socialist planner.<sup>25</sup>

### Market Process and Equilibrium

While the neoclassicist believes, or affects to believe, that the market economy is always in a state of general long-run equilibrium, Austrian economics, from Menger on, indeed from Cantillon on, has concentrated not on equilibrium but on the process by which the market moves toward it. The real world, the day-to-day world of markets, is one where the market is always moving toward equilibrium but never attaining it, since the determinants of market activity: values, resources, technologies, knowledge, products, and so on, are always changing. The Austrians, therefore, concentrate on market processes rather than on the final equilibrium state.

But in contrast to Mises, the Lachmannians, in particular, have thrown out final equilibrium altogether. They regard the entire concept as meaningless. Instead, they virtually use the phrase “market process” as a shibboleth, thereby throwing out not only

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<sup>24</sup> See below, the section on Knowledge and Socialist Calculation.

<sup>25</sup> Alexander Gray’s hilarious and perceptive strictures on Ricardo’s argument against government intervention apply *a fortiori* to the free-market Lachmannians:

Such is the Ricardian scheme of distribution; in place of the old harmony of interest, he has placed dissension and antagonism at the heart of things.... Gone is the large-hearted optimism of Adam Smith, transmuted into a pessimism that will not be comforted. Yet Ricardo remains immovably non-interventionist. . . . In a world of Ricardian gloom one might ask why there should not be interference. An optimist carolling that God’s in His Heaven and that all is right with enlightened self-interest has a right to nail the *laissez-faire* flag to the mast, but a pessimist who merely looks forward to bad days and worse times ought not in principle to be opposed to intervention, unless his pessimism is so thorough-going as to lead to the conviction that, bad as all diseases are, all remedies for all diseases are even worse. (Alexander Gray, *The Development of Economic Doctrine* [1931; London: Longman, 1980], pp. 171—72.)

equilibrium, but the baby of economic theory itself along with the neoclassical bathwater. It is impossible to engage in economic theorizing without employing what Mises called “imaginary constructions” or “thought experiments” (Gedankenexperimenten) which function as the praxeologist’s unique substitute for the laboratory experiments of the physical sciences. In the laboratory, the scientist holds all other variables constant, while he examines the effect of changing one variable upon another. Since human beings cannot be “held constant,” the praxeologist does so in “thought experiments,” by means of the famed *ceteris paribus* clause. It is through such reasoning that the economic theorist concludes, for example, that an increase in the supply of money, the demand for money being held constant, will be bound to lower the value (purchasing power) of the monetary unit. In short, the economic theorist postulates an equilibrium, then mentally changes one variable, say the supply of money, keeps all other relevant variables constant, and examines the effect on prices in general. Refusing to employ equilibrium concepts is necessarily destructive of all economic theory or economic law. *Ceteris paribus* constructions can and do embody reality and economic truth even if the specific constructions are not “realistic” in the sense that they are not happening at that particular moment in time. These theories and laws are realistic because they are deduced from the fundamental and absolutely true axiom of human action, that people continually act by employing means to try to achieve goals. The laws of monetary theory, for example, that an increase in the supply of money, given the demand for money, will lead to a fall in the value of the monetary unit, are eternally and “apodictically” true, regardless of time and place, provided, of course, that money is being used in the economy. Even if there were no money in the world today, or, more specifically, no monetary inflation, the law or construction in question would still be true, only presently not applicable. It is the task of the economic historian or forecaster to apply the theory of monetary inflation to any economy where such inflation may exist.<sup>26</sup>

Mises put it this way:

The specific method of economics is the method of imaginary constructions. . . . An imaginary construction is a conceptual image of a sequence of events logically evolved from the elements of action employed in its formation. It is a product of deduction, ultimately derived from the fundamental category of action, the act of preferring and setting aside. . . . Their function is to serve man in a scrutiny which cannot rely upon his senses. . . . The main formula for designing imaginary constructions is to abstract from the operation of some conditions present in actual action. Then we are in a position to grasp the hypothetical consequences of the absence of these conditions and to conceive the effects of their existence. Thus we

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<sup>26</sup> In his sympathetic discussion of praxeology, Patrick J. O’Sullivan asserts that Mises, as an *a priori*ist, believed that since the fundamental axiom of action is *a priori* to experience, that the deduced laws are simply true, whereas Hayek and Robbins, believing that the axioms are empirically derived, believed that the laws had to be consciously *applied* to empirical states of affairs where the conditions hold. But the need for applicability is maintained by Mises as well as the others, and that need is not related to the philosophic status of the fundamental axioms. Thus, while the basic laws of human action can only be applied to those empirical worlds where *human beings exist*, more narrowly deduced laws, such as the laws of monetary theory, can only be applied to *those empirical societies where money is in use*. See Patrick J. O’Sullivan. in *Ricerche Economiche* 43 (January/June, 1989).

conceive the category of action by constructing the image of a state in which there is no action [final equilibrium], either because the individual is fully contented and does not feel any uneasiness or because he does not know any procedure from which improvement in his well-being [state of satisfaction] could be expected.<sup>27</sup>

Furthermore, by tossing out equilibrium concepts altogether, and in concentrating only on “market processes,” Lachmannians and other non-Misesian Austrians fail to realize that they thereby give up any chance of understanding those “processes” themselves. For these “processes” are really human actions which, unlike the mere motions of stones or atoms, are necessarily purposive and goal-oriented. Therefore, every action on the market must already imply the goal, or end-state, of that action.<sup>28</sup> The action, or “process,” already implies the equilibrium state, even if that state is never fully reached. Once again, a crucial difference is the abandonment, by non-Misesians, of the Misesian concept of action—action that is necessarily goal or end-state directed, and that is purposive, active, and risktaking. Instead of “equilibrium,” these Lachmannians speak of “processes,” which connote impersonal motions and mechanisms rather than the conscious choices of persons engaging in goal-directed activity.<sup>29,30</sup> We have seen, in contrast, that equilibrium constructions are indispensable for all *ceteris paribus* economic thinking, for analyzing actions, and for demonstrating the direction in which the economy is necessarily tending. As Mises indicated in the above quote, final equilibrium is also necessary for analyzing the emergence of profit-and-loss in an uncertain world; for such positive or negative returns would not exist in a world of certainty and changeless final equilibrium. The final equilibrium construct also enables the economist to distinguish short-run entrepreneurial profit-and-loss from returns brought about by time-preference, embodied in the “natural” rate of interest, returns which would still continue to exist in a world of certainty and equilibrium.

Meanwhile, in contrast to the Lachmannians, the Hayekians have preserved the concept of equilibrium, and the view that entrepreneurs are always moving the economy in an equilibrating direction. But the Hayekians, who include Kirzner, are waging the battle on

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<sup>27</sup> Mises, *Human Action*, pp. 236—37.

<sup>28</sup> Professor Hans-Hermann Hoppe illuminated this point in his lecture on monetary theory at the Ludwig von Mises Institute conference on the Federal Reserve at Jekyll Island, in May 1992.

<sup>29</sup> The use of “market process” as a mantra was demonstrated by Professor Don Lavoie, a former Misesian who became a Lachmannian and even a “hermeneutician,” based on the fashionable Continental philosophy of Heidegger and his student Gadamer. Lavoie established a Center for the Study of Market Processes (CSMP) at George Mason University, and in 1983 the Center established a periodical, *Market Process*. Ludwig Lachmann’s major work as a Lachmannian was his volume, *The Market as an Economic Process* (Oxford: Basil Blackwell, 1986). Later, Lavoie organized a Society for Interpretative Economics, which managed to hold one meeting before it folded. It should come as no surprise that Professor Lachmann gave the keynote address at that meeting.

Professor Vaughn concluded her 1990 article on the Austrian revival by hailing the Lavoiean market process approach as the wave of the Austrian future, a view possibly reflecting her position as a board member of the Center. Unfortunately for her prediction, the CSMR minus Professor Vaughn, has now transformed itself into a very different center dedicated to a certain kind of managerial scheme unrelated to economics, let alone to Austrianism or its concerns. Vaughn, “Mengerian Roots,” pp. 403-4.

<sup>30</sup> Kirzner, too, has succumbed, naming his latest collection of essays, *The Meaning of Market Process* (New York: Routledge, 1992).

empiricist rather than praxeological grounds. In other words, the Hayekians claim that the entrepreneurs, in the process of learning from market signals, are in fact moving the economy toward equilibrium. The Lachmannians, of course, claim that entrepreneurs can learn nothing, and that therefore the economy is either moving away from equilibrium, or else in no particular direction. The battle between the two, therefore, is over empirical estimates over rates of speed: the Hayekians claiming that entrepreneurs are learning at a faster pace from the price signals than data are changing, thereby moving the economy toward equilibrium. The Lachmannians, on the other hand, claim that data are changing faster than people can learn (assuming they can learn at all), and that therefore the economy, in fact, is moving away from equilibrium. The dispute is a mere empirical one over rates of speed of change: a dispute which, in the nature of things, can never be resolved. For the Misesian, on the other hand, the entire dispute is misconceived. The logic of the situation demonstrates that man always acts by using reason to improve his lot; so that his action is always “rational,” that is, his actions are always beneficial, always necessarily equilibrating *ex ante*. And the market mechanism is also such that forecasts tend, in general, to pan out as true, so that *ex ante* decisions become validated *ex post*. But choice, and action, are always *ex ante*, and *ex ante* action on the market is always equilibrating. And *ex ante* considerations are what count in analyzing and explaining human action.<sup>31</sup>

#### Coordination: of Plans or Prices?

Wrapped up in its faulty conception of equilibrium is the Hayekian shibboleth about the alleged market function of “coordination of plans.” The concept is not to be discovered in Mises, and for good reason. In the first place, in final equilibrium, in the evenly rotating economy toward which the economy tends but never reaches because of continually changing data, there is no change in the endless round and so no change is expected. All subject “plans” are therefore brought into equilibrium, or coordinated, by definition, in final equilibrium. But while Hayekians and Lachmannians quarrel about whether or not people learn from experience and whether the market is equilibrating and coordinating, the entire controversy is misconceived. For while in non-existing final equilibrium plans are coordinated by definition, why should we expect that outside of equilibrium plans, which are necessarily variable and subjective, will ever be “coordinated,” or brought into equality? In fact, we can say that, given basic data—values, resources, technology—there is far less reason to think that plans will be coordinated than that the market tends toward equilibrium.

Suppose, for example, that we can say that the capital value of a certain firm, in final equilibrium, will be \$100 million, based on future returns and the rate of interest, and that therefore, given 1 million shares of outstanding stock of the firm, the “equilibrium” stock price is \$100. But even if the data are given or frozen, and we can say that the stock price is tending toward \$100, there is no reason to assume that, short of the actual final equilibrium state, that all market participants’ plans will be “coordinated” to understand

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<sup>31</sup> For an exposition of action on the market as always equilibrating out of the very nature and logic of action, and for a critique of the empiricists on this issue, see George A. Selgin, *Praxeology and Understanding: An Analysis of the Controversy in Austrian Economics* (Auburn, Ala.: Ludwig von Mises Institute, 1990).

that the equilibrium price is going to be \$100. Until the end, there can and will be individuals with varying expectations, bulls and bears, and share price volatility until the final state of rest is reached. In short, while all action is equilibrating by its nature, and the market tends to equilibrium if data are frozen, subjective plans will never be “coordinated” until final equilibrium arrives. And since that final state of rest, given the nature of man and of the world, can never come to pass, the entire concept of “coordination of plans” should be tossed out as unhelpful, misleading, and false.

But does this mean that the market never “coordinates,” that we may never speak of coordination on the market? On the contrary, as Professor Salerno has recently shown, coordination occurs effectively, and every day, through the entire price system. Professor Salerno has performed the signal service of reviving William H. Hutt’s theory of price coordination and demonstrating that this Huttian concept is essentially the Misesian view.<sup>32</sup> Not in the Never-Never Land of final equilibrium, but every day in markets, in day-to-day equilibrium, the price system coordinates prices, including wage rates and the prices of other productive factors, so that there is never any shortage or unsold surplus. From day-to-day, then, there may, for various reasons, be misallocations of resources, but never shortages and surpluses, so long as prices are free to move.

Suppose, for example, a typical misallocation of agricultural resources takes place during a war. A country gets into war, supplies of agriculture from other areas are cut off, and there is a great increase in demand for the country’s agriculture. Food and farm prices rise and farm production expands. Then, when the war is over, the agricultural expansion is seen to be excessive for peacetime, and food and farm prices and wage rates fall. Even though there is now “too much” food and too many resources in agriculture to be sustained in peacetime, if prices are free to fall, there is no unsold surplus, either in produce or in labor employment. Even though wartime demand has caused too many resources to move into agriculture, the free price system continues to coordinate—to make sure that there are, nonetheless, no shortages or surpluses in the agricultural sector. In the longer run, of course, the losses in agriculture and the especially low wage rates there, will induce resources to move out of agriculture and into other areas, so that prices and wages will move toward equilibrium in all areas. But at each stage of the process, the price system coordinates successfully.<sup>33</sup>

### Knowledge and Socialist Calculation

It is now universally acknowledged that Ludwig von Mises, allegedly the loser in the famous socialist calculation debate that he launched in 1920, was really right: clearly, socialism cannot calculate, it cannot run a complex modern economic system. But it has only recently become clear, through the insights of Professor Salerno, precisely why Mises was right, and also how the Misesian message was systematically distorted, from

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<sup>32</sup> Salerno, “Commentary: Concept of Coordination,” pp. 325—45.

<sup>33</sup> For a brilliant discussion of price and wage consideration, and the contrast with Keynesian assumptions, see William H. Hutt, *The Keynesian Episode: A Reassessment* (Indianapolis, Ind.: Liberty Press, 1979), pp. 135—77, esp. 137-40, 150 ff. Also see the earlier W.H. Hutt, *Keynesianism—Retrospect and Prospect* (Chicago: Henry Regnery, 1963), pp. 53—81, esp. 54ff.

the 1930s until recent years, by F.A. Hayek and his followers. For Hayek and the Hayekians, obsessed with the alleged “problem of knowledge,” have systematically misinterpreted Mises as maintaining solely that the Socialist Planning Board, facing the uncertainty of a dynamic economy, lacks the knowledge enabling it to plan the production and allocate the resources of a socialist economy. In contrast, the market economy, through its price signals, conveys that needed knowledge from and to the various participants in the market economy.

Mises, while not disputing the importance of knowledge and its dissemination through the price system, was, however, arguing a totally different point. From 1920 on, he reasoned as follows: assume the best for the Social Planning Board. Assume that, by some magical process, it has been able to discover and know absolutely all the value-scales of consumers, all technological methods, and compile an inventory of all resources. Suppose, then, Mises says, we grant total knowledge of all these data to the Socialist Planning Board. It still will not be able to calculate, still will not be able to figure out costs and prices, particularly of land and capital goods, and therefore will not be able to allocate resources rationally. The real problem of the Planning Board, then, the major thing denied that Board by absence of a market, is not knowledge but economic calculation.<sup>34</sup>

Thus, to Hayek, if the Planning Board could by some magic know, as people come to know through the market, consumer values, technologies, and resources, it could rationally plan and allocate resources fully as well as the market. As usual for Hayek and the Hayekians, the argument for the free market and against statism rests only on an argument from ignorance. But to Mises, the problem for the Planning Board is not knowledge but calculability. As Salerno puts it, the knowledge conveyed by present (or “immediate past”) prices rests on values, techniques, and resources of the immediate past. But what acting man is interested in, especially the entrepreneur in committing resources into production and future sale, is future prices and future costs. The entrepreneur, who commits present resources, does so because he appraises—anticipates and estimates future prices—and allocates resources accordingly. It is, then, the appraising entrepreneur, driven by his quest for profits and for avoidance of losses, who can calculate and appraise because a genuine price system exists in the means of production, in land and capital goods, that is, a system of exchanges of privately-owned capital resources. Only such a pricing system allows for calculation.

Salerno points out that for Mises, knowledge and appraisal on the market are complementary, and have very different natures and functions. Knowledge is an individual process, by which each individual entrepreneur learns as much as he can about the largely qualitative nature of the market he faces, the values, products, techniques, demands, configurations of the market, and so on. This process necessarily goes on only in the minds of each individual. On the other hand, the prices provided by the market, especially the prices of means of production, are a social process, available to all

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<sup>34</sup> For a survey and discussion of the arguments in the socialist calculation debate, see Murray N. Rothbard, “The End of Socialism and the Calculation Debate Revisited,” *Review of Austrian Economics* 5, no. 2(1991): 51—76 [reprinted here as Volume I, Chapter 21].

participants, by which the entrepreneur is able to appraise and estimate future costs and prices. In the market economy, qualitative knowledge can be transmuted, by the free price system, into rational economic calculation of quantitative prices and costs, thus enabling entrepreneurial action on the market. As Salerno notes: “competition therefore acquires the characteristic of a quintessentially social process, not because its operation presupposes knowledge discovery [as with Hayek-Kirzner], which is inescapably an individual function, but because, in the absence of competitively determined money prices for the factors of production, possession of literally all the knowledge in the world would not enable an individual to allocate productive resources, economically within the social division of labor.”<sup>35</sup>

In short, the entire Hayekian emphasis on ignorance and “knowledge” is misplaced and misconceived. The purpose of human action is not to “know” but to employ means to achieve goals. As Salerno perceptively summarizes Mises’s position:

The price system is not—and praxeologically cannot be—a mechanism for economizing and communicating the knowledge relevant to production plans [the Hayekian position]. The realized prices of history are an accessory of appraisal, the mental operation in which the faculty of understanding is used to assess the quantitative structure of price relationships which corresponds to an anticipated constellation of economic data. Nor are anticipated future prices tools of knowledge; they are instruments of economic calculation. And economic calculation is not the means of acquiring knowledge, but the very prerequisite of rational action within the setting of the social division of labor. It provides individuals, whatever their endowment of knowledge, the indispensable tool for attaining a mental grasp and comparison of the means and ends of social action.<sup>36</sup>

Mises’s own avowal of the roots of his inquiry into the socialist problem has, until recently, been overlooked in the story of the social calculation debate. It has generally been assumed, understandably, that Mises’s 1920 article arose solely out of curiosity about the arrival of socialism with the advent of the Bolshevik Revolution.

Actually, the main impetus for the study, as Mises has revealed, was the work he did on his monumental *Theory of Money and Credit* (1912). In the process of accomplishing the feat of integrating the theory of money into general marginal utility theory (deducing macro from micro, as it would now be put), Mises realized that, contrary to the earlier Austrians, the market does not impute values directly from consumer preferences to productive factors. Value-scales or preferences, Mises realized, were purely ordinal, a matter of choosing or setting aside; whereas market money prices were quantitative and

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<sup>35</sup> Joseph T. Salerno, “Postscript: Why a Socialist Economy is ‘Impossible,’” in Ludwig von Mises, *Economic Calculation in a Socialist Commonwealth* (Auburn, Ala: Ludwig von Mises Institute, 1990), pp. 60—61. Also see *ibid.*, pp. 51—71.

<sup>36</sup> Joseph T. Salerno, “Ludwig von Mises as Social Rationalist,” *Review of Austrian Economics* 4(1990): 44. Also see *ibid.*, pp. 26—54. These two profound and subtle articles by Salerno are indispensable to the entire Mises vs. Hayek discussion.

cardinal. Only money prices can be imputed and not values directly. It was in ruminating on the ways and means that the market turns the qualitative into the quantitative that Mises arrived at his insight into the reasons that calculation under socialism would be “impossible.”<sup>37</sup>

Until the recent rehabilitation and new explanation of Mises’s position on socialist calculation by Professor Salerno, Mises’s viewpoint had been systematically obscured by modern Austrians as well as by non-Austrians in the debate. Thus, Professor Karen Vaughn, in a Hayekian summary of the calculation debate in the early 1980s, does not even mention Mises’s profound contributions in *Human Action*. In an earlier paper, Vaughn did even more: she actually sneered that “Mises’s so-called final refutation in *Human Action* is mostly polemic and glosses over the real problems.”<sup>38</sup>

Professor Israel Kirzner, on the other hand, takes a diametrically opposite view: that the greatness of the Mises position in *Human Action* is that it joins Hayek in taking a “dynamic” view of the socialist problem, as against the “static” view in Mises’s classic 1920 article. In reality, Mises’s position was equally “dynamic” or “static” throughout; he simply elaborated his older position in *Human Action*. Actually, as Salerno points out, the “later” Mises, in *Human Action* explicitly denies that the key to the calculation problem under socialism is that “all human action points to the future and the future is always uncertain.” This is the Hayek-Kirzner way of conceiving the problem, since, outside of static equilibrium and in a dynamic, changing world, knowledge of the future is always uncertain. But no, says Mises, socialism suffers from

quite a different problem. . . We do not deal with the problem of whether or not the [socialist] director will be able to anticipate future conditions. What we have in mind is that the director cannot calculate from the point of view of his own present value judgments and his own present anticipation of future conditions, whatever they may be. If he invests today in the canning industry, it may happen that a change in consumers’ tastes . . . will one day turn his investment into a

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<sup>37</sup> Mises says in his memoirs: “They [the socialists] failed to see the very first challenge: How can economic action that always consists of preferring and selling aside, that is, of making unequal valuations, be transformed into equal valuations, by the use of equations? Thus the advocates of socialism came up with the absurd recommendation of substituting equations of mathematical catallactics, depicting an image from which human action is eliminated, for the monetary calculation in the market economy.” Ludwig von Mises, *Notes and Recollections* (Spring Mills, Penn.: Libertarian Press, 1978), p. 112. Also see the discussion in Murray N. Rothbard, *Scholar, Creator, Hero* (Auburn, Ala.: Ludwig von Mises Institute, 1988), pp. 35—38, and especially, Rothbard, “The End of Socialism and the Calculation Debate Revisited,” pp. 64—65. Also see Mises, *Human Action*, pp.327—30, p.696; Salerno, “Mises as Social Rationalist,” pp. 39-40, and Salerno, “Why a Socialist Economy is ‘Impossible,’” pp. 60-61. Dr. David Gordon has pointed out to me that, just as Mises showed, by his regression theorem, that money can only arise on the market out of a non-monetary good under barter, so money on the market is needed to transform ordinarily ranked subjective values into money prices which are indispensable for imputations of productivity and for economic calculation by entrepreneurs.

<sup>38</sup> Karen Vaughn, “Critical Discussion of the Four Papers,” in *The Economics of Ludwig von Mises*, Laurence Moss, ed. (Kansas City.: Sheed and Ward, 1976), p. 107. Her Hayekian summary is in her introduction to the reprint of the Misesian Trygve J.B. Hoff, *Economic Calculation in the Socialist Society* (1949; Indianapolis, Ind.: Liberty Press, 1981). See Karen Vaughn, “Introduction,” *ibid.*, pp. ix—xxxvii. By her 1990 article, Vaughn had clearly veered “leftward” into the Lachmannian camp. Also see Rothbard, “The End of Socialism and the Socialist Calculation Debate Revisited,” p. 57n.

malinvestment. But how can he find out today how to build and equip a cannery most economically?

Some railroad lines constructed at the turn of the century would not have been built if the people had at that time anticipated the impending advance of motoring and aviation. But those who at the time built railroads knew which of the various possible alternatives for the realization of their plans they had to choose from the point of view of their appraisements and anticipations and of the market prices of their day in which the valuations of the consumers were reflected. It is precisely this insight that the [socialist] director will lack. He will be like a sailor on the high seas unfamiliar with the methods of navigation.<sup>39</sup>

### Reason: Exchange, Intention, and Design

At the core of the constellation of crucial differences between the Misesian and Hayekian paradigms is their respective attitudes toward human reason. Man, affirms Mises after Aristotle, is the uniquely rational animal; reason is man's unique and essential instrument to find out what his needs and preferences are, and to discover and employ the means to achieve them. Mises's stress on action, on acting man, therefore necessarily stresses the vital importance of human reason. Misesian Man acts, and therefore consciously selects goals, and decides how to pursue them.

Hayek's entire work, on the contrary, is devoted to a denigration of human reason. As David Gordon has pointed out, Hayek virtually assumes that human beings act unconsciously—of course, a contradiction in terms—and therefore that they neither know nor think nor choose. Therefore, their actions do not require understanding; hence Hayek's emphasis that the best that can be done is rely on a blind and unconscious adherence to evolved rules.<sup>40</sup>

Thus, Mises's view of why men participate in the basic form of market interaction—exchange, which also implies participating in the social division of labor. Harking back to the insight of the Scholastics, beginning at least with the great fourteenth-century French philosopher and scientist John Buridan, Mises saw that a man participates in an exchange because he sees that he will benefit more from the good or service received, than the good or service he has to give up. Here is the root of the basic subjective-utility, or Austrian, insight: men engage in exchange because and only because they subjectively prefer what they will receive in exchange to what they give up. Hence, also, Mises's conclusion on how to preserve and maintain the great oecumene, the mighty network, or system, of voluntary, mutually beneficial exchanges that constitute the free-market economy: The mass of the public must learn, must be educated to understand, the vast

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<sup>39</sup> Mises, *Human Action*. p. 700. Also see Rothbard, "The End of Socialism and the Socialist Calculation Debate Revisited," pp. 67—68; and Israel M. Kirzner, "The Economic Calculation Debate: Lessons for Austrians," *Review of Austrian Economics* 2(1988): 1—18. Kirzner's error seems to be tied to his non-Misesian view of the entrepreneur: not as an appraiser of prices and costs, but as someone who is alert to uncertain knowledge of the future.

<sup>40</sup> See in particular, David Gordon, "The Origins of Language: A Review," *Review of Austrian Economics* 2(1989): 245—51.

importance of maintaining and preserving that free market from aggression and coercive interference. They must understand that on preserving and expanding that market network, or oecumene, depends the flourishing and prosperity of the human race: whereas interference with that network can only lead to world-wide misery and impoverishment.<sup>41</sup> It is not, of course, that Mises believes that men will always listen to reason, or follow its dictates; it is simply that, insofar as men act at all, they are capable of following reason, and that pursuing such a course is literally the last best hope for mankind.

One of the remarkable features of Hayek's character was his deviousness in expressing any disagreement with his old friend and mentor. Thus, it was only five years after Mises's death, on the occasion of writing a Foreword to the new edition of Mises's *Socialism*, that Hayek was able to express his harsh disagreement with Mises's rationalist view of why men exchange. Mises had written that he "regards all social cooperation [exchange] as an emanation of rationally recognized utility, in which all power is based on public opinion." But now, in his Foreword written after Mises's death, Hayek writes: "I had always felt a little uneasy about that statement of basic philosophy, but only now can I articulate why I was uncomfortable with it." Hayek then adds patronizingly: "The extreme rationalism of this passage, which as a child of his time he could not escape from, and which he perhaps never fully abandoned, now seems to me factually mistaken. It certainly was not rational insight into its general benefits that led to the spreading of the market economy."<sup>42</sup>

But the point of Mises's "extreme" passage is this: for each particular exchange, each individual only participates in it because he acts consciously, and his reason tells him that he will be better off from making this exchange than from not making it. He will benefit from what he receives compared to what he gives up, and he will do better than from any other alternative exchange. All that this reasoning implies is conscious action. As for the free market economy in general, Mises's theory of government reflects the keen insight of David Hume: that no government, however powerful or coercive, can, in the long run, rule by force alone; that since force, in the long run, lies with the majority of the ruled rather than with the minority of the ruling elite, to maintain their rule the ruling elite must persuade the majority to give it their support. In other words, in the long run, ideas held by the people rule, for good or for ill. Ideas trump brute force. Far from being unrealistic

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<sup>41</sup> On Mises on the indispensable role of reason in exchange, and the contrast with Hayek, see the illuminating article by Salerno, "Ludwig von Mises as Social Rationalist," pp. 26—54.

<sup>42</sup> Ludwig von Mises, *Socialism*, p. 418; EA. Hayek, "Foreword," *ibid.* p. xxiii. Also see Peter G. Klein, "Introduction," *The Fortunes of Liberalism: The Collected Works of FA. Hayek* (Chicago: University of Chicago Press, 1992), 4, pp. 12—13; Hayek, *ibid.*, p. 142.

Hayek's deviousness while Mises was alive may be seen in his 1937 article, "Economics and Knowledge," which marked his turn from a Misesian to a Popperian methodology (that of his old Viennese friend Karl Popper); apparently, the article was meant as an oblique attack on Mises for his allegedly Walrasian-neoclassical approach, and meant as a way to subtly shift Mises to an empiricist, Popperian approach. So oblique was the article, however, that Mises himself misinterpreted it as a Misesian attack on the neoclassicals, and current historians and scholars of the Austrian school are split on what Hayek's article really meant. It is interesting to note that what Hayek *really meant* about very many things is virtually a cottage industry for doctoral students, whereas it is rare that people have to puzzle over what Mises "really meant" See Klein, "Introduction," pp. 10-41.

“extreme rationalism,” the remarkable internal collapse of Communist rule in the Soviet Union and Eastern Europe has borne dramatic testimony to the truth of Mises’s position.<sup>43</sup>

In the passage in which he deprecates Mises’s position, however, Hayek comes up with no counter-argument of his own. If “rational” ideas—in the sense of consciously-held rather than necessarily correct ideas—do not account for the adoption of a market economy, as well as the swing away from it in the twentieth century, what in the world does? Hayek hints that man “chooses” the market economy “only in the sense that he has learned to prefer something that already operated.” Again, Hayek stresses blind habit or custom. Clearly habit plays a role, but if that were all, what accounts for the twentieth-century shift away from the market economy, and, finally, for the internal collapse of the Communist politico-economic system? Hayek’s emphasis on unconscious habit or rule-following thus leaves out critical parts of the answer: such as (a) how do these rules or institutions get adopted in the first place; and (b) how do they ever change, often suddenly? To fall back, as Hayek does, on “evolution” as the sole answer to the first question not only misapplies the very concept of evolution, which requires the existence of genes and mutations; it also fails spectacularly to account for sudden changes in those rules or in society’s acceptance of them. Most glaringly, Hayek’s implicit assumption of human unconsciousness violates the basic fact which we all know from our own experience as axiomatic: that human beings are indeed conscious, and that they therefore act and choose rather than move or “are moved” in an unconscious, robotic, or unmotivated manner.<sup>44</sup>

Hayek presents three crucial concepts as ways of highlighting his reliance on human blindness and irrationality: “spontaneous order”; the “unintended consequences of human action”; and the product of “human action, but not human design.”

We need not tarry on the phrase “spontaneous order,” except to note that the word “spontaneous,” once again, connotes lack of thought, activity that is not consciously

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<sup>43</sup> There has been general agreement that Mises’s claim of the “impossibility” of socialism has been vindicated, with panels at annual economics meetings devoted to the theme of “Mises was Right.” See among others, Stephen Boehm, “The Austrian Tradition: Schumpeter and Mises,” in *Neoclassical Economic Theory, 1870 to 1930*, K. Hennings and W. Samuels, eds. (Boston: Kluwer Academic Publishers, 1990), p.231. There has been no recognition, however, of the Communist collapse vindicating Mises’s position on the long-run dominance of the ideas of the public in government.

<sup>44</sup> How to reconcile Hayek’s dominant “anti-rationalist” position with another strain in his thought: the power of ideas in the long-run to effect social change, and his call for a “trickle-down” strategy of converting top scholars and philosophers to classical liberal views, who will in turn eventually convert lesser professors, who will in turn convert general intellectuals, journalists, and “dealers in second-hand ideas?” See, in particular, Hayek’s “The Intellectuals and Socialism,” first published in the *University of Chicago Law Review* 16 (Spring 1949), and reprinted in Hayek, *Studies in Philosophy, Politics, and Economics* (Chicago: University of Chicago Press, 1967), pp. 178—94.

There are, it seems, three possible ways to explain this anomaly. First, that it is characteristic of Hayek’s intellectual inconsistency and muddle. Second, that it still reflects the more rationalist Hayek I, since it was written in the 1940s, and before the development of his “evolutionary” position. And third, that Hayek sees the only role of ideas as a minority intellectual elite being able to rise above the general torpor and unconsciousness—but that the very best the elite can do is to urge everyone, including themselves, to follow evolved rules blindly.

chosen, but rather purely reflexive and tropistic. It would have been far more accurate to use a term such as “voluntary,” which would at least focus on voluntarily chosen, rather than coerced, actions.

The latter two concepts, of course, are simply variants of each other. All actions have consequences; and Hayek is anxious to emphasize, at every turn, the alleged importance of the unintended rather than intended consequences, thus showing the trivial importance of conscious human action. Humans may act in some sense, but their conscious actions are unimportant, since they do not bring about desired, “designed,” or intended effects. Mises’s analysis, on the contrary, rests squarely upon the Aristotelian insight into action, in which they are shown to be intentional, thinking and action always being guided toward an object. People act all the time, in a large number of respects; we assume that, most, or almost all of the time, people’s actions bring about their intended results. If they did not, the people would not continue to repeat them. Hayek’s own emphasis on habit or custom, indeed, proves the Aristotle—Mises rationalist point: for the habitual repetition means that these actions have repeatedly been successful in bringing about a person’s goals. Thus, if someone lives in Long Island, and every morning takes a train to Penn Station, and then a bus to his job, reversing the process in the evening, his success in grasping cause-and-effect relations and in bringing about his intended consequences leads him to keep repeating these activities.

Furthermore, since all human actions are goal-directed, are intentional, if we do not absolutely know whether or not a person intended the consequences of his actions, we have to presume that he did, unless it can be demonstrated otherwise. Obviously, if a business investor or speculator has suffered losses, these losses were not intended, but apart from such cases the presumption must stay with intention.<sup>45</sup>

Perhaps the best case for stress on unintended consequences comes from analyzing the motive of exchange on the free market and was best expressed in the famous quote from *The Wealth of Nations*: “It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages.”<sup>46</sup>

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<sup>45</sup> Owing to the income tax code, the losses may well have been intended, in order to reduce one’s level of taxable income. But in that case, detailed investigation into the facts would overturn the common-sense presumption that losses would not be intended from the start.

<sup>46</sup> Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, Campbell and A. Skinner, eds. (Indianapolis, Ind.: Liberty Classics. 1981), 1, pp. 26—27. It should be noted that Smith was anti-rationalist as well, if for rather different reasons. Smith was concerned to purge economic theory of all subjective utility considerations, so he had to discard mutual benefit as the reason for exchange. Indeed, in contrast to Mises’s insight that the division of labor (the base of exchange) stems from the diversity and inequality of talents and interests among men, Smith maintained that all people and children are originally almost totally the same, and that the existing division of labor and of occupation willy-nilly pushes them into specialization and differences of interest. As Smith puts it: “the very different genius which appears to distinguish men of different professions . . . is not. . . so much the cause, as the effect of the division of labor.”

If for Smith, the diversity and inequality of talent is not the root cause of the division of labor but the effect, what in the world *is* the root cause? Smith, like many social scientists who do not know the cause of a

To translate this passage into our current concerns: the butcher and the baker's actions result in the intended consequences of yielding them a profit, but, more importantly for society, they result in the unintended consequences of benefiting consumers, indeed society as a whole, in the most efficient possible manner.

This is surely an important and valid point, so far as it goes. But, we might wonder: why the rush to celebrate unintended consequences? Wouldn't it have been better if these pro-consumer or pro-general standard of living consequences had been understood and intended by the actors as well? To put it another way: the butcher, baker, and so on desire and intend the consequences of their production yielding them a satisfying profit. But suppose that they are informed, by economists and others, that their actions also have the effect of helping the rest of society and the general standard of living? Wouldn't they then come to intend this general welfare as well, even conceding that their own self-interest would still be their primary goal? Wouldn't they be likely, at the very least, to feel better and happier about their own activities, knowing now that they benefit the body of consumers as well as themselves? How could such knowledge hurt?

It might be countered that the butcher and baker might well feel better; but apart from that, knowledge of the unintended consequences would have no effect upon their concrete actions on the market. But, on the contrary, knowledge that they are helping the general welfare might well affect their operations rather strongly. Consider the following case: a brilliant entrepreneur is engaged in productive activities. But he has absorbed the general cultural position that by maximizing his profits he is in some way injuring his fellow man. As a result, to assuage his conscience, he deliberately takes actions that will lower his profits—not eliminate them altogether, but lower them from what he considers to be an “extreme” or even “unconscionable” height.

The entrepreneur then reads Mises or some other hard-core free-market economist or journalist. He learns, to his amazement and relief, that the greater the amount of his profits the more he is helping consumers, society as a whole, and his fellow man. Happily, he casts off the guilt that had been plaguing him and changes his actions to engage in a happy and welfare-enhancing maximization of profits.

This is surely not an outlandish case, and it shows why it is better to shed light, to replace ignorance by knowledge, and thereby to show the entrepreneur all the foreseeable consequences of his actions. His actions will now be adjusted to the fact that all their consequences are conscious and intentional. Not only is there nothing wrong with this process, but the life of the entrepreneur and of society will both be improved. Hayek to the contrary notwithstanding, knowledge remains better than ignorance.<sup>47</sup>

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human phenomenon, falls back on some sort of built-in “instinct”: or, as he put it. “a certain propensity in human nature” which has no regard for utility, but is instead, “a propensity to truck, barter, and exchange one thing for another,” *Ibid.*, pp. 25, 28. Or, as Smith rather absurdly put it: “without disposition to truck, barter, and exchange, every man must have procured to himself every necessary and convenience of life which he wanted,” *ibid.*, p. 29.

<sup>47</sup>There is another point: for any particular butcher or baker, the outside observer—the outside economist or social scientist—does not really *know* if he has been enlightened by Misesian or other free-market writers,

And finally, there is another vitally important point, which ties back into the argument about how an exchange economy, the free market economy, must be established and sustained. For spreading knowledge of the happy though currently unintended consequences of their actions may not only alter the actions of unintended consequences; they might imbue the mass of the public, regardless of their occupation, with an appreciation of the enormous benefits of the free-market lattice-work throughout society, and of the horrendous consequences of government interference in that web of the free-market economy. To educate in order to make currently unintentional consequences intentional may well be the only possible route to the salvation of mankind. Truth, understanding, reason, is surely the way to save the free market, not urging blind submission to rules that might not even be appropriate to a market economy.

Another grave problem with the Hayekian doctrine is that the spontaneous order design concept not only exalts blind rules and unconscious action in the market economy; it lets the State off the hook as well. For this emphasis means that not only market actions with beneficent consequences but also State actions with evil consequences are equally unconscious. This means that State acts, instead of being the result of conscious lobbying and the seeking of subsidy and special privilege, simply grew “spontaneously,” like Topsy. No one is to blame for State actions: no motives, no goals, no lobbying, no self-seeking exploitation of taxpayers or competitors. Just as John R. Seeley, in his apologetics for the British empire, claimed it did not expand consciously but only “in a fit of absence of mind,” so the Hayekian mindset, applied to State action, removes guilt or even understanding from analysis of the historical process.

Letting evil off the hook was indeed the origin of Hayek’s cherished unintended consequences, or human action-not-human design concept. Hayek points out that Adam Ferguson, sociologist and old friend and colleague of Adam Smith in the eighteenth century Scottish Enlightenment, coined the concept “the result of a human action, but not the execution of any human design.”<sup>48</sup> What Hayek does not tell us, however, is that Ferguson did not originally employ the concept to analyze the market, or language, or any similar social process. As a young Presbyterian minister, Ferguson, along with his friend, the Reverend Alexander Carlyle, was reeling from the shock of the near-triumph of the Catholic Jacobite Rising of 1745, in which the Jacobites conquered Scotland, and were finally defeated by the Hanoverian troops in northern England. Ferguson and the others were confronted with this grave theological problem: how could God permit the evil Catholics to come so near to triumph? They concluded that while the Catholics, of course, were consciously evil, pursuing evil goals, they were unconsciously being used by God for his own good purposes: namely, to shake the Presbyterian Church of Scotland—God’s Church—out of its lethargy, and to renew its devotion to its true

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or not. The observer may have his suspicions, but suspicions are not knowledge. Ironically, for Hayek or Hayekians to assume without evidence that all butchers, bakers, and so on are ignorant of free-market theory is to arrogantly claim knowledge that they do not, in fact ultimately cannot, have. Perhaps it is the Hayekians, not the Misesians, who suffer from *hubris*.

<sup>48</sup> F.A. Hayek, “The Results of Human Action but not of Human Design,” in *Studies in Philosophy, Politics, and Economics*, p. 96.

purposes. In short, all events in human history, even if seemingly motivated by evil, are all unconsciously working toward good. Out of apparent evil, good: that is God's Providential plan. This truly dangerous doctrine leads straight, of course, to the Whig Theory of History: that whatever is, is right; and that which was, was right. Everything in history moves toward the good, is progressive; there can be no evil or wrong turn in history.<sup>49</sup>

In short: Hayek returns, with a burst, to the Whig theory of history and to a conservatism that justifies all institutions as “evolved,” as part of some presumably beneficent pattern, even though God has now dropped out of the picture. Not only Hayek was influenced deeply by Ferguson; so too was a young graduate philosophy student at the University of Tubingen, G.W.F. Hegel, and his colleagues. Hegel systematized the Ferguson insight into his “dialectic,” by which history, through its “cunning of reason,” moves inexorably according to its divine plan: always bringing good, and a higher stage, out of apparent evil and conflict. Karl Marx, as a Left Hegelian, was to atheize that dialectic. Hayek is in odd, and not particularly wise, company.<sup>5051</sup>

In his incisive contrast of Mises's “social rationalism” with Hayek's irrationalist emphasis on “spontaneous order,” Professor Salerno trenchantly points out that in the Misesian view, man cannot rely on spontaneous “unintended” consequences for successful social change. On the contrary, if men fail to understand rationally the destructive consequences of State intervention, that is, they fail to understand the beneficence of the free market economy, they are likely to wreck the oecumene, destroy capitalism, and return the economy to poverty and barbarism. The division of labor and human prosperity, then, necessarily rest on adoption by the public of the ideology of laissez-faire. If they adopt interventionism, on the other hand, the resulting “social maladjustment, which is inspired by fallacious ideology, carries in its wake the possibility of social disintegration and is more likely the greater the degree to which the consequences of human actions are unintended, or to use Mises's term, “unwitting.” Salerno continues, following Mises, that “to the extent that social norms, policies, and institutions are ‘undesigned,’ are not completely and correctly thought out in advance and accounted for in a logically consistent ideology, to that extent does the continued existence of society become problematic.” But then, “if social disintegration may occur ‘spontaneously,’ due to an ignorance of the remoter consequences of social action, social progress can only be assured by the widespread adoption of an ideology of social life which consciously and correctly accounts for these consequences. This ideology is [laissez-faire] liberalism.”<sup>52</sup>

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<sup>49</sup> See the illuminating work by Richard B. Sher, *Church and University in the Scottish Enlightenment* (Princeton, N.J.: Princeton University Press, 1985), pp. 40—44.

<sup>50</sup> On Hegel and Marx, see Murray N. Rothbard, “Karl Marx: Communist as Religious Eschatologist,” *Review of Austrian Economics* 4(1990): 132—38.

<sup>51</sup> Hayek's praise of the common law as spontaneous and undesigned overlooks the fact that individual judges were consciously discovering, elaborating and applying fundamental legal principles. Reason and design were therefore dominant in common law. The fact that this reason and these laws were not imposed by a sovereign State but elaborated out of long-held legal principles is not relevant to Hayek's claim.

<sup>52</sup> Joseph T. Salerno, “Ludwig von Mises as Social Rationalist,” *Review of Austrian Economics* 4 (1990): 50—51.

Ignorant and “spontaneous” action, then, is far more likely to be like a child’s or a savage’s destruction of fine china than providing a beneficent and flourishing market economy. Directly contrasting Mises and Hayek, Salerno concludes that the rationalist [Misesian] view of social evolution, therefore, is not one of placid and automatic improvement insured by “unintended” consequences, “undesigned” institutions, “tacit” knowledge and “natural selection” of rules of conduct. Social rationalism implies, instead, that human history is the outcome of a conflict between ideologies, which are consciously formulated and adopted by reasoning human beings. Whether an epoch is characterized by social progress, social retrogression, or even social disintegration depends upon which particular ideologies have become current and which individuals have attained ideological “might” defined by as “the power to influence other people’s choices and conduct.”<sup>53</sup>

It would seem that the most plausible case for Hayek’s spontaneous, anti-rational anti-design theory of social life is the advent and development of language. Surely, language, at least, grew like Topsy, and was not rationally created? But, in an instructive essay, David Gordon has shown that recent research has plausibly resurrected the eighteenth-century Enlightenment view of Condillac, as well as of Thomas Reid and Lord Monboddo, that language was consciously created, out of gesture, and, Gordon adds, that gesture was reinforced by play. Gordon also points out that the Enlightenment view was driven out of circulation by the German Romantics, led by Johann Christian Herder, who were concerned to establish their bizarre view that German is the “highest” language by maintaining that it could only have emerged from the ineffable, unconscious, and noble German soul.<sup>54</sup>

Salerno also adds the important point taken from Mises that even language contains an important ideological, and hence conscious, component. Salerno quotes from Mises’s *Theory and History* that language is “the precipitate of a people’s ideological controversies, of their ideas concerning issues of pure knowledge and religion, legal institutions, political organizations, and economic activities. . . In learning their meaning

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<sup>53</sup> Ibid., p. 52.

<sup>54</sup> David Gordon, “The Origins of Language: A Review,” pp. 245—51. Gordon particularly discusses two recent works: G.A. Wells, *The Origins of Language* (Peru, Ill.: OpenCourt, 1987), and J.N. Hattiangadi, *How is Language Possible?* (Peru, Ill.: Open Court, 1987). Also see Hans Aarsleff, *From Locke to Saussure* (Minneapolis: University of Minnesota Press, 1982), for a critical view of the German Romantics on language.

<sup>55</sup> In addition, the Erlangen school of philosophy has emphasized the origin of mathematics and physics in the conscious apprehension of, for example, length, or numbers, in real world objects. See Paul Lorenzen, *Constructive Philosophy* (Amherst: University of Massachusetts Press, 1987). Similar to the language question is the odd view that folk poetry or music was not consciously created by individuals, but grew unconsciously out of the wisdom of the folk. See H.L. Mencken, “Folk-Literature, a Review of Louise Pound, *Poetic Origins and the Ballad*,” in *A Mencken Chrestomathy* (New York: Alfred A. Knopf, 1949), pp. 471—72. Writes Mencken: “German folksong, the loveliest in the world used to be credited to a mysterious native talent in the German yokelry, but scientific investigation reveals that some of the songs regarded as especially characteristic of the folk-soul were actually written by the director of music at the University of Tubingen, Professor Dr. Friedrich Silcher,” *ibid.*, p. 472. Also see Ludwig von Mises. *Theory and History*, pp. 188—89.

the rising generation are initiated into the mental environment in which they have to live and to work. This meaning of the various words is in continual flux in response to changes in ideas and conditions.” Some entire languages, notably modern Gaelic and secular Hebrew, were even deliberate creations and recreations out of ideological will and determination.<sup>56</sup>

It is instructive to contrast the twists and turns of error and fallacy in Hayek’s concept of unintended consequences, including its paean to ignorant and unconscious action, with Mises’s superficially similar but very different stress on remote or unseen consequences of human action. For, rather than Hayek’s relying on spontaneity, or glorifying unconscious action and its unintended consequences, Mises was urgently concerned to have everyone grasp and understand the remote and unseen consequences of their actions, a grasp which they can only attain by means of reason, in this case by praxeological reasoning.

Thus, the Misesian economist Henry Hazlitt, in his best selling *Economics in One Lesson*, makes the centerpiece of his book Frédéric Bastiat’s “broken window fallacy.”<sup>57</sup> A nasty kid hurls a rock and breaks a window. The immediate common-sense reaction is for the onlookers to deplore the action of the kid, and lament the fact that the storekeeper will now have to pay a considerable amount of money to repair the window. But then comes the proto-Keynesian, the Broken Window Fallacy-monger, the second-level sophisticate sneering at the common herd. “No, no, you don’t understand,” he proclaims: “that kid’s action is really good for the economy, because the storekeeper will now spend money on the glazier to repair the window, providing employment for the glazier’s workers, and stimulating the economy. The common-sense view, as usual, is wrong.” But then the economist, the Mises—Hazlitt—Bastiat economist, comes on the scene and rebuts the Broken Window Fallacy-monger. “No, this fool sees only the money that the storekeeper spends on the glazier. But what he does not see is far more important: the money the storekeeper would have spent, had he not suffered loss to his property, either on consumer goods, or on expanding his business. That unseen stimulus is lost. So: the storekeeper is worse off because of the kid’s action, and the economy and society suffer.” Common-sense is vindicated by the third-level farseeing economist. As in so many areas of political economy, we see an alliance on behalf of truth of the common-sense member of the public with the genuine economist, uniting against the sophistries of the second-level pseudo-intellectual and pseudo-economist.

### **Non-Misesian Macroeconomics: Genuine Money or Counterfeiting?**

Professor Erich Streissler, in his discussion of the contributions of Menger and his students, stressed correctly that these were largely in microeconomics. But then he added that Menger “bequeathed to his school a peculiar horror of macroeconomic concepts.” Commenting on Streissler’s paper, Professor Robert Hébert properly took Streissler to task, pointing in particular to Ludwig von Mises as the creator of a peculiarly Austrian form of macroeconomics, building macro concepts upon individualist micro foundations.

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<sup>56</sup> *Ibid.*, pp. 227—32; Salerno, “Mises as Social Rationalist,” p. 53.

<sup>57</sup> Henry Hazlitt, *Economics in One Lesson* (New York: Harper and Bros., 1946).

In particular, Mises integrated monetary theory, and the theory of the value of money, into micro marginal utility, as well as supply and demand theory.<sup>58</sup> Hébert might have added that Mises then built upon that monetary theory in forging his masterful theory of the business cycle. In his early years Hayek (or Hayek I), elaborated upon Mises's cycle theory, in work which later won him the Nobel.<sup>59</sup> Surely, there are no fields that would now be considered more "macro" than monetary and business cycle theory.<sup>60</sup> And yet, Hayek II spent very little time in this area, and the Hayekians and Lachmannians none at all. Kirzner spends all of his time on micro and devotes none to the macro area. The same is true of all of the Lachmann followers, who have not so much bothered to refute the Misesian monetary or business cycle theory as they have ceased to refer to or deal with it. The only Austrians who have dealt with money or business cycle theory, indeed, have been Misesians: among them, in the 1920s and 1930s, Hayek I, Fritz Machlup, Gottfried Haberler, and Lionel Robbins, and, in the years since World War II, Hazlitt, Salerno, Hoppe, Walter Block, and the present writer. The "honor" of macro-economic concepts, in fact, applies only to the various non-Misesians, who have no macro theory of any kind.<sup>61</sup>

There is one unfortunate exception to this rule. In 1976, after Hayek succumbed to hubris upon winning the Nobel Prize, he opened the Pandora's Box of money-crankism by offering a bizarre scheme for private competing currencies.<sup>62</sup> The only common point with his master Mises's view of money was narrowly political: both were opposed to Central Bank control of the money supply. But, apart from that, Hayek violated the rule for valid monetary theory that he himself had adumbrated as Hayek I: that it must, like Mises's theory, be deduced from, and therefore integrated with, a sound general micro theory.<sup>63</sup> Instead, Hayek's doctrine was totally cut off from general economic theory and from Mises's monetary theory as well.

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<sup>58</sup> Erich Streissler, "Menger, Bohm-Bawerk, and Wieser: the Origins of the Austrian School," in *Neoclassical Economic Theory, 1870 to 1930*, K. Hennings and W. Samuels, eds. (Boston: Kluwer Academic Publishers, 1990), p. 170; Robert E Hébert, "Commentary." *ibid.*, pp. 190—200.

<sup>59</sup> In particular, F.A. Hayek, *Monetary Theory and the Trade Cycle* (1933; New York: Augustus M. Kelley, 1966). a translation of a book published in Vienna in 1929; and *Prices and Production* (London: Routledge and Kegan Paul, 1935).

<sup>60</sup> A case could easily be made that Bohm-Bawerk's superb capital-structure theory was "macro" as well as "micro."

<sup>61</sup> In his unpublished comment on my article on "Austrian Definitions of the Supply of Money" at the Windsor Castle Austrian conference in September 1976, indeed, Israel Kirzner took the nihilist line that it was impossible to define the supply of money, since it was an aggregative concept. It is, on the contrary, a happy aggregate of homogeneous units, whether of dollars or gold ounces. Murray N. Rothbard, "Austrian Definitions of the Supply of Money;" in *New Directions in Austrian Economics*, Louis Spadaro, ed. (Kansas City: Sheed Andrews and McMeel, 1978), pp. 143—56; [reprinted here as Volume I. Chapter 16].

<sup>62</sup> FA Hayek, *Denationalization of Money—the Argument Refined* (1976. 3<sup>rd</sup> ed.; London: Institute of Economic Affairs, 1990).

<sup>63</sup> Thus, Hayek I wrote: For "Trade cycle theory. . . as for any other theory, there are only two criteria of correctness. Firstly, it must be deduced with unexceptionable logic from the fundamental notions of the theoretical system; and secondly, it must explain by a purely deductive method those phenomena with all their peculiarities which we observe in the actual cycles." F.A. Hayek, *Monetary Theory and the Trade Cycle*, pp. 32—33.

Hayek's scheme of private individuals or banks issuing their own currencies—a scheme which he himself, in more sober moments, would have dismissed as absurdly “constructivist”—was not so much adopted as coming to serve as inspiration or jumping-off point for other money-crank schemes, which have proliferated ever since. They range from private currencies to schemes for private banks freely inflating credit on top of gold currency reserves. As these proposals have multiplied, however, gold has inevitably dropped out or been pushed out of the picture. Later plans range from banks inflating notes or deposits on top of Federal Reserve Notes even after the Fed has been abolished; gold being a mere shadow helping to prop up the system; and finally schemes where banks clear each others' notes indefinitely with no possibility of the poor public's being able to redeem its way out of bank money. Finally, standard or “high powered” money disappears altogether, and inflationary banks merely redeem their notes and deposits in the equally phony notes and deposits of other inflating banks.”<sup>64</sup><sup>65</sup>

Money-crankism is a common phenomenon of the last two centuries and, as every professor of money and banking who has received lengthy and passionate letters written in crayon on the subject can attest, it always involves schemes for radical expansion of the supply of money. The proposed monetary inflation can either be governmental, or, if proposed by the libertarian-inclined, it can be private. Economically, it makes no real difference, except that empowering every private person to print as much money as possible would bring hyper-inflationary disaster even more quickly.

The first grave fallacy and departure from Misesian doctrine, committed by many of these schemes, not least by Hayek's, is to ignore the fundamental Regression Theorem, which Mises built as a logical law upon Carl Menger's historical insight. To function as a money, an entity must have emerged on the free market out of barter, as a particularly marketable commodity selected on the market as a medium for virtually all exchanges.<sup>66</sup> Nothing can be originally adopted as money by government fiat, or by some sort of social contract; it must originate as a strictly market phenomenon. Nothing can be adopted as a

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<sup>64</sup> Among the culprits are Lawrence White, George Selgin, Kevin Dowd, David Glasner, F. Capie, Leland Yeager, Robert Greenfield, and Richard Timberlake. Even Milton Friedman has lately defended bimetalism, thereby implicitly repudiating the correct monetarist analysis of that system. For critiques of some of these offerings, see Murray N. Rothbard, “The Myth of Free Banking in Scotland,” *Review of Austrian Economics* 2 (1988): 229—45 [reprinted here as Volume II, Chapter 21]; Rothbard, “The Case for a Genuine Gold Dollar,” in *The Gold Standard: Perspectives in the Austrian School*, Llewellyn H. Rockwell, Jr., ed. (1985; Auburn, Ala.: Ludwig von Mises Institute, 1992), pp. 1—17 [reprinted here as Volume I, Chapter 18]; and Rothbard, “Aurophobia: or, Free Banking on What Standard?,” *Review of Austrian Economics* 6, no. 1 (1992): 97—108.

<sup>65</sup> This would be a “libertarian” version of the condition that Professor Paul Cantor, in his stimulating paper, points out: “That is what it meant to have a currency backed by gold—a paper/banknote was redeemable in terms of a real commodity, namely gold, something that had independent value. But in the modern era of fiat money, a banknote just represents another banknote. One dollar bill can merely be exchanged for another dollar bill, but such a transaction has no point anymore, once no real commodity backs the currency. In the modern paper money system, money does not represent anything outside itself; money only represents itself.” Paul A. Cantor, “Hyperinflation and Hyperreality: Thomas Mann in Light of Austrian Economics,” *Review of Austrian Economics* 7, no. 1 (1994): 3—29. Retired banker John Exter likes to refer to fiat money instruments as “IOU nothings.”

<sup>66</sup> For a welcome appreciation of Mises's achievement, see Robert F. Hébert, “Commentary,” pp. 191—95.

money, as a medium of exchange, unless it had a pre-existing purchasing-power as a non-monetary good. Even if Hayek were allowed to issue his proposed private tickets called ducats redeemable in nothing but other ducats—which I think he should legally be allowed to do—no one would accept it as money. It would only have a severely limited value as a curiosity, yet another monument to man's folly. All of the new currency plans, private or public, commit the same grave fallacy.

The other group of plans—which build private banking schemes upon existing currencies—at least do not violate the Regression Theorem. Instead, they take one step further than the State has done in recent centuries: build on pre-existing gold money by eventually converting paper tickets once redeemable in gold into fiat standards of their own. Unfortunately, as the Regression Theorem makes clear, once a paper ticket has won market acceptance by piggy-backing on gold as a redeemable ticket, the government can use its coercive powers to keep the paper in play indefinitely as irredeemable fiat money. The second group of pseudo-Austrian plans propose to construct inflationary private banking schemes on top of existing fiat paper, eventually even getting rid of standard paper money altogether.

Apart from the Regression Theorem, both sets of schemes would institute disaster on a large scale. There are two sets of fallacies committed by all of these proposals. Building on the insights of the Ricardians and the Currency school, as well as on continental monetary theory since the Scholastics, Mises demonstrated that, given the existence of money in the economy, every supply of money is optimal. In short, even though the value, or purchasing power, of money is, like all other goods or services, determined by its supply and demand, there is one crucial difference between money and all other goods. All other goods and services, whether consumer or producer goods or resources, help to alleviate natural scarcity; therefore, other things being equal, any increase in these goods is a net social benefit, easing natural scarcity. But that is not true for money, since the only function of money is to facilitate exchange, to furnish a general medium of exchange and hence a unit of economic calculation. But money performs such a function optimally and fully, regardless of the supply available. An increase in the quantity of money cannot alleviate scarcity and cannot provide a social benefit: it could only dilute the purchasing power of each money unit. An increase in supply can only dilute the exchange effectiveness of each dollar or franc or whatever is the monetary unit.

Any scheme for inflating the money supply, whether private or public, can only redistribute income and wealth, cripple or destroy the unit of calculation indispensable to a modern economy, weaken incentives to save, and generally cripple and eventually destroy the economic system.<sup>67</sup> The eventual end is hyperinflation and economic disaster.

The second basic problem is politico-economic. Any free-market economy must necessarily rest on devotion to the sanctity of private property. It is obvious that rampant

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<sup>67</sup> If money consists of a precious metal, say gold, then while an increase in the supply of gold has no beneficial monetary effect in society, it does confer a benefit by decreasing the scarcity of gold for non-monetary uses, such as jewelry or dentistry.

theft or fraud can only gravely cripple property rights and the free, prosperous economy that emerges from them. For a free society to survive and flourish, property rights must be defended. Most of this defense must occur by incorporation of the supreme value of property rights into the value systems of the broad mass of the public. That can only be accomplished and sustained when the opinion and value molding groups and institutions in society: notably, intellectuals, academics, media, and churches—sustain and promote that value system. When they systematically fail to do so, as we have seen all too clearly in this century, we are all in deep trouble. The frontline of defense against what should generally be a minority of violators of property are the specific institutions of law, police, and courts. Regardless of how these institutions are set up and financed, their defense or protection function is extremely important.

Libertarians, in their zeal for privatizing government functions, tend to forget one vital truth: that some functions of government, such as the Internal Revenue Service or providing concentration camps for dissenters, deserve to be abolished rather than privatized. To put it another way: we must not forget that government is not the only organization that can and does commit crimes. Private persons and organizations, and not only governments, can and do commit robbery, assault, kidnapping, and murder. We must not forget that not every private action deserves our uncritical blessing. The relevance of this seemingly evident truth is that among the crimes private persons commit are fraud, embezzlement, and many forms of theft. One of those forms is forgery, or counterfeiting, in which theft is committed by the forger or counterfeiter who corrupts the marketplace by passing off a fake as the real thing.

Counterfeiting of art despoils the buyers and owners of the art, as well as the painter or his estate, and the owners of the genuine article. But counterfeiting of money wreaks more general havoc. In a society where gold is the only form of money, a person can acquire gold in only three ways: (a) selling a good or service in exchange for a part of the existing gold stock; (b) receiving gold as a charitable gift or bequest; and (c) mining new gold out of the ground. All of these are productive ways of obtaining gold, whether it be through exchange, new gold production, or someone receiving a gift or inheritance granted by another person. But counterfeiting, for example, dressing a base metal to look like gold, despoils not only the particular seller but the entire market economy. The counterfeiter, so long as his crime is not detected, is able to extract unearned income and wealth from producers without their knowledge, to exploit the producers for his benefit, and to lower the purchasing power of the gold unit to everyone in society. But at least there is hope, when counterfeiting is illegal, that it will be discovered and rooted out and the culprits apprehended and stopped.

But when government or its creature, the Central Bank, becomes the legalized counterfeiter, the counterfeit is not only fully detected but bailed by public opinion, often guided and molded by the counterfeiters themselves, as wise economic statesmanship. Then, there is no way to guard the guardians, and the counterfeiter is turned loose to prey on society and inflate at will. The result will be a process of continuing and even accelerating monetary and therefore price inflation.

Such is roughly the course of modern monetary history, particularly in the twentieth century—a history of statism and volatile rates of debasement of the currency unit by the legalized counterfeiters. The result is a veritable and increasingly chaotic Age of Inflation. What is desperately needed is to abolish the counterfeiting. That was the proposal stemming from Mises’s insight into the inevitably destructive effects of paper money and fractional reserve banking. Instead, what our pseudo-Austrian economists propose to do is not to abolish counterfeiting, but to privatize it—to open up the counterfeiting process to “free” private competition.

One of Mises’s favorite quotes on money and banking was from Thomas Tooke: “free trade in banking is tantamount to free trade in swindling.” Tooke and Mises, of course, were referring to fractional reserve banking, in which banks pledge to redeem on demand receipts to non-existent money in their vaults. These bank notes or deposits are just as much counterfeit as warehouse receipts to nonexistent grain, fake receipts that look like genuine warehouse receipts to grain, which were loaned out by grain elevators until recent decades—until, that is, the practice of fractional-reserve issues of receipts in grain, was outlawed and cracked down on.

The champions of free competition in counterfeiting retort that this is simply the market at work, that the market registers a “demand” for more expanded credit, and that the private bankers, these Kirznerian entrepreneurs, are simply “alert” to such market demands. Well, of course, there is always a “demand” for fraud, and embezzlement, on the “market,” and there will always be plenty of “alert” swindlers who are eager and willing to furnish a supply of these items. But if we define the “market” not simply as a supply of desired goods and services, but as a supply of such goods within a framework of inviolate property rights, then we see a very different picture. To paraphrase William Graham Sumner, when A supplies B with a good or service, that is a genuine and unexceptionable market transaction. A is supplying what B demands. But when A and B put their heads together to swindle C, D, and E, that is a horse of a very different color, and surely not a market transaction in the same voluntary sense.

Following a perceptive suggestion of Dr. David Gordon, let us examine a slightly different kind of fractional reserve banking. Instead of issuing deposits or notes which function like counterfeit warehouse receipts to cash, let us assume that these banks actually print dollar bills made up to look like the genuine article, replete with forged signatures by the Treasurer of the United States. The banks print these bills and lend them out at interest. If they are then criticized for what everyone would concede to be forgery and counterfeiting, why cannot these banks reply as follows: “Well, look, we have genuine, non-counterfeit cash reserves of 10 percent in our vaults. As long as people are willing to trust us, and accept these bills as equivalent to genuine cash, what is wrong with that? We are only engaged in a market transaction, no more no less so than any other fractional reserve banking.” And what indeed is wrong about the statement that cannot be applied to any case of fractional reserve banking? If counterfeiting per se is deplorable and to be outlawed, then the same standards must be applied to its surrogate, fractional reserve banking, which is currently legal and which would run rampant in the “free-banking” heaven of our non-Misesian pseudo-Austrians. Conversely, these free-bankers

must then be willing to accept the legality of every person and every bank issuing outright forgeries or counterfeits and simply printing paper dollar bills, which would not be illegal if some “reserve” or other in genuine bills were actually maintained. And if the free bankers must be willing to accept outright “free” counterfeiting of dollar bills, then they also must be willing to endorse its immediate consequences in wildly runaway inflation.

Monetary policy is evidently a strange field, for it is an area where no one, from the writers of crayoned letters on up to F.A. Hayek, seems to be afraid to engage in flights of Utopian fancy, or what Hayek would ordinarily deride as “constructivism.” So I might as well do the same, with the important difference that my proposal lies within the strict bounds of property rights, genuine market commodity money, and Misesian monetary theory.

Ludwig von Mises saw that, once various marketable commodities are chosen on the market to be media of exchange and then to be general media of exchange termed “money,” there is an inexorable market tendency for one commodity money to win out in each society. In every society where they were available, gold and silver soon became the only commodities that survived as moneys, with the relatively more abundant silver used as coins for smaller transactions and the relatively rare gold coins for larger transactions. In each society and country, gold and silver coins circulated at various units of weight determined by the market; generally, the unit of account, the unit used to calculate business accounts, profits or assets, as well as people’s incomes, was the weight of gold or of silver, as denominated in the language of each country. As countries proliferated and discovered each other, the gold and silver coins of the various countries tended to exchange according to their precious metal content, for example, if the U.S. dollar was defined as 1/20 of a gold ounce, and the French franc at 1/100 of a gold ounce, then the “exchange rate” of dollars to francs would naturally be at the ratio of their respective weights: five francs to one dollar. Gold and silver ratios, on the other hand, would tend to be set on the market at the current ratio of the purchasing powers of gold and silver, as determined by the supplies of and demands for the two metals.

Over the centuries, however, governments have interfered with, and crippled, the natural process toward international metallic money. Governments seized the command post of the economy by nationalizing the coin minting function and then facilitated their own debasement of standards of weights of coin by shifting emphasis from the unit of gold or silver weight to tale, or the name itself. By shifting the monetary unit from, say, the dollar as 1/20 of a gold ounce to the dollar itself, the government could repeatedly debase, or lighten, the gold weights of the currency unit. The English “pound sterling,” as its name indicates, used to be worth, indeed used to be defined as, one pound weight of silver; it has now been debased to approximately one half an ounce of silver. Almost as destructive, and facilitating the processes of debasement, was the insistence of most governments on fixing the exchange rate, that is, the price, of silver and gold, that is, instituting “bimetallism.” This bimetallic fixed ratio, usually set initially at the ratio determined by world market prices, inevitably departed from it more strongly as time went on. Gresham’s Law went into effect and caused sudden shortages of the artificially

undervalued metal along with inflows and surpluses of the artificially overvalued one. In a truly free market, government would not fix exchange rates, but would allow countries and societies throughout the market to select media of exchange and units of account: this is what is called “parallel standards” of gold, silver, and possibly other metals, and what has also been called “free metallism.”<sup>68</sup>

A genuine free market in money, then, would allow the market to select whatever metals it wishes as media of exchange and units of account, without government attempts to fix the exchange rates between them.<sup>69</sup>

But one would expect that the world free market, the mighty network of voluntary exchange that Mises called an *oecumene*, would, if unrestricted and given its head, move eventually toward one monetary metal.<sup>70</sup> And, whether it be one or two metals, the currency units would eventually transcend the independent or quasi-independent names given by states, to form a world-wide unity of simple units of weight. The entire world, we might expect, as state interference into the market *oecumene* disappears will speak and reckon no longer in “dollars,” or “francs,” or “marks,” but only in gold ounces or gold grams. That sort of world was, indeed, the attainable dream of many of the economists and statesmen of the nineteenth century, the classic century of the gold standard. In a series of international monetary conferences, which contrasted to twentieth-century ones by not seeking more global government monetary control but greater expression of a unified free market, there were attempts to reach this goal. The idea was first to adjust existing exchange rates slightly to make them multiples of one another, facilitating a phasing out of names and a growing use of explicit units of gold weight in every country. Unfortunately, the vexed silver problem obstructed any

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<sup>68</sup> On parallel standards, see Mises, *Theory of Money and Credit* (New Haven: Yale University Press, 1951), pp. 179ff. On how they worked in medieval and early modern Europe and how bimetallism interfered with them, and provided occasions for debasement, see Luigi Einaudi, “The Theory of Imaginary Money from Charlemagne to the French Revolution,” in *Enterprise and Secular Change*, F.C. Lane and J.C. Riemersma, eds. (Homewood, Ill.: Irwin, 1953), pp. 229-61. On “free metallism,” see two works by William Brough, *Open Mints and Free Banking* (New York: Putnam, 1898), and *The Natural Law of Money* (New York: Putnam, 1894).

<sup>69</sup> Comparing the return to gold coin in Europe after half a millennium in the mid-thirteenth century, in Florence and in Genoa, Professor Lopez, a proud Genoese, writes: “Florence, like most medieval states, made bimetallism and trimetallism [copper] a base of its monetary policy. . . Genoa, on the contrary, in conformity with the principle of restricting state intervention as much as possible, did not try to enforce a fixed relation between coins of different metals. . . basically, the gold coinage of Genoa was not meant to integrate the silver and bullion coinages but to form an independent system.” Robert Sabatino Lopez, “Back to Gold, 1252,” *Economic History Review* (April 1956): 224.

<sup>70</sup> On Mises and the *oecumene*, Joseph T. Salerno, “Ludwig von Mises as Social Rationalist,” pp.26—54, esp. 27—36. Salerno writes of the Misesian *oecumene*, “As the final and full fruition of social evolution driven by the cosmic ontological principle of division of labor, the ‘oecumene’ embraces all of humanity cooperating in hyperspecialized production processes. At any point in history, the evolving *oecumene* is the ‘rational and intended’ outcome of an intersubjective process, whose purpose is the amelioration of scarcity. It exists not as a thing unto itself, but as a complex of social relations which emerges from a common orientation of individual human actions, that is, to use the social division of labor as the means to attain individual goals. Because such relations thus emanate from the will, they must be daily affirmed and recreated in human thought and action.” *Ibid.*, p. 31.

agreement, until of course World War I swept away any search for a genuine international metallic money.<sup>71</sup>

Since World War I, unfortunately, the quest for inter-central bank cooperation, for international monetary coordination, has been a search for a form of monetary internationalism diametrically opposed to the thrust of the nineteenth century. Instead of a search for a world money uncontrolled and unhampered by any State, we see repeated attempts to achieve a form of world governmental coordinated paper inflation. The ultimate Keynesian dream is moving ever closer: to establish a world economic government with a World Reserve Bank issuing a new world paper currency to be called the *bancor* after Keynes, the *unita* after Harry Dexter White, the *phoenix* after the *London Economist*, or whatever. Then, all nations of the world believe they could inflate together, keeping exchange rates fixed and also avoiding the kind of monetary reserve crisis that laid low the phony British-run “gold” standard of the late 1920s, as well as the phony “gold”-tainted Bretton Woods system after World War II. Then, there will be nothing to stop the smooth run of worldwide inflation—until, of course, the market takes the play away from the depreciating world paper currency and the world goes through the fearful holocaust of a worldwide runaway inflation.

But let us return from this grisly scenario to my projected and hoped-for worldwide free market, the interconnected and prospering oecumene. We can project what will happen to this market if it is allowed to evolve without government distortion or interference. We can project, then, a future worldwide free economy, using only metallic money, with the entire world using one unit of weight of gold as money, both as a medium of exchange and as a unit of account. All reckoning will take place in terms of gold ounces or grams, which cannot constitute the world stock of money. It is possible that silver will continue to be a metallic money for smaller denomination transactions, but we can imagine that the market’s quest for efficiency will eventually lead to one metallic money. Money will then be fully private, with no government intrusion, for the gold will both be mined and minted by private firms. (There is no reason to assume that only government is qualified to mint coins. In fact, considering its record of continuing debasement, government is scarcely qualified to mint coins at all.)

A “free market” also means no government interference whatever in the economy. It means that private individuals and firms are free to earn money and profits, and that they are also free to lose. There can be no genuine freedom to choose without a corollary freedom to lose. No firm may be considered “too big to fail.” And so a free market in money necessarily means the abolition of central banking and of so-called deposit “insurance.” Banks must be free to fail.

Indeed, a “free market” necessarily implies total respect for and protection of private property. But this means that rights of private property must always be preserved. This

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<sup>71</sup> See the detailed account in the much neglected work, Henry B. Russell, *International Monetary Conferences* (New York: Harper, 1898). Also see Frederick A.P. Barnard, *The Metric System of Weights and Measures* (New York: Columbia College, 1872), who treats the problem of international unification of monetary units in an appendix as a subset of the problem of unifying all metric measures.

implies not only a cracking down on assault and murder, but also on all forms of theft and fraud, including counterfeiting. Counterfeiting must be prosecuted fully by the law and, more than that, must be scorned and condemned by public opinion. As an advocate of 100 percent reserve banking, of full gold backing for all bank notes and deposits, I recognize that it would be difficult for government to police the banks, banks being notably ingenious in discovering market ways of getting around government regulations. One hundred percent banking must be enforced, not by administrative regulations, but by the legal system. While investigative snoops can hunt down counterfeit warehouse-receipts, it would be far simpler and more effective to crack down immediately and totally on any failure of a bank to pay in full on demand. First, as the Jacksonians wanted, but were never able to get through the Whig-dominated Congress in the late 1830s, at the first sign of such non-payment, the bank must be declared insolvent and its assets liquidated. But, second, these fractional-reserve bankers must be treated not as mere entrepreneurs who made unfortunate business decisions but as counterfeiters and embezzlers who should be cracked down on by the full majesty of the law. Forced repayment to all the victims plus substantial jail terms should serve as a deterrent as well as to mete out punishment for this criminal activity.

I envision the free-market world of the future, then, as one of purely metallic worldwide money. Increases of bank money will not be tolerated and will be treated as the counterfeiting and the invasion of property rights that they really are. The money supply, then, will grow only slowly, concomitant with the slow growth in the stock of the world's gold. The scourge of inflation will finally be lifted from the world; prices will fall, and the more productive the economy, and the more the increase in the supply of goods, the more prices will fall, the cost of living will decline, and the greater will be the increase in the standard of living for everyone. And without fractional reserve banking, there will be no more booms and busts, no more terrible malinvestments, distortions, and shocks of euphoria and distress brought about by business cycles. Investment will be limited to voluntary savings, and therefore there will be no periodic outbreaks of unsound investments that will have to be liquidated by recession. The world economy will at last be secured by the money required for freedom a metallic money, produced by the market and the value of which is decided totally by the market and not at all by government.

Consumers and the economy will be immeasurably freer and sounder, and the only ones who will lose from the development of this market economy are the special interest groups who benefit from government and bank-controlled inflation and who constitute the ruling power elites in our increasingly state-dominated economy.

### **Epilogue: The Modern Austrian Revival**

Professor Karen Vaughn's brief history of the modern Austrian "revival" as a participant-observer is, first of all, a strictly biased account from the Hayekian/Lachmannian point of view. The Vaughn treatment is yet another variant of the Whig theory of the history of thought, this time from a Lachmannian perspective. Being Whiggish, Vaughn's history has to be fitted into the Procrustean mold of early fumbings, improvement, and, at each

step of the way, onward and upward into the light, it begins then, in post-World War II America, with Mises as the admitted carrier of the Austrian tradition; to be improved upon and superseded by Hayek; and then finally, to be crowned by the upward march of nihilist Lachmannia, creative gropings by O'Driscoll and Rizzo, and finally even Lachmann's "narrow" destructionism surpassed by glimpses of a grand and noble new theory, emphasizing "biological evolution," and culminating in the work of several young graduate students of Professor Don Lavoie. In particular, the two works cited by Vaughn as blazing the path toward a grand new Austrian paradigm consist of two articles published in Lavoie's minor and now defunct journal, *Market Process*.

Professor Vaughn leaves out some significant facts from her starry-eyed account. One is that she herself was on the board of Lavoie's Center for the Study of the Market Process, and that she therefore was engaging in a certain amount of special pleading.

In any case: how did our Whiggish neo-Austrian fare in her attempt to capture the historical process, her form of institutionalist Austrianism? In short, how well did she predict the near-term Austrian future? The answer is: not very well. Professor Vaughn's article was written for a conference on the Austrian tradition in economics held in the spring of 1989. In the less than four years that have elapsed since then, the entire Austrian world has changed dramatically. Well, it is a fast-moving world out there, if not quite the "kaleidic" one perceived by Ludwig Lachmann. Since her article was written, the Lachmannian Society for Interpretive Economics, founded by Professor Lavoie, has come and gone, the journal *Market Process* has disappeared, and the Center for the Study of the Market Process has virtually left economics. My own prediction, I dare say better founded than Professor Vaughn's, is that, with the passing away of Professor Lachmann, and more particularly, the loss of interest in economics by its funding source, Lachmannia and the Lavoiean variants will quickly disappear from the scene. Not being a Whig historian, this development does not unsettle me in the least.<sup>72</sup>

Let us return to Professor Vaughn's history of the Austrian revival. In order to praise the later developments, she is forced to disparage the earlier ones, particularly the noble struggle of Ludwig von Mises and even more those of us who have continued in the older and therefore allegedly discredited Misesian paths. Part of her form of Whig mythology is that Hayek must be painted as far superior to Mises. So we have Mises grudgingly hailed as single-handedly preserving the Austrian school in the United States in the 1940s, 50s, and 60s. She disparages Mises as an outsider to academia, as not being able to secure an official teaching position because of his "outspoken antistatist views," and because of his unfortunate "emphatic style." She is forced to admit that while Hayek, whom she claims to be "ultimately . . . more important in shaping the Austrian revival," actually emigrated to the United States in the 1940s, and while Hayek taught at the same

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<sup>72</sup> In her latest discussion of Austrian economics, Vaughn, while quietly and necessarily abandoning the Lavoiean project and dropping all references to it, is still searching for some mixture of "evolution" and institutionalism as the way out for Austrian economics. Karen I. Vaughn, "The Problem of Order in Austrian Economics Kirzner vs. Lachmann," *Review of Political Economy* 4, no. 3 (1992): 25 1—74.

time at the University of Chicago, it was unaccountably “his older colleague Mises who was responsible for bringing Austrian economics to America.”<sup>73</sup>

What she fails to mention, since it would correct her deprecation of Mises, is that Hayek too, despite his definitely unemphatic style, could not find an official academic post in the United States, and that his salary, too, was financed by the William Volker Fund, the same organization that financed Mises’s professorial post because it “knew of [Mises’s] lifelong antistatist fight.” The Volker Fund financed Hayek’s professorial position for the same reason.

Moreover, the reason why Hayek did not help spark an Austrian revival in the United States, despite his years of teaching at Chicago, is that Hayek was not the sort of teacher to ignite or inspire student interest. Hayek was barred from teaching economics at the University of Chicago by the economics department, and so he had to teach at the Committee on Social Thought, a charmingly interdisciplinary graduate department, but whose PhDs, being outside orthodox department lines, were not exactly designed for scholarly careerism. But more important than that: Hayek did not have the personality as a teacher to inspire students or disciples. Unlike Mises, who was unfailingly charming and devoted to spurring productivity among his students, Hayek was cool and aloof, only answering specific questions put to him by his doctoral students, and never engaging them in conversation or discussion. Hence, Hayek did not help spark an Austrian revival. Also, as Vaughn briefly admits, Hayek had not yet come up with his “evolutionary” and other philosophic studies. His first alleged masterwork, *The Constitution of Liberty*, published in 1960, was political philosophy rather than economics, and it was a political philosophy that properly carried no weight, being generally demolished by such Austrian critics as his student Ronald Hamowy.

Finally, Hayek retired from the University of Chicago in 1961, and since Chicago refused to pay him a pension since it had never paid him a salary, Hayek was forced to leave the United States and go to Germany, where he was able to draw a salary at the University of Freiburg. From 1961 on, Hayek no longer resided in the United States, and this important fact, curiously omitted from Vaughn’s account, played an important role in Hayek’s not being central to the Austrian revival which Vaughn dates from the South Royalton Conference in 1974.<sup>74</sup> As Vaughn points out, Hayek’s coincidental receiving of the Nobel prize later in the fall of 1974 clearly ignited a general and continuing interest in and study of Hayek and the entire Austrian tradition.

Historical accuracy compels me to take up Professor Vaughn’s comparative treatment of Professor Kirzner and myself, undoubtedly the two most productive American students of Mises, both of whom had published important Austrian works before the South Royalton year of 1974. I, she says, was “Mises’s faithful interpreter to the radical libertarian fringe

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<sup>73</sup> Vaughn, “Mengerian Roots,” p. 396.

<sup>74</sup> Vaughn attributes the alleged neglect of Hayek at the South Royalton conference to the fact that I “did not think much of Hayek’s politics or economics.” Very true, except that I had no control over the papers of the two other major participants: Israel Kirzner and Ludwig M. Lachmann. Vaughn, “Mengerian Roots,” p. 402n.

. . . young people, many of them free-market radicals who had discovered the work of Mises and who had listened to the Austrian folklore at Murray Rothbard's knee."<sup>75</sup> So here I am, in Professor Vaughn's account, a preacher of Misesian folklore to youthful free-market libertarians. In the meanwhile, while I was dispensing Misesian folklore to bedazzled youth, what was Professor Kirzner doing? He, "against overwhelming odds, attempted to carry on Mises's work in the context of the mainstream academic community."<sup>76</sup>

There are two fundamental flaws with Vaughn's historical account, convenient though it may be for her own Whiggish folklore of Up from Mises to Lachmann and Lavoie. One is, that I too, was an academic. At the time of South Royalton, I was a professor of economics at the Polytechnic Institute of Brooklyn; perhaps, bedazzled youth that she may have been at the time, she did not realize that I was not a full-time folklorist. The second deals with Professor Kirzner's role. While Kirzner is a distinguished scholar and contributor to the Austrian tradition, even though he too has strayed from Mises in later years, he was scarcely, at that point, a heroic struggler for Austrianism against its academic enemies. In fact, Israel Kirzner kept a very low Austrian profile at New York University. I myself became friendly with someone who had received a PhD under Kirzner in the late 1960s, and he had no idea whatever what Austrian economics was or that his doctoral mentor was connected with it.

Vaughn mentions that the Institute for Humane Studies sponsored the week-long scholarly Austrian conference at South Royalton, as well as two others in the next two years, one at the University of Hartford, which she does not name, and one at Windsor Castle, England; important volumes of papers emerged from both the South Royalton and Windsor Castle conferences.

But then Vaughn does not raise the question: what in the world happened to these annual high-level scholarly conferences, that did so much to advance the Austrian School's discipline and interest in Austrian economics? What happened is that these conferences disappeared, since the major funding source, whom I refer to as The Donor, shifted his focus of interest. The shift was away from Misesian radicalism and consistency, both in Austrian economics, notably praxeology, and in political economy, in the form of consistent laissez-faire. By the late 1970s, The Donor decided that what Vaughn refers to as Mises's "outspoken antistatist views" and "emphatic style" were too candid and uncompromising to be palatable to the Powers That Be or respectable to other funding sources, the federal government, or the leaders of academia. For all of these reasons, The Donor, followed by the eager recipients of his largesse, decided to set up moderate think tanks for public policy and to dilute Austrian economics to become respectable and non-threatening to academia. In academia, he thereby encouraged various outreaches: to Marxists, to hermeneuticians and deconstructionists, indeed to anyone and everyone put off by Ludwig von Mises's intransigent devotion to truth and to liberty. Hence, no more scholarly Austrian conferences, but only fellowships and programs promoting non- or anti-Misesian views in the name of Austrian economics.

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<sup>75</sup> Ibid., p. 399.

<sup>76</sup> Ibid.

If Professor Vaughn were really interested in chronicling a battle for Austrian truth “against overwhelming odds,” she would ponder the tremendous achievement of Llewellyn H. Rockwell, Jr., in founding the Ludwig von Mises Institute ten years ago. For Lew Rockwell founded the Institute with no endowment, no pledges, no Big Daddy. All he had was the gleam of a lifelong idea: to found an institute dedicated to Ludwig von Mises and promoting the Misesian paradigm in Austrian economics. In fact, Big Daddy, the aforesaid Donor, was furious at Rockwell’s plan to found the Mises Institute, and had the unmitigated gall to “order” him not to do so. When Lew went ahead despite this order, The Donor engineered a determined boycott, both of the Institute, and of the later establishment of the only scholarly Austrian journal, *The Review of Austrian Economics*. There is good news to report at this Tenth Anniversary Conference of the Mises Institute. In the first place, this scholarly conference in Austrian economics continues the Windsor Castle tradition; let us hope it is the first of many. And second, The Donor has lost interest in Austrian economics and in ideology. The Mises Institute’s stunningly successful summer conference, its “Mises University,” is just about the only instructional summer conference remaining in Austrian economics. And as we have developed more and more outstanding Misesians, the Misesian paradigm has not only revived as a result of the Mises Institute’s success: it is now virtually the only paradigm left in the field. Instead of the Whiggish history of a straight line onward and upward from Mises to the students of Lavoie, what we have is a three phase history, a zig-zag history of clashing paradigms and ideologies. The first phase was The Revival, beginning in the summer and fall of 1974 with the South Royalton Austrian conference and the award to Hayek of the Nobel Prize; but this expansion phase ended sometime in the late 1970s, after Windsor Castle, and was succeeded by Phase II, a decline and degeneration of Austrian economics away from the Misesian paradigm and into various fallacious variants and deviations. But then, as the Mises Institute got under way in the 1980s, Phase III, the Renaissance, developed, culminating in the recent successes of the Mises Institute, the pullout from the field by The Donor, and the subsequent triumphal restoration of the Misesian paradigm. The difference from the late 1970s is that the Misesian paradigm is now established on a higher level than two decades ago; not only are there far more younger Misesians, and bound to be still more in the years ahead; not only are the “middle generation” of renegade anti-Misesians fading away, but of course Misesians have learned more in these two decades, ever honing and sharpening our Misesian knowledge in the course of waging struggles against these deviations and fallacies.

And so the truly good news of this Tenth Anniversary Conference of the Mises Institute is that I stand here, and the conference itself bears witness, to proclaim victory, to announce, at long last, the triumph of the Misesian paradigm in the Austrian home that Mises himself created. The great Ludwig von Mises could ask for no greater tribute.