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Neither Heat Nor Light

by Jeffrey M. Herbener

We are privileged to live in fascinating and exciting times. Only socialists and bureaucrats could not be breathless over the collapse of communism. The economics profession too is undergoing fundamental change, though, unfortunately, at a much more leisurely pace.

Already showing chinks in their armor, mainstream economists not only failed to predict the communist collapse of 1989 (the Friedmanite hallmark of economic science), but have been at a complete loss to explain it, let alone to provide a policy of desocialization when asked. When the godfather of neoclassical economists, Paul Samuelson, continued to state in the 1989 edition of his economics textbook, "The Soviet economy is proof that, contrary to what many skeptics had earlier believed, a socialist command economy can function and even thrive," cheers began turning to jeers.

This latest in a long line of failures of Keynesian and neoclassical economists has heightened the anticipation of a fundamental shift in economic theory. However, forums to voice criticisms of mainstream economics poses dangers as well as opportunities. Any of a host of cranks, regardless of past refutations, can now obtain a new hearing. As mainstreamers lose their nerve, seemingly impotent to stem the tide of criticisms recently advanced, the economics profession may soon be up for grabs.

Enter Philip Mirowski, a Veblenian institutionalist, to the contest as a voracious critic of neoclassical economics. Following Veblen he has, in prior works, advanced the thesis that neoclassical economics is a somewhat inaccurate adoption of a mid-nineteenth century branch of physics he calls proto-energetics; and since that branch of physics is now discredited so should neoclassical economics be. The first part of his thesis is an important insight that can help to clarify all critiques of neoclassical economics. The second part is much less convincing. And like Veblen, he is less effective as a builder of a positive replacement than as a critic.

In his latest book, *More Heat than Light* (Cambridge: Cambridge University Press, 1990), he goes



Jeffrey M. Herbener

far beyond his original thesis, attempting to demonstrate that neoclassical economics is a misguided, perhaps even sinister, effort to adapt economics to the suspect, if not fallacious, paradigm of Western science: the metaphor of energy. He says, "The only way to fully comprehend value theory in economics is to situate it within the pyramid of Figure 3.1, the metaphorical simplex of energy, motion, body, and value, and to regard it as part and parcel of the same structures that undergird Western physics. The payoff to this reconceptualization of value theory is a

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clarification of the entire history of economic thought" (pp. 141-42).

This is a grandiose claim, simple and provocative but one that is ultimately a failure. Mirowski certainly has ample evidence for his assertion that the founders of neoclassical economics cribbed their theory from physicists of the mid-nineteenth century. And thus, neoclassical value theory and the perspectives of neoclassical economists on competing value theories can be better understood by seeing the physics parallels. Mirowski provides more insight to what he has said before on this count. However, beyond this his thesis is unconvincing as his framework does nothing to advance the knowledge of value theory *per se*. But first an overview.

He borrows a stage of history analysis from the Polish historian Witold Kula who states that history moves through three stages of metaphor: anthropometric (human body is a measuring device), lineamentric (numbers are specific to each object), and syndetic (unified numbers based on nature) (p. 109). Each stage is identified by its unique treatment of the metaphors of body, motion, and value. In the anthropometric stage the three are seen as one, in the lineamentric the three are separate and at war, and in the syndetic there is unification of metaphors by a fourth one, energy (p. 109). Thus, in the last stage the consolidations hinge on conservation principles and invariance principles (p. 109).

Physics was in the lineamentric stage from the sixteenth century through the mid-nineteenth giving us rational mechanics and theories of fluids and ethers in the discussions of heat, light, magnetism, and electricity (p. 119). This period coincided with the lineamentric stage in economics ushered in by Adam Smith and the classical economists (p. 143), who advanced beyond the primitive anthropometric stage begun by Aristotle (p. 144).

The syndetic stage begins with the discovery of energy conservation which led to the unification of the metaphors of different disciplines: in biology via the gene, in physics via energy, and in economics via fiat money (p. 115). Within the metaphorical simplex, the social blends with science as individuals in different disciplines work on different aspects of the unify-

ing metaphor. This stage coincides with the rise of the world mercantile economy and institutions of world industrial economy, because economic phenomena changed the perception of the metaphor of value and therefore the metaphor of motion (p. 119).

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mid-nineteenth century physicists.*

Unfortunately, economics did not fully attain its metamorphosis in the syndetic stage and thus, has not yet emerged into the stage of modern science.

Some examples of the interplay of the social to the physics: the "vectors of trade" point to Holland in early modern Europe and thus Descartes used accounting to establish his physics (p. 121); Leibniz worked in mines and thus was able to apply conservation principles to human action (p. 122); Bernoulli used economic metaphors and Carnot "derived the first law of thermodynamics from an economic metaphor" (pp. 124-25); the debasing of money caused one of the foundations of energy to collapse and forced physicists to change the energy metaphor (p. 135); radiation is based on central banking (p. 137).

The breakdown of the energy concept is evidence of the latest stage, syndetic metro, Mirowski says, where "metaphors are reconciled by realizing that each is a fiction, but the same fiction, a fiction necessary for the organization of human discourse" (p. 137). Metaphor is a framework for "discourse."

He seems to be arguing that all scientists have a Marxian "false consciousness," feverishly pursuing metaphors inside their circle while posing concern for truth to those on the outside, and that this activity blends across disciplines as they work on different "faces" of the metaphor. Each discipline appeals to the metaphors established by the others when dealing with criticism (p. 116). As with all models of historical determinism, however, not all thinkers are under this spell. Not surprisingly, those that Mirowski favors seem able to transcend the metaphor, providing important, but until Mirowski, incomplete criticisms of the framework.

Not until the last paragraph of the book does he reveal the true purpose of his work: to convince the reader that culture must be central to "any logical economic theory." He approvingly quotes Gunnar Myrdal on the subject of the, "countless errors...that no living man can yet detect, because of the fog within which our type of Western culture envelops us. Cultural influences have set up the assumptions about

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the mind, the body and the universe with which we begin; pose the questions we ask; influence the facts we seek; determine the interpretation we give these facts; and direct our reactions to these interpretations and conclusions" (p. 401). Just as all historicists before him, Mirowski does not appreciate that, while important in studies of history, culture does not trump science, either in physics or economics.

His fashionably disparaging view of Western thought aside—is there really an Eastern physics to juxtapose with the Western, when one drops an apple in China, does it fall upward?—this raises another question, viz., why did science arise in Western culture? For a historicist, if culture determines science and science is the touchstone of modern civilization, then Western culture must be rated superior to the non-Western ones; yet, Mirowski concludes the opposite.

Contra Mirowski, methodology is important in the sciences, both natural and human. He claims that to discover what is accepted as scientific knowledge one must apply a hermeneutic approach (his to be precise) to the history of science; following a "rote" method is useless. In the natural sciences, however, this is wrong because the knowledge therein is demonstrated in repeated experimentation, by others, before being accepted. It may be true that how a person decides to view that knowledge and integrate it with other knowledge is not susceptible to such a procedure but that does not allow contradiction of what was learned.

In the sciences of human action, his claim is also erroneous since a process of validation exists in this realm too, viz., the repeatable mental experiments of praxeology conducted by independent minds.

Mirowski's thesis appears superficially plausible because one seeking to understand the world does fit knowledge gained from different disciplines about different subjects into a coherent framework. This is the hallmark of a sound world view.

A scientific endeavor is that part of a world view characterized by an accepted method for validating knowledge that can be employed by others who either corroborate it or dispute it. The natural sciences employ the inductive method of repeated experimentation while the human sciences use the deductive method of praxeology. The latter is based on the irrefutable presuppositions of human action while the former is based, in addition to those, on the existence of an independent reality.

In both cases invariants are necessary in constructing explanations; in the sciences of human action these are rationality and the mental presuppositions of action, while the natural sciences depend upon not only rationality but the existence of a reality apart from ourselves.

However, this framework does not have to be

metaphoric, and it is much to the credit of Western thinkers that their framework is grounded not on mythical metaphors, but on truths that can be independently validated by others.

Other types of knowledge, e.g., historical, cannot be obtained in these ways but must be, at least partially, based on judgments and then systematized into a coherent framework. This leads not to scientific knowledge but to what Ludwig von Mises called understanding.

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No one is born with a world view but must construct one over time, putting the pieces together as best he can. While an individual can live with inconsistencies and thus, a defective world view, science cannot and must reconcile them in some fashion as individuals within the discipline bring up these inconsistencies and challenge the existing framework or results.

Mirowski is quite right to claim that individuals develop science within a culture that influences the questions they ask. That is why having a "rote" method is crucial to scientific endeavors. The key question is, which is the correct framework? Clearly, Mirowski has selected the wrong one in the metaphor of energy.

Consider what he concludes from the history of physics: the energy concept is dead (p. 99); energy is equivalent to conservation laws (p. 13); conservation laws are necessary for causal analysis (p. 160); all of Western thought is predicated on the energy concept (p. 8). Thus, not only is neoclassical economics dead so is all of Western thought and especially economics (pp. 107, 116).

His conclusion about physics is, "late 20th century physics is a frightening and demoralizing place: a universe sprung full-blown from nothing; no real natural laws; chaos wherever one turns; the physical world a speculum serving us back our own gaze...It also corrodes and debases every little piety we may happen to cherish" (p. 140).

It is difficult to keep up with the rapid changes in physics, and Mirowski is behind the times. Chaos is not everywhere one turns. Chaos theory applies only to systems that are initial condition sensitive, such as global weather. This has no more to do with economic theory than the calculus does. Also, the systems described by chaos theory are not chaotic at all

but can be analyzed by the advanced mathematics of the theory itself.

They are chaotic only in the sense that simple mathematical techniques cannot describe them. The difficulty of predicting the outcome of a chaotic system has to do with the extreme accuracy of the measurements necessary and the precision of the calculations required, not with the absence of conservation laws.

Randomness is precluded by the very existence of human action, i.e., purposeful behavior. If the universe were actually chaotic, no one could meaningfully strive toward the attainment of an end with the application of means according to ideas. Action would be impossible.

Even if one wishes to apply chaos theory outside of its realm, it does not necessitate the eastern mysticism view of dancing wu li masters advocated by Mirowski. Several authors, e.g., Nick Herbert, have shown that many different views are consistent with chaos theory, some of them Western and rational.

Contra Mirowski, twentieth-century physics is neither frightening nor demoralizing. Far from the demise of natural law and the disintegration of physics into hermetically sealed categories, physics is moving toward integration and Grand Unification Theory. The overriding theme is unification, order, explanation, prediction, in short all the attributes associated with the natural sciences. The dream of being able to understand the world around us is alive and well.

Mirowski twists this fact with the claim that pre-twentieth century physicists had a Laplacian dream, i.e., one set of equations that determine the motion of everything forever.

But one awakens from this at the mere suggestion of Godel's theorem, viz., every non-trivial set of equations must have conditions set outside the system. Furthermore, as with randomness, determinism is precluded by the irrefutable fact that human action exists. Only robotic activity could occur in a completely deterministic world. There could be no choice, no striving, no evaluation, no learning—in short, no action.

Consider the following as an illustration of Mirowski on physics: he is fond of telling us that modern physics has shown that something can come from nothing, and in fact "the universe is a free lunch." (Presumably this is the basis of his belief that scarcity is a "morality play.") From this he concludes that the first law of thermodynamics, that paragon of natural law, is not a law at all. But no such conclusion follows. The first law of thermodynamics states that a *natural* process cannot bring something into existence from nothing. Certainly no person has ever witnessed a violation of this law. The "new inflationary theory of the universe" does imply that the uni-

verse came from nothing and that the universe had a beginning but these facts do not undermine the first law in the least. They require a scenario for the creation of the universe consistent with all three principles—anything else is profoundly unscientific.

Science cannot even explain the initial conditions of the phenomena under study. While the new inflationary theory of the universe is a vast improvement over the big bang theory, allowing us to go all the way back to the beginning avoiding the "plank time" problem, neither it nor any other theory of physics can explain the initial conditions that created what we see from the big bang. Just as seeing the expanding path of pellets and smoke from a shotgun blast allows us to trace backwards to their initial position, the new inflationary theory allows us to trace back to the initial position of the stuff of the universe. In neither case does physics explain, even if it discovers them, the initial conditions that determine the path of things once set in motion. Yet the motion and asymmetry of the universe is predetermined by these initial conditions just as a person's body is determined by the information contained in genes.

Mirowski also misunderstands, or ignores, information theory and the generalized second law of thermodynamics. The latter states that natural processes on average mix things over time. If so then there is no reasonable material explanation of the tremendous unmixed state of things in the universe. The patterns produced by nature are simple, i.e., they contain less information. When these patterns are made, e.g., crystals, information is always lost. Natural processes cannot produce the complex patterns we actually see in the universe.

Mirowski is not only skeptical of a Supreme Intelligence but of human intelligence as well, leading him at one point to decry the productivity of man's rearrangement of physical matter. He is quite right to point out that the first law prevents man from creating matter and energy out of nothing; but he is quite wrong when he asserts that the second law plays havoc with point-input point-output models and the idea that more roundabout processes are more productive (pp. 321, 327). (It is also hypocritical of him to state that no natural laws exist and then use natural laws to discredit the concepts of scarcity and production.)

Physically, the productivity of man's action is in the information added to the stuff when man acts. This is seen most dramatically today in gene therapy but is no less evident when man builds a factory or a machine. In fact, the major instrument of man's advancement is the expression of his intellect via capital goods.

The creation of capital goods does not add matter or energy, it adds information and thus, complexity or design that is useful to man. Only *natural* processes are subject to the second law, which raises the

question, if man's activity, guided by intellect, cannot add productivity, how can nature, without intellect, add complexity via evolution? Just as there is too much information evident in an electron microscope to attribute its existence to natural processes, there is too much information in a protein molecule to attribute its existence to natural processes. The universe contains approximately 270 bits of information whereas a simple bacterium contains over one million bits.

Furthermore, fundamentally, productivity is a subjective concept, one that is meaningless outside the context of an observing intellect.

Consider another sample of Mirowski on physics: science is moving toward a world subject to change, diversity, indeterminacy, and at one with the observer (p. 275). Quantum theory is a set of laws about the relationship between observer and the objects of the universe. It splits the universe into two types of items, classical and quantum. The latter are subject to quantum laws, the former are not. Quantum theory precludes precisely what Mirowski asserts about the observer. In fact, quantum theory implies that items in the universe have no known objective characteristics unless an observer is present.

Since doing science is human action the same prerequisites apply to the natural sciences. Neither Newtonian physics nor Euclidian geometry nor Cartesian analysis has been refuted by modern physics. The latter depends on them for construction of the instruments that allow the observations that provide their empirical foundation. Modern physics has shown them to be special cases of more general principles encompassing a broader range of phenomena. This is progress in the natural sciences, viz., moving from describing a limited number of cases to a larger number of cases. Despite Mirowski's denigration of engineers—"In my experience, they often look up certain calculations based on crude empirical techniques rather than explicit physical laws, and then arbitrarily multiply the requirements by ten for safety's sake"—the machines still work, and rational mechanics is alive and well as is rational analysis.

Outside the boundary of his critique of major neoclassical economists, his "clarification" of the history of economic thought based on the metaphor of energy breaks down. Here are a few examples: Thorstein Veblen and Nicholas Georgescu-Roegen are the "most profound economic philosophers of the twentieth century," a fact in honor of which he dedicates the book; Aristotle is the beginning of all economic thought *because* others have written a lot about what he said (p. 144); Thomas Aquinas followed Aristotle's naive equal value in trade view (p. 146); the schoolmen were equivalence-of-value theorists (p. 149); some of the Mercantilists were the best economists of their time (p. 149); Adam Smith and J.B. Say

were apologists for the merchant class against the physiocrats who favored agriculture (p. 161); Turgot was confused and advocated "the denial of value" which led him into self contradiction (p. 163); Menger did not have the least idea of mathematical analysis and was "innocent" of physics and therefore unqualified to attack the German historicists (p. 260); Eugen von Böhm-Bawerk was a second-rate neoclassical economist who was not qualified to criticize Marx's labor theory of value because he used a substance theory of value himself (p. 282); F.A. Hayek, "one of a very few remaining representatives of the Mengerian tradition of Austrian economics [in 1942]," was a Don Quixote, "tilting at scientific socialism in blissful ignorance..." (p. 355), is "superficial" in his treatment of physical theory, and "deficient" in his understanding of metaphors, and he "misrepresented" the history of thought and made "absurd" claims and "smeared" the German historical school (p. 356); Ludwig von Mises is so insignificant that Mirowski does not even mention Mises's existence.

Mirowski says that F. A. Hayek was a Don Quixote "tilting at scientific socialism in blissful ignorance."

The reason Mirowski avoids the work of Ludwig von Mises is Mises's demonstration of the prerequisites for acquiring knowledge concerning human action. Mises showed the proper separation and relationship between the theory and history of human action, viz., theory is constructed praxeologically from the universal presuppositions of action, without incorporating knowledge of specific historical events and then is used to understand the unique events of history. Mirowski notwithstanding, the specific, unique episodes of history are insufficient building blocks of a theory of human action.

Being a historicist, Mirowski argues that one must understand history to understand theory. Perhaps, then, this sampling of his pronouncements concerning economic theory will not be shocking: shares of stock are ownership of nothing (p. 120); money is the abstraction of economic value (p. 123); it is "self denying" to reduce value to a single index (p. 151); trade is equivalence of value (p. 134); economic theory is like a house of mirrors (p. 140); economic theory is neither true nor false but metaphorically determined by the particular stage it is in (p. 143); if value has no quantitative representation then economics cannot be scientific (p. 151); "One of the great fallacies of economic reasoning is to confuse requisite with productive" (p. 160); "there is no such thing as causal

analysis without [conservation principles] "(p. 160); J.B. Say did not understand his own law which was the basis of a "mere polemical assertion of the market's efficacy based on little more than bravado" (p. 170); the law of one price is unjustified fiat (p. 236); the physics metaphor was the "inertial guidance system for research" and the major determinate of economic theory (p. 279); scarcity is not a permanent feature of human life but a "morality play" (p. 294); the second law of thermodynamics precludes more roundabout methods of production from being more productive (p. 321); production is the expression of the conviction that there is progress in material life (p. 322); the only progress in value theory in the twentieth century is Sraffian/Marxian (p. 351); we must use a substance theory of value, otherwise no coherent, transitive, connected system of prices exist (p. 352); "the nature of science is far too elusive for any adherence to some rote method to be an effective or plausible substitute. The only proof of this statement can be historical, irredeemably inductive" (p. 368); markets cannot undo things (p. 390). No wonder he states that this book risks his reputation in the community of economists (p. 1).

What he has produced is the latest in a line of hermeneutical conversations designed not only to entertain and amuse but to "deconstruct" neoclassical economics (p. 384). Once the reader understands this he can simply go along for the ride, one that he will enjoy roughly in proportion to the extent he agrees with Mirowski. A word of caution in this age of sensitivity: he does not treat the reader with much care. For example, in his introduction to chapter two on the history of the energy concept he states that having learned about this subject, "I guarantee that afterward nothing will ever seem the same" (p. 12). Then in the introduction to chapter three he tells his readers that chapter two has been a setup: "Let us say I have just subjected you to a similar sort of experience" (p. 99) to involve us in his hermeneutical plot. To avoid his literary battering, I suggest that the reader start at the end of the book and read the chapters in reverse order. This hermeneutic also makes his thesis more intelligible.

Beyond cute, there is a harmful side to Mirowski: misquotes and misrepresentations. One particularly disquieting example of misrepresentation is a quote of Pierre Duhem, viz., "The history of physics shows us that the search for analogies between two distinct categories of phenomena has perhaps been the surest and most fruitful method of all the procedures put into play in the construction of physical theories" (pp. 277-78). Mirowski deconstructs this as "I propose that we take Duhem's words seriously...He did not merely say that metaphors were fruitful, he said metaphor was a method of theory construction" (p. 278). Since his entire book is predicated on the thesis of metaphor this sets one aback. To take

Duhem's words seriously should imply, at least, that one not change them. What Duhem said concerned analogy not metaphor, the two are distinct. An analogy is a similarity, e.g., money indicates the degree of scarcity of a good like a thermometer indicates the temperature in a room, while a metaphor is a figure of speech in which a quality is given to something to which it is not literally applicable, e.g., Ludwig von Mises had nerves of steel. Mirowski seems aware of the distinction during his conversation about metaphors in poetry (p. 278). Yet his assertions about neoclassical economics seem to rely on analogy not metaphor. Duhem also spoke about *physical* theories, not economic ones. (The book is marred by several typographical errors and omissions, not the least of which is the absence of the source of Duhem's quote.) But all is fair in hermeneutic deconstruction.

Analogy seems an almost indispensable tool for explaining physics to the non-mathematical. When one attempts to explain the meaning of the knowledge in the natural sciences the task is different than that of discovering this knowledge. Mises put it succinctly by stating that we do not know what electricity is but we do know what utility is. The corollary is that we can understand the process of human action but not those of nature (pp. 135-36). Physicists describe those processes but that does not make them meaningful. It is this duality of things (a necessary implication of quantum theory) that allows for the plethora of analogies and/or metaphors in the attempts to explain physical activity. The physicist must use analogies to convey the meaning of the equations that describe physical processes. Some of them will be more appropriate than others for the task and can differ from person to person depending on their range of experience with the items used as an analogy.

The most famous common analogy to explain the Newtonian view of the universe was the clock. This works as an analogy only if the person understands the working of a clock. Mirowski would have us believe that the ruling metaphor of all western thought is energy. Unfortunately, energy cannot be a metaphor, because no one knows what energy is. It is energy that requires a metaphor to be explained or at least illustrated. Energy, as Mirowski admittedly uses it, is not a metaphor but a framework of thinking about the world.

Mirowski traces the history of science in general and the energy concept in particular from Aristotle to the present. The purpose of extending the purview to Aristotle is unclear (why not begin with Solomon? he was also a wise but "non-scientific" thinker) but the effect is to allow Mirowski to demonstrate that all previous scientists were wrong. This is hardly a telling point; in fact it is a necessary (but not sufficient) characteristic of a progressing discipline. It is also true that today's geniuses in physics will be ridiculed by future Mirowskis. This is a consequence not of

history but of man's frailty and ignorance.

More to the point for Mirowski's thesis, economists who crib their economics from the latest fad in physics, or mathematics, as the neoclassicals did, will be ridiculed tomorrow. While this is surely a damaging fact for the neoclassical school, it is no less so for Mirowski's apparent acceptance of game theory as a model for economic theory. He believes his application of more advanced mathematics will, presumably, usher economics into the syndetic metro stage at last since it is consistent with institutionalism. Being an institutionalist he argues that institutions are essential to economic theory and adds that game theory is central to institutions. However, since von Neumann and Morganstern's seminal work in this area, it has been known that game theory requires its own set of conservation laws and variation principles, the very concepts Mirowski claims have been destroyed.

His lack of a principled case against using mathematics to develop economic theory severely reduces the force of Mirowski's criticism, since neoclassical economists could respond by arguing that human action is a special case for which proto-energetics is an appropriate technique. Therefore, more advanced physics does not matter any more for economics than for rational mechanics. It is up to Mirowski to demonstrate the efficacy of game theory in the area based on subjective utility and the inapplicability of field theory to economic activity. (He has only argued that field theory is no longer the cutting edge in physics. It is a non sequitur to conclude that therefore neoclassical economics is refuted as well.)

Again, Ludwig von Mises provided the forceful refutation of neoclassical theory by demonstrating a principled case against using mathematics in building economic theory. Utility is subjective, having no extensive objective property subject to measurement; therefore, no unit of utility can exist. All mathematical analysis is predicated on the (conceptual) existence of a unit and thus cannot apply to human action.

Neoclassical economics has staying power not solely from its alignment with physics but because of its claim to be grounded on the requisites of all economic theory, utility. It has taken a correct starting point, i.e., utility, and gone down the wrong path, i.e., the mathematical, not seeing or admitting that the two are incompatible. Both its theoretical and empirical components have become unintelligible and useless in explaining and predicting real world events. Once this happens something must give, some part of the framework must be adjusted or the results must be rejected or a person must live with inconsistencies.

Mirowski notwithstanding, the marginalist revolution did occur but was coopted by mathematically inclined economists.

Utility is real and essential for economic theory.

What we must do as a profession now is put economics back on the correct path begun by Menger and blazed by Böhm-Bawerk and Mises. We must avoid what Mirowski calls a clarion call, which is really a siren song, to irrationality. ■

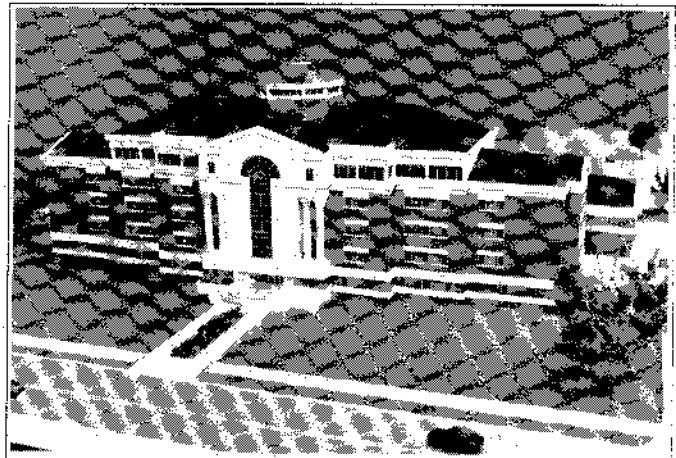
Mises Institute to Move Operations to New Building

The Mises Institute is building a new home on the Auburn University campus," announced Institute president Llewellyn H. Rockwell. "It will be no palace, just spartan and shoestring, as usual for us.

"Since we will have, for the first time, space for all our operations, we will be closing our small Lawrence Fertig Center near George Mason University, but not our programs, including our scholarships for GMU graduate students, our Austrian Economics Colloquium under the direction of adjunct scholar Dr. Roy Cordato of the Institute for Research into the Economics of Taxation, and our Washington Lecture Series.

The student study center in the new Auburn building will be dedicated to the memory of Lawrence Fertig—entrepreneur, scholar of Austrian economics, and friend of Ludwig von Mises and the Mises Institute—who helped make possible Mises's visiting professorship at New York University. NYU refused to make Mises a regular member of the faculty during his many years there, or to pay him a salary. Free-market businessmen like Fertig did the job."

Rockwell added that the "Institute's center at the University of Nevada, Las Vegas, consisting of Professors Murray N. Rothbard and Hans-Hermann Hoppe, as well as a team of top graduate students, is not affected." ■



The architect's model of the new business school building on the campus at Auburn University.

In Memory of Ludwig M. Lachmann

by Roger Koppl

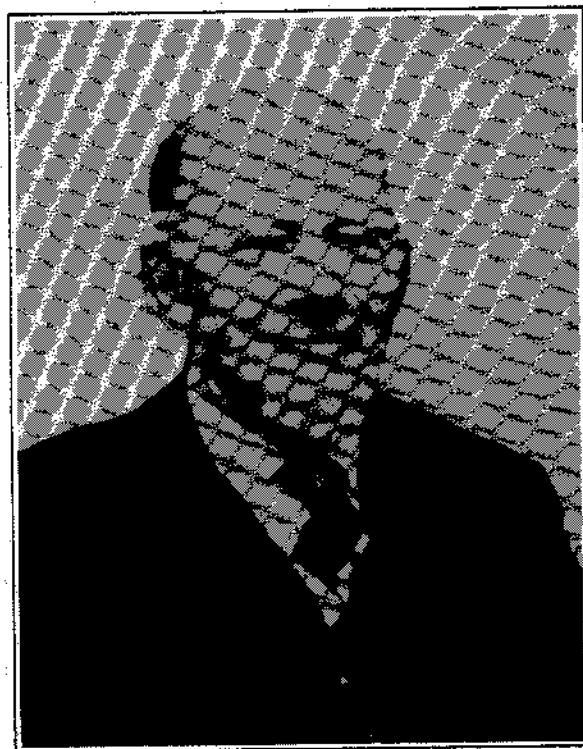
With the passing of Ludwig Lachmann, subjectivist economics has lost one of its great pillars. Lachmann was born in Berlin on February 1, 1906. He died in Johannesburg, South Africa, on December 17, 1990. In the interval the economics profession enjoyed the attentions of an extraordinary mind. He was the guiding light and inspiration to a generation of radical subjectivists inside and outside the Austrian school. He was one of the great old men of the profession and his passing is a painful loss. Those of us who had the fortune to meet and know him will also feel the painful loss of a special personality.

I remember being a graduate student at New York University during the years in which Lachmann was a member of the Austrian colloquium. We were lucky to have Lachmann's stimulating presence. He created an extraordinary intellectual atmosphere of scholarly seriousness and purpose.

Ludwig Lachmann and Israel Kirzner had been friends and allies for years. But they could not agree on certain fundamental points of social science. Every week at the seminar table we were confronted with the conflict between these two leading Austrians. Our thinking was shaped by this conflict. We were brought into serious discussion of fundamental issues. Even the students who rejected Lachmann's position were shaped by his presence. They had to know why they rejected his position and they had to defend their own views against the doubts he raised. To be students in such an environment was incredible good luck. It is the lot of most graduate students in economics, however serious, to be preoccupied with passing exams and learning mathematics. We were learning economics and participating in serious discussions with some of the best minds in the profession.

Lachmann was always available for discussions with graduate students. He encouraged us to apply our minds to the issues of economic theory. We were thinking, challenging ideas, and being challenged. Lachmann taught us what the leading problems of economics theory are. He pursued them with undeviating attention.

Lachmann's career as an economist began in his native Berlin during the years of the Weimar Republic. In 1924 he enrolled in the University of Berlin where Werner Sombart would become his



Ludwig M. Lachmann

dissertation advisor. As a member of the 'younger historical school,' Sombart had a respect for the ideas of Max Weber and a distaste for the Austrian school. Luckily, while a student in Berlin, Lachmann hired Emil Kauder as his tutor. Studying both Pareto and the Austrians, they came to view the subjective theory of value as essentially correct and the general equilibrium theory of Walras and Pareto as inadequate. Thus, Lachmann ended his studies in Germany an adherent of both the method of understanding (*verstehen*) practiced by German interpretive sociology and of the Austrian theory of marginal utility.

The intellectual position to which Lachmann was led by his studies with Kauder was hardly welcome or natural in German academic circles. The German historical school had always been hostile to the Austrians. Moreover, Lachmann was a liberal and, in his own words, "support for, and understanding of, the market economy, never very strong in these circles, had almost vanished" by the late twenties.¹ Lachmann was to spend most of his professional life defending positions that were dismissed out of hand by academic orthodoxy.

Lachmann, twice damned as both Jew and liberal, left Hitler's Germany for England in 1933. There he studied under Hicks and Hayek at the London School of Economics. In London, he

met another student of Hayek, George Shackle. But it was not Shackle who taught him the importance of expectations in economics. It was through his contacts with another refugee scholar, Paul Rosenstein-Rodan, that Lachmann learned the importance of expectations. Rosenstein-Rodan had been an assistant to Hans Mayer, who held Menger's chair in the University of Vienna. "It was Rosenstein-Rodan," Lachmann once explained, "who in discussing Austrian trade cycle theory with me said, 'Ah yes, but whatever happens in the business cycle is in the first place determined by expectations.'"² The subjectivism of expectations was to become a peculiarly Lachmannian theme.

In the early thirties, Hayek's thought dominated discussion at the LSE. The Great Depression put an end to that. Keynes had the right medicine. Or so it seemed. Hayek and the Austrians were eclipsed. Hicks, Kaldor, Lerner, and Shackle were all swept away by the Keynesian tide. Even Robbins quietly distanced himself from his early indiscretion, the Mises-Hayek theory of the trade cycle. As Walter Grinder has put it, by the time the war was on, "the only consistent and thoroughgoing Hayekians left were Lachmann and Hayek himself."³ Lachmann found himself in considerable intellectual isolation once again, just as in Berlin before.

After a fellowship which permitted Lachmann to visit many schools in the United States including the University of Chicago where he participated in Frank Knight's seminar, Lachmann taught at the University of London and then the University of Hull. In 1949, he was appointed to the chair in Economics and Economic History at the University of Witwatersrand in South Africa. During these years he developed his radical subjectivist position with a marked constancy of purpose. This steadfast cleavage to Austrian principles doomed him to relative obscurity.

The renaissance of the Austrian school began with the South Royalton, Vermont Conference in 1974 at which Lachmann was an attendee. A program in Austrian economics was begun under the direction of Israel Kirzner and soon came to be centered at New York University. At Professor Kirzner's invitation, Lachmann was brought to NYU in 1975 as a visiting research professor. Until 1987 when his health prevented it, Professor Lachmann travelled each Spring to NYU to participate in the Austrian Economics Colloquium and give a seminar on "Topics in Advanced Economic Theory."

In these final years Lachmann's patient exposition of the radical subjectivist views finally received the sort of attention it deserved. Young Austrians

were not the only students coming under his influence. Post Keynesians and other opponents of neoclassical orthodoxy also discovered him. It is a sure sign of the influence he exerted that his students even spent time learning to imitate his voice and gestures.

It is widely recognized that Lachmann was a radical subjectivist who believed that "expectations are as subjective as preferences."⁴ It is less widely recognized, I believe, how he was led to this conviction. In *The Legacy of Max Weber*, Lachmann proposed to replace Max Weber's "ideal type" with the concept of "the plan" as the foundation for social science theorizing. Citing Alfred Schutz, Lachmann argued that the possibility of interpreting human action by "revealing the plans which guide it" constituted both "the foundation of the method of interpretation" and "a vindication of the plea for the methodological autonomy of the social sciences."⁵ If we graft to this branch of thought G.L.S. Shackle's emphasis on the creativity and spontaneity of the human mind, we come close to Lachmann's own position.

Weber built on the ideal type. Mises built on the categories of action. Hayek employed the concept of rule-guided action. Lachmann shifted the focus from action to plan. This shift draws one's attention to the fact that the plan is an emanation of the spontaneous activity of the mind and cannot, therefore, be predicted. It is, I believe, this shift from action to plan that led Lachmann from the subjectivism of ends to the subjectivism of expectations. The questions and difficulties raised by this shift formed the subject of his own research. They play the same role in the work of many of his students and admirers. We no longer have the benefit of his guidance, but we will continue to work on the problems he taught us to recognize.

Professor Lachmann leaves behind a worthy legacy. In addition to a substantial body of writings, he leaves behind a generation of economists who feel for him the deepest respect and gratitude. But no legacy will negate the loss. Professor Lachmann is gone and his extraordinary mind with him. We will miss him.

¹"Forward" to Ludwig von Mises, *Epistemological Problems of Economics*. New York: New York University Press, 1981.

²"An Interview with Ludwig Lachmann," in *The Austrian Economics Newsletter* (Fall, 1978).

³"In Pursuit of the Subjective Paradigm," Introduction to Ludwig Lachmann, *Capital, Expectations, and the Market Process*. Kansas City: Sheed Andrew and McMeel, 1977.

⁴*Ibid.*, p. 15.

⁵*The Legacy of Max Weber*. Berkeley: Glendessary Press, 1971, p. 30. ■

The Collected Works of F. A. Hayek An Update

The third volume of *The Collected Works of F. A. Hayek* will be published this spring by Routledge and the University of Chicago Press. Edited by the late W. W. Bartley, the founding editor of the project, and Stephen Kresge, the new general editor, this volume is titled *The Trend of Economic Thinking: Essays on Political Economists and Economic History*. It is a new collection of essays by Hayek, several previously unpublished and a few translated for the first time. The core of the volume is four essays on English and Continental monetary history and policy, written in German in the 1920s as part of a larger project when Hayek was director of the Institut für Konjunkturforschung (Austrian Institute for Business-Cycle Research). Hayek never finished the larger project and the essays were never published; he later turned the rest of his notes over to his research assistant Vera Smith (later Lutz), who used them in preparing her now-classic *Rationale of Central Banking* (just reprinted by Liberty Press).

The Trend of Economic Thinking is the second volume of the *Collected Works* to appear in print (though it is labeled as volume 3), volume 1 being *The Fatal Conceit*. Volume 2, *The Uses and Abuses of Reason, The Counter-Revolution of Science and Other Essays*, has been delayed and will most likely come out in 1992.

In addition to the articles published in 1952 as *The Counter-Revolution of Science* this volume will contain some related essays and may include selections from Hayek's long correspondence with the philosopher Sir Karl Popper, his longtime colleague and friend. The fourth volume, *The Fortunes of Liberalism: Essays on Austrian Economics and the Ideal of Freedom*, edited by Peter Klein of the University of California, Berkeley, and the Mises Institute, has been completed and is presently under review by the publishers. This volume gathers Hayek's writings on the Austrians (including seven essays on Mises) along with some material on the rediscovery of liberalism in postwar Europe and the Mont Pèlerin Society. As with volume 3, almost half the contents have not been published before or are presented for the first time in English.

The Collected Works, projected at around 19 volumes in all, will continue with further collections of short essays and reviews, reprints of Hayek's existing books, and correspondence and interview volumes, drawing on the resources of the Hayek papers at the Hoover Institution archives at Stanford University.

The manuscripts for many of these volumes are already in the hands of established scholars in the various fields in which Hayek wrote. Lawrence White of the University of Georgia will edit *The Pure Theory of Capital*; Antony Flew of Bowling Green State University will edit *Law, Legislation, and Liberty*; Chandran

Kukathas of the University of New South Wales, author of a book called *Hayek's Liberalism*, will edit *The Constitution of Liberty*; Jeremy Shearmur of the Institute for Humane Studies will edit a collection titled *Philosophy, Politics and Economics*. ■

"Eastern Europe: Mises Was Right"

Leland Yeager, the Ludwig von Mises Professor of Economics at Auburn University, organized twin sessions at the Southern Economic Association and American Economic Association meetings on the economics of Ludwig von Mises and the lessons of Eastern Europe.

At the 60th Annual conference of the Southern Economic Association (November 18-20 in New Orleans) the session was titled "Eastern Europe: Mises Was Right." Papers were presented by Murray Rothbard ("Ludwig von Mises and the Collapse of Socialism"), Gertrude Schroeder Greenslade of the University of Virginia ("The Dismal Fate of Soviet-Type Socialism"), and John Moore of George Mason University ("Yugoslav Socialism"). All three papers concluded that socialism was a dismal failure and that Ludwig von Mises was on the mark with his critique of socialism.

The three discussants were Roger Koppl of Fairleigh Dickinson University, Aubrey Drewry of Birmingham-Southern College, and James Dorn of Towson State University and editor of the *Cato Journal*. The discussants did their best to draw further lessons, to assess the agreement with Mises's views in the world today, and to interject controversy. For example, Koppl, Rothbard, and others skirmished over the question of whether socialism were possible in a theoretical world (rather than the real world).

The session at the American Economic meetings (December 28-30, Washington, D.C.) was also well attended and expanded with the presence of Yuri Maltsev of the U.S. Institute of Peace and the Ludwig von Mises Institute as an additional panelist.

The session, retitled "Eastern Europe: Perspectives of Austrian Economics," found presenters and discussants alike searching for the implications of Mises's ideas and their impact on the future course of events. ■

Market Process to Suspend Publication—Praxis to Continue

The Center for the Study of Market Process has suspended publication of *Market Process*. In the spring of 1990, volume 8 of the *Market Process* newsletter was issued in an expanded, journal-like format. No

further issues have been produced to date and no further issues are planned.

The hurdle from newsletter to journal status is a costly one, as editor Don Lavoie noted in the first issue. In that issue he requested that readers subscribe to *Market Process* in order to defray the additional costs of the journal. Academic journals are not only extremely costly, they are time consuming and there is tremendous competition for good articles and good reviewers.

The Center plans to continue the publication of *Praxis* which will provide information about the activities of the Center and developments in "market process economics." In other developments, the Center marked its 10th anniversary with a celebration dinner on November 10th, 1990 and has announced that Professor Walter Williams of George Mason University will be the new chairman of the Center's board of directors. ■

Book Reviews

Breaking the Banks: Central Banking and Free Banking Solutions

Richard Salsman

Great Barrington, Mass: American Institute for
Economic Research, 1990

Business cycles, chronic inflation, and now the S&L crisis; these dramatic failures of the central banking system have vaulted free banking into the academic mainstream. The history and theory of free banking is now regularly debated and discussed in the top monetary journals. Richard Salsman, a New York city banker and graduate of the NYU economics program, has extended, reviewed and summarized the most important historical and theoretical aspects of this literature for an audience who will be crucial players in the coming policy debates: the bankers.

Breaking the Banks, which contains a lengthy annotated bibliography, is a good introduction to the free banking literature. The main contributions, however, flow from Salsman's perspective as a banker.

After a short introduction, on the importance of sound banking for a healthy economic system, Salsman explains the standard measures of commercial bank stability. These are: (1) capital adequacy, (2) asset quality, (3) liquidity, (4) profitability, and (5) management quality. Chapter three then looks at the theory of central banking and its effects on commer-

cial bank stability in terms of the above indicators.

Chapter four examines, from the same perspective, the historical record. Chapter five introduces free banking theory and the likely effects of free banking on the banking system. And chapter six examines the historical record in this regard. Two following chapters tie up loose ends. In the final chapter Salsman criticizes recent reform proposals and outlines his own plan for the transition from central banking to free banking and the establishment of sound money (he thinks monies would be largely based on gold under free banking).

A brief overview of Salsman's analysis of the effects of central banking on capital adequacy reveals the type of issues *Breaking the Banks* is concerned with. The excess of assets over liabilities is the value of the bank to its owners, the shareholders. This equity capital "serves as a cushion to absorb operating losses and asset (primarily loan) defaults" (p. 9). Therefore, all else being the same (such as riskiness of assets) the lower the equity-capital the greater the possibility of insolvency.

The amount of equity-capital tends to decline in a central bank system. In banking as in all industries the tax deductibility of interest expenses, but not dividends, encourages the use of debt rather than equity. But the banking industry is encouraged to debt finance in a number of additional ways. For example, one advantage of equity over debt financing is that debt financing carries the burden of possible bankruptcy (failure to pay bondholders their contractually agree upon interest payments). But deposit insurance and lender of last resort privileges reduce the possibility of bankruptcy even if insolvency occurs. Under the "too big to fail" doctrine the central bank effectively guarantees that a big bank will never face bankruptcy. These factors subsidize debt financing, reduce the use of "cushioning" equity-capital and thereby increase bank risk.

Most fundamentally, the very purpose of central banking is to inflate the money supply at a rate exceeding that of real growth. Because of the intimate connection between money and credit this means that deposits and loans are created faster than real capital is accumulated in the economy. A bank could raise more equity and refuse to increase its loans and deposits in order to maintain a high equity-capital to asset ratio but in a central bank system with guaranteed deposits the return from doing so is artificially low, making such actions uncompetitive. Capital adequacy invariably declines under these conditions.

Some trenchant criticism of current reform proposals like private deposit insurance are made in the final chapter. Salsman argues that "government deposit insurance is inherent in a central banking system because central banking creates systematic weakness and instability in the industry. No private sector insurance industry would be willing or able to underwrite such risk" (p. 129).

Given the present mixed system, unfortunately, Salsman is incorrect when he says that a private sector insurance industry would be unwilling to underwrite bank deposits. In my judgment the industry would be more than happy to write such insurance even though they would be unable to do so in the long run, as Salsman correctly points out. The problem is that regardless of whether or not there is private insurance, the central bank (and ultimately the government) will continue to act as lenders and guarantors of last resort. The only difference is that under a private insurance scheme they will have to guarantee the insurers. The insurers will know this in advance and will themselves face the same incentives the banks face under the present system—risk is effectively subsidized so insurers will extend insurance to banks at uneconomically low prices.

Private insurance in a central bank system is potentially worse than the present system. First, the private, free enterprise aspects of the system will be blamed for the crash when it eventually occurs. Second, under a private insurance system a single insurance firm will insure many banks. If one or several of these banks becomes insolvent, insurance will be handled in the private sector. But sooner or later many banks will become insolvent at one time, the private insurance system will go bankrupt and the government will have to intervene. A large infrequent crash of this sort may be worse than many smaller but more frequent shocks. The government could promise never to bail out a private insurance system but this promise is not time consistent and therefore not credible.

Loosening restrictions on the fields banks may enter raises further problems. If banks become more closely intertwined with commerce and industry, and deposit insurance continues to exist, whether it be that of the FDIC or some sort of private/central-bank mix, then the possibility of cross subsidization occurs. Through careful manipulation the insurance system—which is nominally intended to protect bank deposits—may end up protecting business ventures. Monitoring and regulation may offset this to some extent but excessive regulation is the problem privatizing insurance was supposed to solve.

This analysis accords with the general tenor of Salsman's own, as he puts it, "the FDIC supports regulation on the grounds that it must protect the deposit fund. The Federal Reserve supports regulation on the grounds that it must protect the money supply and control bank access to its discount window. Central banking is a package deal... To oppose regulation effectively, it is necessary to oppose the basic features of central banking that make it necessary... We will continue to have unsound banking as long as we have unsound money and we will continue to have unsound money as long as we have both government money and unlimited government" (pp. 129-30). ATT ■

Economic Policy and the Market Process: Austrian and Mainstream Economics

K. Groenvelde, J. A. H. Maks, J. Muysken
Amsterdam: North-Holland, 1990

Everybody likes to see rigorous exchanges between scholars of different economic schools on public policy. Although an attempt to do that, the result of *Economic Policy and the Market Process* is less than fully satisfying. The problems: (1) the editors are largely outsiders to the Austrian tradition and are not as conversant in Austrian literature as one has come to expect after 120 years of subjectivist-marginalist thought, (2) the mainstreamers are not mainstreamers at all but unreconstructed social democrats remarkably unsympathetic to the language of market economics, (3) no discussion arises as to the political theories of the contributing social democrats, and (4) the organization of the book leans toward incoherence.

The collection is not without its redeeming values, however. It contains some excellent individual contributions by three Austrians (Israel Kirzner, Don Bellante, Pascal Salin), one proto-Austrian (Roland Vaubel) and one Chicagoite (Yale Brozen).

It also contains a fair number of intellectual amusements along the way, for example, the utter naivete of social democrats who place as much faith in the voting mechanism of democracy as communists do in central planning. It would be a shame if the book's real contributions are forgotten in the thick of such amusements.

The editors recognize that Austrians represent the most thorough refutation of social democracy. (Unfortunately, they are incorrect in seeing it as the most prominent.) In this volume, the Austrian wins the debate in every case on merit only. What else can be said, for example, about a radical and persuasive case for free banking (by Vaubel) coupled with a reply written by an employee of a central bank who concludes that "countries are well-advised to stick to the practice of granting a legal monopoly to their central banks" since "modern central banks are very aware of their public function" (pp. 290, 300)? If a real economist is to debate the failures of public housing, he should prefer to have a HUD bureaucrat as his opponent.

The editors provide a sympathetic summary of Austrian economics in their introduction. They fairly represent the dynamism of the Austrian model, the emphasis on change and uncertainty, and the important role for price signals, the de-emphasis on aggregate analysis, and the policy implications that follow from these positions. But they gloss over real internal controversies, such as the role of equilibrium and entrepreneurship, and hardly mention important considerations of methodology as a unifying theme.

In his contribution, Kirzner helps to correct for the failings of the editors. In 16 pages he summarizes

the essence of the Austrian paradigm and what he regards as his most important contributions to it. Thus he covers how markets work, questions of equilibrium, discovery and entrepreneurship, prices and profits, competition and monopoly, socialism and calculation, and the perils of regulation. His article is a model of economic coherency, a short and integrated presentation of the Austrian position (although he too neglects method).

In response to Kirzner, we witness an unsympathetic Angus Maddison (University of Groningen) complaining that Kirzner's paper is so "abstract" that it makes "no reference to contemporary economic problems of a kind you might find in an OECD report, a budget speech, or a central bank report." Maddison wonders where Kirzner's discussion is of macroeconomic considerations like "GDP Growth Potential" and "Transparent Redistributive Policies," the absence of which is supposed to make one wonder whether Kirzner is doing economics at all. And the worst crime of all: "There is no empirical evidence" (p. 40).

If empirical evidence is what these "mainstreamers" want, then Yale Brozen's (University of Chicago) contribution offers an overwhelming, 41-page, purely empirical case for the market with 79 footnotes demonstrating the failure of interventionism. Alas, social democrat Arnold Heertje (University of Amsterdam) is not impressed. He is "struck by [Brozen's] emphasis on empirical results," but displays an Austrian's skepticism of such results: "it would not be too difficult to produce evidence which just 'proves' the opposite of what Brozen likes to indicate" (p. 107).

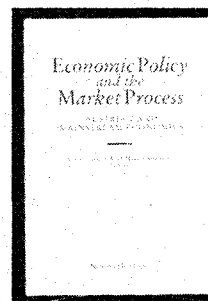
J. A. Kregel, a post-Keynesian, next argues that the most important goal of economic policy is to restrain "unbridled self-interest" through "market design" and policies to "assure the constricting forces of competition" (by which he means carving up market lots according to a government plan). Groenveld responds by reminding Keynesians of the entrepreneurial penchant for adjusting their behavior to regulations and thus evading the law's intent.

H. W. de Jong offers a contribution to the theory of competition using the policy of the European Community as the backdrop. Entirely ignoring recent work by Austrians and others against "competition policy," he proceeds to offer a very long litany of alleged crimes against competition that the government ought to rigorously prosecute. As draconian as the EC's monopoly policy is, de Jong wants more. Brozen responds with a theoretical argument against any restrictions that would end up "protecting competitors, not competition" (p. 142), and Stephen C. Littlechild (University of Birmingham) offers a small piece showing the difficulties associated with distinguishing efficient mergers from inefficient ones.

The Austrian theory of labor markets is thoroughly and persuasively presented by Don Bellante (University of South Florida). His respondent is so-

cial democrat P. Keizer (University of Limburg) who presents the most naive case for democracy seen in years. For him, the proof that welfarism, unionism, and wage policies work is in that such institutions are "produced" by the democratic process and are *therefore* socially optimal. "Democracy should imply above all else a respect for decision taken by majorities" (p. 168), he says, because "democracy is the most progressive discovery process for the production of collective goods" (p. 170).

Pascal Salin tackles the issue of business cycles from an Austrian point of view (citing Hayek, Mises, Rothbard and Garrison) and does an outstanding job of it. He is careful to distinguish his position from that of the monetarists who overlook intertemporal coordination problems associated with even marginal central bank monetary expansion. The respondent, J.C. Siebrand (Erasmus University) has a difficult time with Salin since "I must confess I do not recognize the world in which we live in the picture he sketches. His world is very abstract" (p. 227).



The final Austrian-oriented contribution is by Roland Vaubel, who argues for competition in currency and against the theory that money is a public good. Most notable is his argument against all government intervention in the supply of money.

What is never explicitly dealt with in this volume, but nonetheless constantly lies beneath the surface, is the apparent political agenda of the "mainstream" economists. While the Austrians struggle to maintain the standards of value-free science, in objectively spelling out the consequences of intervention, the social democrats advance views as if their economic theory and their political agenda were one in the same.

When two world views clash, as Austrian economics and social democracy do, it would have been in everyone's interest to have the Austrians directly take on what lies at the root of their opponents' views: the idea of equality. It is their egalitarianism, which is never argued for but only asserted, which supports their faith in democracy. The Austrians should have a chance to ask whether the democratic regime invariably produces a mixed economy; if so, what type of political regime is necessary to support an Austrian economic program? Without such frank discussion, there can be no meaningful exchange of views. There

will only be bantering between one group presenting a corpus of economic thought and another asserting a political program. JAT ■

Taxpayers in Revolt: Tax Resistance During the Great Depression

David T. Beito
Chapel Hill: University of
North Carolina, 1989

Franklin D. Roosevelt's New Deal government is usually thought of as a force for economic liberation. But there is another side to the story, as told in this important revisionist work by David T. Beito. He shows an aspect of the government apparatus not usually noticed, that of the oppressor of the common man in his struggle to pay his bills. There's not much economic theory here, but it helps support the case for the free economy.

The tax strike is a fierce weapon because all government ultimately relies on the consent of the governed; the public must pay the taxes and obey government dictates. The strikers of the early 1930s exhibited a distrust of maneuverings of politicians and bureaucrats. Their goal: to prevent a political power grab by placing severe constraints on government spending.

Taxpayer groups sprang up in every major city around the country, and Beito documents the major cases. Especially notable is the case of Chicago where a taxpayer group sent the local government looking to Congress for a bailout. The Chicago strike, says Beito, was "the biggest concerted tax strike since the aftermath of the Revolutionary War."

Tax problems and scandals were pervasive in Chicago during the twenties, and the citizens had become cynical about the nature of politics. By the time the depression hit, the public was ideologically primed to strike. Because of widespread complaints, in 1928, the city agreed to reassess property taxes, and taxpayers got a two-year tax holiday. Two years later, the government ordered the public to pay the stalled taxes—three years of taxes due in a sixteen-month period. The Chicago tax strike began.

The flagship of the ensuing strike was the Association of Real Estate Taxpayers (ARET), which had a paid membership of 30,000 at its height. ARET's leaders, although newly wealthy, were not part of Chicago's business, governmental, or banking elite and they effectively represented the interests of the 30,000 pending appeals from taxpayers who had not paid their property taxes. By 1931, though, only 55 percent of the total levies had not been collected before the penalty date. A year later, the city had become helpless. Officials actually considered shutting down the public schools. In 1932, they went to Congress begging for financial help.

As the number of strikers mounted, the media closed ranks against ARET, with the Chicago *Evening Post* declaring that non-payers had "shirk[ed] the responsibilities and duties of citizenship." The radios and newspapers shut out pro-tax strike ads and messages; yet they ran ads promoting the government's "Pay-Your-Taxes" campaign.

Powerful local bankers now depended on tax money, like First National Bank of Chicago chairman Melvin Traylor who led the fight to smash the strikers. "The whole situation goes back to the fact," Traylor argued, "that you can't run a government unless the people pay their taxes." He might have added that neither can one run a municipal bond-holding bank without taxes.

The Chicago strikers were ultimately undone. The government hit the high-profile leaders of the movement, turning off their government-supplied water, taking their business licenses, and revoking their permits for electric signs, driveways, and use of government property (sidewalks and streets). The government won the propaganda battle. And it had the force of law. But the Chicago strike was unusually successful in that it held off the revenueurs for two years.

Beito is alert to how Great Depression tax revolts illustrate libertarian class analysis. The tax strikers were, by and large, middle-class people trying to pay their bills. Those who propagandized against the strikers were the upper-class social elite, including public-school teachers, bureaucrats and politicians, entrenched corporate interests, the banking industry and other bond holders.

What motivated the strikers? Professor Beito offers a theory. "It was not so much that taxpayers... cynically adopted an anti-big-government pose when the depression cut into their incomes," he says. Rather, "the depression forced taxpayers to think for the first time about the burden and perforce the purpose of high taxes." They became—in the popular term of the period—"tax conscious."

The tax revolt died after 1933. Why did the movement fail to achieve its most radical ends? First, many taxpayers got relief. Second, New Deal ideology overwhelmed its few opponents. Third, tax strike organizations were rife with internal disputes that crippled them. And fourth, leaders developed a propensity toward ideological sellout.

As powerful as these four factors were historically, there is also a more important institutional reason tax revolts fail. Strikers will always run up against the familiar problem of the Prisoner's Dilemma: to succeed, everyone must rely on everyone else's cooperation, despite incentives pushing everyone toward defection. If mutual trust slips even a little bit, the whole cooperative pact can unravel. This kind of Prisoner's Dilemma is tough to overcome in absence of profound moral courage.

Professor Beito has assembled reams of pathbreaking research into an extraordinary work that is also a joy to read. It invites a totally new understanding of those watershed years. Perhaps not unwittingly, it also constitutes a radical case for private property against encroachments by the state and its connected interests. JAT ■

Book Bites

Austrian Economics

Edited by Stephen Littlechild
Edward Elgar: 1990

This 3-volume set represents a valuable addition for those doing serious research in Austrian economics. Stephen Littlechild has collected 93 entries divided into 14 sections and 3 volumes. This collection is yet another statement of the splendid history, strong resurgence, and bright future of the Austrian school of economics.

Littlechild's selection of articles is not and was not intended to be a "greatest hits" of Austrian economics. Articles which have been extensively reprinted or were readily available from other sources were avoided in lieu of articles more difficult to obtain or published in unusual places. Other entries could not be included because permission to reprint could not be obtained or they were too costly to obtain.

This is not to imply that all of the classics are absent. Hayek's "The Use of Knowledge in Society," Menger's "The Origin of Money," Mises's "Economic Calculation in the Socialist Commonwealth," Rothbard's "Towards a Reconstruction of Utility and Welfare Economics," and many other famous contributions are included. Many articles are from foreign sources, and newsletters such as the *Austrian Economics Newsletter*, excerpts from books, and reference works.

One result of these limitations and guidelines is that the collection is weighted in the direction of the ultra subjectivists, Ludwig M. Lachmann and G.L.S. Shackle, as well as the contributions of Friedrich von Weiser, whose work American Austrians have shown a reluctance or aversion to. The set does contain a good sampling of the contributions of the latest generation of Austrians—Don Lavoie, George Selgin, Larry White, Mario Rizzo, Hans Hoppe, Richard Ebeling, Karen Vaughn, Jack High, Roger Garrison, and philosopher/economist Barry Smith.

The most entries (12) come from F.A. Hayek. Kirzner has 11, Mises and Lachmann have 7 each and

Rothbard contributed 6.

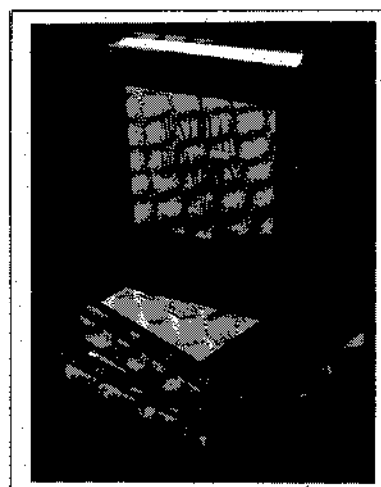
Each volume has an identical preface and an introduction which briefly discusses many of the individual entries, their significance, and the related body of literature. Each introduction contains a list of references and further reading which enhances the research value of the collection.

Volume 1 covers the history of Austrian thought and methodology. The first two parts are on "The Early Austrian School," and "The Austrian School Founders." A third section called the "Modern Austrian School," contains Hayek's Nobel Lecture, but is otherwise unfocused. This is then followed by two important and extensive sections on "Subjectivism" and "Methodology." Of particular note in this volume are three papers which discuss Mises's seminar, and papers on the debates on subjectivism, empiricism, and even hermeneutics.

Volume 2 covers macroeconomics. The sections include "Capital and Interest Theory," "Money and Banking: The Nature of Money," "Money and Banking: Public Policy," and "Business Cycles and Macroeconomics." Together with the references for further reading this volume provides a good overview of Austrian "macroeconomics."

Volume 3 opens with three parts on "The Competitive Market Process," dealing respectively with "Equilibrium, Market Process, and Competition." The 18 entries highlight the Austrian school's emphasis of the role of competition and market processes. This is followed by a solid section of five articles on "Central Planning," and an interesting although disparate collection of seven articles on "Public Policy."

The articles are reprinted directly from the original sources. While this does result in an awkward appearance, and in some cases light copy, it does avoid problems referencing the articles. Given the mission and constraints of this project, Littlechild has supplied a valuable and well-balanced product. MR ■



**Klarheit und Methode: Felix
Kaufmanns Wissenschafts-theorie:
Studien zur österreichischen
Philosophie**

H. G. Zilian
Amsterdam: Rodopi, 1990

This is the first extensive treatment of the philosophy of the science of Felix Kaufmann (1895-1949), a philosopher and legal theorist close to Mises, Hayek and Alfred Schutz, and author of *Methodology of the Social Sciences* (Oxford: Oxford University Press, 1944). Zilian deals extensively with the issue of methodological individualism, with the theory of action, and also with the question of the *a priori* nature of economic laws, and he sheds new light on the detailed discussions of these matters in the Mises seminar in Vienna.

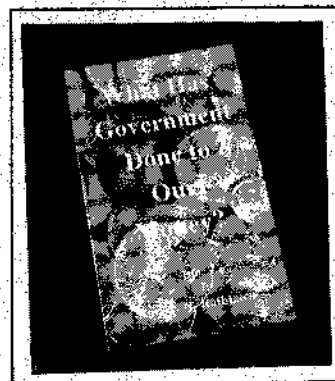
His work includes also a detailed critical treatment of Husserl's thinking insofar as this exerted an influence on Kaufmann, and the volume is of interest for its treatment of topics such as inner perception and synthetic *a priori* knowledge which served as point of contact between the Vienna circle and the phenomenological movement. The volume shows also how Husserlian ideas can be extended into the sphere of the social sciences, including economics and jurisprudence, and thus in this respect, too, it throws light on Misesian methodology.

The author is consistently contemptuous in his treatment of both Husserl and Mises, however, so that he rarely manages to give an adequate account of the inner workings of their ideas. Barry Smith ■

**What Has Government Done
to Our Money?**

Murray N. Rothbard
Auburn, Ala.: Ludwig von Mises Institute, 1990

Rothbard's famous essay on Austrian monetary and banking theory and policy is back, but this time in a beautiful new 120-page edition (with a spine so it won't slip to the back of the bookshelf). Although first published in 1963, and updated periodically, the content holds up remarkably well as an introduction to free-market monetary thought. Also added to this new edition are an introduction by Mises Institute president Lew Rockwell, and comments by Rothbard on the prospect for the European Currency Unit and the trend toward globally fixed exchange rates, both of which he sees as dangerous precursors to global inflation.



The opening section lays out the theory that money arose on the market out of barter and tends to take on definite forms according to its usefulness. All this is familiar to anyone who has had a first-year money and banking course. But what is different is his integration of money's origins to the development of banks as money warehouses. He sees no reason why free-market monetary institutions (including private coinage) couldn't be stable and efficient had the government not intervened in the market.

The government's motive for monopolizing currency and cartelizing banking is purely self-interest. In its desire for revenue in addition to taxation, it derives great benefit from expanding the money supply through a variety of means, including buying debt and lowering reserve requirements. The government must monopolize the currency in order to make this possible.

Most useful is Rothbard's 9-stage history of the monetary breakdown of the West. Starting with the classical gold standard of 1815, he takes us through to the present day to show how government has systematically undermined the gold standard to replace it with a fiat money standard. Most complete is his analysis of the breakdown of J. M. Keynes's Bretton Woods System of international money.

Clearly, a key attraction that Rothbard has toward a free-market gold standard is his belief that as long as the monetary system is in private hands, and the unit of account is clearly defined, the government cannot use it to enhance its power over the economy. Thus the acceptance of Rothbard's policy prescription (an established gold standard with 100% demand deposit reserves) relies on an acceptance of limited government and laissez-faire economics. For the free marketer, *What Has Government Done to Our Money?* is a testament to the essential radicalism and coherency of Austrian economic policy. It is good to have this gem back in print. RRH ■