

The Austrian

A PUBLICATION OF THE MISES INSTITUTE

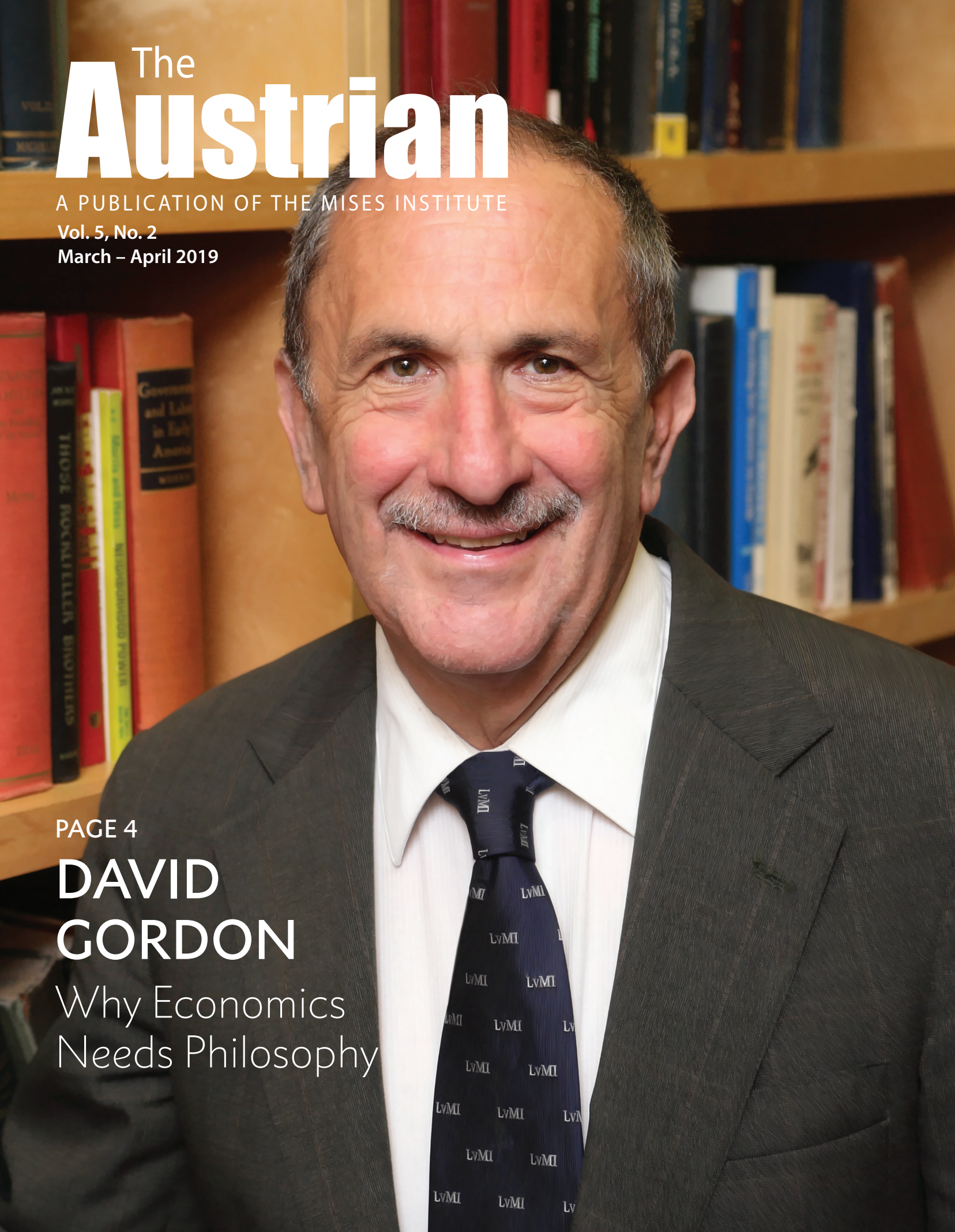
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DAVID GORDON

Why Economics
Needs Philosophy





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From the publisher

Jeff Deist

In 1974, the late Ayn Rand addressed a graduating class of new Army officers at West Point with a provocative talk titled “Philosophy: Who Needs It.” Note the lack of any question mark after the title; it’s a declaration which suggests we all do. To Ms. Rand it was abundantly clear the young men in the audience needed philosophy, and needed it urgently. The assumptions they had lived with until that day, assumptions governing their thoughts and actions, must be examined if they meant to become fully competent adults.

Not long after Rand’s death in 1982 a collection of her nonfiction essays was published under the same title as a challenge to the anti-intellectual tenor of her age. She thought philosophy presented essential questions for all serious people, not just high-minded intellectuals. In her view everyone needed philosophy to grapple with the nature of the world around them, to understand how humans acquire and process knowledge, and to address the morality of right and wrong. Without philosophical moorings, Rand’s fictional antagonists lived as irredeemably flawed “whim worshipers,” as men without purpose. Their lives were *ad hoc*. Her protagonists, in stark contrast, understood and applied philosophy as deeply relevant to their goals and actions.

Economics also needs philosophy, and of course the Austrian school of economics did not materialize out of the ether. Ludwig von Mises applied philosophy to his work perhaps more than any other modern economist, and by doing so created a framework unmatched by today’s “small” economics, to borrow Dr. Peter Klein’s phrase. Part One of Mises’s *magnum opus Human Action*, which many readers consider the “philosophical” portion of the book, deals with nothing less than the enormous problem of defining and refining an epistemological system proper to the social science of human action.

Praxeology, the methodology of economics Mises largely constructed, has clear epistemological and metaphysical foundations. Human reason and its applications, in particular the relationship between purposeful action, means, and ends, are at the core of Misesian economics. Axioms, understood through *a priori* knowledge, are the building blocks and starting point of economic knowledge. This epistemological grounding, which made Mises a “literary economist” in the eyes of his critics, stands as a rebuke to the empiricism that corrodes economics today.

Our feature interview with Dr. David Gordon gets to the heart of the philosophical thought of Mises and other great Viennese thinkers. What we call Austrian economics today was in part born out of rebellion against the German Historical school, which dominated legal and philosophical thought in nineteenth-century Germany. Historicists, anti-theoretical by definition, could not conceive of an economics that existed independently of general social knowledge. In fact — much like many western progressives today — they didn’t understand economics as a science at all, much less a discipline worth studying on its own.

But Menger and Mises knew economics could not be reduced to mere historical data collection, or to a rote study of personal and state finances. Economics is not a subset of history or sociology, but a robust study of humans and their

“The relation between reason and experience has long been one of the fundamental philosophical problems. Like all other problems of the critique of knowledge, philosophers have approached it only with reference to the natural sciences. They have ignored the sciences of human action.”

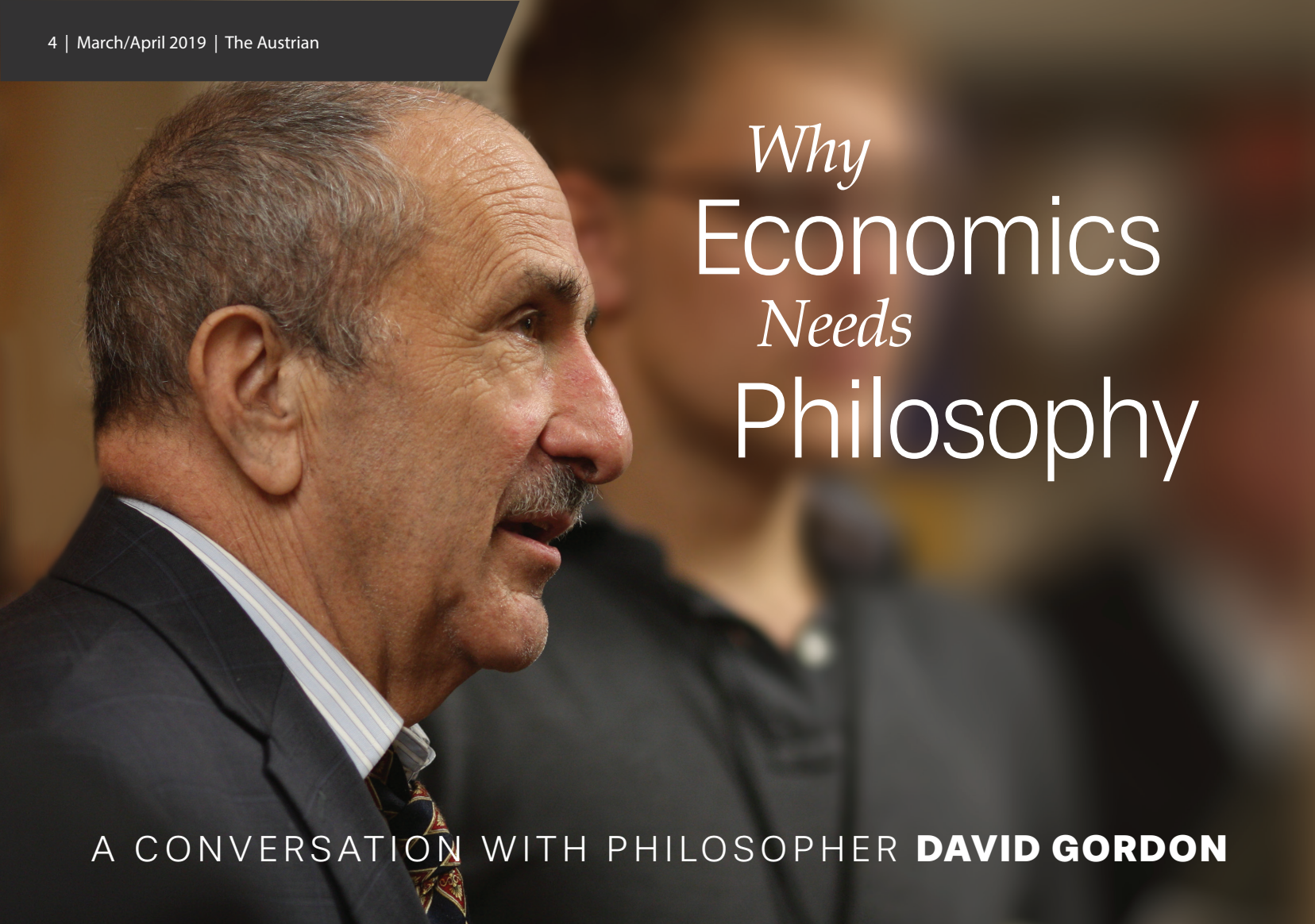
— Ludwig von Mises

means-ends choices. Austrians went beyond classical and neo-classical economics and built a modern edifice using praxeology, an edifice that stands and grows today. Thankfully we have David Gordon to help us better understand its foundations.

Dr. Gordon also contributes his regular book review, featuring the new title *Money and Government: The Past and Future of Economics* by Robert Skidelsky. Approaching the book with Murray Rothbard’s distinction between power and market in mind, Gordon tells us it’s clear Skidelsky favors the former. Money, markets, trade, and even war must be viewed through the lens of the state and its goals. But the author at least gives a nod to Hayek, and admits to the “intellectual corruption” and hubris of Keynesian policymakers.

We hope you enjoy this issue of *The Austrian*, and hope you stay connected and engaged with the Mises Institute. We have events planned later this year you won’t want to miss, including: a research conference in Auburn with Dr. Hans-Hermann Hoppe; a scholar’s conference in New York City at The Kings College; and a summit in Los Angeles at the wonderful California Club where Mises spoke in October 1944. Please join us! 

Jeff Deist is president of the Mises Institute.



Why Economics Needs Philosophy

A CONVERSATION WITH PHILOSOPHER **DAVID GORDON**

David Gordon is a Senior Fellow at the Mises Institute. He was educated at UCLA, where he earned his PhD in intellectual history. He is the author of *Resurrecting Marx: The Analytical Marxists on Exploitation, Freedom, and Justice*, *The Philosophical Origins of Austrian Economics*, *An Introduction to Economic Reasoning*, and *Critics of Marx*. He is also editor of *The Essential Rothbard*, *Secession, State, and Liberty* and co-editor of *H.B. Acton's Morals of Markets and Other Essays*. Dr. Gordon is the editor of *The Mises Review*, and a contributor to such journals as *analysis*, *The International Philosophic Quarterly*, *The Journal of Libertarian Studies*, and *The Quarterly Journal of Austrian Economics*.

JEFF DEIST: Does economics need philosophy? The idea of a school of economics having a philosophical underpinning might strike some people as odd. Why should economists care about philosophy at all?

DAVID GORDON: Well, that's a very good question. You see, what Mises held was that economics has a distinct method or way of proceeding, and he felt that way of proceeding was under criticism by many philosophers and social scientists of his time. I think for Mises, what was always primary was to vindicate economic theory against its detractors. He wasn't trying to construct a philosophical system. But if people criticized economics and said "well, there's something wrong with Austrian economics because it doesn't depend on verifying things empirically," Mises wanted to come up with a reply to that, so that was what really got him into philosophy.

JD: For purposes of this conversation, logic is a critical branch of philosophy. What should we think about rhetoric?

DG: Well, clearly logic is a branch of philosophy. It brings in all the sciences which use logic. Rhetoric is the general study of techniques of persuasion.

There are philosophers who have written about rhetoric, Aristotle and others, but that would be a somewhat broader category than they wrote about. To the extent you're interested in persuading others of the truth, you could consider economics rhetorical, but one point that people miss is when you're elaborating a structure of argument, it doesn't involve necessarily arguing in the sense of trying to have an actual debate where you have an adversary you're trying to win over.

JD: Let's start with Aristotle then. Can we trace a line from him to Menger, Böhm-Bawerk, and Mises?

DG: I think this is one point Murray Rothbard stressed very much. In the pamphlet I wrote called *Philosophical Origins of Austrian Economics*, I tried to elaborate upon that. I'm not sure everything I said in that pamphlet was right. What Aristotle thought was that in science we're really proceeding deductively from first principles. He says this in the *Posterior Analytics*. So, we start off with a fundamental principle. We're starting from what Aristotle thought: that there are essences of things and substances which means that the essence is the property something has that makes it that thing. Like "what is a human being?" It's a rational animal. Aristotle thought we could discern these essences and that's a theme you get in both Mises and Rothbard who started with the action axiom that human beings act.

Mises didn't really use an Aristotelian method, but Menger was very influenced by Aristotle. Menger studied philosophy with Franz Brentano, who was one of the great authorities on Aristotle of the nineteenth century. So Menger took a lot of his notion of method from Brentano who was this Aristotelian figure. And I think that Rothbard, in particular, argues that praxeology, the science of human action, could be understood in this Aristotelian way as knowledge of essences. It's a bit different from Mises, but I think it's a very valuable way to proceed.

JD: Modern economics, of course, doesn't start for several hundred more years. Menger doesn't publish his *Principles of Economics* until 1871. Talk about some

of the interim thinkers of the 1600s and 1700s. What about Locke? What was his influence on the Austrian school?

DG: Locke had a very interesting theory of knowledge that was a bit different from Aristotle's. Locke thought, like Aristotle, there were essences of things, but he thought we really can't know what they are. We're cut off from essences. So, we do have some knowledge. We can prove we exist. We know God exists. He thought we could derive ethics as some kind of deductive system and he also thought we know there is something behind our experience, but we can't really know what it was. So it's a much more skeptical view. But Locke certainly had influence on economics. Remember in *Human Action*, Mises talks about action as the relief of felt uneasiness.

Mises held that economics has a distinct method or way of proceeding, and he felt that way of proceeding was under criticism by many philosophers and social scientists of his time. That was what really got him into philosophy.

I think that comes from Locke. That's his phrase, "felt uneasiness." But Locke wasn't especially influential in Austrian economics. He had the labor theory of value as well as the labor theory of original acquisition, and that wasn't so influential with Austrians. I would say his influence on Austrians was much more in the area of political philosophy with his views on natural law and his particular defense of a somewhat libertarian view. In some respects, he was close to being an anarchist, with significant differences.

CONTINUED ON NEXT PAGE

JD: So we fast-forward to the 1700s. Talk about the German Historical school, which in part the Viennese economists rebelled against.

DG: The Austrians thought there are economic laws that are true for everybody. We have the law of supply and demand, which applies regardless of where you are in time. We could apply the law in primitive societies, we can apply it in the Middle Ages. Everywhere. The German Historical school said no, there are different stages of history and each stage would have its own laws that when you're investigating, economics, you're interested in the particular. One should amass as many facts as one can and maybe be able to get some inductive generalization about what applies to particular periods. So, it isn't that you can reason out things before, looking at

The Austrians thought there are economic laws that are true for everybody. We have the law of supply and demand, which applies regardless of where you are in time.

the empirical facts. You could find, for example, that free trade benefits certain economies at certain periods, but not in others.

The theories of Gustav Schmoller, Adolph Wagner, and various others were important. Schmoller was very influential in scholarship about the history of Prussia. He wrote a great deal on the Prussian economy. Mises's view of this was very interesting. He said, the real thrust of the Historical school's views is that they didn't like the idea that there were economic laws because this might limit what the state could do. Suppose, for example, we know by applying basic economic principles, that if you put into effect minimum wage laws, it's going to cause unemployment. So then, if you don't want unemployment,

you can't put in minimum wage laws. You shouldn't do that, but the German Historical school didn't like that and they said this is limiting the state. So, in Mises's view, they were trying to undermine economic theory to promote their ends.

JD: They're talking about economics as a historical discipline, with no universal laws or independent theory. It can't be studied independently of history and other fields. Menger and Mises reject this.

DG: Yes, that's right. Instead of thinking, as Mises did, there is a science that we can get just by thinking about our notion of action — trying to figure out what's involved in that — they said we have to study the particular. Some of them did very important work on particular historical periods, but they didn't believe in economic laws. So, they would say, we have to just study what's going on at the time. We might eventually be able to come up with some kind of generalization that would apply to different periods, but not for now.

JD: And the German Historical school still held sway, in Germany and the Austro-Hungarian Empire, well into the 1800s and even 1900s.

DG: Yes. They lasted through the twentieth century. One of the great figures of the school was Werner Sombart, whom Mises knew. They were on fairly friendly terms. He was teaching until 1930, when they were really dominant. When the German historians named the Austrian school as opposed to the German Historical, the term "Austrian" was coined with the implication that Austria was stuck in the past, the future was really with Germany and Prussia. So, if you say "the Austrian school," you're saying "outdated reactionary group," rather than progressive. They were certainly influential, not only in Germany, but they were very similar to a group in the US called the Institutionalists, who were very influential in the late nineteenth century and early twentieth century. There were even Austrians who were influenced by the Historical school. So, Mises had them very much in mind when he was writing *Human Action*, this was one of the main groups he wanted to oppose.

JD: Of course, there are two other Germans we need to consider, Hegel and Immanuel Kant. Both lived into the 1800s, but not by much. Talk about both these figures and their influence on Austrian thought.

DG: Kant said that in philosophy people hadn't agreed on what the correct solution is to the various philosophical problems, like how can we prove that God exists or how we know if there is an external world. So, there are all sorts of disagreements on all of these various philosophical systems. He said the philosophers have so far made a basic mistake. Instead of asking, "what is the nature of the world," what they should be studying is our knowledge. We should ask, "what are the categories that we use in trying to get knowledge?" And by thinking about that, then we would get some answers to the philosophical questions. For Kant, we can't know the world as it is in itself. All we can know is the world as we construct it through using our concepts. There is a given element also, which is intuition. You get to space and time through intuition and we apply concepts to that, so that gives us the world that we know, which he called appearance. That's the only world accessible to us.

JD: No wonder Ayn Rand called him evil. Constructing reality and using intuition certainly sounds very un-Randian.

DG: Oh yes, you know, she called him the machine gunner of the mind. There's something to be said for that and it does introduce some kind of a skeptical way of looking at things, but Kant didn't think he was a skeptic. He thought the world of appearances is the one we're dealing with. So we do have knowledge of that.

But there are various views on what the relation is between the world that we know, which is called the phenomenal world, and then this other noumenal real world. So, he then thought that limits our knowledge. However, we could go beyond that in a certain way because we also know we're ethical beings. We can recognize through reason that we have certain requirements, certain things we ought to do, just by thinking about them. He thought we could, from the concept of what we ought to do, get a notion of what was ethically required. This is his famous categorical imperative. When he applied this to his political views in practice to a large extent, it was reminiscent

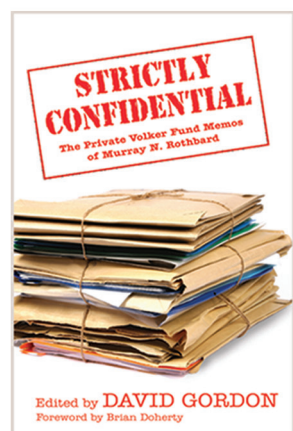
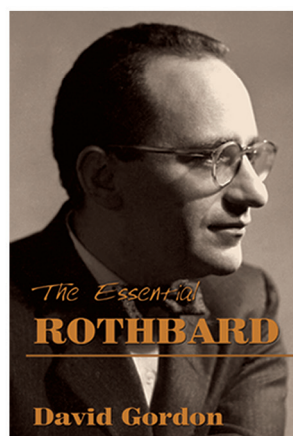
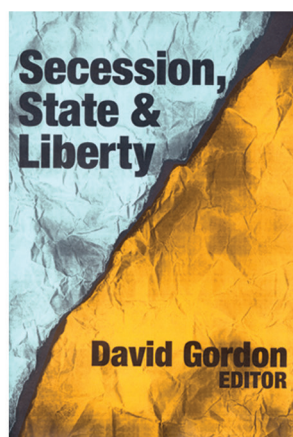
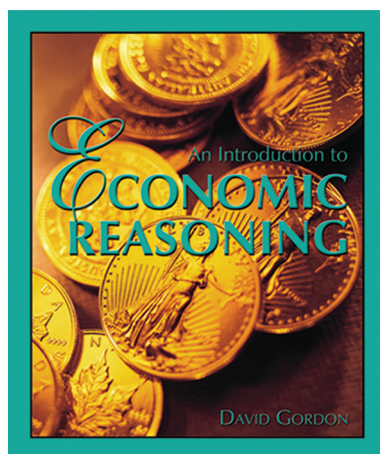
of classical liberalism. He believed in property rights and favored some sort of welfare state, but it would have to be very limited. He favored a peaceful foreign policy. He wanted some kind of federation of republics.

Now, Hegel reacted very much to this. He thought Kant was a great philosopher, but he said, "look, Kant is wrong in thinking that we're limited to our own concepts. We really do know the world as it exists." The mistake he thought Kant made was that Kant is assuming that there is some kind of separation between reason and the world. In fact, the world is rational, the world is reason developing itself, so there is no separation between the two and our minds are really just reason coming into consciousness. So, Hegel thought, that as the universe develops, rationality is increasingly coming to self-consciousness. And in ethics, in political philosophy, Hegel reacted somewhat against Kant. He said Kant is right that there is a sphere of freedom, but where he made the mistake is trying to come up with these abstract rules that were completely separate from the concrete lives of real people. In Hegel's view, this concrete life is manifested in the state. A famous sentence from one of his writings is, "The State is the march of God on Earth." That's not a very classical liberal state, although if you look at his main work on political philosophy, which is called *Philosophy of Right*, Hegel says that people are free to make exchanges. But this isn't freedom fully developed. It develops more when you have the state.

Hegel thought that up to this time, the Prussian state, as a limited monarchy, was the highest development of reason. He didn't claim this would always be true, but at that time, the Prussian state was the most advanced. Hegel was quite aware of economics. He read Adam Smith and James Steuart, who was an early mercantilist writer. But he didn't really develop an economic theory.

JD: Kant also discussed the importance of *a priori* knowledge, which is reflected in Misesian praxeology. How does Kant help us understand economics?

DG: In this way, suppose we get the law of supply and demand, thinking about who has a surplus or a shortage. But we know that minimum wage laws will result in unemployment. So then, if we can figure this out *a priori*, then we don't have to say, "well, this is just a hypothesis,



let me apply it to the real world and maybe it will turn out that minimum wages don't cause unemployment." We will be able to tell because we have this economic law that there will always be some effect from the minimum wage law. It may be that other things will override it, but we'll know that the law has some effect in the world. It isn't something that we have to investigate. So, the way it applies to economics is that it enables us to have a theoretical discipline that isn't subject to further testing. We can be wrong and make mistakes in our deductions, but we can't be wrong in the sense that it's open to future investigation whether our reasoning, even if it is correct, arrives at truth or not. If we reason correctly from true premises, then what we come up with is true, then that's it. That's unpopular with many philosophers.

JD: Contrast this with the logical positivists of Mises's time. His own brother, Richard, the mathematician, disagreed with him very strongly on method and logic for example. Give us the context of the time in which Mises developed his views, and the opposition he faced.

DG: There was a group of logical positivists, the Vienna Circle, originally headed by Moritz Schlick, who was a professor of philosophy at Vienna and a lot of the top philosophers of that time attended that group. They said there is *a priori* knowledge, but this is just really conventional, this is just definitions or parts of definitions. So, what they would say is, suppose I say something like this: "we choose our most highly valued preference." We have a preference scale, this one is the one that ranks highest, so I'm going to choose that. They said, "that doesn't tell you anything. That's a tautology because it's just saying you're choosing whatever one you're choosing. You're just defining the highest value preference is the one you in fact, choose."

For the Vienna Circle, if you want to know what's true in the world, the only way we can find out is by investigating, by doing empirical work. One example they might use: suppose one says, "how many people are going to attend the Austrian Economics Research Conference next month?" The way you would find out is to see how many people show up. We couldn't figure that out just by thinking about it. They have to find out by using their senses, their empirical senses, what actually is the case. But in the Austrian view — Mises's view — that isn't always true. Sometimes you can realize things have to be a certain way just by thinking about them. The positivists say no, if it isn't empirical knowledge, then it's a tautology. It doesn't tell you anything. So, they said, "if you want to know what's going on in the world, you just have to look at matters, investigate them." What you would get would not be what *has* to be the case, but just what *is* the case. "Laws" developed this way would really not be statements of what's necessary in this very strong sense that we have in other types of scientific laws like math.

JD: What would you say is Mises's best rebuttal to this? Where in his writings, whether in *Human Action* or perhaps in *The Ultimate Foundation of Economic Science*, does he lay out his best philosophical case for the method of economics? Where do we find his most philosophical work?

DG: Well, I would say probably two. The first, say, 110 or 150 pages of *Human Action*. The second chapter of the book is titled “The Epistemological Problems of the Sciences of Human Action.”

JD: I noticed to my surprise that Kant is not specifically mentioned in *Human Action*. Mises mentions him very briefly in *Liberalism*, but as you point out even when Mises resorts to Kantian language nothing in his argument depends on Kant. Elaborate on this for us.

DG: Suppose you don’t know the game of chess, have never heard of it and then you see people moving these pieces on a board and just see them moving them in various ways. You wouldn’t understand what’s going on unless you had the concept of chess, you wouldn’t be able to figure out what they’re doing. Similarly, we can see people moving their bodies in various ways, but we wouldn’t know what they’re doing. But, once we have Mises’s concept of action we can understand things. So, in that respect, that’s a Kantian idea that you have to have certain concepts in order to understand what’s going on in various activities. But Mises doesn’t depend on particular controversial points in Kant’s theory of knowledge by any means. He’s not adopting a Kantian system at all, I don’t think, even though Mises is a very widely read scholar in philosophy and other disciplines.

Nevertheless, it’s sometimes surprising the range of Mises’s knowledge. For example, in *Human Action*, when he’s talking about quantum mechanics, he says quantum mechanics has some implications for free will. So, he quotes works on quantum mechanics. He’s up on all sorts of things, but he isn’t adopting a particular school.

I should say also: One thing I see when I talk of *Human Action* over a great many years at the Mises Institute is that a mistake a lot of people make is, they think well, because Mises discusses philosophical topics, they think he’s trying to solve some philosophical problems. One problem is: how do we know that there is a real world out there? Maybe we just have certain experiences and you could imagine, Descartes’s malicious demon that’s

deceiving us, how do we know the world really exists? That isn’t a problem he is addressing, he’s not trying to solve problems of philosophical skepticism. It would be odd if we were saying how to explain the recession of 2008, it would be kind of strange to say, “well look, how can you talk about explaining the recession in 2008 when we haven’t even proved there’s an external world yet.” That wouldn’t make sense. So, we need to get he’s talking about the world we live in and he’s seeing economics as one of the sciences. It’s not part of philosophy.

Mises is not trying to solve problems of philosophical skepticism. He’s talking about the world we live in and he’s seeing economics as one of the sciences. It’s not part of philosophy.

He’s just thinking that there’s a particular method in science, an *a priori* method that we can use. This is one of his objections to Karl Popper, who was a philosopher also from Vienna, and had some connection with the Vienna Circle but reacted very strongly against them. But Popper had a view that a statement is scientific if it can be falsified. So, they say, well, economics, as Mises conceded, it wouldn’t be falsifiable because if these laws of economics were *a priori* truths, then nothing can show they’re false. What Mises said is if you’re trying to come up with what is scientific, you should look at the actual sciences in question. You should do that and take that into account in trying to come up with your criteria of what’s a scientific statement.

JD: Let’s talk about the philosophy of Murray Rothbard.

DG: Rothbard was a very systematic thinker. He was interested in a great many things, but Rothbard in his philosophical views, he had been very much influenced by Aristotle and Thomas Aquinas and he made a study of scholastic philosophy. So he adhered to this view where he studied the essences of things in order to gain knowledge of them. He was able to absorb information very rapidly and had tremendous bibliographic knowledge and if you asked him something, he could just give you a bibliography immediately. He knew scholastic material very well and studied it a lot. For a while, his group, which was called The Circle Bastiat, attended sessions of Ayn Rand's circle. Rand was a remarkable thinker in her own right. Although she hadn't studied history of

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philosophy very systematically, she developed views that were in many respects similar to those of Aristotle. So, there was some convergence there. He didn't really take it from her, but there was some convergence, because he was in his philosophical focus, very much an Aristotelian, like her. He didn't really write on metaphysics, he wrote on epistemology insofar as it applies to economics, but he was very influenced by Aristotelian and Thomistic ethics and developed that further. He developed natural law thinking on that basis.

JD: We think of Aquinas as a philosopher, as a legal theorist, and of course as a religious thinker. Most people

probably think of him more as a religious thinker than a philosopher *per se*.

DG: The relation between theology and philosophy is one of the most contested topics in the study of Aquinas. I would say he was a philosopher as well as a theologian in that a good many of his works are commentaries on Aristotle. He wrote books on how you could convert people who don't accept Christianity, not presupposing that theology is true. For him, in fact, there was some knowledge that could be obtained just by reasoning, and there was certain knowledge that couldn't be obtained by reasoning. This you could get only by faith, which is from revelation. But for him, even some of the knowledge obtained through reasoning could show why we should accept the Church's teachings.

JD: When Rothbard makes the normative case for *laissez-faire* in *The Ethics of Liberty*, he makes that normative case without appeal to higher powers. He relies on a secular morality as the foundation for a free and just society. What's his biggest influence there?

DG: Well, I think in this he talks about people as self-owners. You could say "why are we self-owners?" I think he would rely on an Aristotelian focus.

JD: Maybe this is my own Protestant upbringing, but when we talk about self-ownership it sounds inherently incompatible with Christianity. If you're a Christian you believe you were made in the image of God, and thus you're not some wholly independent being. You don't "own" yourself as part of God's creation.

DG: Yes. Well, that's a very interesting objection. If you look at Locke, Locke did believe that God really owns everybody. He also defends the self-ownership principle.

JD: God owns everybody?

DG: The claim here is God created us so God really owns us. But under that, we're in charge of our own lives, so it's something like this: suppose for all practical purposes, unless God is directly trying to tell us something,

we're in charge of our own lives. The fact God owns everything doesn't mean someone else can go around saying, "I'm God's representative, so you have to do this, do that." No one has direct access to God in that way that would justify that person imposing various limits on what a person can do. The notion of God owning us does have some bite to it in the real world. For example, many theologians have thought it's wrong for you to commit suicide. Because God owns you, you don't have the right to end your own life because that would be inconsistent with God's ownership. You could say, you could acquire property in the world because subject to God's ultimate ownership, you're really free to homestead land at least under certain conditions.

Rothbard is probably best called agnostic. I think his atheism wasn't as strong in his later years as earlier. His later position is something like, if there is a God, his actions and his knowledge would be so far different from normal, we wouldn't really be able to grasp what he was doing. This is more in conformity with Aristotle because Aristotle did believe that God really takes no notice of what's going on in the world and Aristotle says God is thinking about his own activities, his own being, and is not concerned with human beings.

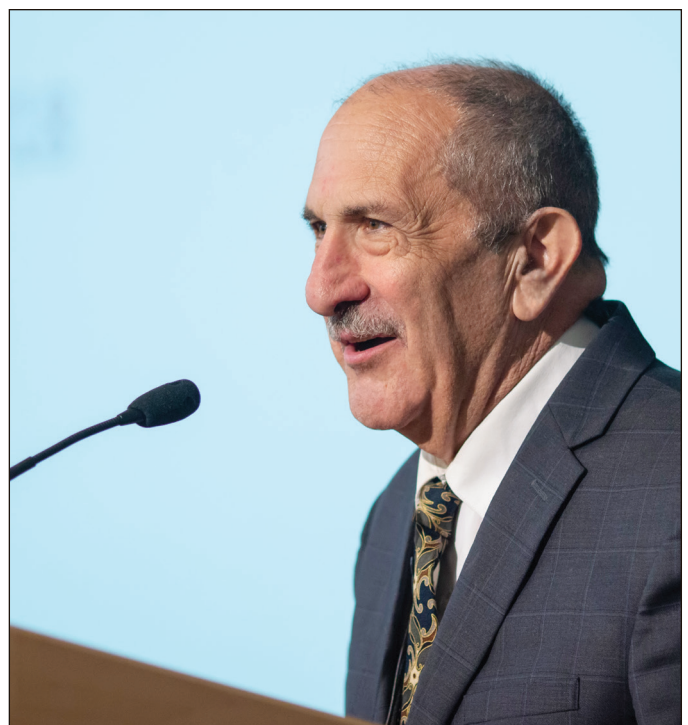
JD: David, let's talk about Ayn Rand. Both Mises and Rothbard knew her personally, and both socialized with her at one time. Many people think she was a highly derivative philosopher, that she didn't exhibit much original thought. Many people disagree, and think she was a brilliant philosopher who developed a fully complete system of original ideas on her own. Tell us about her relationships with Mises and Rothbard, how they may have influenced her, and vice-versa.

DG: It is true that some of her thought certainly resembles Aristotle in many points, but she was able to get a lot of her views independently. I think in some respects, she deviated in an incorrect way from Aristotle. She was certainly a significant thinker in philosophy. I frequently disagree with her, but she's certainly someone who's worth reading.

We also know a bit about her thinking on Mises because she used to make notes on books she was reading. We have her notes on *Human Action* and one note on that

always makes me laugh. She said that Mises usually talks about supply and demand, but one place he talks about demand and supply and she thought that there was something suspicious about that, but she didn't say what it was. So, she thought Mises was extremely good with economic theory, but she thought he didn't have the right theory of knowledge. She took him to be a Kantian and she didn't like this. They met a few times in person and Mises liked her *Atlas Shrugged*. He thought she was portraying the businessman as a hero, she was really doing something very valuable, but apparently they didn't get along. There's this story Henry Hazlitt invited both for dinner and they had some big falling out. They both had very strong personalities.

Now, Murray Rothbard, when he first heard about her, he tended not to like her much because he thought she was a very dogmatic thinker and if you disagreed with her, she would exclude you and he thought the tendencies in her personal way of dealing with people, he didn't like. So, he tended very much to stay away from her and was suspicious of her, but when *Atlas Shrugged* came out, he really liked it, admired her writing, so for a while, his group met with her group, but they didn't get along. The thing she most opposed in Murray's thinking was that Murray did not believe in the need for government, the



state would be replaced by competing protection agencies. She was very much against that. She thought that would lead to having no law and order. There were also other issues as well.

JD: There's a famous conversation, recounted in Nathaniel Branden's biography of Rand, where she asked Rothbard how police and court services would be provided under anarchy. Rothbard responds with "private, competing defense agencies" and Rand expressed in horror: "You mean as in civil war?" Let's just say their respective philosophies of governance diverged.

DG: There were other issues as well. One was that Murray's wife, JoAnn Rothbard, also a great friend of mine, was a quite devout Protestant. So Rand wanted her to listen to some tapes by Nathaniel Branden on why God doesn't exist and he felt that any rational person after listening to these tapes would be converted to atheism. So, if they listened to them and if she wasn't converted to atheism, then Murray should divorce her. Of course, he wasn't having any of that.

Another issue came up that goes back to some of the things we were talking about earlier on philosophy. Murray wrote an essay for a volume called *The Mantle of Science* where he was talking about arguments for free will. One of the arguments that's sometimes given is, supposing determinism were true, then the argument is, "well, suppose I'm saying determinism is true, so then am I saying it is because I'm being pre-determined to say that? But if I'm being determined to say that, then I'm not evaluating it rationally. So, then if determinism is true, I could never know it to be true." This is an argument that a lot of philosophers have used. Interestingly, one of the ones who uses an argument like that is Kant. But Murray thought that to be nice to the Randians, he cited part

of Barbara Branden's master's thesis where she said that, and used that argument. So then, when the volume came out, for some reason the citations to Branden were taken out, and Rand and Branden and the Rand group got very angry about it. They said, "oh, he's plagiarized Barbara Branden." In fact, the argument wasn't original with her, it's a very common argument. So, they were very angry and they protested, and they went to the publisher. And then Murray wrote to Mises, and Mises replied and said, "what's going on here, everybody knows about this argument, what are they complaining about?" But the Randians never forgot it.

JD: David, one final question. Menger, Mises, Hayek, and the older Austrians all pre-dated the rise of post-modern philosophy in the late twentieth century. Did Rothbard address postmodernism, and what effects do you think it has on economics today?

DG: Rothbard did address postmodernism in his essay "The Hermeneutical Invasion." There are many different varieties of postmodernism but in general, postmodernists attack the notion of truth as fixed and unalterable. Rothbard resisted this, relying on his Aristotelian realistic views. Fortunately, postmodernism hasn't influenced economics as much as it has the humanities. ■■■





The Real State *of the* Union

THE MISES INSTITUTE IN ORLANDO



The Mises Institute returned to Orlando this February to discuss "The Real State of the Union." **Robert Murphy** and **Jeff Deist** both offered analysis on the current economic and political climate in the US at a sold-out crowd at the University of Central Florida. They were joined by talk radio host **David Gornoski**, who talked about America's growing culture war, and Praxis apprentice **Lena Wang** who offered her own personal experience with the failing US university system.

Audio from the event is available at **Mises.org/ORL19**.

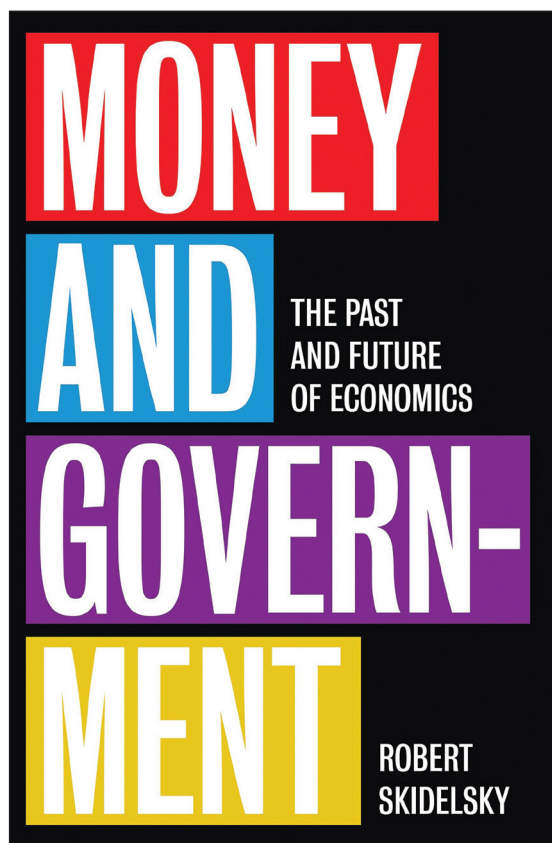
Special thanks to **Mr. and Mrs. Greg Roe** for making this event possible.



SKIDELSKY'S PUSH FOR MODERN MERCANTILISM

DAVID GORDON
REVIEWS

Money and Government:
The Past and Future of Economics
Robert Skidelsky
Yale University Press, 2018
xiv + 402 pages



The title of Murray Rothbard's *Power and Market* provides a useful entry to understanding Robert Skidelsky's long and learned book. Rothbard drew a contrast between peaceful cooperation through the free market and State coercion. Which do you support, he asks: power or market? Skidelsky, a historian and economist who has written admiring biographies of Keynes and the British fascist Oswald Mosley, is for the most part clear in his answer: power should prevail over the market.

Thus, although he notes that mercantilism rests on economic fallacies, he still thinks this system has much to be said for it. "Rising prices were associated with prosperity; falling prices with dearth. This correlation led a group of seventeenth-century thinkers called mercantilists to identify money with wealth. The more money a kingdom had, the wealthier it was; the less, the poorer." This view is mistaken: mercantilism was based on the "fallacy that exporting is better than importing and that the object of economic policy should therefore be to secure a favourable balance of trade ... of course, all countries cannot achieve a trade surplus simultaneously, so the pursuit of these policies involved continuing trade wars between the leading European powers."

But what is wrong with trade wars? "The mercantilists believed that state activity and spending could galvanize the growth of national wealth. War was an investment decision by the state: the state needed sufficient revenue to conquer foreign markets." Why rely on peaceful exchange when you can take what you want by force?

In addition, war has another benefit: it reduces inequality. "Recently, discussion of distribution has centred on the fact, and meaning, of the sharp rise in inequality since the 1970s, particularly in the United States and Britain. The most notable contributions here are Thomas Piketty's *Capital in the Twenty-First Century* (2013) ...

and Walter Scheidel's *The Great Leveler* (2017). ... Both attribute the great compression of wealth and incomes in the middle years of the last century to the effects of the two world wars and Great Depression."

Skidelsky is not content to urge the merits of power over market. He wishes to challenge advocates of the free market on their own ground. They take as their standard the welfare of consumers and on that basis argue for voluntary exchange. The fundamental argument of his book is that, in doing so, they fail to realize the disruptive effect of money. In a barter economy, Say's Law, which Skidelsky wrongly states as "the infamous ... Law that supply creates its own demand" holds true. As W.H. Hutt pointed out in his major study *A Rehabilitation of Say's Law*, the law is better stated as "all power to demand is derived from production and supply." Another way to state the law is "the supply of a good on the market is demand for other goods." There can be no overproduction that covers all of the economy.

Once money enters the scene, the situation alters. Instead of spending their money on consumption or investment goods, people can hoard money. "Speculators, too, have always known that in disturbed times they can profit from being liquid. Increased propensity to hoard, what Keynes called the 'speculative demand for money,' thus arises from increased uncertainty. It slows down the economy by slowing down the spending of money on currently produced goods and diverting it into financial operations. Thus money earned in producing goods

may be unavailable for spending on those goods, causing unemployment."

As Skidelsky tells the tale, neoclassical economists who favored the free market attempted to solve this problem through the quantity theory of money. By varying the quantity of money, the monetary authorities could keep the value of money stable. In that way, the fears of speculators would be calmed and hoarding averted or countermanded. Milton Friedman's monetarism is the best known example of this view, but Knut Wicksell, and even Keynes before the *General Theory*, supported it. As Keynes came to realize, though Friedman did not, monetarism does not work. The central monetary authority is unable to control the money supply in the way this theory supposes.

Although Skidelsky mentions Austrian economics several times, he never confronts the Austrian criticism of his entire line of reasoning. In the Austrian view, he has gotten wrong both the alleged problem posed by hoarding and the alleged "cure" that the proponents of the free market suggest for it.

As Murray Rothbard has pointed out in *Man, Economy, and State*, allocation of resources between consumption and investment depends on the rate of time preference. The demand to hold money creates no special problem for this allocation. In assuming otherwise, Keynes and his followers wrongly took the loan rate of interest to be primary, when in fact it is subordinate to



the primary determinant of the rate of interest, the aforementioned rate of time preference

Rothbard explained the basis of the Austrian account of the interest rate in this way: “People, therefore, allocate their money, among consumption, investment, and hoarding. The proportion between consumption and investment reflects individual time preferences. To think of the rate of interest as ‘inducing’ more or less saving or hoarding is to misunderstand the problem completely. ...

One grave and fundamental Keynesian error is to persist in regarding the interest rate as a contract rate on loans, instead of the price spreads between stages of production.” In contrast to the Keynesian fear that expectations of falling consumption demand will lead to a cycle of further price falls and lowered expectations, Rothbard says, “The expectation of falling factor prices speeds up the movement toward equilibrium and hence toward the pure interest rate as determined by time preference.”

Moreover, the speculative bubbles that Keynes feared stem not from sudden and mysterious collapses of the “animal spirits” of investors but rather from injections of bank credit in fractional reserve banking, a system unsustainable without state control of the money supply. Skidelsky is well aware of this

theory but has little to say about it, perhaps because he does not like its consequences for policy: “The causes of the crash of 1929 have been much disputed. Friedrich Hayek claimed that it was a result of excessive credit creation in the United States. In his account, the price stability of the mid-1920s, so much praised by the monetary reformers, was an indication of inflation, not of equilibrium, since productivity gains would have naturally

It is ironic that Skidelsky takes the failure of monetarism, a form of state intervention, to show the defects of the unhampered market economy.



produced a falling price level. ... ‘Excessive credit creation’ became the standard ‘Austrian’ explanation of the 1929 collapse. It resurfaced to explain the crash in 2008. ... On the Austrian analysis, recessions give a chance to re-allocate ‘mal-invested’ productive factors to efficient uses. They should therefore be allowed to run unhindered until they have done their work. Economists whose common sense had not been completely destroyed by their theories rejected the drastic cure of destroying the existing economy in order to rebuild it in the correct proportions.” Skidelsky is sure that allowing prices to fall in a depression would ruin the economy, but as James Grant shows in his outstanding *The Forgotten Depression*, the US government did exactly that in coping with the downturn in 1920–1921, and the result was a speedy recovery. Skidelsky cites Grant’s book in his bibliography but ignores its relevance to his complaint against the “drastic cure.”

Further, Austrians reject the quantity theory of money. Mises in *The Theory of Money and Credit* said about it: “There is no justification whatever for the widespread belief that variations in the quantity of money must lead to inversely proportionate variations in the objective exchange value of money, so that, for example, a doubling of the quantity of money must lead to a halving of the purchasing power of money.” Austrians thus oppose endeavors by the state to stabilize the value of money based on this theory. It is ironic that Skidelsky takes the failure of monetarism, a form of state intervention, to show the defects of the unhampered market economy.

Our account of Skidelsky's book now takes a surprising turn. Although he opposes the free market, he is not prepared to dismiss entirely the views of the Austrians. To the contrary, he considers Hayek a great thinker and recognizes that his warnings against government intervention have merit. "Liberalism, or social democracy, unraveled with stagflation and ungovernability in the 1970s. ... Keynesian/social democratic policymakers succumbed to hubris, an intellectual corruption that convinced them they possessed the knowledge and the tools to manage and control the economy and society from the top. This was the malady against which Hayek had inveighed in his classic *The Road to Serfdom* (1944)."

Skidelsky recognizes that the Keynesians had no adequate answer to the "stagflation" of the 1970s. He also recognizes the force of the "public choice" analysis of government though he by no means commits himself fully to it. "Its main thrust was to emphasize the importance of

the private incentives facing politicians and bureaucrats. The Keynesian-social democratic state was modelled as a private interest masquerading as guardian of the public interest. This was back to Adam Smith." Skidelsky errs, though, when he says that "Public choice theory is simply rational expectations theory applied to government. It takes from REH [rational expectations hypothesis] the methodology of modelling public policies as the solution to individual maximization problems." This is not correct. The basis of the theory is that politicians are self-interested actors, but this does not commit one to a particular model of how such actors behave.

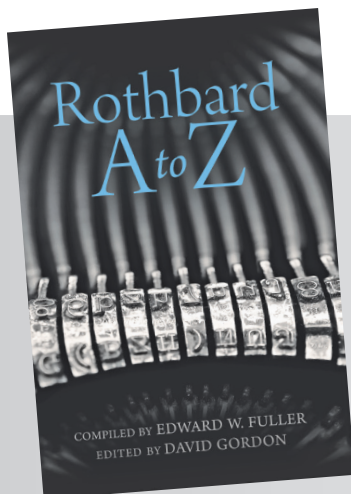
Even readers who disagree with the thrust of the book will benefit from Skidelsky's wide learning. The author sometimes makes mistakes. He says, "The French state, which emerged from the war [WWII] as the nation's chief investor, did not have to learn its statism from Keynes; Colbert had pointed the way in the eighteenth century." That was a neat trick for Colbert, who died in 1683. He calls the well-known businessman and New Deal financial expert Beardsley Ruml "Rummel." But the slips are few and minor.

Just as in his earlier book *How Much Is Enough?* (2012), Skidelsky manifests an inordinate distaste for money and "greed." Far better in his eyes is the pursuit of power by the State, even at the cost of wars and massive public debt. Some of us will not agree. ■■■

David Gordon is Senior Fellow at the Mises Institute, and editor of *The Mises Review*.

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- March 23, 2019** 70th Birthday Party for Hans-Hermann Hoppe; Mises Institute
- April 11, 2019** Jeff Deist at Young Americans for Liberty; Kent State University
- May 28, 2019** Jeff Deist at the Pittsburgh Federalist Society
- June 2–7, 2019** Rothbard Graduate Seminar; Mises Institute
- July 14–20, 2019** Mises University; Mises Institute
- September 28, 2019** Libertarian Scholars Conference; New York, NY
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Jeff Deist, MISES INSTITUTE

Jeff Deist *in* Mexico City

Mises Institute president Jeff Deist recently visited Mexico City at the invitation of several former Mises University students.

Deist spoke to student groups at the National Autonomous University of Mexico, the Panamerican University, and the Ibero-American University. He also addressed the Congress of Mexico City about promoting markets and property in Latin America.

He appeared in a network television interview with Sergio Sarmiento, who hosts the longest-running interview show in Mexico on TV Azteca. They discussed the legacy of Ludwig von Mises, who delivered a series of lectures in Mexico City in 1942 to bankers and businessmen.

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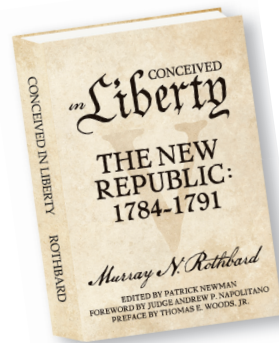


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